



Com Dev International Ltd.  
Fourth Quarter & Year-End Report – Fiscal 2011  
For the Period Ended  
October 31 2011

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS



### INTRODUCTION

The following Management's Discussion and Analysis (MD&A) provides information that management believes is relevant to an assessment and understanding of COM DEV International Ltd's ("the Company", or "COM DEV") consolidated results of operations and financial condition. This discussion should be read in conjunction with the Company's audited consolidated financial statements including the notes thereto, for the year ended October 31, 2011 ("the Consolidated Financial Statements"). The Consolidated Financial Statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) and are reported in Canadian dollars. Unless otherwise noted, the information contained herein is dated as of January 12th, 2012.

### CAUTION REGARDING FORWARD-LOOKING INFORMATION

Certain statements contained in this report contain forward-looking statements, including, (without limitation) statements concerning possible or assumed future results of operations of the Company preceded by, followed by or that include the words "believes", "expects", "anticipates", "estimates", "intends", "plans", "forecasts", "guidance", or similar expressions. Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions and the Company's actual results may differ materially from those anticipated in these forward-looking statements. Additional information relating to the Company and the risks inherent in its business is provided in the Company's Annual Information Form for the year ended October 31, 2011 and other documents available on SEDAR at [www.sedar.com](http://www.sedar.com).

This Management's Discussion and Analysis (MD&A) contains financial outlooks in several areas, notably: in discussing new orders. Readers are again cautioned that these financial outlooks are provided solely to provide a view of the operations through the eyes of management, based on management's current expectations in these areas, and should not be used for any other purpose. Readers are reminded that, as noted above, financial outlooks are not guarantees of future performance, and should not be considered such, since actual results may differ materially from those expressed in the financial outlooks.

### USE OF NON-GAAP MEASURES

In this MD&A, we provide information about orders and contract backlog. Orders and backlog measures are not defined by Canadian generally accepted accounting principles (GAAP) and our measurement of them may vary from that used by others. The Company measures orders as the sum of fully executed contracts from our customers. The Company measures backlog as the sum of all customers' orders at contract value (including the contract value of change notices subsequently received) to date, less revenue recognized against those orders, plus or minus the impact of foreign exchange fluctuations on orders denominated in foreign currency. The Company includes in its backlog determination, only those amounts that are covered by contracts. While we believe that long-term backlog trends serve as a useful metric for assessing the growth prospects for our business, backlog is not a guarantee of future revenues and provides no information about the timing on which future revenue may be recorded.

## OVERVIEW

COM DEV is a leading global designer, manufacturer and distributor of space communications and space science products and systems. The Company began operations in 1974 and completed its initial public offering in December 1996. The Company is headquartered in Cambridge, Ontario, Canada, with additional operations in Aylesbury, England; Ottawa, Ontario, Canada; El Segundo, California; and Xian, China. The Company's common shares trade on The Toronto Stock Exchange under the symbol "CDV". COM DEV employed 1,229 people around the world as of October 31, 2011, compared to 1,296 people as of October 31, 2010.

COM DEV designs and manufactures advanced instruments and microwave products for space satellites ("Space segment") such as multiplexers, filters, switches, surface acoustic wave (SAW) devices, signal processors, satellite payloads, and micro-satellite spacecraft. The products are sold to substantially all of the major satellite prime contractors and many government space agencies for use in commercial communications, military/defense communications and space science satellites. Recently, the Company commenced sales of information ("Data Services segment") from its own satellites through its majority owned subsidiary, exactEarth™. Commercial operations for exactEarth™ commenced in June 2010 with data being available from three satellites, and it has continued since then to expand its customer base, as well as its space and ground infrastructure.

## OVERALL PERFORMANCE

During the Company's 2011 fiscal year, twenty-six satellite programs were awarded in the global space market, compared with thirty-two in 2010. The number of transponders on these satellites totalled 1,298 in 2011, representing a 11% decrease from the 1,459 transponders awarded in the global market in 2010. Transponders are a measure of the satellites capacity and this capacity can vary significantly between satellites. Generally, a higher number of transponders is favourable for COM DEV as this provides an indication of the demand for the Company's traditional passive microwave product lines. The breakdown of satellites and transponders awarded between the three market sectors (commercial, civil, and military/defense) can be summarized as follows:

### Years Ended October 31

<u>Sector</u>	<u>2011</u>		<u>2010</u>	
	<u>Satellites</u>	<u>Transponders</u>	<u>Satellites</u>	<u>Transponders</u>
Commercial	18	1,058	21	1,065
Civil	6	112	8	246
Military / Defense	2	128	3	148
<b>Total</b>	<b>26</b>	<b>1,298</b>	<b>32</b>	<b>1,459</b>

Of the twenty-six satellite programs announced in 2011, COM DEV has won orders on eighteen and is in the running to secure work on four others. This compares to 2010, when of the thirty-two satellites announced in the market, COM DEV was able to secure work on twenty-seven and is in the running to secure work on two others. ♦

exactEarth™, the Company's data services business of which it shares ownership with HISDESAT, continued to successfully progress its business plan during 2011. During the year, exactEarth™ launched and commissioned its EV2 satellite and continued the build out of its other assets in order to add to its constellation. exactEarth™ had orders of \$9.5 million (2010: \$2.1 million) and generated revenues of \$4.6 million (2010: \$1.9 million) and a net loss of \$7.6 million (2010: \$6.1 million net loss). The loss attributable to the Company in the year is \$5.6 million (2010: \$5.8 million net loss) which represents the Company's ownership share of exactEarth™. The Company remains committed to the exactEarth™ business plan and expects that positive earnings levels will follow soon after the commissioning of the balance of its satellite constellation. ♦

In 2011, COM DEV received orders for a total of \$187.8 million in new business, compared with \$209.9 million in the previous year. Of these new orders won in 2011, 56% came from the commercial sector of the space market, 23% from the civil sector, and 21% from the military/defense sector. By comparison, of the business won in 2010, 79% came from the commercial sector, 10% from the civil sector and the remaining 11% from the military sector. The civil and military/defense segments continue to be plagued by uncertainty as the various government organizations have been slow to award new contracts due to ongoing budget pressures. Significant management time and attention are being spent to manage this situation however it is expected that this environment will continue for the foreseeable future. ♦

Included in the \$187.8 million of new orders received in 2011 are orders received under Authorities to Proceed (ATPs). In recent years, as delivery schedules have become more critical, customers are increasingly using ATPs as a way to start a subcontractor working, under contract, on a program while the full contract negotiations are concluded. COM DEV includes only the work for which it has contractual coverage in its reported orders and backlog. In the case of ATP awards, the Company includes only the value of the ATP, not the expected full value of the contract. Only after contract negotiations are completed, and the customer has awarded COM DEV the full contract, does the Company include the value above the ATP in its orders and backlog. At the end of 2011, the amount of potential order value in excess of ATP, which management expects to realize, stood at \$20.4 million. ♦ This compares to \$9.8 million at the end of 2010. The expected full contract amounts are based on bid values, and the historically high percentage of ATPs being ultimately turned into full contract values.

The Company closed out 2011 with backlog totalling \$126.1 million, which is down from the 2010 level of \$148.6 million. Approximately 28% of the 2011 (2010: 11%) closing backlog is expected to be realized beyond the end of the Company's 2012 fiscal year. ♦ Backlog represents the amount of orders for which the Company has not yet recognized revenue and therefore the expected amount of backlog to be realized beyond the upcoming fiscal year is based on the current projections for project performance.

Volatility in exchange rates between the Canadian dollar (CAD) and foreign currencies such as the U.S. dollar (USD), the Euro (EUR) and the British Pound (GBP) impact on the business as a large portion of the Company's revenues are billed in non-Canadian currencies (predominately USD) and held on the Company's balance sheet in the form of cash, receivables and payables. According to the Bank of Canada, the average closing USD/CAD exchange rate during 2011 was \$0.9868, which compares to the 2010 average of \$1.0382. The Company continually mitigates its foreign exchange risks through the use of derivatives and included in the foreign exchange gains and losses are the results of the Company's hedging program that resulted in a gain of \$0.4 million in 2011 (2010: \$4.6 million gain).

Gross margin percentage rates were higher for the year compared to a year earlier, averaging 22.9% in 2011 compared with 20.4% in 2010. This improvement can be attributed to reduced impact from five programs which had a significant impact to the 2010 financial results. These five programs represented approximately 1.9% of our 2011 revenues and negatively affected 2011 gross margins by approximately \$8.0 million. In 2010, these same five programs represented approximately 9.5% of revenues and lowered gross margin by \$15.0 million. Completing these programs as soon as possible is Management's priority and doing so should eliminate continued drag on gross margins. As at the end of 2011, four of the five programs were essentially complete and the last project should be completed within the first half of 2012. ♦

During the year, the Company recognized a \$13.3 million (2010: \$2.1 million) Investment Tax Credit (ITC) in its research and development (R&D) funding. The ITC recognized represents the tax savings gained from R&D expenditures made in prior periods. With the inclusion of this ITC and with the normal external funding sources, there was a net recovery of \$7.0 million of research and development expense for 2011, compared to \$6.6 million net expense in 2010. Excluding the effects of the ITC, the Company saw an increase in gross R&D spending, but a decline in the level of net spending as a result of the Company's success in finding external funding sources for

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♦ Forward-looking Information. Please refer to Caution Regarding Forward-looking Information on Page 1 of this document.

its research and development activities. The Company remains committed to its R&D technology roadmap and continues to review its R&D projects to ensure that they are still aligned with overall corporate objectives and strategies and will continue to search for opportunities to have these projects funded from external sources.

Also during the year, the Company recorded a charge of \$2.2million related to a reduction in force that was announced in the third quarter. This reduction in force impacted the Company's Canadian government-facing division to the greatest extent, driven by continued uncertainty surrounding Canadian government funding of space programs, and delays in the awarding of new programs. Of the 73 employees displaced in this reduction, 40 were employed in this division.

The Company's \$32 million operating line of credit remains undrawn at the end of fiscal 2011 except for \$3.2 million (\$0.5 million in 2010) in the form of guarantee letters issued by the bank on behalf of the Company to customers in the normal course of operations and to government agencies while certain tax objections are resolved. During the year, the Company increased the term debt by \$15 million through GE Capital to fund the second tranche of equity financing required by the exactEarth™ division as well as for general corporate purposes. Payments against the Company's term debt are being made in accordance with the terms of the borrowing agreement. The amount outstanding on all long-term debt at the end of 2011 was \$23.6 million (\$16.5 million at the end of 2010).

For an analysis of risks faced by the Company, please refer to the section "Business Risks and Prospects", included later in this MD&A.

SELECTED ANNUAL INFORMATION\* (prepared in accordance with Canadian GAAP)

<u>(in thousands of dollars, except per share amounts)</u>	<u>Years Ended October 31</u>		
	<u>2011</u>	<u>2010</u>	<u>2009</u>
Revenue	\$ 203,915	\$ 220,921	\$ 240,410
Net income	\$ 11,555	\$ 2,426	\$ 15,268
Net income attributable to shareholders	\$ 13,606	\$ 2,694	\$ 15,306
Earnings per share, basic & diluted	\$ 0.18	\$ 0.04	\$ 0.21
Total Assets	\$ 249,942	\$ 242,466	\$ 235,218
Long-term financial liabilities	\$ 17,199	\$ 12,993	\$ 15,273
Cash dividend declared	\$ -	\$ -	\$ -

\* For 2011 to 2010 year-to-year variation commentaries, see the additional comments included in Results of Operations sections below.

**RESULTS OF OPERATIONS**

Revenues

<u>(in millions of dollars)</u>	<u>Years Ended October 31</u>		
	<u>2011</u>	<u>2010</u>	<u>% change</u>
Commercial satellite programs	\$ 124.7	\$ 143.8	(13.2%)
Civil (government) programs	\$ 41.1	\$ 49.9	(18.0%)
Military and defense programs	\$ 37.4	\$ 27.2	37.0%
<b>Total Revenue</b>	<b>\$ 203.2</b>	<b>\$ 220.9</b>	<b>(8.1%)</b>

Total revenue for the Company in 2011 was \$203.2 million compared to \$220.9 million in 2010. The biggest percentage decrease was seen with the Company's civil customers where revenues in the year were 18.0% lower than a year earlier. As highlighted in the past year, the decline in the revenue from these customers is the result of the reduced order levels booked for the past several quarters. Some of the large civil programs are approaching completion and in the absence of substantial replacement orders to replenish backlog, the revenue stream has been somewhat reduced in this segment.

Backlog

<u>(in millions of dollars)</u>	<u>Years Ended October 31</u>		
	<u>2011</u>	<u>2010</u>	<u>% change</u>
Commercial satellite programs	\$ 63.3	\$ 95.9	(34.0%)
Civil (government) programs	\$ 36.5	\$ 28.1	29.9%
Military and defense programs	\$ 26.3	\$ 24.6	6.9%
<b>Total Backlog</b>	<b>\$ 126.1</b>	<b>\$ 148.6</b>	<b>(15.1%)</b>

The Company's overall backlog of work at the end of 2011 fell 15.1% as compared to the ending 2010 backlog. Ultimately, the backlog is a measure of the Company's orders for which revenue has not been recognized and consequently, backlog levels are heavily influenced by the timing of orders and of revenues.

