



**2006**  
Nine Month Report

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

*The following management's discussion and analysis ("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 November 1, 2006 at which time 145.5 million shares were outstanding, should be read in conjunction with the unaudited interim consolidated financial statements for the nine months ended September 30, 2006 and the audited annual consolidated financial statements, including the notes thereto included in the Company's December 31, 2005 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 generally accepted accounting principles ("GAAP") and presented in **thousands of Canadian dollars** (except the per share amounts) 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](http://www.SEDAR.com).

On July 20, the Company announced that it expected to receive cash proceeds of approximately US\$1.9 million upon completion of a sale transaction involving one of its long-term investments, Medsite, Inc., from its Portfolio Investments business segment. Approximately 10% of the proceeds are to be held in escrow for a period of up to one year following completion of the transaction. Since the announcement, the payment of funds has been delayed and is now expected sometime during November. Medsite, Inc. has changed its name to MSTE Holdings, Inc.

On September 14, Sirit announced that EPCglobal Inc. awarded its hardware certification and interoperability marks to the Company for its INfinity 510 UHF RFID reader. EPCglobal Inc. is the not-for-profit organization whose mission is to drive the commercial adoption of the Electronic Product Code (EPC) in global supply chains. Sirit was one of only two recipients of both certifications during 2006. In addition to the marks awarded to Sirit, two OEM partners Datamax and Paxar also received interoperability marks for their products powered by Sirit's INfinity 9311 UHF reader module.

On September 18, Sirit announced that it entered into an OEM agreement with Dallas-based EFKON USA, Inc., a provider of intelligent transportation systems (ITS) and advanced vehicle communications. EFKON USA will integrate Sirit's Title 21-based toll transponder technology into its Pronto™ tag system used for open road tolling and parking and access control and HOTShot™, a battery and solar powered system for high occupancy tolling (HOT) that uses smart cards and biometric identification for virtually failsafe authentication. Sirit's underlying 915 MHz toll technology, based exclusively on the open Title 21 standard, provides the platform for these solutions.

### **Subsequent Events**

On October 19, the Company announced that it was taking actions to match operating expenditures with anticipated revenue generation with the intent to be cash flow neutral by the fourth quarter of 2007. Action items include reducing headcount by approximately 25% and closing two office locations, one in Loughborough, England and one of two locations in Raleigh, North Carolina. Severance and related costs

## Sirit Inc.

### MANAGEMENT'S DISCUSSION AND ANALYSIS

are expected to be approximately \$0.4 million and will be expensed primarily in the fourth quarter of 2006.

On October 25, Sirit announced a closed-loop application utilizing the IDentity MaX product with an automotive customer consisting of 500 gate, desktop and mobile RFID readers for automatic vehicle identification (AVI) including customized Microsoft-based system software solutions. The project is expected to generate \$1.0 million of revenue over a six month period commencing in November 2006.

### RESOURCES

#### Cash Flows, Liquidity and Capital Resources

Total cash and cash equivalents at September 30, 2006 was \$9.0 million, a \$2.7 million decrease over the balance of \$11.7 million at June 30, 2006 and a \$2.9 million increase from December 31, 2005. The Company utilized \$2.2 million to support operations, \$0.4 million to fund working capital and \$0.1 million to purchase capital assets during the quarter.

#### Operating Activities

Sirit utilized \$5.7 million of cash to fund operating activities for the nine months ended September 30, 2006 (first nine months of 2005 - \$4.3 million). Approximately \$2.2 million of the total was spent during the third quarter of 2006 (third quarter of 2005 - \$1.5 million). The additional cash spent during the first nine months of 2006 compared to the prior year as well as when comparing Q3 2006 to Q3 2005 relates to supporting additional staff and locations associated with the SAMSys Technologies Inc. ("SAMSys") and TradeWind Technologies LLC ("TradeWind") acquisitions which were completed early in the second quarter of 2006. Included in the year-to-date 2006 cash outlay are severance costs of approximately \$0.4 million, with \$0.1 million spent in the third quarter.

Total working capital (excluding cash and cash equivalents) at September 30, 2006 was \$1.0 million compared to \$0.6 million at June 30 and \$0.4 million at December 31, 2005. The change from December 31, 2005 is due to the following fluctuations:

Accounts receivable increased by \$0.7 million from \$2.9 million at December 31, 2005 to \$3.6 million at September 30, 2006. Accounts receivable is consistent with the balance at June 30, 2006 of \$3.4 million. This increase from December figures is due to higher sales levels overall during 2006. (\$5.1 million in the third quarter of 2006 compared to \$4.3 million in the fourth quarter of 2005). The average age of receivables has improved from an annual average of 64 days in 2005 to 54 days in the first nine months of 2006.

