



2005
Nine Month Report

Sirit Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following MD&A has been prepared to help investors understand the financial performance of the Company and provides information that management believes is relevant to an assessment and understanding of the Company's risks, opportunities and performance measures. Management has prepared this document in conjunction with its broader responsibilities for the accuracy and reliability of the financial statements and the development and maintenance of appropriate internal controls in its effort to ensure that the financial information is complete and reliable. The Audit Committee of the Board of Directors, consisting of three independent directors, has reviewed this document and all other publicly reported financial information, for integrity, usefulness, reliability and consistency.

This discussion, which has been prepared as of October 20, 2005 at which time 92,958,401 shares are outstanding, should be read in conjunction with the unaudited consolidated financial statements for the period ended September 30, 2005 and the audited consolidated financial statements, including the notes thereto included in the Company's December 31, 2004 annual report. This discussion contains forward-looking statements that involve inherent risks and uncertainties. The Company's actual results and the results of its investees may differ materially from those anticipated in these forward-looking statements. All amounts presented in this MD&A are in accordance with Canadian GAAP and presented in thousands of Canadian dollars unless otherwise specifically noted.

GENERAL

Sirit Inc. ("Sirit" or "the Company") is a Radio Frequency Identification ("RFID") company that designs, develops, manufactures and sells RFID products and solutions. For over 12 years, Sirit and its subsidiaries have been delivering RFID products and solutions to customers based primarily in the United States and Canada and also growing throughout the Americas, Europe and Asia. More information on the Company can be found at www.SEDAR.com.

On September 1, 2005 Sirit announced the appointment of Mr. David Andrews as Chairman of the Board to replace Mr. William W. Staudt. Mr. Andrews joined the Board in April 2005 and continues to serve as a member of the Compensation Committee and as the Chairman of the Audit Committee. Mr. Andrews has 27 years of management and executive experience in the technology sector with Fortune 500 companies including Compaq, Tandem and Unisys, as well as a number of Canadian technology companies and is currently the Chairman of the Board of Coss Systems Inc., a global provider of software solutions for the manufacturing marketplace. Mr. Andrews is a Chartered Accountant with the Institute of Chartered Accountants of Ontario.

On September 7, 2005 Sirit announced a significant milestone with the shipment of its 250,000th RFID reader. The Sirit readers have been installed to support applications in supply chain, parking and access control, product verification, cashless payments and retail inventory control and include both the INfinity and IDentity series of readers.

At the EPCglobal™ Exhibition in Atlanta, Georgia on September 14, 2005, Sirit introduced its latest UHF EPCglobal™ compliant reader module, the INfinity 210. Designed for integration into handhelds, portable data terminals, printers, label applicators, mobile computers and other OEM devices, Sirit's INfinity 210 simultaneously supports multiple RFID tag protocols including EPC Class 0, EPC writeable Class 0 / Class 0+, EPC Class 1, and EPC UHF Gen 2 (C1G2) standards.

In September 2005, the Company took action to reduce expenses through staff and discretionary expense reduction and consolidation of certain organizational functions. As part of this effort, Mr. Don Bergeron was named Vice President, Operations, who, in addition to overseeing manufacturing activities, will assume management of engineering and development responsibilities from Mr. Loek d'Hont, Chief Technology Officer, who has left the Company.

The Company updated its expectations for annual 2005 revenue levels, noting 2005 revenue is anticipated to be approximately 20-25% below previous year results. The revenue shortfall is attributable to

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unusually strong sales in 2004 of electronic toll tags as customers offered promotional programs and took shipment of high volumes of tags. While Sirit has not lost a single Toll customer, agency consolidation and higher customer inventory levels built in the previous year have resulted in reduced or delayed toll tag orders in the current fiscal year. Sirit believes that toll tag orders will experience growth in 2006 compared to 2005. Overall, the Company anticipates revenue will grow in all of its market applications in 2006.

On September 29, 2005 Sirit announced the appointments of Messrs. Art Mesher and Cal Haverstock to the Board of Directors. Mr. Art Mesher is Chief Executive Officer of Descartes Systems Group Inc., a leading provider of on-demand technology and services where he oversees the Company's strategic operations with direct responsibility for the Executive Management team. In 1998, Mr. Mesher joined Descartes where he led the creation of the first on-demand logistics network that provides application and communication capabilities. Mr. Cal Haverstock is President and CEO and a member of the Board of Directors of Playdium Corporation, where he has spearheaded the restructuring and refinancing of the company. In addition, Mr. Haverstock is President and Chairman of Haverstock Associates, a consulting firm focused on strategic corporate optimization.