## Net Income Attributable to Shareholders

	<u>Years Ended October 31</u>		
<u>(in millions of dollars except earnings per share)</u>	<u>2011</u>	<u>2010</u>	<u>% change</u>
Net Income Attributable To Shareholders	\$ 13.6	\$ 2.7	403.7%
Earnings per share basic and diluted	\$ 0.18	\$ 0.04	350.0%

In Q4 2010, HISDESAT purchased a 27% ownership interest in the Company's exactEarth™ division. The net income attributable to Shareholders reflects the Company's consolidated income less 27% of exactEarth's net loss for the periods subsequent to HISDESAT's investment. The net income attributable to shareholders in 2011 was \$13.6 million compared with \$2.7 million in 2010. The increase is the result of improved gross margins, lower net R&D expense, lower Selling expense, lower General expense and lower Other expense. Offsetting these were a higher provision for taxes and higher foreign exchange loss. All of these items are discussed in more detail below.

## Gross Margin

	<u>Years Ended October 31</u>		
<u>(in millions of dollars)</u>	<u>2011</u>	<u>2010</u>	<u>% change</u>
Total gross margin	\$ 46.6	\$ 45.1	3.3%
Total gross margin %	22.9%	20.4%	2.5%

Gross margins for 2011 averaged 22.9% compared to 20.4% in 2010. The gross margins in the Space Equipment Segment were approximately 2.7% higher in 2011 than they were in 2010. This year over year increase in the margins occurred despite the revenue impact from an approximate 5% weakening of the value of the U.S. dollar when compared to the Canadian dollar and from a significant drop in the gross margins from Canadian government orders. The average gross margin percentage increased primarily as a result of the diminishing impact from the five problem programs discussed in the past several quarters. These five programs represented approximately 1.9% (2010: 9.5%) of our 2011 revenues and negatively affected 2011 gross margins by approximately \$8.0 million (2010: \$15.0 million). Four of the five programs are now essentially complete and the remaining one is scheduled to be complete in the first half of fiscal 2012. Accordingly, the impact from this remaining program is expected to be less than 2% of revenues in Q1 2012. ♦

## Research and Development (R&D)

	<u>Years Ended October 31</u>		
<u>(in millions of dollars)</u>	<u>2011</u>	<u>2010</u>	<u>% change</u>
Total R&D spending before funding	\$ 13.3	\$ 12.4	7.3%
Total R&D funding received	\$ (7.0)	\$ (3.6)	94.4%
Investment tax credits recoverable	\$ (13.3)	\$ (2.1)	533.3%
<b>R&amp;D, net of funding</b>	<b>\$ (7.0)</b>	<b>\$ 6.6</b>	<b>n/a</b>

During the year, the Company recognized a \$13.3 million (2010: \$2.1 million) Investment Tax Credit (ITC) in its research and development funding. The ITC recognized represents the tax savings gained from R&D

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expenditures made in prior periods. With the inclusion of this ITC and with the normal external funding sources, there was \$7.0 million net recovery of research and development compared to \$6.6 million of expense in 2010. It is important to note that R&D costs noted in the table above reflect only Company-funded research and development activities (net of any external offset funding received). Customer-funded development costs are included in the Company's cost of revenue figures.

#### Other Expenses

<u>(in millions of dollars)</u>	<u>Years Ended October 31</u>		
	<u>2011</u>	<u>2010</u>	<u>% change</u>
Selling expense	\$ 11.4	\$ 11.8	(3.4%)
General expenses	\$ 17.6	\$ 20.7	(15.0%)
Interest expense	\$ 0.9	\$ 0.6	50.0%
Foreign exchange loss / (gain)	\$ 0.9	\$ (2.6)	n/a
Other expense	\$ 3.0	\$ 3.4	(11.8%)

#### *Selling and General Expenses*

Selling expenses were lower by \$0.4 million in 2011 compared to 2010. Selling expenses fluctuate from quarter to quarter and year to year depending on the bids and proposal work that is underway. General expenses for 2011 were \$17.6 million compared with \$20.7 million in 2010. The \$3.1 million decline in general expenses are primarily as a result of continued focus on rationalization of spending throughout the Company.

#### *Interest Expense*

The Company incurred net interest charges of \$0.9 million in 2011 which was higher than the net interest expense incurred in 2010 of \$0.6 million. The Company borrowed \$15 million in the second quarter of 2011 and the higher interest expense reflects the cost of this debt. The term debt attracts interest at rates varying from LIBOR plus 225 bps to LIBOR plus 360 bps and at banker's acceptance rates plus 4.9%.

#### *Foreign Exchange*

The foreign exchange loss in 2011 was \$0.9 million, compared with a gain of \$2.6 million in 2010. Foreign exchange amounts in the Consolidated Statements of Operations include realized and unrealized gains and losses that result from balance sheet translation of foreign denominated balances, realized gains and losses from settling U.S. dollar hedge contracts, and mark to market valuation adjustments on the Company's outstanding U.S. dollar hedge contracts. They do not include the impact of foreign exchange fluctuations on customer program values, and their resulting profitability, which is reflected in the revenue, cost of revenue, and gross margin sections of the Consolidated Statements of Operations.

The impact of translation of outstanding foreign denominated balance sheet items and of settling these items into cash during the year was a loss of \$1.3 million, compared to a loss of \$2.0 million in 2010.

The Company attempts to mitigate the impact of sudden changes in foreign currency rates by entering into derivative contracts. The Company reflects the change in the fair value ('mark to market') of the unexpired contracts as part of its foreign exchange expense or gain in the quarter. In 2011, there was a \$2.9 million loss in the mark to market valuations on the U.S. dollar derivative contracts, compared to an unrealized exchange gain of \$1.1 million in fiscal 2010. The impact from settling U.S. dollar hedge contracts was a gain of \$3.3 million in 2011 (2010: \$3.5 million gain).

#### *Other Expense*

Other Expenses in 2011 includes restructuring of \$2.2 million (2010: \$3.3 million), as a result of reductions in force in both years, financial expenses of \$0.3 million (2010: \$0.6 million) and miscellaneous expenses of \$0.5 million (2010: \$0.5 million income).

## Financial Position

The following chart outlines the significant changes in the balance sheet between October 31, 2011 and October 31, 2010:

(in millions of dollars)	Increase/ (Decrease)	Explanation
Cash and cash equivalents	\$ 10.2	Refer to Statement of Cash flows
Accounts receivable	\$ 3.2	Normal fluctuation in billings and collections. The Company does not have any significant allowances for doubtful accounts.
Inventory	\$ (11.1)	General inventory levels rose by \$1.1 million with the balance of the decrease in inventory from a reduction of contracts-in-progress inventory. The contracts-in-progress balance will vary from quarter to quarter depending on the Company's billing and revenue profiles.
Prepaid and other	\$ (1.9)	General prepaid expenses were recognized at a faster rate than new prepaids were recorded. These amounts fluctuate normally throughout the year depending on vendor payment terms and the nature of the expense.
Property, plant & equipment	\$ 0.4	Capital expenditures of \$9.5 million less \$7.2 million of depreciation, \$1.4 million of disposals and \$0.5 million of foreign exchange translation adjustment.
Intangible assets	\$ 1.3	Intangible expenditure of \$6.0 million less \$4.5 million of amortization and \$0.2 million of foreign exchange adjustment.
Accounts payable and accrued liabilities	\$ (1.6)	Normal accounts payable payment cycle.
Deferred revenue	\$ (13.5)	Deferred revenue reflects the amount of billings that occur 'in advance' of the Company recognizing revenue. The decrease in the year reflects this timing difference on several projects where revenue outpaced the billings.
Loans payable	\$ 7.0	Advance of \$15.0 million term loan from GE Capital plus \$0.5 million advance from SODP less payments of \$8.0 million and foreign exchange translation and other adjustments of \$0.5 million
Contributed surplus	\$ 2.1	Refer to Consolidated Statements of Changes in Equity
Deficit	\$ (13.6)	Net income attributable to shareholders.
Non-controlling interest	\$ 0.6	Refer to Consolidated Statements of Changes in Equity
Accumulated other comprehensive income	\$ (0.4)	Refer to Consolidated Statements of Changes in Equity

## Liquidity and Capital Resources

<u>(in millions of dollars)</u>	<u>Year Ended October 31</u>		
	<u>2011</u>	<u>2010</u>	<u>% change</u>
Cash from operating activities	\$ 14.7	\$ 13.6	8.1%
Net increase / (decrease) in cash	\$ 10.2	\$ (4.0)	N/A
Property, Plant and Equipment additions	\$ 9.5	\$ 13.8	(31.2%)
Acquisition of Intangible assets	\$ 6.0	\$ 10.9	(45.0%)

The Company generated \$14.7 million of cash from operating activities in 2011, compared with 2010 when \$13.6 million was generated. The Company invested \$7.5 million in working capital in 2011 which compares to the \$0.3 million generated from working capital in 2010. This investment in working capital was mainly the result of higher accounts receivable and lower deferred revenue.

The Company's operating credit line of \$32 million was not drawn upon at the end of 2011, except for \$3.2 million (2010: \$0.5 million) in the form of guarantee letters issued to customers in the normal course of operations by the bank on behalf of the Company and to government agencies while certain tax objections are resolved. In addition to this operating line of credit, the Company also has a treasury risk management facility to facilitate hedging of currency related risks arising in the normal course of operations. Under these facilities, the Company is required to maintain certain financial ratios, which the Company has met as of October 31, 2011.

During the year, GE Capital Solutions made available additional term loan facilities to the Company. This agreement provides for a term loan facility of up to \$15.0 million CAD. The full \$15.0 million was drawn upon in the year and this term loan matures on March 28, 2015. The amount owing on this term loan and the previously drawn term loan at the end of 2011 was \$18.9 million (2010: \$12.4 million). Additional details of these loans can be found in Note 10 of the consolidated financial statements.

In the fourth quarter of 2010, the Company added a strategic investor in its data services subsidiary, exactEarth™ Ltd., that will play an important role in delivering and growing the exactEarth™'s exactAIS™ service in the marketplace. HISDESAT committed \$15 million for a 27% equity interest in exactEarth™ with an initial cash investment of \$12.3 million with the remaining cash payment of \$2.7 million being received on March 30, 2011. The cash investment will support exactEarth™'s on-going business operations and the deployment of additional space and ground infrastructure.

In 2010, the Company entered into an agreement to receive a conditional grant from The Ontario Ministry of Economic Development and Trade under the Next Generation of Jobs Fund. The grant was conditional upon maintaining a minimum number of employees and project investment with repayment provisions if these conditions are not met. At the end of 2011, management did not have sufficient confidence in future Space program funding levels to support the conditions of the grant and, therefore, voluntarily withdrew from the program. Accordingly, at October 31, 2011, all amounts pertaining to this agreement were adjusted. At that time a total of \$1.5 million (\$1.4 million in 2010), had been accrued, of which \$1.1 million was credited against property, plant, and equipment, and \$0.4 million was applied against project costs included in the cost of revenue.

### Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements, other than operating leases disclosed in the Notes to the Consolidated Financial Statements, as at the end of the 2010 fiscal year.

### Transactions with Related Parties

The Company had no transactions with related parties in 2011.

### Proposed Transactions

The Company has no firm proposed transactions as at October 31, 2011.

## Fourth Quarter

The Company booked \$54.2 million in new orders in the fourth quarter of fiscal 2011, compared with approximately \$78.8 million in the fourth quarter of 2010 and \$47.4 million of the third quarter of 2011. It is important to note that contract awards in the space market are typically characterized as lumpy, which historically has resulted in uneven new order levels on a quarter-by-quarter basis. Revenues for the fourth quarter were \$49.9 million, compared with \$50.5 million in the prior quarter, and \$51.5 million in the fourth quarter of fiscal 2010. Gross margins were 23.8% in the fourth quarter, down from 27.4% in the prior quarter, and up from 19.9% in the fourth quarter of fiscal 2010. The year over year increase in fourth quarter margins reflected the decreased impact of prior cost growth on the five programs noted previously.

During the fourth quarter, the Company generated \$0.8 million in cash from operating activities, compared with the prior quarter where the Company generated \$1.3 million in cash from operating activities. In the fourth quarter of 2010, the Company generated \$1.8 million in cash from operating activities.

The Company invested \$5.4 million in capital asset and in intangible asset additions during the fourth quarter of 2011. The Company invested \$7.3 million in capital and intangible assets during the fourth quarter of fiscal 2010 and \$10.0 million in capital and intangible assets in the third quarter of 2011. The Company ended the quarter with \$27.6 million in cash, compared with \$34.8 million at the end of the prior quarter, and \$17.4 million at the end of the fourth quarter of fiscal 2010.

## Contractual Obligations (in thousands of dollars)

	<u>Total</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017 &amp; beyond</u>
Long-term debt *	\$ 23,554	\$ 8,867	\$ 5,769	\$ 4,767	\$ 2,980	\$ 965	\$ 206
Operating Leases	\$ 3,567	\$ 2,238	\$ 906	\$ 304	\$ 69	\$ 50	\$ -
Capital Leases	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Purchase Obligations **	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other Long-term obligations ***	\$ 5,860	\$ 543	\$ 603	\$ 673	\$ 502	\$ 479	\$ 3,060
Total contractual obligations	<u>\$ 32,981</u>	<u>\$ 11,648</u>	<u>\$ 7,278</u>	<u>\$ 5,744</u>	<u>\$ 3,551</u>	<u>\$ 1,494</u>	<u>\$ 3,266</u>

\* Long-term debt appears on the balance sheet using the effective interest rate method of valuation.