Inventory has increased by \$1.3 million from a balance of \$2.0 million at December 31, 2005 to \$3.3 million at September 30, 2006. Inventory increases have been the result of inventory assumed in the recent acquisitions as well as new product builds including the IDentity MaX and the INfinity 510.

Prepays and deposits increased from \$0.1 million at December 31, 2005 to \$0.4 million at September 30, 2006 due to the timing of payments for normal operating activities.

Accounts payable and accrued liabilities balance increased to \$5.0 million at September 30, 2006 compared to \$3.5 million at December 31, 2005 and down slightly from \$5.2 million at June 30, 2006. The increase since the beginning of the year corresponds with higher purchasing volumes to support new products as well as increased sales throughout 2006.

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#### Investing Activities

The Company utilized \$0.1 million in the third quarter of 2006 to purchase capital assets and \$2.9 million in the first nine months of 2006 for all investing activities (third quarter of 2005 - \$0.1 million; first nine months of 2005 - \$0.2 million). Substantially all of the cash utilized for investing activities during 2006 relates to the acquisitions of SAMSys and TradeWind during the second quarter of 2006. The Company completed its acquisition of the assets and undertaking of SAMSys on April 13, 2006 for a gross total of \$4.3 million, including acquisition costs. The acquisition included cash of approximately \$2.5 million, for a net cash outlay of just over \$1.8 million. On April 3, 2006, the cash portion of the acquisition of TradeWind was just over \$0.8 million, including acquisition costs.

#### Financing Activities

The Company generated a total of \$11.6 million from financing activities during the first nine months of 2006 (first nine months of 2005 - \$0.3 million). Cash was generated in Q2 2006 from a public offering of 48,500,000 shares at a share price of \$0.26 for gross proceeds of \$12.6 million. Expenses related to this offering totaled \$1.1 million for net proceeds of \$11.5 million.

#### Commitments

Commitments are comprised of premises rental costs associated with the Company's six operating locations. Three of these locations were assumed during Q2 2006 through the acquisitions of TradeWind (located in the state of Tennessee) and SAMSys (two locations in the state of North Carolina). The Company announced early in the fourth quarter of 2006 that two locations would be closing; the office in the United Kingdom and one in North Carolina. As at September 30, 2006, rental costs are expected to be incurred as follows:

	<b>Payments due by Period (\$000's)</b>				
Contractual Obligations	<b>Total</b>	<b>Up to 1 year</b>	<b>2 to 3 years</b>	<b>4 to 5 years</b>	<b>Over 5 years</b>
Premises Leases	<u>\$ 1,326</u>	<u>\$ 530</u>	<u>\$ 617</u>	<u>\$ 179</u>	<u>\$ -</u>

As at September 30, 2006, certain accounts receivable and inventory are pledged as security in connection with accounts payable in the amount of \$0.8 million (December 31, 2005 - \$1.0 million).

There were no additional commitments entered into during the third quarter of 2006.

#### Related Party Transactions

The Company incurred directors' fees of twenty six thousand dollars for their services during the third quarter of 2006 (third quarter of 2005 - forty seven thousand dollars).

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#### RESULTS

For the three and nine months ended September 30, 2006 compared to the three and nine months ended September 30, 2005

	Three months ended September 30		Nine months ended September 30	
	2006	2005	2006	2005
Revenue	\$ 5,086	\$ 3,107	\$ 16,006	\$ 12,165
Cost of sales	3,399	2,070	10,480	7,949
Gross profit	1,687	1,037	5,526	4,216
Expenses	4,382	2,923	12,577	9,838
Operating (loss)	(2,695)	(1,886)	(7,051)	(5,622)
Write-down of investment	-	(900)	-	(900)
Interest income, net	81	27	166	103
<b>Net (loss)</b>	<b>\$ (2,614)</b>	<b>\$ (2,759)</b>	<b>\$ (6,885)</b>	<b>\$ (6,419)</b>
<b>Basic and diluted (loss) per share</b>	<b>\$ (0.02)</b>	<b>\$ (0.03)</b>	<b>\$ (0.06)</b>	<b>\$ (0.07)</b>
<b>Basic and diluted weighted average number of shares outstanding ('000s)</b>	<b>145,527</b>	<b>92,864</b>	<b>117,893</b>	<b>92,525</b>
<b>Total assets</b>	<b>\$ 26,431</b>	<b>\$ 19,279</b>	<b>\$ 26,431</b>	<b>\$ 19,279</b>
<b>Total long-term financial liabilities</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>

#### Revenue

Revenue for the nine months ended September 30, 2006 was \$16.0 million, or a 32% increase when compared to the first nine months of 2005. Revenue for the third quarter of 2006 was \$5.1 million, or 64% higher than the third quarter of 2005. A further detailed analysis of revenue follows:

#### Automatic Vehicle Identification (AVI) Applications

AVI revenue increased from \$9.3 million for the first nine months of 2005 to \$12.5 million for the first nine months of 2006; a 34% increase year-over-year. Revenue increased from \$2.6 million in Q3 2005 to \$3.7 million in Q3 2006. AVI revenue represents 78% of total year-to-date revenue compared to 76% in 2005. AVI applications can be further broken down between toll applications and parking and access control ("PACS") applications.