Subsequent to quarter end, on October 13, 2005 Sirit announced its successful bid for a CDN \$4.0 million, 10 month supplier contract of RFID toll tags to its long time customer, Bay Area Toll Authority ("BATA") in California. The contract calls for Sirit to deliver RFID toll transponder technology commencing November 2005, with associated revenue to be recognized commencing in the fourth quarter of 2005.

RESOURCES

Cash Flows, Liquidity and Capital Resources

The Company's total cash and cash equivalents at September 30, 2005 is \$7.0 million, reflecting the use of \$0.9 million during the third quarter from a balance of \$7.9 million at June 30, 2005. Year-to-date the Company has utilized \$3.0 million of cash from a balance of \$10.0 million at December 31, 2004. Cash resources have been applied to support development efforts and normal operations.

The Company reclassified its investments to short-term during the third quarter to reflect the Company's intention to sell these investments to exit its Portfolio Investments Business Segment and utilize any cash generated from the disposition to support its ongoing RFID operations. The Company took a write-down on Medsite, Inc. of \$0.9 million during the quarter to reflect its estimation of net realizable value based on a shorter term view and similar market transactions. Management will be performing further evaluation of its non-core investments during the fourth quarter which may result in additional write-downs.

Operating Activities

During the third quarter of 2005 cash utilized to support continuing operations was \$1.4 million with \$4.2 million spent year-to-date. This is compared to cash utilized for continuing operations in the third quarter of 2004 of \$0.4 million and cash generated in the first nine months of 2004 of \$0.4 million.

Sirit's working capital position, (which includes total current assets less total current liabilities), at September 30, 2005 is \$11.6 million compared to \$8.9 million at June 30, 2005 and \$11.5 million at December 31, 2004. The change in working capital has resulted from the reclassification of \$4.2 million of investments from long-term to short-term and the use of working capital and cash of \$1.5 million to fund operations. Further details regarding the remaining fluctuations of key balances which comprise working capital are noted as follows:

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The decrease in accounts receivable of \$1.0 million during the third quarter and \$1.4 million since December 31, 2004 results from an improved ageing profile of total receivables when compared to December as well as lower sales year-to-date. When compared to June 30, 2005, the overall ageing profile has remained consistent, with the decline in total receivable balance due to lower sales during the third quarter when compared to the second quarter.

Accounts payable and accrued liabilities at September 30, 2005 decreased by \$0.5 million from June 30, 2005 and \$0.1 million from December 31, 2004. The decline in payables and accruals during the third quarter is the result of lower volumes of product purchases consistent with lower sales, reduction of year-end bonus accrual and partially offset by the remaining \$0.1 million of severance accrual. The lower volumes of purchases accounts for the majority of the change in payables and accruals since December 31, 2004.

Inventory at September 30, 2005 has remained consistent with the balance at June 30, 2005. Late in the third quarter, Sirit introduced the INfinity 210 UHF module, representing the latest UHF technology. During a period of product introduction it is necessary for the Company to maintain inventory to support older product lines while building for the new introductions.

The decrease in prepaids and deposits of \$0.2 million since June 2005 and \$0.5 million since December 31, 2004 reflects utilization of certain prepaid development activities as well as normal usage of prepaid items such as insurance which coincide with the calendar year.

Investing Activities

There were minimal investing activities during the nine months of 2005. The Company invests on an as needed basis for capital assets to support ongoing operations.

Financing Activities

Cash generated from the exercise of options in the first nine months of 2005 reached \$0.3 million. This is compared to the first nine months of 2004 when the Company closed the second tranche of its financing with J.L. Albright III Venture Fund for net cash proceeds of \$5.0 million plus the exercise of options for almost \$0.4 million.

Commitments

The following reflects the Company's commitments under premises leases for the next 5 years. The Company has committed to a new 64 month lease for its head office premises in Toronto, Canada, in addition to its leased offices in Carrollton, Texas and Loughborough, England. The value of these three lease commitments is reflected in the amounts noted below.

| | Payments due by Period | | | | |
|-------------------------|-------------------------------|---------------------|---------------------|---------------------|---------------------|
| Contractual Obligations | Total | Up to 1 year | 2 to 3 years | 4 to 5 years | Over 5 years |
| Premises Leases | <u>\$ 1,465</u> | <u>\$ 347</u> | <u>\$ 657</u> | <u>\$ 425</u> | <u>\$ 36</u> |

There are no commitments to purchase capital assets at this time.