\*\* Defined as an agreement to purchase goods and services that is enforceable and legally binding on the Company and that specifies all significant terms including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transactions.

\*\*\* Includes expected future benefit payments to certain employees under a defined benefit pension plan (refer to note 16 for details on the employee future benefit plans) and for certain termination benefits.

## Financial Instruments and Other Instruments

The Company realizes a significant portion of its revenues in U.S. dollars and incurs most of its expenses in Canadian dollars. The Company utilizes foreign exchange options to hedge the net cash flow risk associated with forecasted transactions in foreign currencies but does not enter into derivatives for speculative purposes. The Company utilizes derivative instruments to manage the risk associated with anticipated cash flows that will be denominated in foreign currencies. The Company does not designate or measure the effectiveness of the derivative instruments as hedges of specific firm commitments or forecasted transactions and, accordingly, does not meet the requirements of CICA Handbook Section 3865, Hedges, to apply hedge accounting. The Company generally uses foreign exchange put options and related call options to manage foreign currency risk related to sales to customers in the United States and United Kingdom.

Derivative financial instruments are carried at their fair values. Realized and unrealized gains and losses associated with the derivative instruments are included in "foreign exchange loss (gain)" in the Consolidated Statements of Operations. In 2011, the unrealized loss from the change in fair value of the Company's hedge options was \$2.9 million (2010: \$1.1 million gain) and the realized gain was \$3.3 million (2010: \$3.5 million gain). Additional information of the Company's hedge contracts can be found in note 10 (Bank Indebtedness, Loans Payable, and Other Financial Instruments) in the Notes to the Consolidated Financial Statements.

The Company is exposed to credit risk on derivative financial instruments arising from the potential for counterparties to default on their contractual obligations to the Company. The Company minimizes this risk by limiting counterparties to these contracts to Canadian Schedule A Chartered Banks.

### Summary of Quarterly Financial Information (Unaudited) (in thousands of dollars, except earnings per share figures)

Fiscal 2011 Quarters	January 31	April 30	July 31	October 31
Total revenue	\$ 48,689	\$ 54,164	\$ 50,453	\$ 49,889
Net income attributable to shareholders	\$ 1,272	\$ 3,025	\$ 4,238	\$ 5,071
Net income per share (basic and diluted)	\$ 0.02	\$ 0.04	\$ 0.05	\$ 0.07

Fiscal 2010 Quarters	January 31	April 30	July 31	October 31
Total revenue	\$ 56,687	\$ 60,415	\$ 52,333	\$ 51,486
Net income attributable to shareholders	\$ 2,245	\$ 4,105	\$ (1,715)	\$ (1,941)
Net income per share (basic and diluted)	\$ 0.03	\$ 0.05	\$ (0.02)	\$ (0.02)

Historically, the Company's revenues have been lowest in the first quarter. This is due to the fact that the first quarter has the lowest number of working days as the operations shut down over the Christmas period for maintenance and vacation. Since the Company reports revenue on a percentage of completion basis, the lower number of workdays typically translates to less revenue.

## Critical Accounting Estimates

The preparation of the Company's consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. These estimates are based upon management's historical experience and various other assumptions that are believed by management to be reasonable under the circumstances. Such assumptions and estimates are evaluated on an ongoing basis and form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

Management believes the following critical accounting policies affect its more significant estimates and assumptions used in the preparation of its consolidated financial statements.

### *Revenue Recognition*

The Company generally provides goods and services to its customers under long-term contracts. The Company recognizes revenue on long-term contracts on the percentage of completion basis, based on costs incurred relative to the estimated total contract costs. Losses on such contracts are accrued when the estimate of total costs indicates that a loss will be realized. Contract billings in excess of cost and accrued profit margins are included as deferred revenue and included in current liabilities.

A portion of the Company's revenue is derived from the sale of goods and services on short-term agreements and purchase orders as well as "cost-plus" government contracts. The revenue from short-term agreements and purchase orders are recognized when the goods and services are delivered to the customer and collection is reasonably assured. Cost-plus contract revenue is recognized as eligible costs are incurred on the applicable contracts.

### *Project Costs to Complete*

At the outset of each customer project, an estimate of the total expected cost to complete the scope of work under contract is made. During the course of the projects, these estimates are reviewed and revised to reflect current expectations of cost to complete, and total cost. These estimates are based on specific knowledge of the status of the project, as well as historical understanding of costs on similar projects. Cost elements include material, direct labour, and overhead costs, with labour and overhead costs being determined using pre-established costing rates applied to estimated labour hours required to complete the scope of work under contract. These estimates are reviewed on a monthly and quarterly basis to ensure the estimates reflect the current expectations for total costs, however this is not a guarantee that unforeseen or additional costs could be incurred, which would have an impact on project total cost, reported revenue, and gross margins. Management believes it has a review procedure in place to ensure the validity of these estimates at the time they are made.

### *Useful Life of Intangible and Long-Term Assets*

The Company has established policies for determining the useful life of its intangible and long-term assets, and amortizes the costs of these assets over those useful lives. The useful life for each category of asset is determined based on the expectation of its ability to continue to generate revenues, and thus, cash flows for the Company. This ability is tested periodically to ensure the conditions still exist to allow the asset to be reflected at its net-recorded value in the accounts of the Company, and any impairment to the valuation is reflected in the accounts at the time the impairment is determined.

### *Income Tax Liabilities*

The Company establishes a tax provision based on its calculation of taxable income in any year. Occasionally, the Company is subjected to audits by various federal and provincial agencies. When adjustments are proposed, the Company assesses its position with respect to the issue, and when it considers the Company's position to be correct, may object to proposed adjustments. Management estimates the likelihood of succeeding in its position, and where appropriate, provides for amounts estimated to be payable, or reports in notes to the Company's financial statements. For a complete description of carry-forward tax balances, the future tax asset and associated valuation reserve against that future tax asset, see Note 4 to the 2011 audited Consolidated Financial Statements.

### *Contract Penalties*

In some cases, the Company enters into contracts with its customers for the delivery of equipment, where penalties are incurred for late delivery. When the Company wins these orders, it assumes that the cost of the penalties will not be incurred unless the project schedule indicates that contracted delivery dates will not be met. At that time, the individual projects are charged with the cost associated with expected penalties.

## **Changes in Accounting Policies including Initial Adoption**

### *International Financial Reporting Standards (IFRS)*

The CICA Accounting Standards Board has announced that Canadian publicly accountable enterprises will adopt IFRS as issued by the International Accounting Standards Board effective for fiscal years beginning on or after January 1, 2011 and therefore will commence in the first quarter of the Company's 2012 fiscal year, including comparative figures.

The Company has established a project team led by finance management, and is receiving assistance from Ernst & Young LLP ("E&Y") for the IFRS conversion project. Key personnel, Board and Audit Committee members are receiving ongoing topic specific training to prepare for the transition to IFRS.

We describe below our IFRS changeover plan, key deliverables and their status, and the significant known impacts on our financial reporting to allow readers to obtain a better understanding of the resulting possible effects on our financial statements and operating performance measures. Readers are cautioned, however, that it may not be appropriate to use such information for any other purpose. This information reflects our most recent assumptions and expectations; circumstances may arise, such as changes in IFRS, regulations or economic conditions, which could change these assumptions or expectations. We will continue to monitor and adjust for any changes to the standards to ensure the reader is kept abreast of such developments.

The Company is following a five phase approach to ensure successful conversion to International Financial Reporting Standards. The five phases are:

#### 1. IFRS diagnostic impact assessment

Perform a high-level review to identify significant differences between Canadian Generally Accepted Accounting Principles ("GAAP"), as adopted by COM DEV, and IFRS.

Status: This phase is complete.

#### 2. Design and planning

Using the outputs from the diagnostic assessment, a master plan for the conversion project will be compiled. This plan will include schedules, resource requirements and output specifications.

Status: This phase is completed.

#### 3. Solution development

The Company will carry out a full assessment of the changes required to accounting and business systems in order to migrate to IFRS. This phase included developing and updating accounting policies including identification and selection from the different IFRS 1 first-time adoption exemptions available at the date of the transition. The Company will also identify required changes to internal control over financial reporting and disclosure controls and procedures to ensure (1) appropriate controls are designed to support reporting under IFRS and (2) shareholders are informed of the anticipated effects of IFRS transition.

Status: This phase is completed.

#### 4. Implementation

During this phase, the Company is implementing the solutions identified in Phase 3. The culmination of this phase will be collection of all the financial information necessary to produce IFRS-compliant financial statements, embedding IFRS in business processes and Audit Committee approval of IFRS financial statements.

Status: Phase 4 is in process and will continue through Q1 of 2012.

## 5. Post implementation review.

This phase will be to ensure on-going compliance with IFRS and to take into account the changing IFRS landscape.

Status: To commence in Q1 2012.

The diagnostic impact assessment identified several areas that require a significant degree of effort to quantify the impact on the opening balance sheet and to put in place procedures and controls to efficiently and effectively address the particular IFRS difference on an ongoing basis. In particular, assessments were carried out in the areas of revenue recognition, property, plant and equipment, impairment and taxes.

Changes to policy and procedure resulting from transition to IFRS will not result in significant changes to IT systems.

### **First-time Adoption of IFRS**

IFRS 1 first-time adoption of IFRS generally requires that all IFRS are applied retrospectively and that adjustments arising from the application of IFRS are to be recognized in retained earnings as of the date of the first comparative balance sheet. However, there are a number of mandatory and optional exemptions from the retrospective application requirement. The following are some of the significant optional IFRS 1 exemptions the Company expects to apply in its first IFRS financial statements.

#### *Business Combinations*

IFRS 1 permits an entity to elect not to restate business combinations prior to the date of transition to IFRS. The Company will elect not to retrospectively restate past business combinations.

#### *Fair Value as Deemed Cost*

An election to use fair value of property, plant and equipment as deemed cost at the transition date is available under IFRS 1. The Company will use historical cost and not elect to use fair value as deemed cost.

#### *Employee Benefits*

The Company may elect to recognize all cumulative actuarial gains and losses in retained earnings at the date of transition under IFRS 1. COM DEV will elect to recognize their cumulative actuarial losses in retained earnings.

#### *Cumulative Translation Differences*

IFRS 1 allows an entity to elect not to recalculate translation differences retrospectively. When this election is made, the cumulative translation difference for all foreign subsidiaries is deemed to be nil at the date of transition. The Company will elect to use this exemption and will clear the cumulative translation difference to opening retained earnings.

### **Expected Areas of Significance**

The key areas where we expect accounting policies may differ, either due to policy choice or differences between Canadian GAAP and IFRS, which may impact the Company's consolidated financial statements, are discussed below.

#### *Property, Plant and Equipment*

Under IFRS, after the initial recognition, fixed assets can be measured using the cost model or the revaluation model while Canadian GAAP does not allow revaluation. The Company will continue to use historical cost as its measurement basis.

IFRS requires componentization, where an item of property, plant and equipment has a significant component with a different expected useful life from the main item, IFRS requires that component to be depreciated separately based on the components own useful life. Canadian GAAP is similar in this respect; however it has often not been applied to the same extent due to practicality and/or materiality. For COM DEV, buildings are comprised of various components for which different useful lives, and therefore rates of depreciation, were identified. Componentization of the buildings will result in a decrease in net book value and decreased periodic depreciation compared to Canadian GAAP.♦

The mandatory annual evaluation of useful life and residual value under IFRS has a significant impact on depreciation and on opening net book value of assets due to retrospective reassessment of useful lives upon

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♦ Forward-looking Information. Please refer to Caution Regarding Forward-looking Information on Page 1 of this document

transition. The Company expects that due to an overall increase in useful life, the net book value of Property, Plant and Equipment will increase upon transition resulting in an increase in periodic depreciation. ♦

#### *Impairment of Long Lived Assets*

IFRS requires a single-step approach for impairment testing of individual assets or a group of assets in cash generating units (CGUs) on the basis of independent cash inflows whereas Canadian GAAP uses a two-step approach. When profiling future cash flows of an asset or CGU, IFRS requires the analysis to be based on pre-tax cash flows discounted using a pre-tax risk rate. This requirement differs from the Canadian GAAP test based on undiscounted cash flows. The change in impairment test methodology results in asset impairment that was not recognised under Canadian GAAP. The change in impairment test methodology will result in asset impairment under IFRS, where there was no impairment under Canadian GAAP. There are also provisions under IFRS for the subsequent reversal of these impairment charges if circumstances change such that the previously determined impairment is reduced or eliminated.

#### *Revenue Recognition*

The revenue recognition standard under IFRS includes specific and mandatory criteria for determining whether construction contracts should be segmented or if multiple construction contracts should be combined. The standard addresses variations to original contract terms or claims for reimbursement that are not included in the contract price. The requirement to segregate or combine contracts will impact the calculation of revenue using the percentage complete method. Business processes to assess the appropriate method of revenue recognition based on project specific conditions have been designed.