Toll revenue in the third quarter of 2006 was 3.1 million; a \$1.1 million or 55% increase over the third quarter of 2005. Year-to-date 2006 toll revenue has increased to \$10.6 million; a \$3.2 million increase or 43%, compared to the \$7.4 million in the first nine months of 2005. The third quarter of 2005 reflected the largest impact from consolidation of three toll agencies in 2005 with minimal purchases from these agencies during that quarter. The 2006 third quarter and year-to-date toll transponder sales have demonstrated a continued rebound from the prior year. Toll transponder revenue during the third quarter does not include the anticipated opening of the SR-125, which has experienced construction delays. Revenue from this new toll road in California will not commence until sometime during the first quarter of 2007. As well, fluctuations in timing of other customer orders have delayed shipments by approximately one month which reduced third quarter revenue and will likely impact fourth quarter revenue.

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PACS revenue for the nine months and three months ended September 30, 2006 remained consistent compared to the same periods of 2005 at \$1.9 million and \$0.6 million respectively.

#### **Radio Frequency Solutions (RFS) Applications**

RFS revenue reached \$3.5 million through the first nine months of 2006 compared to \$2.9 million in the first nine months of 2005, a 21% increase. Third quarter RFS revenue was \$0.5 million in 2005 compared to \$1.4 million in 2006. RFS revenue represents 22% of total revenue for the first nine months of 2006, a decrease from the 24% in 2005.

The increase in RFS sales during the third quarter of 2006 when compared to the same period in 2005 reflects growth in small closed-loop opportunities as well as contributions from customers and products acquired earlier in the year.

Quarterly RFS revenue continues to be unpredictable as large-scale implementations are not yet mainstream.

#### **Gross Margin**

Gross margin for the third quarter and first nine months of 2006 of 33.2% and 34.5% respectively remained consistent with the 33.4% and 34.7% reported in the corresponding periods of 2005. Gross margin for the third quarter of 2006 has also remained consistent with the 33.4% reported in the second quarter of 2006.

#### **Selling, General and Administrative Expenses (SG&A)**

Total SG&A expenses for the first nine months of 2006 were \$7.2 million, an increase of \$1.2 million from the \$6.0 million in the same period of 2005. Third quarter SG&A expenses increased from \$1.5 million in the third quarter of 2005 to \$2.4 million in the third quarter of 2006. These expenses were comprised of the following:

Salaries and benefits of \$1.2 million (third quarter of 2005 - \$0.6 million) were \$0.6 million lower than the \$1.8 million incurred during the second quarter of 2006. The increase over the prior year was due primarily to management's decision during Q3 2005 to reduce year-end bonuses. The net impact year-over-year of this decision was approximately \$0.5 million. The remaining difference is due to an increase in overall staff count from the acquisitions. Total staff complement at September 30, 2006 was 25 compared to 22 at September 30, 2005. The decrease from Q2 2006 relates primarily to severance costs incurred during that quarter.

The remaining SG&A expenses in the third quarter of \$1.2 million were consistent with the second quarter of 2006 and reflect an increase of \$0.3 million compared to \$0.9 million reported in the third quarter of 2005. The increase in Q3 2006 when compared to Q3 2005 reflects higher rent, professional and travel expenses required to support the recent acquisitions.

#### **Stock-Based Compensation**

Stock-based compensation of \$0.2 million (third quarter of 2005 - \$0.2 million) remained consistent with the prior year as minimal options were issued during the quarter.

#### **Development Expenses**

Development expenses increased by \$0.7 million to \$1.6 million in the third quarter of 2006 (third quarter of 2005 - \$0.9 million). The increase results from additional development staff related to the SAMSys

## Sirit Inc.

### MANAGEMENT'S DISCUSSION AND ANALYSIS

and TradeWind acquisitions as well as costs to finalize and obtain certifications for the INfinity 510. Development staff complement at September 30, 2006 was 31 compared to 13 at September 30, 2005.

#### Other Expenses

During the third quarter of 2005, the Company wrote-down one of its long-term investments by \$0.9 million.