As at September 30, 2005, certain accounts receivable and inventory are pledged as security in connection with accounts payable in the amount of \$178 (June 30, 2005 – \$468).

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There were no additional commitments out of the ordinary course of business entered into during the third quarter of 2005.

Related Party Transactions

The Company incurred directors fees of \$47 for their services during the third quarter (nil in the third quarter of 2004).

The Company paid \$3 to a director for consulting services (nil in the third quarter of 2004) and \$21 to a second director for legal services during the third quarter (\$27 in the third quarter of 2004).

There were no other related party transactions during the third quarter of 2005.

RESULTS

For the three and nine months ended September 30, 2005 compared to the three and nine months ended September 30, 2004

| | Three months ended Sept 30 | | Nine months ended Sept 30 | |
|---|----------------------------|-----------|---------------------------|-----------|
| | 2005 | 2004 | 2005 | 2004 |
| Revenue | \$ 3,107 | \$ 5,162 | \$ 12,165 | \$ 15,623 |
| Cost of Sales | 2,070 | 2,925 | 7,949 | 9,067 |
| Gross profit | 1,037 | 2,237 | 4,216 | 6,556 |
| Expenses | 2,923 | 2,919 | 9,838 | 7,137 |
| Operating (loss) | (1,886) | (682) | (5,622) | (581) |
| Net (loss)/income | \$ (2,759) | \$ (642) | \$ (6,419) | \$ 1,837 |
| Basic and diluted (loss)/income per share | \$ (0.03) | \$ (0.01) | \$ (0.07) | \$ 0.02 |
| Total assets | \$ 19,279 | \$ 25,639 | \$ 19,279 | \$ 25,639 |
| Total long-term financial liabilities | \$ - | \$ - | \$ - | \$ - |

Revenue

The following summarizes the significant components of revenue for the third quarter and first nine months of 2005:

- For the third quarter of 2005, reported revenue is \$3.1 million, a decline of approximately \$2.1 million when compared to the third quarter of 2004. Total revenue for the nine months ended September 30, 2005 is \$12.2 million, lower by approximately \$3.4 million or 22% when compared to the first nine months of 2004.
- Due to the continued strengthening of the Canadian dollar against the US dollar, total revenue for the first nine months of 2005 has been negatively impacted by approximately \$1.0 million when compared to the same period in 2004. Without this foreign exchange impact, year-to-date revenue for 2005 would be \$13.2 million or approximately 15% lower than year-to-date revenue reported in 2004.

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- The Company anticipates annual 2005 revenue to be in the range of 20% to 25% below annual 2004 reported revenue, including the negative impact of foreign exchange.
- A further analysis of revenue by the Company's primary RFID applications follows.

Automatic Vehicle Identification (AVI) Applications

- Revenue generated from AVI applications in the third quarter of 2005 is \$2.6 million compared to \$4.2 million for the third quarter of 2004. Through the first nine months of 2005, AVI application revenue represents 76% of total revenue or \$9.3 million compared to 82% or \$12.9 million for the same period in 2004. The \$3.6 million decline represents a 28% drop in revenue when compared to the first nine months of 2004.
- The AVI applications can be further broken down between Toll applications and Parking and Access Control (PACS) applications. Toll applications represents \$7.4 million and PACS applications represents \$1.9 million of the total AVI application revenue for the nine months ended September 30, 2005.
- The PACS applications revenue for the first nine months of 2005 has remained stable on a comparative basis with 2004, even when including negative foreign exchange impact. The Toll applications revenue decline in the current quarter has resulted from customers building inventory levels in the prior year which have not recurred in the current year, the consolidation of three Toll customers into one agency resulting in lower transponder orders and negative impact of foreign exchange. Included in Toll revenue is \$0.4 million from an integration project completed during the quarter.

Radio Frequency Solutions (RFS) Applications

- For the 2005 third quarter, RFS product revenue was \$0.5 million or 16% of total revenue compared to \$1.0 million or 19% of the 2004 third quarter revenue. Year-to-date revenue earned on the Company's RFS applications represents 24% of total revenue or \$2.9 million.
- RFS revenue has increased by almost 5% or just over \$0.1 million for the first nine months of 2005 compared to the prior year. Sales of RFS product have slowed in the third quarter due to the slower than anticipated implementation of RFID applications in the Supply Chain. Sales of RFS product are expected to fluctuate on a quarterly basis as one-off tests and pilots continue but are not predictable as to timing, size or value of each project.
- The Company continues to support the view that the overall RFID market remains in the very early stages of implementation. It is therefore impossible to reasonably estimate future deployment wins and associated revenue potential.