The total amount of revenue and gross margin reported under IAS 11 and Canadian GAAP will ultimately be the same, but the timing of revenue recognition will differ and reported gross margin may be negatively affected under IAS 11 until the construction contract is completed. Due to timing differences, the Company expects that when it reports FY12 revenue, the comparable FY11 revenue under IFRS will vary from the previously reported FY11 revenue under Canadian GAAP. ♦

#### *Income Taxes*

IAS 12 — Like Canadian GAAP, deferred income taxes under IFRS are determined using the liability method for temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes, and by generally applying tax rates applicable to the Company to such temporary differences. Deferred income taxes relating to temporary differences that are in equity are recognized in equity and under IFRS subsequent adjustments thereto are backward-traced to equity. IFRS prohibits recognition where deferred income taxes arise from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither accounting nor taxable net earnings. Deferred tax amounts are not expected to change upon implementation of IAS 12. IAS 1 requires that deferred tax assets and liabilities are classified as non-current. Therefore, the current future income taxes will be reclassified to long term future income taxes.

SR&ED investment tax credits (ITCs) are recorded as an offset to R&D expense under Canadian GAAP. IAS 12 requires tax credits that are dependent on future taxable income to be included in the calculation of income tax expense and ITCs not dependent on future taxable income to be treated as a grant and therefore offsets the applicable expense or capital item. The Company is currently evaluating the nature of its ITCs to determine the appropriate recognition treatment.

#### *Provisions, Contingent Liabilities and Contingent Assets*

IAS 37 — Provisions, contingent liabilities and contingent assets, requires a provision to be recognized when: there is a present obligation as a result of a past transaction or event; it is probable that an outflow of resources will be required to settle the obligation; and a reliable estimate can be made of the obligation. "Probable" in this context means more likely than not. Under Canadian GAAP, the criterion for recognition in the financial statements is "likely", which is a higher threshold than "probable". Therefore, there may be some provisions or contingent liabilities that would meet the recognition criteria under IFRS that were not recognized under Canadian GAAP.

Under IAS 11 and IAS 37, expected losses on construction contracts will be recorded as provisions. Under Canadian GAAP expected losses were recognized against revenue and accounted for with contracts in progress in inventory or deferred revenue.

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♦ Forward-looking Information. Please refer to Caution Regarding Forward-looking Information on Page 1 of this document

The Company has made changes to processes and systems for the 2011 fiscal year. The Company has tracked transactions under IFRS during fiscal 2011 for comparative purposes in the 2012 financial reporting year. The Company is unable to fully quantify the impact of adopting IFRS at this time.

## **Business Risks and Prospects**

### *Failure to Perform Contracts*

Contracts for the Company's products may include penalties and/or incentives related to performance, which could materially affect operating results. Management provides for any anticipated penalty costs in its estimates of the costs to complete a contract and the contract generally limits any penalties to 5% or less of the contract value. The Company's products are complex, use sophisticated technologies and often involve a lengthy development and manufacturing cycle. In addition, these products are integral to the customer's satellite payload and alternate sources of supply may not be available in the time required, or at all. Consequently, any failure by the Company to satisfy its contractual obligations could trigger losses in excess of the value of the contract. Since the Company often works on large individual contracts, the claims against the Company could be material.

### *Project Performance*

Any inability of the Company to execute customer projects in accordance with requirements, including adherence to delivery timetables, could have a material adverse effect on the Company's business, operations and prospects.

### *Satellite Launch Delays or Failures*

The Company's exactEarth™ subsidiary derives its revenue from selling data-based services from satellites equipped with AIS receivers. The Company's ability to control launch schedules is limited and launch delays could adversely affect the Company's ability to earn revenues. Similarly, if a satellite were to fail in orbit or were to enter an incorrect orbit then the Company's revenue would be adversely affected.

### *Fluctuations in Operating Results*

The Company's revenues and earnings fluctuate from quarter to quarter, or year to year, based on customer requirements and the timing of orders. While the Company recognizes revenue on a percentage of completion basis for long-term contracts, it has experienced fluctuations in its quarterly operating results and anticipates that such fluctuations may continue. The Company's revenue is derived in large part from long-term fixed price contracts, some of which are subject to significant technology risk. As a result, the Company's financial reporting relies upon management's estimates of earned revenues and the costs required to complete the project. Revision to the estimates used in the preparation of the Company's financial results could have a material impact on financial results of future periods. There can be no assurance that levels of profitability will not vary significantly among quarterly or annual periods. The Company's operating results may fluctuate as a result of many factors, including increased competition, the size and timing of significant customer orders, cancellations of significant projects by customers, changes in operating expenses, changes in the Company's strategy, changes in personnel, foreign currency exchange rates and general economic and political factors.

The Company's expense levels are based in significant part on its expectations regarding future revenues. Accordingly, the Company may be unable to adjust spending in a timely manner to compensate for any unexpected revenue shortfall. Any significant revenue shortfall could therefore have a material adverse effect on the Company's results of operations.

### *Competition*

COM DEV's competitors, who are generally its customers, are larger, better capitalized and have greater resources than the Company. The Company believes that its ability to compete depends in part on a number of competitive factors, some of which are outside its control, such as innovative products or cost-saving production techniques developed by the Company's competitors. There can be no assurance that the Company will be able to compete successfully with its existing competitors or with new competitors.

### *Foreign Exchange Risk*

The Company carries on a significant portion of its business in the United States and elsewhere outside Canada, and the majority of its sales outside of Canada are made in U.S. dollars. Any weakening in the value of the U.S. dollar, British Pounds or Euro against the Canadian dollar would result in lower revenues and margins for the Company when stated in Canadian dollars. The Company does engage in hedging its U.S. dollar-denominated net cash flows, and is actively targeting efficiency improvements in its operations, both in terms of productivity and cost control. These measures will continue to be taken regardless of the currency environment. The Company also seeks to contract in Canadian dollars in its Canadian operations wherever possible.

### *Tax Assessments*

In prior fiscal years, the Company has undergone audits by Canada Revenue Agency and the Ontario Ministry of Finance. As a result of the audits, several adjustments to prior year returns have been proposed for capital taxes and corporate minimum taxes. The disputed tax amounts, which have been paid, total \$3.3 million, including accrued interest. The Company has considered the proposed assessments and opposes several matters based on its interpretation of the tax rules and has made submission to the tax authorities on this basis.

In a recent audit by the Canada Revenue Agency, an assessment was received in the third quarter of 2011 that indicated that the Company failed to make required withholdings on payments made to certain vendors from 2006 to 2010. Management does not agree with several of the findings and has accordingly filed a Notice of Objection for items that total approximately \$2.6 million. A letter of credit has been issued in favour of Canada Revenue Agency to secure this disputed amount.

The Company is currently unable to determine the likelihood of success of its objections to the proposed assessments. Any amount of tax liability arising from these assessments will be recorded when the probable amounts can be determined.

### *Timing Risks*

There can be no assurance that the market demand for the Company's products will translate into orders within the time frames anticipated. The timing and extent of satellite procurement, and the Company's ability to secure project orders stemming from anticipated satellite procurement activity could have a material adverse effect on the Company's business, operations and prospects.

### *Reliance on Significant Customers and Credit Concentration*

The satellite industry is characterized by a small number of prime contractors, which represents most of the Company's customer base. The relatively small number of customers leads to a concentration of the Company's revenues and accounts receivable. If one or more customers were to delay, reduce or cancel orders, the overall orders of the Company may fluctuate and could adversely affect the Company's operations and financial condition. While the Company's accounts receivable tend to be concentrated, many of our customer receivables, by virtue of their non-Canadian status are insured with Export Development Canada ("EDC"). While the Company expects to be able to continue to access receivables insurance through EDC, there is no assurance that this will be the case, and any subsequent credit loss could have a material adverse effect on the business and its financial condition. COM DEV is increasing its penetration with a number of smaller satellite manufacturers, as well as in satellite market segments outside the traditional commercial communications sector, to help mitigate the risk associated with having a small number of customers.

### *Changing Business Conditions*

The Company'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 the Company is unable to respond to and manage changing business conditions, the quality of the Company's services, its ability to retain key personnel and its results of operations could be materially adversely affected. The Company has recently expanded into the U.S. with the purchase of a facility to be used to design, engineer, and produce equipment for its customers involved in U.S. government satellite programs. The inability to effectively address this new market could result in a material adverse effect on the results of the Company's operations.

### *Dependence on Key Personnel*

The Company is highly dependent on the continued service of and its ability to attract and retain qualified technical and engineering personnel. The competition for such personnel is intense and the loss of particular persons, as well as the failure to recruit additional key technical personnel in a timely manner, could have a material adverse effect on the Company's business.

### *Future Capital Requirements*

The Company's future capital requirements will depend on many factors, including the development of new products, the progress of the Company's research and development efforts, the rate of expansion and the status of competitive products. Depending on these factors, the Company may require additional financing which may or may not be available on acceptable terms. If additional funds are raised by issuing equity securities, dilution to the existing shareholders may result. If adequate funds are not available, the Company may not be able to achieve its growth objectives and operational targets, which could have a material adverse effect on the Company's business.

### *Global Economic Environment*

Recent events have demonstrated that businesses and industries throughout the world are very tightly connected to each other. Thus, events seemingly unrelated to the Company or to its industry, such as the recent extraordinary developments in global financial markets, may adversely affect the Company over the course of time. For example, rapid changes to foreign currency exchange rates may adversely affect the Company's financial results. Credit contraction in financial markets may hurt the Company's ability to access credit in the event that it identifies an acquisition opportunity or some other opportunity that would require a significant investment in resources. Government payments to support financial institutions and other distressed industries may reduce the amount of money governmental agencies have to spend on space and defence related projects. A reduction in credit, combined with reduced economic activity, may adversely affect prime contractors and other businesses that collectively constitute a significant portion of the Company's customer base. As a result, these customers may need to reduce their purchases of COM DEV's products or services, or the Company may experience greater difficulty in receiving payment for the products or services that these customers purchase from the Company. Any of these events, or any other events caused by turmoil in world financial markets, may have a material adverse effect on the Company's business, operating results, and financial condition.

### *New Market Risks*

The Company has identified, as part of its strategic direction, civil/government, and military/defense markets for its product and service offerings. While the Company has seen some success in initial penetration into these markets, there can be no assurance, given the Company's limited experience and operating history in these markets, that the Company's investment and efforts in these markets will be successful. Failure to succeed in the civil/government and military/defense markets may adversely affect the Company's future business, financial condition and operating results.

### *New Products and Technological Change*

The market for the Company's products is characterized by rapidly changing technology involving industry standards and frequent new product introductions. The Company's success will depend upon market acceptance of its existing products and its ability to enhance its existing products and to introduce new products and features to meet changing customer requirements. A current example of this is the Company's efforts to exploit its Automatic Identification System (AIS) detection and de-collision capabilities by entering the AIS data sales market through its new subsidiary Company, exactEarth™ Ltd. There can be no assurance that the Company will be successful in identifying, developing, manufacturing and marketing new products or enhancing its existing products. The Company's business will be adversely affected if the Company incurs delays in developing new products or enhancements or if such products or enhancements do not gain market acceptance. In addition, there can be no assurance that products or technologies developed by others will not render the Company's products or technologies non-competitive or obsolete.

### *Intangible Asset Impairment*

The Company has recognized certain development activities as an intangible asset. The Company assesses these assets periodically to evaluate if value recognized as an asset has become impaired. If the Company were to determine that the applicable expected future cash flows do not support the intangible asset book values,

impairment would need to be recognized that could have an adverse impact on the financial results of the Company.

#### *Product Failure*

COM DEV operates in a market where product reliability is essential. While the Company enjoys a strong reputation for product reliability, any significant product failure could materially affect the Company's reputation, revenue and future business prospects.

#### *Regulatory Environment for Technology and Materials*

Certain of the Company's programs are subjected to export controls either domestically or through International Traffic in Arms Regulations (ITAR). This regulatory environment places strict controls over receipt, use, transfer, and export of technology, material, and equipment. While the Company understands the requirements of these controls and regulations, there is no assurance that these regulations, or their interpretations by regulatory authorities, will not change in a way that would cause a material adverse effect to the Company's business, operations and prospects.

#### *Risks Associated with Intellectual Property*

The Company's success is dependent upon proprietary technology. The Company relies upon patent protection to protect its proprietary technology. In addition, the Company attempts to protect its trade secrets and other proprietary information through agreements with customers, suppliers, employees and consultants and other security measures. There can be no assurance that the steps taken by the Company in this regard will be adequate to prevent misappropriation or independent third-party development of its technology. Furthermore, the laws of certain countries in which the Company sells its products do not protect the Company's intellectual property rights to the same extent as do the laws of Canada or the United States.

Although the Company believes that its products and technology do not infringe patents or other proprietary rights of others, there can be no assurance that third parties will not claim that the Company's current or future products infringe the patents or other proprietary rights of others. Any such claim, with or without merit, could result in costly litigation or could require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company or at all.