#### Quarterly Results

	2006 3rd Q	2006 2nd Q	2006 1st Q	2005 4th Q	2005 3rd Q	2005 2nd Q	2005 1st Q	2004 4th Q
Revenue	\$ 5,086	\$ 5,536	\$ 5,384	\$ 4,254	\$ 3,107	\$ 4,632	\$ 4,426	\$ 4,876
Net (loss)/income for the period	(2,614)	(3,278)	(993)	(2,279)	(2,759)	(2,619)	(1,041)	(913)
Net (loss)/income per share, basic and diluted	\$ (0.02)	\$ (0.03)	\$ (0.01)	\$ (0.02)	\$ (0.03)	\$ (0.03)	\$ (0.01)	\$ (0.01)

Third quarter revenue increased across all areas reflecting both increased demand for toll transponders and RFS product sales into closed-loop applications and additional products assumed from the second quarter acquisitions. Q3 2006 expenses include higher salaries, overheads and development expenditures to support the two acquisitions.

Revenue in the second quarter of 2006 was higher than the second quarter of 2005 due to increased toll transponder sales as sales return to historical levels. Net loss for the second quarter of 2006 was higher due primarily to incremental salaries, benefits, SG&A and development expenses related to the SAMSys and TradeWind acquisitions.

Revenue in the first quarter of 2006 was higher than the first quarter of 2005 due to increased toll transponder sales. Net loss for the first quarter was consistent with the prior year as increased sales are offset by increased development expenditures as well as a slight decrease in gross margin.

The 2005 fourth quarter revenue was lower than the fourth quarter of 2004 which included revenue from the installation of a traffic management system in the state of Florida which did not recur in the fourth quarter of 2005. Toll transponder sales improved during the 2005 fourth quarter when compared to the third quarter of 2005. Net loss for the 2005 fourth quarter included a further write-down of long-term investments by \$1.1 million.

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

Second quarter 2005 net loss included lower than anticipated AVI revenue in addition to 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 transponders which were lower when compared to the first quarter of 2004. The net loss primarily resulted from increased costs as a result of on-going development efforts and normal operations with a lower revenue base as noted above due to delayed timing of shipments.

## **Sirit Inc.**

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

### **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, 2005 and the Annual Information Form dated March 16, 2006. 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 2005 Annual Report. This analysis contains forward-looking statements that may differ materially from future actual results.

#### **Ability to Achieve Commercialization on a Timely Basis**

Sirit's success will depend, to a great extent, on its ability to achieve commercial sales of products incorporating its RFID technology on a timely basis. There can be no assurance that Sirit's technology and products based on such technology will achieve commercial acceptance on a timely basis or that, if market acceptance is achieved, Sirit will be able to maintain such acceptance for a significant period of time. Failure to obtain commercial sales, or to achieve commercial sales on a timely basis, would have an adverse impact on Sirit's financial condition and its ability to sustain its operations.

#### **Ability to Achieve Commercial Acceptance**

Sirit's targeted end-users will be required to make significant investments in their business processes and systems in order to achieve the intended benefits associated with RFID technology. There is no assurance that targeted end-users will be willing to make these investments and adopt RFID technology or, if they are, that they will choose Sirit's RFID products and services. Although development of Sirit's products has been largely completed, sales of Sirit's current products, which to date have been primarily for evaluation and pilot testing purposes have yielded inconsistent revenues and there is no assurance that Sirit's products will achieve commercial acceptance.

#### **Management of Expanding Operations**

If Sirit achieves significant commercial sales of its products, it will be required to expand its operations rapidly, which will place significant demands on Sirit's managerial, operational and financial personnel and systems. There can be no assurance that Sirit's systems, procedures, controls and existing facilities will be adequate to support expansion of Sirit's operations. Sirit's future operating results will substantially depend on the ability of its officers and key employees to manage changing business conditions and to implement and improve its operational, financial control and reporting systems. If Sirit is unable to respond to and manage changing business conditions, the quality of Sirit's products and services, its ability to retain key personnel and its results of operations could be materially adversely affected.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

### **Intellectual Property Rights**

Sirit's success and competitiveness substantially depends on its internally-developed proprietary technologies which are protected through trade secrets, trademarks, copyrights and patents. Patent applications and trademark registrations may not be approved, or, if approved, may be challenged by third parties or invalidated. In addition, patents granted to Sirit may not provide a distinctive or enduring competitive advantage.

Sirit is also dependent on proprietary technologies licensed from third parties. There can be no assurance that these third party licenses will continue to be available to Sirit in the future or that they will not be successfully challenged by third parties.