Gross Margin

Gross margin for the third quarter of 2005 is 33.4% compared to 43.3% reported in the third quarter of 2004. Year-to-date gross margin for 2005 is 34.7% compared to 42.0% in 2004. The decline in gross margin for the third quarter as well as year-to-date for 2005 results from the fixed portion of overhead costs which represents a larger percentage of the lower sales base.

Selling, General and Administrative Expenses (SG&A)

- Total SG&A expenses for Q3 2005 were \$1.7 million compared to \$1.8 million in Q3 2004. These expenses are split into two major categories as follows:

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- The Q3 2005 salaries and benefits of \$0.8 million (Q3 2004 - \$0.9 million) are lower than prior year due to management's decision to reduce 2005 year-end bonuses impacting the expense by \$0.2 million. SG&A employees at September 30, 2005 and 2004 total 22. During the quarter, the Company reduced its SG&A staff as efficiencies were identified in an effort to reduce operating costs. Included in the salaries and benefits are stock compensation costs of \$0.2 million compared to less than \$0.1 million in Q3 2004.
- The remaining Q3 2005 SG&A expenses of \$0.9 million (Q3 2004 - \$0.9 million) have remained stable with recurring expenses such as travel, rent and professional fees representing the largest remaining components of SG&A.

Development Expenses

- Development expenses for Q3 2005 totaled \$0.9 million (Q3 2004 - \$0.6 million). Development efforts continue to be focused primarily on products to support RFS applications. The Company introduced its INfinity 210 module late in the third quarter of 2005. Included in the third quarter development expenses was severance of \$0.1 million relating to the reduction of 4 development staff.
- Development staff complement at September 30, 2005 was 13 compared to 14 at September 30, 2004 and 17 at June 30, 2005. The staff reductions which occurred in the third quarter will not impact the Company's development efforts as staffing changes reflect the Company's commitment to continuously review its ongoing needs to ensure efficient operations in the current environment.

Quarterly Results

| | 2005 3rd Q | 2005 2nd Q | 2005 1st Q | 2004 4th Q | 2004 3rd Q | 2004 2nd Q | 2004 1st Q | 2003 4th Q |
|--|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Revenue | \$ 3,107 | \$ 4,632 | \$ 4,426 | \$ 4,876 | \$ 5,162 | \$ 5,525 | \$ 4,936 | \$ 4,089 |
| Net income/(loss) from continuing operations | (2,759) | (2,619) | (1,041) | (913) | (642) | 1,889 | 590 | (526) |
| Net income/(loss) for the period | (2,759) | (2,619) | (1,041) | (913) | (642) | 1,889 | 590 | (526) |
| Net income/(loss) per share, from continuing operations, basic and diluted | \$ (0.03) | \$ (0.03) | \$ (0.01) | \$ (0.01) | \$ (0.01) | \$ 0.02 | \$ 0.01 | \$ (0.01) |
| Net income/(loss) per share, basic and diluted | \$ (0.03) | \$ (0.03) | \$ (0.01) | \$ (0.01) | \$ (0.01) | \$ 0.02 | \$ 0.01 | \$ (0.01) |

The 2005 third quarter revenue decline is attributable to lower Toll transponder sales along with a lower level of RFS application sales when compared to Q2 2005. The net loss includes a write-down of one non-core investment of \$0.9 million plus \$150 of severance costs associated with staff reductions which occurred during the quarter.

Second quarter 2005 net loss included lower than anticipated AVI revenue plus non-recurring adjustments totaling \$1.2 million during the quarter and continued RFS application development efforts.

The first quarter 2005 revenue was impacted by the timing of shipments of Toll transponders which were lower when compared to the first quarter of 2004. The net loss results from on-going development efforts and normal operations with a lower revenue base.

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During the third and fourth quarters of 2004, the Company significantly increased its development efforts totaling \$1.3 million and was negatively impacted by foreign exchange costs of \$0.6 million.

The decline in fourth quarter revenue in 2004 is due to reduced sales and available shipping times over the holiday seasons in Canada and the US.

The gain on sale of one of the Company's long-term investments totaling \$2.0 million was included in the Q1 and Q2 2004 net income. Included in the Q1 2004 net income was the one-time sale of an intangible asset of \$294.

Due to rapidly changing market conditions during the second half of 2003, management had changed its strategy with respect to one of its AVI applications. As a result, in Q4 2003, the Company wrote-off \$245 of deferred development costs and \$260 of deposits associated with this development effort.