#### *Seasonal Volatility*

The Company recognizes revenue based on percentage of completion in accordance with its stated accounting policy. Since the recognition of revenue is determined by costs incurred on projects compared to total expected costs, and since a large portion of the Company's project costs are labour, any quarter with fewer working days will cause suppression in labour effort exerted on projects, and consequently, revenue recognized. Typically, the Company slows production during the Christmas holiday season to provide time for maintenance and facilities improvements to take place. As a result, the Company's first quarter revenues are typically the lowest of the year.

#### *Sources of Supply*

The Company uses some subcomponents for which there is only a single source of supply. As a result, the Company may occasionally suffer shortages of such subcomponents, which shortages may have short-term adverse effects on the Company's sales. Although the Company seeks to reduce exposure to single source suppliers through a continual evaluation of competent alternate sources of supply, the loss of certain of these suppliers, or the inability of certain of these suppliers to deliver to the Company on a timely basis, could have a material adverse effect on the Company's operations and prospects.

## CONTROLS AND PROCEDURES

### Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable, but not absolute, assurance that material information required to be publicly disclosed by a public company is communicated in a timely manner to senior management to enable them to make timely decisions regarding public disclosure of such information. We have conducted an evaluation of our disclosure controls and procedures as of October 31, 2011 under the supervision, and with the participation of, our Chief Executive Officer and our Chief Financial Officer. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures (as this term is defined in the rules adopted by Canadian securities regulatory authorities) are effective in providing reasonable assurance that material information relating to COM DEV is made known to them and information required to be disclosed by us is recorded, processed, summarized and reported within the time periods specified under applicable law.

### Management's Annual Report on Internal Control over Financial Reporting

Internal control over financial reporting is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis. Additionally, projections of any evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Our management used the Committee of Sponsoring Organizations of the Treadway Commission (COSO) framework to evaluate the effectiveness of internal control over financial reporting. Our Chief Executive Officer and our Chief Financial Officer have assessed the effectiveness of our internal control over financial reporting and concluded that, as at October 31, 2011, such internal control over financial reporting is effective and that there were no material weaknesses.

### Changes in Internal Controls over Financial Reporting

There have been no changes in our internal controls over financial reporting that occurred during the quarter ended October 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Outstanding Share Data

Details of the Company's outstanding share data as of January 12<sup>th</sup>, 2012 are as follows:

Common shares	76,394,409
Options on common shares	874,804

Each option is exercisable for one common share of the Company.

# INDEPENDENT AUDITORS' REPORT

To the Shareholders of  
**COM DEV International Ltd.**

We have audited the accompanying consolidated financial statements of **COM DEV International Ltd.**, which comprise the consolidated balance sheets as at October 31, 2011 and 2010, and the consolidated statements of operations, changes in equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

## **Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

## **Auditors' responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

## **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of **COM DEV International Ltd.** as at October 31, 2011 and 2010 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Kitchener, Canada,  
January 12, 2012.

*Ernst & Young LLP*

Chartered Accountants  
Licensed Public Accountants

COM DEV International Ltd.  
Consolidated Statements of Operations  
(Canadian dollars in thousands, except for per share figures)

For the year ended October 31	2011	2010
Revenue (note 15)	\$ 203,195	\$ 220,921
Cost of revenue	156,614	175,802
Gross margin	<u>46,581</u>	<u>45,119</u>
Research and development costs	13,318	12,366
Research and development recovery	6,961	3,629
Investment tax credits recoverable	13,317	2,100
Net research and development (recovery) expense	<u>(6,960)</u>	6,637
Selling expenses	11,367	11,845
General expenses	17,638	20,689
Operating income	<u>24,536</u>	5,948
Interest expense	888	553
Foreign exchange loss (gain)	914	(2,578)
Other expense (note 14)	3,009	3,432
Income before income taxes	<u>\$ 19,725</u>	<u>\$ 4,541</u>
Income tax expense (note 4)	8,170	2,115
Net income	<u><u>\$ 11,555</u></u>	<u><u>\$ 2,426</u></u>
Attributable to:		
Shareholders	\$ 13,606	\$ 2,694
Non-controlling interest (notes 5(b) & 6)	<u>(2,051)</u>	<u>(268)</u>
	<u><u>\$ 11,555</u></u>	<u><u>\$ 2,426</u></u>
Earnings per share (note 12(e))		
Basic and diluted earnings per share	\$0.18	\$0.04
Basic weighted average number of shares	76,394,409	76,137,922
Diluted weighted average number of shares	76,460,835	76,282,809

COM DEV International Ltd.  
Consolidated Balance Sheets  
(Canadian dollars in thousands)

	As at October 31, 2011	As at October 31, 2010
<b>Assets</b>		
Current		
Cash and cash equivalents	\$ 27,618	\$ 17,436
Accounts receivable	47,563	44,357
Inventory (note 3)	47,763	58,827
Prepays and other	1,422	3,274
Income taxes recoverable (note 13(d))	4,788	4,615
Future income tax assets - current (note 4)	3,477	4,175
	<u>132,631</u>	<u>132,684</u>
Property, plant and equipment (notes 5(a) & 8)	76,201	75,770
Intangible assets (note 9)	29,178	27,862
Goodwill	2,200	2,252
Future income tax assets - long term (note 4)	9,732	3,898
Total assets	<u>\$ 249,942</u>	<u>\$ 242,466</u>
<b>Liabilities</b>		
Current		
Accounts payable and accrued liabilities	\$ 26,373	\$ 27,928
Income taxes payable	302	-
Deferred revenue (note 3)	9,653	23,170
Current portion of loans payable (note 10 (b))	8,867	6,401
	<u>45,195</u>	<u>57,499</u>
Long term		
Loans payable (note 10 (b))	14,687	10,115
Accounts payable and accrued liabilities	930	968
Employee future benefits (note 16)	1,582	1,910
	<u>17,199</u>	<u>12,993</u>
Total liabilities	<u>62,394</u>	<u>70,492</u>
Shareholders' equity		
Share capital (note 12 (a))	345,666	346,068
Contributed surplus	9,407	7,314
Deficit	(172,459)	(186,065)
Non-controlling interest (notes 5 (b) & 6)	8,977	8,328
Accumulated other comprehensive loss	(4,043)	(3,671)
Total shareholders' equity	<u>187,548</u>	<u>171,974</u>
Total liabilities and shareholders' equity	<u>\$ 249,942</u>	<u>\$ 242,466</u>

On behalf of the Board:

\_\_\_\_\_  
Terry Reidel  
Chairman of the Board

\_\_\_\_\_  
Kym Anthony  
Chairman of the Audit Committee

COM DEV International Ltd.  
Consolidated Statements of Cash Flows  
(Canadian dollars in thousands)

For the year ended October 31	2011	2010
<b>Operating activities</b>		
Net income	\$ 11,555	\$ 2,426
Amortization (notes 8 & 9)	11,670	11,261
(Gain) loss on disposal of assets	(253)	175
Defined benefit plan expenses (note 16)	563	944
Defined benefit plan contributions (note 16)	(857)	(779)
Stock compensation expense	1,557	1,293
Employee stock ownership plan awards	222	198
Fair value adjustment for SODP loan (note 10)	(78)	(855)
Investment tax credits recoverable	(13,126)	(2,100)
Future tax expense (note 4 (a))	8,005	1,942
Unrealized foreign exchange loss (gain) on derivatives (note 10(c))	2,920	(1,144)
	<u>22,178</u>	<u>13,361</u>
Net change in non-cash working capital items	<u>(7,455)</u>	<u>251</u>
<b>Operating activities</b>	<u><b>14,723</b></u>	<u><b>13,612</b></u>
<b>Financing activities</b>		
Shares issued	514	-
Shares repurchased and cancelled (note 12 (a))	(514)	-
Non-controlling interest investment, net (note 6)	2,612	11,952
Advance of long term debt (note 10)	15,522	4,696
Repayment of long term debt	(7,977)	(6,331)
<b>Financing activities</b>	<u><b>10,157</b></u>	<u><b>10,317</b></u>
<b>Investing activities</b>		
Acquisition of property, plant and equipment	(9,466)	(13,849)
Proceeds on disposal of property, plant and equipment	1,568	-
Acquisition of intangible assets	(5,956)	(10,926)
Business acquisitions (note 5)	-	(2,127)
<b>Investing activities</b>	<u><b>(13,854)</b></u>	<u><b>(26,902)</b></u>
Effect of exchange rate changes on cash	<u>(844)</u>	<u>(995)</u>
Net increase (decrease) in cash	10,182	(3,968)
Cash and cash equivalents, beginning of year	17,436	21,404
Cash and cash equivalents, end of year	<u><u><b>\$ 27,618</b></u></u>	<u><u><b>\$ 17,436</b></u></u>
Interest paid	<u><u><b>\$ 950</b></u></u>	<u><u><b>\$ 560</b></u></u>
Taxes paid	<u><u><b>\$ -</b></u></u>	<u><u><b>\$ 173</b></u></u>

COM DEV International Ltd.  
Consolidated Statements of Changes in Equity  
(Canadian dollars in thousands)

For the year ended October 31, 2011	Total	Deficit	Accumulated Other Comprehensive Loss	Share Capital	Non-controlling interest	Contributed Surplus
Balance, October 31, 2010	\$ 171,974	\$ (186,065)	\$ (3,671)	\$ 346,068	\$ 8,328	\$ 7,314
Comprehensive income						
Net income (loss)	11,555	13,606	-	-	(2,051)	-
Foreign currency translation adjustments (net of taxes of \$nil)	<u>(372)</u>	<u>-</u>	<u>(372)</u>	<u>-</u>	<u>-</u>	<u>-</u>
	11,183	13,606	(372)	-	(2,051)	-
Common stock issued	514	-	-	871	-	(357)
Common stock repurchased and cancelled (note 12(a))	(514)	-	-	(1,273)	-	759
Expense recognized for ESOP awards	222	-	-	-	-	222
Non-controlling interest investment (note 6)	2,612	-	-	-	2,700	(88)
Expense recognized for stock-based compensation and long-term incentive plans	1,557	-	-	-	-	1,557
Balance, October 31, 2011	<u>\$ 187,548</u>	<u>\$ (172,459)</u>	<u>\$ (4,043)</u>	<u>\$ 345,666</u>	<u>\$ 8,977</u>	<u>\$ 9,407</u>
<hr/>						
For the year ended October 31, 2010						
Balance, October 31, 2009	\$ 157,909	\$ (188,759)	\$ (2,507)	\$ 345,885	\$ 486	\$ 2,804
Comprehensive income						
Net income (loss)	2,426	2,694	-	-	(268)	-
Foreign currency translation adjustments (net of taxes of \$nil)	<u>(1,164)</u>	<u>-</u>	<u>(1,164)</u>	<u>-</u>	<u>-</u>	<u>-</u>
	1,262	2,694	(1,164)	-	(268)	-
Common stock issued	-	-	-	183	-	(183)
Expense recognized for ESOP awards	198	-	-	-	-	198
Non-controlling interest purchase adjustment (note 5(b))	(640)	-	-	-	(465)	(175)
Non-controlling interest investment (note 6)	11,952	-	-	-	8,575	3,377
Expense recognized for stock-based compensation	1,293	-	-	-	-	1,293
Balance, October 31, 2010	<u>\$ 171,974</u>	<u>\$ (186,065)</u>	<u>\$ (3,671)</u>	<u>\$ 346,068</u>	<u>\$ 8,328</u>	<u>\$ 7,314</u>

**COM DEV INTERNATIONAL LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**October 31, 2011**  
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**1. Summary of Significant Accounting Policies**

These consolidated financial statements of COM DEV International Ltd. (the "Company") have been prepared by management in accordance with Canadian generally accepted accounting principles on a basis consistent with prior periods. All financial amounts are expressed in thousands of Canadian dollars, except per share information or as otherwise indicated. These consolidated financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

**a) Basis of Consolidation**

The consolidated financial statements include the accounts of all of the Company's subsidiaries with inter-company transactions and balances eliminated. The Company's principal wholly owned subsidiaries are COM DEV Limited ("CDL"), COM DEV Europe Limited ("CDE"), COM DEV USA LLC ("CDU"), COM DEV US Property LLC ("CD US Property"), COM DEV Consulting Ltd. ("CD Consulting"), and Xi'an COM DEV Microwave Electronics Company Limited ("Xian"). The Company's 73% owned subsidiary is exactEarth Ltd.

**b) Use of Estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Estimates include, but are not limited to, the value of contract work in progress and recognition of revenue related to the percentage of completion of contract work, the determination of doubtful accounts, impairment of long-lived assets, intangibles, and goodwill, useful lives of intangible assets and property, plant, and equipment, determination of net recoverable value of assets, contracts in progress, and future income tax assets, valuation of employee future benefit liabilities, and contingencies. Actual results could differ from these estimates.

**c) Cash and Cash Equivalents**

Cash and cash equivalents consist of balances with banks and short-term investments that mature within 90 days from the date of acquisition. Short-term deposits are carried at their fair values. Fair values of short-term investments with maturity less than 90 days approximate the carrying amount.

**d) Inventory**

Inventories, other than contracts in process, are valued at the lower of cost on a weighted average basis and net realizable value. Cost of raw materials includes the purchase cost and the cost incurred in bringing each product to its present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. Items that are written down to net realizable value are adjusted back up to cost if there is a subsequent increase in the net realizable value. The majority of inventory is raw materials and component parts held for use in the contracts in progress projects and are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost.