From time to time, third parties may assert claims or initiate litigation against Sirit alleging that Sirit's products infringe their proprietary rights and Sirit may become increasingly subject to claims of infringement or misappropriation of the intellectual property rights of others. In addition, Sirit may in the future initiate claims or litigation against third parties for infringement of its proprietary rights. Litigation claims, with or without merit, could be time-consuming and costly, divert management's attention, cause product shipment delays, and require Sirit to develop non-infringing technology or enter into royalty or licensing agreements. Such agreements, if required, may not be available on acceptable terms, if at all, which could have a material adverse effect on Sirit's business, financial condition and results of operations.

Sirit may be subject to additional risks as it enters into transactions in countries where intellectual property laws are not well developed or are poorly enforced. Legal protections of its rights may be ineffective in such countries. Litigation to defend and enforce its intellectual property rights could result in substantial costs and diversion of resources and could have a material adverse effect on Sirit's business, financial condition and results of operations, regardless of the final outcome of such litigation. Despite Sirit's efforts to safeguard and maintain its proprietary rights in Canada, the United States and abroad, there can be no assurance that it will be successful in doing so, or that the steps taken by Sirit in this regard will be adequate to deter misappropriation or independent third-party development of its technology or to prevent an unauthorized third party from copying or otherwise obtaining and using its products or technology. Any of these events could have a material adverse effect on Sirit's business, financial condition and results of operations.

### **Complexity of Products**

Many of Sirit's new products and products under development are highly complex and innovative. As a result, they may contain defects or errors that are detected only after installation into its customers' systems which could have a negative impact on Sirit's future revenues and its ability to meet its projections.

### **Dependence on Resellers and Distributors**

Sirit intends to achieve some of its sales through value-added resellers and distributors. Reliance upon third-party distribution sources subjects Sirit to risks of business failure by such value-added resellers and distributors, as well as credit, inventory and business concentration risks. In addition, if there is a shortfall in demand from third-party distribution sources, Sirit's operating results may be negatively affected.

### **Dependence on Customers**

Sirit is dependent on a number of significant customers and on large complex contracts with respect to sales of the majority of its products and services. In fiscal 2005, two customers accounted for approximately 17.2% and 16.1% of total consolidated revenues. If any significant customer discontinues its relationship with Sirit for any reason, or reduces or postpones current or expected purchase

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

commitments for its products and services, it could have a material adverse effect on Sirit's business, operating results and financial condition.

**Integration of Acquisitions**

Sirit recently completed two acquisitions and continues to seek out opportunities to acquire or invest in businesses, products and technologies that expand, complement or are otherwise related to Sirit's current business. These activities create risks such as the need to integrate and manage the businesses and products acquired with the business and products of Sirit, additional demands on Sirit's management, resources, systems, procedures and controls, disruption of Sirit's ongoing business, and diversion of management's attention from other business concerns. Such acquisitions, investments or other business collaborations may involve significant commitments of financial and other resources of Sirit. Any such activity may not be successful in generating revenue, income or other returns to Sirit, and the financial or other resources committed to such activities will not be available to Sirit for other purposes. Sirit's inability to address these risks could negatively affect Sirit's operating results.

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

	<b>As at September 30 2006</b>	<b>As at December 31 2005</b>
<b>Assets</b>		
<i>Current Assets</i>		
Cash and cash equivalents	\$ 8,961	\$ 6,079
Accounts receivable	3,614	2,941
Inventory	3,264	2,020
Prepays and deposits	398	108
	<u>16,237</u>	<u>11,148</u>
Long-term investments	3,182	3,182
Property and equipment	1,221	838
Intangible assets	1,875	370
Deferred development costs	11	59
Goodwill	3,905	2,829
	<u>\$ 26,431</u>	<u>\$ 18,426</u>
<b>Liabilities</b>		
<i>Current Liabilities</i>		
Accounts payable and accrued liabilities	\$ 5,045	\$ 3,526
Deferred revenue	859	815
Warranty obligations	369	290
	<u>6,273</u>	<u>4,631</u>
<b>Shareholders' Equity</b>		
Share capital	47,847	35,195
Contributed surplus	1,912	1,316
Deficit	(29,601)	(22,716)
	<u>20,158</u>	<u>13,795</u>
	<u>\$ 26,431</u>	<u>\$ 18,426</u>

**Commitments and guarantees (note 6)**

Approved by the Directors:

"N. Dawalibi"  
Director

"H. Johnson"  
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	
	2006	2005	2006	2005
<b>Revenue</b>	\$ 5,086	\$ 3,107	\$ 16,006	\$ 12,165
Cost of Sales	3,399	2,070	10,480	7,949
<b>Gross profit</b>	<u>1,687</u>	<u>1,037</u>	<u>5,526</u>	<u>4,216</u>
<b>Expenses</b>				
Selling, general and administrative	2,387	1,515	7,197	6,049
Stock-based compensation	168	203	596	786
Development	1,551	899	4,044	2,481
Amortization	262	157	621	457
Foreign exchange loss	14	149	119	65
	<u>4,382</u>	<u>2,923</u>	<u>12,577</u>	<u>9,838</u>
<b>Operating (loss)</b>	(2,695)	(1,886)	(7,051)	(5,622)
Write-down of investment	-	(900)	-	(900)
Interest income, net	81	27	166	103
<b>Net (loss) for the period</b>	<u>\$ (2,614)</u>	<u>\$ (2,759)</u>	<u>\$ (6,885)</u>	<u>\$ (6,419)</u>
Deficit, beginning of period	<u>(26,987)</u>	<u>(17,678)</u>	<u>(22,716)</u>	<u>(14,018)</u>
<b>Deficit, end of period</b>	<u>\$ (29,601)</u>	<u>\$ (20,437)</u>	<u>\$ (29,601)</u>	<u>\$ (20,437)</u>
<b>Basic and diluted (loss) per share</b>	<u>\$ (0.02)</u>	<u>\$ (0.03)</u>	<u>\$ (0.06)</u>	<u>\$ (0.07)</u>
<b>Basic and diluted weighted average number of common shares ('000s)</b>	<b>145,527</b>	<b>92,864</b>	<b>117,893</b>	<b>92,525</b>

See accompanying notes

**Sirit Inc.**  
**Interim Consolidated Statements of Cash Flows**  
(expressed in thousands of Canadian dollars)  
Unaudited

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Cash provided by/(used in):</b>				
<b>Operating Activities</b>				
(Loss) from operations	\$ (2,614)	\$ (2,759)	\$ (6,885)	\$ (6,419)
Items not involving cash and cash equivalents (note 5a)	430	1,260	1,217	2,143
	<u>(2,184)</u>	<u>(1,499)</u>	<u>(5,668)</u>	<u>(4,276)</u>
Net change in non-cash working capital items (note 5b)	(423)	626	(141)	1,176
	<u>(2,607)</u>	<u>(873)</u>	<u>(5,809)</u>	<u>(3,100)</u>
<b>Investing Activities</b>				
Additions to property and equipment	(120)	(73)	(274)	(238)
Acquisitions, net of cash acquired	-	-	(2,667)	-
	<u>(120)</u>	<u>(73)</u>	<u>(2,941)</u>	<u>(238)</u>
<b>Financing Activities</b>				
Public offering of common shares, net of associated expenses	(38)	-	11,523	-
Issuance of common shares upon exercise of stock options	1	29	109	310
	<u>(37)</u>	<u>29</u>	<u>11,632</u>	<u>310</u>
Exchange rate impact on cash and cash equivalents	-	7	-	21
	<u>-</u>	<u>7</u>	<u>-</u>	<u>21</u>
<b>Increase/(Decrease) in cash and cash equivalents</b>	(2,764)	(910)	2,882	(3,007)
Cash and cash equivalents, beginning of period	11,725	7,924	6,079	10,021
	<u>11,725</u>	<u>7,924</u>	<u>6,079</u>	<u>10,021</u>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 8,961</b>	<b>\$ 7,014</b>	<b>\$ 8,961</b>	<b>\$ 7,014</b>
<b>Cash and cash equivalents consist of:</b>				
Cash and deposit accounts with banks	\$ 1,392	\$ 692	\$ 1,392	\$ 692
Short-term commercial paper	7,569	6,322	7,569	6,322
	<u>7,569</u>	<u>6,322</u>	<u>7,569</u>	<u>6,322</u>
	<b>\$ 8,961</b>	<b>\$ 7,014</b>	<b>\$ 8,961</b>	<b>\$ 7,014</b>

See accompanying notes

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

The accompanying interim 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 unaudited consolidated 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 Sirit Inc. ("Sirit" or the "Company") for the year ended December 31, 2005. 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. Note disclosures have been presented for material updates to the information previously reported.

**2. ACQUISITIONS**

- (a) On April 3, 2006, the Company completed the acquisition of all of the outstanding shares of TradeWind Technologies LLC ("TradeWind"), a private Knoxville, Tennessee based radio frequency identification ("RFID") development company. The results of TradeWind's operations have been included in the unaudited interim consolidated financial statements since that date. TradeWind specializes in the development of high frequency ("HF") products and brings to Sirit an immediate complementary suite of HF plug and play readers.

Sirit acquired TradeWind for aggregate consideration of \$1,858 including US\$600 (CDN\$702) cash, 3,000,000 common shares valued at \$1,020 and associated acquisition costs of \$136. The value of the 3,000,000 common shares issued was \$0.34 per share and was determined based on the average market price of Sirit's common shares over the five trading days prior to and the five trading days subsequent to the public announcement of the acquisition (February 27, 2006).