SIGNIFICANT ACCOUNTING POLICIES AND MANAGEMENT ESTIMATES

There have been no material changes to the significant accounting policies and management estimates presented in the Annual Report of the Company as at December 31, 2004 and the Annual Information Form dated March 22, 2005. Please refer to these reports for a detailed analysis of the significant accounting policies and estimates made by management at that time.

RISKS

Sirit's management team has the responsibility for the daily evaluation and management of risk factors affecting the Company. Management's assessment of the most significant potential risks which would have the greatest impact on the Company over the ensuing 12 to 24 months given currently available information, and except as noted below have not changed significantly from those presented in the 2004 Annual Report. This analysis contains forward looking statements that may differ materially from future actual results.

RFID Adoption Rate

Sirit has been an active participant in the most prominent trade shows and conferences through the first nine months of 2005, including EPCglobalTM in September 2005. The Company viewed several key themes emerging from these conferences. First, RFID continues to gain greater mindshare with organizations looking to improve efficiencies within their supply chains. Second, RFID technology continues to improve, specifically with respect to tag sensitivity, a key to improving read rates, with each new generation of chip technology. Third, major organizations other than Wal-Mart and the U.S. Department of Defense are moving somewhat slower than expected in their adoption of RFID. The Company believes that while RFID will achieve the prominence expected within the supply chain and closed-loop applications, adoption rates will be somewhat slower overall than 2004 research might have indicated. Sirit is financially positioned to manage potential slowdowns in the adoption rate or rapid technological changes that may result given its cash and working capital balances, as well as the recurring revenues earned from its AVI applications.

Investments

Sirit currently owns three minority interest investments recorded at approximately \$4.2 million. There is a risk that these organizations will face operating or market risks not currently foreseen by local management. Sirit faces the risk that it will not be able to liquidate these investments and realize the reported carrying values. Sirit reviews the valuation of these investments on a regular basis.

Sirit Inc.
Interim Consolidated Balance Sheets
(expressed in thousands of Canadian dollars)

Unaudited

| | As at September 30 2005 | As at December 31 2004 |
|--|--|---------------------------------------|
| Assets | | |
| <i>Current Assets</i> | | |
| Cash and cash equivalents | \$ 7,014 | \$ 10,021 |
| Accounts receivable | 1,932 | 3,319 |
| Inventory | 1,617 | 1,296 |
| Investments (note 2) | 4,291 | - |
| Prepays and deposits | 244 | 716 |
| | <u>15,098</u> | <u>15,352</u> |
| Long-term investments | - | 5,191 |
| Property, plant and equipment, net | 856 | 896 |
| Intangible asset, net | 421 | 573 |
| Deferred development costs, net | 75 | 123 |
| Goodwill | 2,829 | 2,829 |
| | <u>\$ 19,279</u> | <u>\$ 24,964</u> |
| Liabilities | | |
| <i>Current Liabilities</i> | | |
| Accounts payable and accrued liabilities | \$ 2,454 | \$ 2,596 |
| Deferred revenue | 778 | 913 |
| Warranty obligations | 225 | 310 |
| | <u>3,457</u> | <u>3,819</u> |
| Shareholders' equity | | |
| Share capital (note 3) | 35,137 | 34,763 |
| Contributed surplus (note 3d) | 1,122 | 400 |
| Deficit | (20,437) | (14,018) |
| | <u>15,822</u> | <u>21,145</u> |
| | <u>\$ 19,279</u> | <u>\$ 24,964</u> |

Commitments and guarantees (note 6)

Approved by the Directors:

"N. Dawalibi"
Director

"D. Andrews"
Director

See accompanying notes

Sirit Inc.**Interim Consolidated Statements of Operations**

(expressed in thousands of Canadian dollars except per share amounts)

Unaudited

| | Three Months Ended | | Nine Months Ended | |
|--|---------------------------|--------------------|--------------------------|--------------------|
| | September 30 | | September 30 | |
| | 2005 | 2004 | 2005 | 2004 |
| Revenue | \$ 3,107 | \$ 5,162 | \$ 12,165 | \$ 15,623 |
| Cost of Sales | 2,070 | 2,925 | 7,949 | 9,067 |
| Gross profit | 1,037 | 2,237 | 4,216 | 6,556 |
| Expenses | | | | |
| Selling, general and administrative | 1,718 | 1,762 | 6,835 | 5,009 |
| Development | 899 | 591 | 2,481 | 1,389 |
| Amortization | 157 | 129 | 457 | 388 |
| Foreign exchange | 149 | 437 | 65 | 351 |
| | 2,923 | 2,919 | 9,838 | 7,137 |
| Operating (loss) | (1,886) | (682) | (5,622) | (581) |
| Gain on sale of investment | - | - | - | 2,019 |
| Write-down of investment (note 2) | (900) | - | (900) | - |
| Other income | - | - | - | 294 |
| Interest income, net | 27 | 40 | 103 | 105 |
| Net (loss)/income for the period | \$ (2,759) | \$ (642) | \$ (6,419) | \$ 1,837 |
| Deficit, beginning of period | (17,678) | (12,463) | (14,018) | (14,942) |
| Deficit, end of period | \$ (20,437) | \$ (13,105) | \$ (20,437) | \$ (13,105) |
| Basic and diluted (loss)/income per share | \$ (0.03) | \$ (0.01) | \$ (0.07) | \$ 0.02 |