Contracts in process are valued at cost plus accrued profit margins, less billings issued to

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date and less the full amount of any anticipated losses.

**e) Property, Plant and Equipment**

Property, plant and equipment are stated at cost, and amortization is recorded, at rates sufficient to write-off the costs over the estimated useful lives of the assets, using the straight-line method as follows:

Buildings	–	forty years
Machinery	–	five to fifteen years
Electrical equipment, furniture and fixtures	–	five to ten years
Computer hardware and software integral to the hardware on which it operates	–	three to five years

**f) Goodwill**

Goodwill represents the excess of consideration paid over the fair value of the total identifiable tangible and intangible assets acquired. Goodwill is tested for impairment in accordance with the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3064, on at least an annual basis or upon the occurrence of certain events or circumstances which may indicate that the asset might be impaired. CICA 3064 requires goodwill impairment to be assessed at a reporting unit level. The Company has defined the reporting units to be CDI, CDL, CDE, exactEarth Ltd., and the U.S. operations (CDU, CD US Property and CD Consulting). All of the goodwill acquired has been allocated to the U.S. operations reporting unit.

The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit including goodwill is compared with its fair value. Fair value of the reporting unit is measured using a discounted cash flow model. When the fair value exceeds the carrying amount, goodwill is considered not to be impaired and the second step is considered unnecessary. In the event that the fair value of the reporting unit, including goodwill, is less than the carrying value, a second step is performed whereby the implied fair value of goodwill is compared with its carrying amount to measure the impairment loss, if any. The implied fair value of goodwill is determined in the same manner as the value of goodwill is determined in a business combination using the reporting unit fair value as if it was a purchase price. When the carrying amount of goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess and is presented as a separate line on the Consolidated Statements of Operations. Any impairment of goodwill is written off against income in the period that such impairment becomes evident.

**g) Intangible Assets**

Finite life intangible assets are valued at cost less accumulated amortization, which is provided at rates sufficient to write-off the costs over the estimated useful lives of the assets, using the straight-line method as follows:

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Patents	– up to seventeen years
Customer relationships	– the term of the programs up to eight years
Non-compete agreement	– over term of agreement (three years)
Acquired processes	– over the expected life of the technology up to five years
Computer software not integral to the hardware on which it operates	– three to five years
Internally developed technology	– five to seven years

Patent costs represent amounts paid to third parties for the development or acquisition of patents.

Costs that are directly attributable to the development and testing of identifiable and unique internally developed technology controlled by the Company are recognized as intangible assets when the criteria specified in CICA Handbook Section 3064 are met. Capitalized costs include employee costs for staff directly involved in technology development and other expenditures directly related to the project. Other development expenditures that do not meet the capitalization criteria under CICA Handbook Section 3064 are recognized as research and development expense as incurred.

**h) Impairment of Long Lived Assets**

When events and circumstances warrant a review, the Company evaluates the carrying value of its long-lived assets for potential impairment. An impairment loss is recognized when the estimated net recoverable amount of a long-lived asset is less than its carrying value. The impairment loss is measured as the excess, if any, of the carrying value over the fair value of the asset. Any impairment in these assets is written off against income in the year that such impairment becomes evident.

**i) Leases**

Leases that transfer substantially all of the benefits and risks of ownership of the leased assets to the Company are capitalized by recording the present value of future minimum payments under the lease as a capital asset and a liability on the Consolidated Balance Sheets. Assets recorded under capital leases are amortized using the rates consistent with those used by the Company for similar assets. All other leases are accounted for as operating leases and the related lease payments are expensed as incurred.

**j) Income Taxes**

The Company uses the liability method to account for income taxes. Under this method, future income tax assets and liabilities are determined based upon differences between the financial reporting and tax bases of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. In assessing the realizable amount of future tax assets, management considers whether it is more likely than not that some portion or all the benefit of the future income tax assets will be realized. The ultimate realization of future tax assets is dependent upon the generation of future taxable income and/or tax planning strategies.

**k) Revenue Recognition**

The Company generally provides goods and services to its customers under long-term contracts. The Company recognizes revenue on long-term contracts on the percentage of

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completion basis, based on costs incurred relative to the estimated total contract costs. Losses on such contracts are accrued when the estimate of total costs indicates that a loss will be realized. Contract billings in excess of recognized revenue are included as deferred revenue and included in current liabilities.

A portion of the Company's revenue is derived from the sale of goods and services on short-term agreements and purchase orders as well as "cost-plus" government contracts where the Company recovers its' costs plus a profit margin as set out in the contract. The revenue from short-term agreements and purchase orders are recognized when the goods and services are delivered to the customer and collection is reasonably assured. Cost-plus contract revenue is recognized as eligible costs are incurred on the applicable contracts.

**l) Research and Development**

The Company is engaged at all times in research and development work. The Company expenses research and development costs as incurred, unless they meet Canadian generally accepted accounting principles for recognition as an internally generated intangible asset. Investment tax credits ("ITC's") reduce research and development expense and/or intangible assets in the same period in which the related expenditures are charged to earnings or capitalized, provided there is reasonable assurance the benefit will be realized. Otherwise the incentives are recorded when the benefit is expected to be realized.

Research and development costs that are funded by the Company are presented separately on the Consolidated Statements of Operations. Research and development costs that are funded by customers or other programs are included in cost of revenue. Government grants, ITC's, and other funding for research activity are presented as a reduction of the related expense. The Company estimated that there is reasonable assurance that a portion of the ITC's earned in prior years will be realized and recognized ITC's of \$13,317 in 2011 (\$2,100 in 2010), which are included in net research and development (recovery) expense in the Consolidated Statements of Operations.

**m) Foreign Currency Translation**

Foreign denominated monetary items of Canadian operations are translated into Canadian dollars at the exchange rate in effect at year-end. Transactions in foreign currencies are translated at the rate prevailing at the time of the transaction. The resulting gain or loss from translation is recorded in income.

The accounts of the Company's self-sustaining foreign operations, CDE, CDU, CD US Property, CD Consulting, and Xian, are translated using the current rate method, whereby assets and liabilities are translated at the exchange rate in effect at the Consolidated Balance Sheet date and revenue and expenses are translated at the average rate for the period, which approximates the rate prevailing at the time of the transaction. Unrealized translation gains and losses are deferred and included in Accumulated Other Comprehensive Loss ("AOCL").

**n) Derivative Financial Instruments**

The Company, in the management of its foreign currency exposures, utilizes derivative financial instruments. The Company generally uses foreign exchange put options and related call options to manage foreign currency risk related to sales to customers in the United States and United Kingdom. The Company has elected not to apply hedge accounting and, accordingly, carries derivatives at their fair value on the Consolidated Balance Sheets. Changes in the fair value of derivatives are recognized in "Foreign exchange (gain) loss" on the Consolidated Statements of Operations.

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**o) Government Assistance**

Government assistance is periodically received in the form of grants or loans that may be repayable in the form of royalties based on future sales levels related to the technology funded. Amounts that are repayable will be accounted for in the period in which conditions arise that will cause repayment. Government assistance with predetermined repayment requirements or conditional criteria is recorded as a liability when received or until the conditions are satisfied. If no predetermined repayment requirements exist, the assistance is treated as a reduction in the cost of the related item.

**p) Earnings Per Share**

Basic earnings per share is calculated on the basis of income attributable to holders of common shares, divided by the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated giving effect to the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares using the treasury stock method. The treasury stock method assumes that proceeds received from the exercise of the in-the-money stock options together with unamortized compensation expense are used to repurchase common shares at the prevailing market rate, thereby reducing the number of shares otherwise used to calculate the diluted earnings per share.

**q) Stock-Based Compensation, Employee Share Ownership Plan (“ESOP”) and Long Term Incentive Plan (“LTIP”)**

The Company provides compensation to employees in the form of a stock option plan. The Company only grants stock options with an exercise price equal to the market value of the underlying stock on the date of grant. The Company employs a fair value method of accounting for all options granted to employees or directors. The fair value of the direct grants of stock is determined by the quoted market price of the Company’s stock at the time of the award and the fair value of stock options is determined using the Black-Scholes option pricing model. The fair value of awards issued is recorded over the period of vesting as compensation expense and contributed surplus. When the options are exercised, the proceeds received, together with any related amount in contributed surplus, are credited to share capital.

Direct grants of stock to employees and stock options granted to non-employees are being accounted for in accordance with a fair value method of accounting for stock-based compensation.

The Company offers employees the option of contributing a portion, between 2.5% and 10%, of their gross salary towards the purchase of common shares of the Company through the ESOP. The Company issues one share for every four shares that employees purchase during the plan year, which runs from March 1 to February 28. The Company’s matching contribution will be issued to the employee contingent upon the employee remaining employed by the Company on the date one year following the end of the plan year. The fair values on the date that the employees commit to purchase shares are used to determine the applicable compensation expense to the Company. The compensation expense is recognized over the period from the date the employee acquires the shares to the date the Company-matching shares are issued to the employee. The accumulated amount of ESOP shares charged to income but not yet issued is included in contributed surplus.

In 2009, the Company established an LTIP for executives and certain employees. Under the terms of this plan, participants are eligible to receive incentive remuneration in the form of Restricted Share Units (“RSUs”) and/or Performance Share Units (“PSUs”). RSUs are time based and will vest automatically (“cliff vest”) three years after the grant

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date. Each RSU, once vested, entitles the holder to receive one common share of the Company. The Company intends to buy common shares on the open market to satisfy obligations under the plan, but has the option to satisfy obligations in cash. The value of the RSUs is based on the fair market value of the Company's shares on the day of the grant and accounted for as an equity settled instrument. The estimated fair value of the RSUs is amortized to expense over the vesting period.

The value of the PSUs is based on the fair market value of the shares on the day of the grant and is accounted for as an equity settled instrument. The vesting term of the PSUs is three years commencing on the date of the grant, and incorporates performance vesting features based upon achieving certain return on net assets and revenue growth targets established over the vesting period. Each PSU, once vested, entitles the holder to receive one common share of the Company. The Company intends to buy common shares on the open market to satisfy obligations under the plan, but has the option to satisfy obligations in cash. The estimated fair value of the PSUs that are expected to achieve the performance targets is amortized to expense over the vesting period. If, in the future, the performance criteria are expected to not be met, then the change is treated as a change in estimate and therefore, the cumulative effect of the change will be adjusted through income in the period.

**r) Employee Future Benefit Plans**

**Defined Contribution Pension Plan**

The Company sponsors a defined contribution pension plan for certain of its employees. The cost of providing benefits through the defined contribution pension plan is charged to income in the period in which the contributions become payable.

**Defined Benefit Pension Plan**

The defined benefit plans cover former L-3 Electron Technologies Employees. Retirement benefits are based on the employee's service and compensation history. Some of the employees are required to contribute towards the cost of their plan benefits. The employer's portion of plan costs is actuarially determined using the projected benefit method pro-rated on service and management's best estimate of high quality long-term bond rates, salary escalation and retirement ages of employees. Differences arising from plan amendments, changes in assumptions and experience gains and losses are recognized in income over the expected average remaining service life of employees. Gains related to plan curtailments are recognized when the event precipitating the curtailment has occurred. Actuarial gains and losses are amortized using the 10% corridor method where the Company recognizes amortization of actuarial gains or losses in a period in which the unamortized net actuarial gain or loss exceeds 10% of the greater of the accrued benefit obligation or the fair value of the plan assets at the beginning of the year. Plan assets are measured at fair value. The assets supporting the pension benefits are held in a separate trustee pension fund.

**Non-Pension Benefits**

The Company accounts for the cost of employer provided non-pension retirement benefits including medical and vision benefits for eligible retirees, their spouses and qualified dependents on an accrual basis. These costs are recognized in income in the period in which the services are rendered and actuarially determined using the projected benefit method pro-rated on service and management's best estimate of high quality long-term bond rates, retirement ages of employees and expected health care costs.

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**s) Financial Instruments**

The Company has classified its financial instruments as follows:

- Cash and cash equivalents are classified as held-for trading.
- Accounts receivable are classified as loans and receivables.
- Bank indebtedness is classified as held-for-trading.
- Accounts payable and accrued liabilities and long-term debt are classified as other liabilities.
- Derivative financial instruments are classified as held-for-trading.

All financial instruments are initially recognized at fair value and are subsequently accounted for based on their classification. The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arms-length transaction between knowledgeable, willing parties who are under no compulsion to act. The fair value of a financial instrument on initial recognition is the transaction price, which is the fair value of the consideration given or received.

Subsequent to initial recognition, financial assets and liabilities classified as held-for-trading are measured at fair value with changes in fair value recorded on the Consolidated Statements of Operations. The fair values are based on quoted market bid prices if available, otherwise fair value is obtained using discounted cash flow analysis. Financial assets classified as loans and receivables, and other financial liabilities are carried at amortized cost using the effective interest rate method. Fees associated with obtaining long-term debt are included in the financial liability and amortized using the effective interest method.