The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition. The purchase price allocation is preliminary and subject to refinement as Sirit is in the process of finalizing the valuation of the purchase price allocation.

Intangible assets	\$ 840
Goodwill	1,076
Total assets acquired	<u>1,916</u>
Current liabilities	(58)
Total liabilities assumed	<u>(58)</u>
<b>Net assets acquired</b>	<b><u>\$ 1,858</u></b>

The intangible assets acquired consist of RFID reader-writer technology and software developed by TradeWind. The entire balance is being amortized straight-line over the estimated useful life of 5 years. The nine months ended September 30, 2006 includes amortization of these intangible assets since the date of acquisition of \$70.

- (b) On April 13, 2006, the Company completed the acquisition of the assets and undertakings of SAMSys Technologies Inc. ("SAMSys") out of a court appointed receivership proceeding. The results of SAMSys' operations have been included in the unaudited interim consolidated financial statements since that date. SAMSys was a publicly listed company on the TSX (symbol SMY) and provided RFID reader hardware solutions to customers in the automatic identification and data capture industry, specifically targeting supply chain management and asset management targets.

The aggregate purchase price was \$4,335 including \$4,000 in cash and \$335 in associated acquisition costs. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The purchase price allocation is preliminary and subject to refinement as Sirit is in the process of finalizing the valuation of the purchase price allocation.

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

Current assets	\$	3,672
Property and equipment		380
Intangible assets		967
Total assets acquired		<u>5,019</u>
Current liabilities		<u>(684)</u>
Total liabilities assumed		<u>(684)</u>
<b>Net assets acquired</b>	<b>\$</b>	<b><u>4,335</u></b>

The intangible assets acquired consist of technology related to a new platform for UHF readers and RFID tag and module technologies. The entire balance is being amortized straight-line over the estimated useful life of 5 years. The nine months ended September 30, 2006 includes amortization of these intangible assets since the date of acquisition of \$81.

**3. SHARE CAPITAL**

(a) Common shares issued and outstanding:

	<b>Shares</b>	<b>Amount</b>
<b>Balance at December 31, 2005 and March 31, 2006</b>	<b>93,273,786</b>	<b>\$ 35,195</b>
Issued on public offering	48,500,000	12,610
Issued on TradeWind acquisition (note 2)	3,000,000	1,020
Issued on exercise of stock options	750,000	108
Expenses related to stock issuances	-	(1,049)
Balance at June 30, 2006	145,523,786	47,884
Issued on exercise of stock options	7,695	1
Expenses related to stock issuances	-	(38)
Balance at September 30, 2006	<b>145,531,481</b>	<b>\$ 47,847</b>

(b) During the second quarter of 2006, the Company completed a public offering of 48,500,000 common shares of Sirit at a price of \$0.26 per common shares, for total gross proceeds of \$12,610. The Company incurred expenses totalling \$1,087 related to this equity offering.

(c) During the period July 1, 2006 to September 30, 2006, the Company granted 132,000 stock options to employees. During the period of April 1, 2006 to June 30, 2006, the Company granted 1,359,000 stock options to employees and directors. All options were issued with an exercise price equal to market value at grant date and vest over a three year period. The Company determines compensation costs on options granted based on the fair value at the grant date in accordance with the fair value based method of accounting for stock-based compensation. Assumptions used in the Black-Scholes option-pricing model are as follows:

Risk-free interest rate	4.09% - 4.47%
Expected life	3 years
Expected volatility	74% - 77%
Expected dividends	Nil

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

The following summarizes stock option activity for the nine months ended September 30, 2006:

	<b>Number of Options</b>	<b>Weighted Average Exercise Price</b>
<b>Sirit Transaction Options Outside the Plan</b>		
Balance, December 31, 2005 and June 30, 2006	240,292	\$0.14
Exercised	(7,695)	(0.13)
Expired/terminated	-	-
	<u>          </u>	<u>          </u>
Balance, September 30, 2006	232,597	\$ 0.14
<b>Options Outstanding Inside the Plan</b>		
Balance, December 31, 2005 and March 31, 2006	7,599,233	\$ 0.68
Granted to employees and directors	1,359,000	0.28
Exercised	(750,000)	(0.14)
Expired/terminated	(698,333)	(1.37)
	<u>          </u>	<u>          </u>
Balance, June 30, 2006	7,509,900	\$ 0.61
Granted to employees	132,000	0.23
Exercised	-	-
Expired/terminated	(2,132,800)	(0.50)
	<u>          </u>	<u>          </u>
Balance, September 30, 2006	<u>5,509,100</u>	<u>\$ 0.64</u>
Total options outstanding at September 30, 2006	<u>5,741,697</u>	<u>\$0.62</u>
Options exercisable at September 30, 2006	<u>2,261,758</u>	<u>\$0.61</u>
Options available for issuance at September 30, 2006	<u>2,934,218</u>	