See accompanying notes

Sirit Inc.**Interim Consolidated Statements of Cash Flows**

(expressed in thousands of Canadian dollars except per share amounts)

Unaudited

| | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|--|--|-------------------------|---|-------------------------|
| | 2005 | 2004 | 2005 | 2004 |
| Cash provided by/(used in): | | | | |
| Operating Activities | | | | |
| (Loss)/income from continuing operations | \$ (2,759) | \$ (642) | \$ (6,419) | \$ 1,837 |
| Items not involving cash and cash equivalents (note 5a) | 1,260 | 201 | 2,143 | (1,446) |
| | <u>(1,499)</u> | <u>(441)</u> | <u>(4,276)</u> | <u>391</u> |
| Net change in non-cash working capital items (note 5b) | 626 | (812) | 1,176 | (810) |
| | <u>(873)</u> | <u>(1,253)</u> | <u>(3,100)</u> | <u>(419)</u> |
| Investing Activities | | | | |
| Additions to property, plant and equipment | (73) | (119) | (238) | (294) |
| Proceeds on sale of investment | - | - | - | 3,036 |
| Investment in Horizon Wimba, Inc. | - | - | - | (36) |
| | <u>(73)</u> | <u>(119)</u> | <u>(238)</u> | <u>2,706</u> |
| Financing Activities | | | | |
| Issuance of common shares, net of associated expenses | 29 | 357 | 310 | 5,373 |
| | <u>29</u> | <u>357</u> | <u>310</u> | <u>5,373</u> |
| Exchange rate impact on cash and cash equivalents | <u>7</u> | <u>-</u> | <u>21</u> | <u>3</u> |
| (Decrease)/increase in cash and cash equivalents | <u>(910)</u> | <u>(1,015)</u> | <u>(3,007)</u> | <u>7,663</u> |
| Cash and cash equivalents, beginning of period | 7,924 | 11,282 | 10,021 | 2,604 |
| Cash and cash equivalents, end of period | <u>\$ 7,014</u> | <u>\$ 10,267</u> | <u>\$ 7,014</u> | <u>\$ 10,267</u> |
| Cash and cash equivalents consist of: | | | | |
| Cash and deposit accounts with banks | \$ 692 | \$ 2,354 | \$ 692 | \$ 2,354 |
| Short-term commercial paper | 6,322 | 7,913 | 6,322 | 7,913 |
| | <u>\$ 7,014</u> | <u>\$ 10,267</u> | <u>\$ 7,014</u> | <u>\$ 10,267</u> |

See accompanying notes

Sirit Inc.**Notes to the Consolidated Financial Statements (unaudited)****(expressed in thousands of Canadian Dollars except per share information)****1. BASIS OF PREPARATION**

The accompanying unaudited consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements. Accordingly, certain disclosures normally included in annual financial statements prepared in accordance with Canadian generally accepted accounting principles are not provided. These interim financial statements have been prepared based on the accounting principles consistent with those used in the annual audited consolidated financial statements and should be read in conjunction with the annual audited financial statements of the Company for the year ended December 31, 2004. The results of the operations for the interim period are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year.

2. INVESTMENTS

Investments are recorded at the lower of cost and estimated net realizable value and include:

| | September 30 | December 31 |
|----------------------------|---------------------|--------------------|
| | 2005 | 2004 |
| Medsite, Inc. | \$ 3,033 | \$ 3,933 |
| Applied Data Systems, Inc. | 739 | 739 |
| Horizon Wimba, Inc. | 519 | 519 |
| | \$ 4,291 | \$ 5,191 |

As part of management's continuous review of the valuation of its investments, during the third quarter of 2005 management reduced the estimated net realizable value of its investments by \$900. The valuation is based on common valuation techniques and includes comparisons with similar market transactions. The decision was made to reclassify the investments as short-term as management is actively seeking to sell its position in each of the above companies.