In accordance with CICA Handbook Section 3862, Financial Instruments – Disclosures, the Company categorizes its fair value measurements according to a three-level hierarchy. The hierarchy prioritizes the inputs used by the Company's valuation techniques. A level is assigned to each fair value measurement based on the lowest level input significant to the fair value measurement in its entirety. The three levels of the fair value hierarchy are defined as follows:

Level 1 – fair value measurements that reflect unadjusted, quoted prices in active markets for identical assets and liabilities that the Company has the ability to access at the measurement date.

Level 2 – fair value measurements using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in inactive markets, inputs that are observable that are not prices (such as interest rates and credit risks) and inputs that are derived from or corroborated by observable market data.

Level 3 – fair value measurements using significant non-market observable inputs. These include valuations for assets and liabilities that are derived using data, some or all of which is not market observable data, including assumptions about risk.

**Embedded Derivatives**

The Company enters into certain non-financial instrument contracts, which contain embedded foreign currency derivatives. Where the contract is not leveraged, does not contain an option feature and is denominated in a currency that is commonly used in the economic environment where the transaction takes place, the embedded derivative is not accounted for separately from the host contract. Changes in the fair value of embedded derivatives will be recognized on a basis consistent with the host contract on the Consolidated Statements of Operations.

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**2. Future Accounting Changes**

**International Financial Reporting Standards**

The CICA Accounting Standards Board has announced that Canadian publicly accountable enterprises will adopt IFRS as issued by the International Accounting Standards Board effective for fiscal years beginning on or after January 1, 2011 and therefore will commence in the first quarter of the Company's 2012 fiscal year, with comparative figures.

The Company has made changes to processes and systems during the 2011 fiscal year, and has established a transition plan to ensure the conversion to IFRS. The Company will record transactions under IFRS during fiscal 2011 for comparative purposes in the 2012 financial reporting year. The Company is unable to fully quantify the impact of adopting IFRS at this time. However, the Company expects the transition to IFRS to impact the accounting and disclosure regarding revenue recognition, assessment of impairment of long-lived assets, income taxes, and amortization of long-lived assets.

**3. Inventory and Deferred Revenue**

Inventory is comprised of:

	2011	2010
Raw Materials	\$14,895	\$13,831
Contracts in process – costs and profits earned in excess of progress billings	32,868	44,996
Total Inventory	\$47,763	\$58,827

The amount of inventory recognized as an expense and included in cost of revenue accounted for other than by percentage-of-completion method during the year ended October 31, 2011 was \$2,967 (\$3,572 in 2010). The amount charged to net income and included in cost of revenue for the write-down of inventory for valuation issues during the year ended October 31, 2011 was \$721 (\$455 in 2010). There was a reduction in the cost of revenue for a reversal of previous write-downs of raw materials for the year ended October 31, 2011 of \$1,523 (\$520 in 2010). Management reviewed the previous write-downs of raw materials and determined certain parts will be useable on future profitable customer contracts where there was no previously expected usage.

Deferred revenue is comprised of:

	2011	2010
Contract billings in excess of cost and accrued profit margins earned on contract work in process	\$ 9,653	\$ 23,170

**4. Income Taxes**

**a) Reconciliation of Income Tax Rates**

The difference between the amount of the consolidated provision for income taxes and the amount computed by multiplying income before taxes by the statutory tax rate is reconciled as follows:

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	<u>2011</u>		<u>2010</u>	
Income before non-controlling interest and income taxes multiplied by the Company's tax rate	\$5,637	<u>28.58%</u>	\$1,430	<u>31.50%</u>
Differences in income taxes resulting from:				
Non-deductible expenses	97		199	
Utilization of losses and SR&ED pool not previously recognized for accounting purposes	(640)		(4,840)	
Tax rate changes in utilization of losses not recognized for accounting purposes	(308)		(460)	
Losses not recognized for accounting purposes	3,219		5,613	
Other	165		173	
Income tax expense	<u>\$8,170</u>		<u>\$2,115</u>	
Less: current tax expense	165		173	
Future tax expense	<u>\$8,005</u>		<u>\$1,942</u>	

**b) Tax effects of significant temporary differences and investment tax credits are as follows:**

	<u>2011</u>	<u>2010</u>
<b>Assets</b>		
Tax paid reserves	\$ 2,380	\$ 1,969
Research and development incentives	51,206	42,092
Loss carry forwards	18,717	18,835
	<u>\$72,303</u>	<u>\$62,896</u>
<b>Liabilities</b>		
Deferred revenue	\$11,029	\$7,739
Capital assets	2,593	1,178
	<u>\$13,622</u>	<u>\$8,917</u>
Net future income tax assets	\$58,681	\$53,979
Valuation allowance	45,472	45,906
Future income tax asset	\$13,209	\$8,073
Less: current portion of future income tax asset	3,477	4,175
Future income tax asset – long term	<u>\$9,732</u>	<u>\$3,898</u>

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**c) Carry Forward Amounts**

The Company has non-refundable investment tax credits, which total \$46,740 federally and \$4,822 provincially. These investment tax credits are available to offset future federal and provincial income taxes payable. The Company has federal and provincial operating loss carry forwards in Canada of \$16,885. The carry forwards subject to expiration are as follows:

	Federal Investment Tax Credits	Ontario Investment Tax Credits	Operating Loss Carry Forward
2018	1,476	--	--
2019	2,179	--	--
2020	2,168	--	--
2021	1,409	--	--
2022	1,468	--	--
2023	1,165	--	--
2024	936	--	--
2025	2,829	--	--
2026	3,804	--	15
2027	4,038	--	--
2028	4,702	--	--
2029	6,758	1,626	2,969
2030	7,006	1,587	5,775
2031	6,803	1,609	8,126
	<u>\$46,740</u>	<u>\$4,822</u>	<u>\$16,885</u>

In Canada, the Company has unclaimed scientific research and experimental development ("SRED") tax pools of \$44,891, for both federal and provincial purposes, which are available to offset future taxable income. These SRED amounts have an unlimited carry forward period. The Company's subsidiary in the United Kingdom has tax loss balances with unlimited carry forward periods of \$25,441 (£15,865). The Company's US subsidiaries have federal loss carry forwards of \$20,730 (\$20,799 USD) that expire between 2019 and 2028 and California state loss carry forwards of \$9,504 (\$9,535 USD) that expire between 2020 and 2029. In addition, the Company has capital loss carry forwards in the amount of \$5,111 which have an unlimited carry forward period and can be used to offset any future capital gains.

**5. Acquisition**

**a) Routes AstroEngineering Ltd.**

In 2010, the Company purchased substantially all of the assets of Routes AstroEngineering Ltd. for cash consideration. The bargain purchase transaction resulted in a gain due to liquidity concerns of the seller.

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The business combination has been accounted for using the purchase method and the Company has included the results of operations in its consolidated financial statements from the date of acquisition effective April 15, 2010.

The fair value of the assets acquired and the liabilities assumed, agreed upon by the parties, is summarized in the following table:

Total purchase price	<u>\$ 1,487</u>
Allocated to:	
Equipment	\$ 26
Land and building	1,200
Current assets	1,023
Current liabilities	(92)
Net assets acquired	<u>\$ 2,157</u>
Gain from bargain purchase	<u>670</u>

In 2010, the gain of \$670 resulting from the excess of fair value of net assets acquired over the purchase price was recognized in other expense, and direct costs of the acquisition of \$170 were included in other expense on the Consolidated Statements of Operations.

In 2011, SRED refundable tax credits were received and related liabilities paid relating to 2010 balances.

**b) Xian**

In 2010 the Company achieved 100% ownership of Xian by purchasing the non-controlling interest for cash consideration of \$640. In accordance with the adoption of CICA Handbook Section 1602, Non-controlling Interests, changes in a parent's ownership in a subsidiary that do not result in a loss of control are accounted for as equity transactions. In connection with the acquisition, \$175 was charged to contributed surplus in 2010 as follows:

Total purchase price	\$ 640
Less: non-controlling interest at date of purchase	<u>465</u>
Excess to contributed surplus	<u>\$ 175</u>

**6. Non-controlling Interest**

In September 2010, the Company added a strategic investor in its data services subsidiary, exactEarth Ltd., that the Company believes will play an important role in delivering and growing the Company's exactAIS™ service in the marketplace. HISDESAT Servicios Estratégicos S.A., a major Madrid-based satellite operator and service provider that sells data to more than 25 government customers around the world, has invested \$15,000 for a 27% equity interest in exactEarth with an initial cash investment of \$12,300 in 2010, and the remaining \$2,700 paid on March 30, 2011. In the year ended October 31, 2011, issue costs of \$88 (\$348 in 2010), relating to the investment have been included in contributed surplus. The cash investment will support exactEarth's on-going business operations and the deployment of space and ground infrastructure.

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At October 31, 2011, non-controlling interest is comprised of the following:

<u>Non-controlling interest</u>	<u>2011</u>	<u>2010</u>
Balance as of October 31,	\$ 8,328	\$ -
Issuance of 2,460,000 shares to HISDESAT representing 27% ownership	2,700	12,300
Allocation of investment to contributed surplus	-	(3,725)
Net loss attributable to non-controlling interest – post investment	(2,051)	(247)
Balance as of October 31,	<u>\$ 8,977</u>	<u>\$ 8,328</u>
 <u>Allocation to contributed surplus</u>		
Allocation of investment to contributed surplus	\$ -	\$ 3,725
Issue costs	(88)	(348)
Total Allocation to contributed surplus	<u>(\$ 88)</u>	<u>\$ 3,377</u>

**7. Government Assistance**

In 2010, the Company entered into an agreement to receive a conditional grant from The Ministry of Economic Development and Trade under the Next Generation of Jobs Fund up to a maximum of \$12,228 for eligible project costs during the period from May 2009 to May 2014. The grant is conditional upon maintaining a minimum number of employees and project investment. There are repayment provisions if these conditions are not met. During the year ended October 31, 2011, as a result of increased uncertainty of government funding for Space programs in Canada, the Company ceased accruing amounts receivable under this agreement. At that time a total of \$1,486 (\$1,377 in 2010), had been accrued, of which \$1,103 was credited against property, plant, and equipment, and \$383 was applied against project costs included in the cost of revenue. In addition, management did not have sufficient confidence in future Space program funding levels to support the conditions of the grant and, therefore, voluntarily withdrew from the program. Accordingly, at October 31, 2011, all amounts pertaining to this agreement were reversed.

**8. Property, Plant and Equipment**

Property, plant and equipment are comprised as follows:

	<u>2011</u>			<u>2010</u>		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Land	\$ 7,784	\$ --	\$ 7,784	\$8,320	\$ --	\$ 8,320
Buildings	41,495	16,198	25,297	42,132	14,477	27,655
Machinery	19,168	10,823	8,345	19,286	8,838	10,448
Electrical equipment	93,475	62,131	31,344	85,861	59,885	25,976
Computer hardware	20,488	18,499	1,989	19,987	18,081	1,906

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Furniture and fixtures	7,570	6,128	1,442	7,312	5,847	1,465
	<u>\$189,980</u>	<u>\$113,779</u>	<u>\$76,201</u>	<u>\$182,898</u>	<u>\$107,128</u>	<u>\$75,770</u>

In 2011, included in property, plant and equipment is \$15,370 of machinery and equipment that has not yet commenced being amortized as the assets are capital in progress and not yet ready for use. In 2010, included in property, plant and equipment was \$13,966 of machinery and equipment, \$17 of buildings and furniture and fixtures, and \$1,654 of computer hardware that had not yet commenced being amortized as the assets were capital in progress and not yet ready for use. There were no capital leases entered into during fiscal 2011 and 2010.

Amortization of property, plant and equipment for the year was \$7,206 (\$7,303 for 2010).

**9. Intangible Assets**

Intangible assets are comprised as follows:

	2011			2010		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Patents	\$9,051	\$4,406	\$4,645	\$8,919	\$3,687	\$5,232
Customer relationships	5,495	3,064	2,431	5,573	2,402	3,171
Non-compete agreement	1,655	1,383	272	1,684	1,064	620
Acquired processes	464	325	139	475	237	238
Computer software	19,224	12,204	7,020	17,637	10,536	7,101
Internally developed technology	16,156	1,485	14,671	12,121	621	11,500
	<u>\$52,045</u>	<u>\$22,867</u>	<u>\$29,178</u>	<u>\$46,409</u>	<u>\$18,547</u>	<u>\$27,862</u>

Included in intangible assets is computer software of \$3,379 (\$3,411 in 2010), a non-compete agreement of nil (\$408 in 2010), and internally developed technology of \$13,062 (\$10,851 in 2010) that have not yet commenced being amortized as they are still in progress and not yet ready for use.

Amortization of intangible assets for the year was \$4,464 (\$3,958 for 2010).

**10. Bank Indebtedness, Loans Payable, and Other Financial Instruments**

**a) Bank Indebtedness**

The Company's bank has made available working capital facilities to the Company. This agreement provides for an operating facility of up to \$32,000 (\$32,000 in 2010). The only outstanding drawings against this operating facility at year-end are \$3,156 in the form of guarantee letters issued to customers and government agencies in the normal course of operations by the bank on behalf of the Company. The interest rate applicable to the operating credit facility available from the Company's bank is the chartered bank prime rate plus 0.75%. This facility is provided subject to certain covenants, including certain minimum financial ratios.