(d) The following table reconciles contributed surplus for the nine months ended September 30, 2006:

	<b>Amount</b>
<b>Balance at December 31, 2005</b>	<b><u>\$ 1,316</u></b>
Stock-based compensation on stock options granted	<u>202</u>
Balance at March 31, 2006	1,518
Stock-based compensation on stock options granted	<u>226</u>
Balance at June 30, 2006	1,744
Stock-based compensation on stock options granted	<u>168</u>
<b>Balance at September 30, 2006</b>	<b><u>\$ 1,912</u></b>

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

	<b>September 30</b>	<b>December 31</b>
	<b>2006</b>	<b>2005</b>
Radio Frequency Identification Business	\$ 23,249	\$ 15,244
Portfolio Investments Business	3,182	3,182
	<b>\$ 26,431</b>	<b>\$ 18,426</b>

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

	<b>2006</b>		
	<b>RFID</b>	<b>Portfolio</b>	
	<b>Business</b>	<b>Investments</b>	<b>Total</b>
Revenue	\$ 16,006	\$ -	\$ 16,006
Expenses	23,057	-	23,057
Operating (loss)	(7,051)	-	(7,051)
Interest income, net	166	-	166
<b>Net (loss) for the period</b>	<b>\$ (6,885)</b>	<b>\$ -</b>	<b>\$ (6,885)</b>

	<b>2005</b>		
	<b>RFID</b>	<b>Portfolio</b>	
	<b>Business</b>	<b>Investments</b>	<b>Total</b>
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
<b>Net (loss) for the period</b>	<b>\$ (5,519)</b>	<b>\$ (900)</b>	<b>\$ (6,419)</b>

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

	<b>2006</b>		
	<b>RFID</b>	<b>Portfolio</b>	
	<b>Business</b>	<b>Investments</b>	<b>Total</b>
Revenue	\$ 5,086	\$ -	\$ 5,086
Expenses	7,781	-	7,781
Operating (loss)	(2,695)	-	(2,695)
Interest income, net	81	-	81
<b>Net (loss) for the period</b>	<b>\$ (2,614)</b>	<b>\$ -</b>	<b>\$ (2,614)</b>

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

	<b>2005</b>		
	<b>RFID Business</b>	<b>Portfolio Investments</b>	<b>Total</b>
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
<b>Net (loss) for the period</b>	<b>\$ (1,859)</b>	<b>\$ (900)</b>	<b>\$ (2,759)</b>

**5. SUPPLEMENTARY DISCLOSURES RELATED TO CASH FLOWS**

(a) Items not involving cash and cash equivalents:

	<b>Three months ended September 30</b>		<b>Nine months ended September 30</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Amortization	\$ 262	\$ 157	\$ 621	\$ 457
Stock-based compensation	168	203	596	786
Write-down of investment	-	900	-	900
	<b>\$ 430</b>	<b>\$ 1,260</b>	<b>\$ 1,217</b>	<b>\$ 2,143</b>

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

	<b>Three months ended September 30</b>		<b>Nine months ended September 30</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Accounts receivable	\$ (219)	\$ 1,042	\$ (673)	\$ 1,387
Inventory	(99)	(66)	(1,244)	(321)
Prepays and deposits	(53)	192	(290)	472
Accounts payable and accrued liabilities	(130)	(494)	1,519	(142)
Deferred revenue	116	(37)	44	(135)
Warranty obligations	(38)	(11)	79	(85)
Non-cash working capital assumed on acquisitions	-	-	424	-
	<b>\$ (423)</b>	<b>\$ 626</b>	<b>\$ (141)</b>	<b>\$ 1,176</b>

**6. COMMITMENTS AND GUARANTEES**

(a) As at September 30, 2006, certain accounts receivable and inventory are pledged as security in connection with accounts payable in the amount of \$766 (December 31, 2005 - \$1,017).

**Sirit Inc.**

**Notes to the Interim Consolidated Financial Statements (unaudited)**  
**(expressed in thousands of Canadian Dollars except per share amounts)**

(b) The Company's total future minimum operating lease commitments are summarized as follows:

	<u>Amount</u>
2006 (3 months)	\$ 141
2007	477
2008	333
2009	232
2010	143
Thereafter	<u>-</u>
	<u>\$ 1,326</u>

**7. RELATED PARTY TRANSACTIONS**

The Company incurred directors fees of \$26 for their services during the third quarter of 2006 (\$47 in the third quarter of 2005). The fees were included in selling, general and administrative expenses.