3. SHARE CAPITAL

(a) Common shares issued and outstanding:

| | Shares | Amount |
|--|-------------------|------------------|
| Balance at December 31, 2004 | 92,147,001 | \$ 34,763 |
| Issued on exercise of stock options | 694,230 | 310 |
| Transfer from contributed surplus on exercise of stock options | - | 10 |
| Issued for services rendered | 50,000 | 54 |
| Balance at September 30, 2005 | 92,891,231 | \$ 35,137 |

(b) During the period July 1, 2005 to September 30, 2005, the Company granted 100,000 stock options to an employee. Total options issuances year-to-date are 2,838,400. The Company determines compensation costs on options granted based on the fair value at the grant date consistent with the fair value method of accounting for stock-based compensation. The stock-based compensation expense related to stock options included in selling, general and administrative expenses and in contributed surplus was \$203 in the third quarter (\$72 in the third quarter of 2005), with a year-to-date total of \$732 (\$177 in 2004).

(c) On April 21, 2005, the Company issued 50,000 shares to an executive of the Company for services rendered. The Company determined compensation cost on these shares based on the fair value at the grant date. The stock-based compensation expense included in selling, general and administrative expenses associated with this issuance in the second quarter of 2005 was \$54.

(d) The following table reconciles contributed surplus for the nine months ended September 30, 2005:

Sirit Inc.**Notes to the Consolidated Financial Statements (unaudited)****(expressed in thousands of Canadian Dollars except per share information)**

| | <u>Amount</u> |
|--|------------------------|
| Balance at December 31, 2004 | \$ 400 |
| Stock based compensation on stock options granted | 732 |
| Transfer from contributed surplus on exercise of stock options | <u>(10)</u> |
| Balance at September 30, 2005 | <u>\$ 1,122</u> |

- (e) Basic net income/(loss) per common share is computed by dividing net income/(loss) for the period by the weighted average number of common shares outstanding during the period. Diluted net income/(loss) per common share is computed using the treasury stock method whereby the weighted average number of common shares used in the basic net income/(loss) per common share calculation is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued at the beginning of the period or at time of issuance, if later. Potential common shares are excluded from the calculation if their effect is anti-dilutive.

The following table reconciles the basic weighted average number of common shares outstanding to the diluted weighted average number of common shares outstanding:

| | Nine months ended September 30 | |
|---|--|--------------------------|
| | 2005 | 2004 |
| Weighted average number of shares outstanding - basic | 92,525,273 | 87,303,974 |
| Dilutive effect of stock options | - | <u>3,332,795</u> |
| Adjusted weighted average number of shares outstanding - diluted | <u>92,525,273</u> | <u>90,636,769</u> |
| | Three months ended September 30 | |
| | 2005 | 2004 |
| Weighted average number of shares outstanding - basic and diluted | <u>92,863,731</u> | <u>88,842,703</u> |

At September 30, 2005, as a result of losses applicable to the common shares, the outstanding options are excluded in the diluted loss per share calculation as their inclusion would be anti-dilutive.

4. SEGMENTED INFORMATION

The Company operates in the technology sector in two reportable business segments. The Company's assets by business segment are as follows:

| | September 30 | December 31 |
|---|-------------------------|-------------------------|
| | 2005 | 2004 |
| Radio Frequency Identification Business | \$ 14,988 | \$ 19,773 |
| Portfolio Investments Business | 4,291 | 5,191 |
| | <u>\$ 19,279</u> | <u>\$ 24,964</u> |

Sirit Inc.**Notes to the Consolidated Financial Statements (unaudited)**
(expressed in thousands of Canadian Dollars except per share information)

For the nine months ended September 30, the Company's revenue and expenses by reportable business segment are as follows:

| | 2005 | | |
|---|--------------------------|----------------------------------|-------------------|
| | RFID Business | Portfolio Investments | Total |
| Revenue | \$ 12,165 | \$ - | \$ 12,165 |
| Expenses | 17,787 | - | 17,787 |
| Operating (loss) | (5,622) | - | (5,622) |
| Write-down of investment | - | (900) | (900) |
| Interest income, net | 103 | - | 103 |
| Net (loss)/income for the period | \$ (5,519) | \$ (900) | \$ (6,419) |

| | 2004 | | |
|---|--------------------------|----------------------------------|-----------------|
| | RFID Business | Portfolio Investments | Total |
| Revenue | \$ 15,623 | \$ - | \$ 15,623 |
| Expenses | 16,204 | - | 16,204 |
| Operating (loss) | (581) | - | (581) |
| Other income | 294 | - | 294 |
| Gain on sale of investment | - | 2,019 | 2,019 |
| Interest income, net | 105 | - | 105 |
| Net (loss)/income for the period | \$ (182) | \$ 2,019 | \$ 1,837 |

For the three months ended September 30, the Company's revenue and expenses by reportable business segment are as follows:

| | 2005 | | |
|----------------------------------|--------------------------|----------------------------------|-------------------|
| | RFID Business | Portfolio Investments | Total |
| Revenue | \$ 3,107 | \$ - | \$ 3,107 |
| Expenses | 4,993 | - | 4,993 |
| Operating (loss) | (1,886) | - | (1,886) |
| Write-down of investment | - | (900) | (900) |
| Interest income, net | 27 | - | 27 |
| Net (loss) for the period | \$ (1,859) | \$ (900) | \$ (2,759) |

| | 2004 | | |
|----------------------------------|--------------------------|----------------------------------|-----------------|
| | RFID Business | Portfolio Investments | Total |
| Revenue | \$ 5,162 | \$ - | \$ 5,162 |
| Expenses | 5,844 | - | 5,844 |
| Operating (loss) | (682) | - | (682) |
| Interest income, net | 40 | - | 40 |
| Net (loss) for the period | \$ (642) | \$ - | \$ (642) |

Sirit Inc.**Notes to the Consolidated Financial Statements (unaudited)**
(expressed in thousands of Canadian Dollars except per share information)**5. SUPPLEMENTARY DISCLOSURES RELATED TO CASH FLOWS**

(a) Items not involving cash and cash equivalents:

| | Three months ended | | Nine months ended | |
|----------------------------|---------------------------|---------------|--------------------------|-------------------|
| | September 30 | | September 30 | |
| | 2005 | 2004 | 2005 | 2004 |
| Amortization | \$ 157 | \$ 129 | \$ 457 | \$ 388 |
| Gain on sale of investment | - | - | - | (2,019) |
| Write-down of investment | 900 | - | 900 | - |
| Loss on disposal of assets | - | - | - | 8 |
| Stock compensation costs | 203 | 72 | 786 | 177 |
| | \$ 1,260 | \$ 201 | \$ 2,143 | \$ (1,446) |

(b) Net change in non-cash working capital items:

| | Three months ended | | Nine months ended | |
|--|---------------------------|-----------------|--------------------------|-----------------|
| | September 30 | | September 30 | |
| | 2005 | 2004 | 2005 | 2004 |
| Accounts receivable | \$ 1,042 | \$ (677) | \$ 1,387 | \$ (881) |
| Inventory | (66) | 277 | (321) | (60) |
| Prepays and deposits | 192 | (785) | 472 | 52 |
| Accounts payable and accrued liabilities | (494) | (6) | (142) | (266) |
| Deferred revenue | (37) | 520 | (135) | 625 |
| Warranty obligations | (11) | (141) | (85) | (280) |
| | \$ 626 | \$ (812) | \$ 1,176 | \$ (810) |

6. COMMITMENTS AND GUARANTEES

(a) As at September 30, 2005, certain accounts receivable and inventory are pledged as security in connection with accounts payable in the amount of \$178 (December 30, 2004 - \$892).

(b) The Company's total leased premises commitments are summarized as follows:

| | Amount |
|-----------------|-----------------|
| 2005 (3 months) | \$ 94 |
| 2006 | 335 |
| 2007 | 328 |
| 2008 | 329 |
| 2009 | 236 |
| Thereafter | 143 |
| | \$ 1,465 |

7. CONTINGENCIES

The Company faces potential contingencies, such as contract disputes, tax issues or lawsuits, as part of its ongoing operations and judgment is required when assessing each situation. The Company is not able to determine with reasonable accuracy the outcome of any potential contingency and may take reserves in certain situations.

Sirit Inc.

Notes to the Consolidated Financial Statements (unaudited)

(expressed in thousands of Canadian Dollars except per share information)

8. RELATED PARTY TRANSACTIONS

The Company incurred directors fees of \$47 for their services during the third quarter of 2005 (nil in the third quarter of 2004). The fees were included in selling, general and administrative expenses.

In the third quarter of 2005, the Company paid consulting fees to one of its directors totalling \$3 (nil in the third quarter of 2004). The Company also paid \$21 to one of its directors for legal services (\$27 in the third quarter of 2004). These amounts were included in selling, general and administrative expenses.