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The collateral for this arrangement includes a general security agreement on certain assets of the Company, security under Section 427 of the Bank Act (Canada), as well as assignment of insurance policies.

As at October 31, 2011, the Company was in compliance with its bank covenants.

Interest paid on bank indebtedness during the year was \$nil (\$nil in 2010).

**b) Loans Payable**

Loans payable are comprised as follows:

	<u>2011</u>	<u>2010</u>
GE Capital Solutions USD loans (i)	\$ 5,958	\$ 12,445
GE Capital Solutions CAD loan (i)	12,943	-
Government of Canada (ii)	139	201
Government loan – SODP (iii)	4,514	3,870
	<u>23,554</u>	<u>16,516</u>
Less: current portion of loans payable	<u>(8,867)</u>	<u>(6,401)</u>
Long term loans payable	<u>\$ 14,687</u>	<u>\$ 10,115</u>

Principal repayments are due as follows:

For the year ending	
2012	\$ 8,982
2013	6,111
2014	5,023
2015	3,107
2016	1,044
2017	435

- i) The interest rate applicable to the GE Capital Solutions USD loans is the LIBOR rate plus a rate that varies between 2.25% and 3.60%.

The collateral for these arrangements includes a general security agreement on the capital assets of the Company as well as assignment of insurance policies.

The GE Capital Solutions USD loans are being amortized over 5 years with quarterly payments of principal and interest totaling \$6,534 (\$6,579 USD) in 2011 (\$6,877 (\$6,579 USD) in 2010). Interest paid on the GE Capital Solutions USD loans in the year was \$316 (\$317 USD) and \$532 (\$509 USD) in 2010.

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During the year, GE Capital Solutions made available term loan facilities to the Company. This agreement provides for a term loan facility of up to \$15,000. The full \$15,000 was drawn upon in the year. This term loan matures on March 28, 2015. The interest rate applicable to the term loan is based on the banker's acceptance rate plus 4.90%. This facility is provided subject to certain covenants, including certain minimum financial ratios. The collateral for this arrangement includes a general security agreement on the property, plant, and equipment of the Company, subject to the prior charge of the bank. The security is subject to certain permitted liens, existing indebtedness, and existing security documents.

The GE Capital Solutions CAD loan is being amortized over 4 years with quarterly payments of principal and interest in 2011 totaling \$2,129 (nil in 2010). Interest paid on the GE Capital Solutions CAD loan in the year was \$443 (nil in 2010).

- ii) The Company has a product development agreement with Technology Partnerships Canada (TPC) that provides partial funding for certain research and development projects. Royalties of 4.9% are to be paid on annual gross product revenues resulting from the project to March 1, 2013. If total royalties paid by March 1, 2013 are equal to or exceed \$3,263, the payment obligation will be terminated. If total royalties paid at that date are less than \$3,263, the payment obligation shall continue until March 1, 2016 or until \$3,263 is paid, whichever comes first. A royalty payment of \$152 was made in 2011 (\$84 in 2010). It is not possible to determine the timing of the ultimate amount that will be repaid in connection with this arrangement and, accordingly, no amount is accrued.
- iii) The Government of Canada loan in conjunction with TPC is without interest or specific security with payments due annually until March 2013. The carrying value of the Government of Canada loan included in loans payable was arrived at using a discount rate of 6% on these minimum amounts only. During 2011 and 2010 installment payments totaling \$74 were made, reducing the carrying value, net of the effective interest, to \$139 as at October 31, 2011 (\$201 in 2010).

In 2010, the Company entered into a contribution agreement with The Federal Economic Agency for Southern Ontario, ("SODP"). The contribution agreement is in the form of a non-interest bearing loan. The repayable contributions are based on the Company's Microsatellite Infrastructure Satellite project costs incurred between November 2009 and June 2010 in amounts not exceeding the lesser of: a) 50% of eligible capital costs and 75% of eligible non-capital project costs and b) \$5,218. The repayment term for the loan is a five year amortization period with 60 monthly payments of \$87 for a total of \$5,218 beginning April 2012. In the year ended October 31, 2011, the Company received the remaining contribution of \$522 (\$4,696 in 2010).

The SODP loan has no specific security with payments starting in April 2012 and continuing monthly until March 2017. The Company has recorded the SODP loan at fair value which is less than the cash received as there is no stated interest rate.

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**c) Financial Instruments – Risk Management Objectives and Policies**

**Fair Values**

For the Company's cash and cash equivalents, accounts receivables and accounts payable and accrued liabilities, the fair values approximate their respective carrying amounts due to their short maturities. The fair values of foreign currency call and put option contracts have been estimated using market quoted rates of foreign currencies. These option contracts have been classified as Level 2 within the 3-level, fair value hierarchy. The Government of Canada loan, included in loans payable, has a fair value at October 31, 2011 of \$138 (\$202 in 2010) that approximates the carrying value of \$139. The SODP loan, included in loans payable, has a carrying value at October 31, 2011 of \$4,514 (\$3,870 in 2010) which approximates the fair value as the loan was recorded at fair value when the cash was received and the prime rate has not changed in the past year. The fair value of both the Government of Canada loan and SODP loan are calculated using discounted cash flows with a discount rate comprised of the Bank of Canada prime rate plus 2% which is indicative of the Company's borrowing rate. Recording the SODP loan carrying value to the fair market value when cash was received resulted in a gain, reducing "Other expense" by \$78 (\$855 in 2010), on the Consolidated Statements of Operations. The fair value of the GE Capital loans, included in loans payable, approximates the carrying value due to their variable interest rate terms policy.

**Foreign Currency Risk**

**Transaction Exposure**

The Company is exposed to foreign exchange risk as a result of transactions in currencies other than its functional currency, the Canadian dollar. The majority of the Company's revenues are transacted in U.S. dollars. Portions of the revenues are denominated in Canadian dollars, British Pounds, and Euros. Purchases of raw materials, and other expenses, consisting primarily of the majority of salaries, certain operating costs and manufacturing overhead, are incurred primarily in Canadian dollars. The Company utilizes foreign exchange put options and related call options contracts to hedge the net cash flow risk associated with forecasted transactions in foreign currencies but does not enter into derivatives for speculative purposes. The Company does not designate or measure the effectiveness of the derivative instruments as hedges or specific firm commitments or forecasted transactions and accordingly does not meet the requirements of CICA Handbook Section 3865 - Hedges. Management policy is to mitigate between 75% and 100% of the foreign exchange fluctuations on expected USD net cash flows.

**Translation Exposure**

The Company's foreign operations, CDE, COM DEV USA LLC, COM DEV US Property LLC, COM DEV Consulting Ltd., and Xian, are considered self-sustaining. Accordingly, assets and liabilities are translated into Canadian dollars using the exchange rates in effect at the balance sheet dates. Unrealized translation gains and losses are deferred in AOCL. The accumulated currency translation adjustments are recognized in income when there is a reduction in the net investment in the foreign operations.

Foreign currency risks arising from translation of assets and liabilities of foreign operations into the Company's functional currency are generally not hedged, however, the Company does hedge this risk with respect to the U.S. operations. Effective September 1, 2008, the

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Company began to hedge the translation risk by designating the U.S. dollar denominated loans used in the acquisition of the U.S. Operations as a hedge of the net investment. The foreign exchange on the translation of the US dollar denominated loans is also recorded in AOCL, as the hedge is considered effective.

The Company's derivatives, which are not designated in hedging relationships, are classified as held-for-trading and the changes in fair value are recognized on the Consolidated Statements of Operations. During the year ended October 31, 2011, the fair value of derivatives classified as held-for-trading decreased by \$2,920 (increased by \$1,144 in 2010).

At October 31, 2011 approximately 32% of cash and cash equivalents, 41% of accounts receivables, and 29% of accounts payable and accrued liabilities are denominated in foreign currencies (October 31, 2010 – 30%, 52%, and 35%, respectively). These foreign currencies include the U.S. dollar, British Pound, and Euro.

The Company is exposed to foreign exchange risk on the following cash, accounts receivable, and accounts payable, denominated in foreign currencies:

Currency	Cash	Accounts Receivable	Accounts Payable
USD	\$ 8,653	\$ 15,360	\$ 5,504
GBP	£ 173	£ 164	£ 493
EUR	€ -	€ 2,927	€ 692

As at October 31, 2011, the Canadian dollar amount that could be received under Canadian / U.S. foreign currency call options was \$65,117 (\$42,929 in 2010) and the amount that could be paid under foreign currency put options was \$170,795 (\$58,583 in 2010). The average contractual exchange rate on the call options was 1.0635 and on the put options was 1.0406. The settlement dates of all the outstanding contracts are distributed over the next two years. The exchange rate at October 31 was 0.9967 (1.0202 in 2010).

During 2011 the Company recorded a net realized gain of \$3,313 (\$3,466 in 2010) and net unrealized loss of \$2,920 (gain of \$1,144 in 2010) on foreign currency options that have been included in "foreign exchange loss (gain)" on the Consolidated Statements of Operations. At October 31, 2011 the fair value of option contracts of \$1,152 (\$1,768 in 2010) is included in "Accounts payable and accrued liabilities" with \$638 included in "Current" and \$514 included in "Long term" on the Consolidated Balance Sheets. At October 31, 2010 the fair value of option contracts of \$1,768 was included in "Prepays and other" on the Consolidated Balance Sheets.

The majority of the Company's foreign exchange risk resides with U.S dollar and Euro transactions, with minimal impact on transactions in British Pounds. To evaluate the sensitivity of net income to a reasonably possible change in the US dollar and Euro exchange rates, various exchange rates were entered into models which considered the valuation impact to customer contracts, hedging contracts, US dollar cash balances and US and Euro denominated monetary balance sheet items. During 2011, the impact if the US dollar had appreciated in value by 5% used as an indicative range in a volatile currency environment, would have been an increase in net income of \$5,790 (\$5,309 in 2010). Had the US dollar depreciated by 5%, the impact would have been a decrease in net income of \$5,833 (\$5,517 in 2010). During 2011, the impact had the Euro appreciated in value by 5% would have resulted in an increase in net income of \$1,052 (\$707 in 2010). Had the Euro depreciated by 5%, the impact would have been a decrease in net income of \$1,052 (\$707 in 2010).

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**Interest Rate Risk**

The Company's risk exposure to market interest rates, in the form of cash flow interest rate risk, relates primarily to the Company's long-term debt obligation with GE Capital Solutions with floating interest rates.

The Company's policy is to review its borrowing requirements on a continual basis and to enter into fixed or variable interest rate borrowing arrangements as required.

To evaluate the sensitivity on net income from possible changes in interest rates, the impact of an interest rate change was modeled on the floating rate borrowings while all other variables were held constant. Based on these assumptions, the impact for the year ended October 31 from a 100 basis point increase in interest rates, as indicative of the change in prime lending rates over the past year, would have been a decrease in net income of \$173 (\$158 in 2010) and an increase in net income of \$173 (\$158 in 2010) if there had been a 100 basis point decrease.

**Credit Risk**

The maximum exposure to credit risk at the balance sheet date is best represented by the carrying amount of the Company's accounts receivable, unbilled contracts in progress, and derivative financial instruments. The Company is exposed to credit risk from the potential default by counterparties that carry the Company's cash, cash equivalents, and derivative financial instruments, and attempts to mitigate this risk by dealing only with large financial institutions with good credit ratings. All of the financial institutions within the bank syndicate providing the Company's credit facility meet these qualifications.

Credit risk also arises from the inability of customers to discharge their obligation to the Company. The satellite industry is characterized by a small number of prime contractors, which represents most of the Company's customer base. The relatively small number of customers leads to a concentration of the Company's revenues and accounts receivable. COM DEV is increasing its penetration with a number of smaller satellite manufacturers, as well as in satellite market segments outside the traditional commercial communications sector, which helps mitigate the risk associated with having a small number of customers. If one or more customers were to delay, reduce or cancel orders, the overall orders of the Company may fluctuate and could adversely affect the Company's operations and financial condition. The Company, in the normal course of business, monitors the financial condition of its customers and reviews the credit history of each new customer. The Company manages the collection risk on foreign receivables by carrying credit insurance through Export Development Canada that insures 90% of receivables, primarily those from foreign customers, to protect against commercial and political risk. Trade receivables are non-interest bearing and are generally on 30-60 day terms. There are balances past due and the Company has recorded an impairment allowance of \$20 included in "Account receivable" on the Consolidated Balance Sheets (nil in 2010). Four customers comprise 59% of accounts receivable as at October 31, 2011 (five comprised 75% in 2010).

The Company has reviewed its outstanding trade receivables and unbilled contracts in progress in detail and has determined that the aging profiles are within historical expectations. The Company has historically had no impairment of its trade receivables and unbilled contracts in progress.

**Liquidity Risk**

Liquidity risk is the Company's ability to meet its financial obligations when they come due. The Company monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of its financial assets (eg. accounts receivables, other

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financial assets), liabilities (eg. payables, loans), and projected cash flows from operations. The Company's objective is to maintain a balance between continuity of funding and flexibility through borrowing facilities available through the Company's bank and GE Capital Solutions, finance leases and purchase contracts. The Company's bank facility includes a treasury risk management facility to facilitate hedging of currency related risks arising in the normal course of operations. The Company's policy is to ensure adequate funding is available from operations, established lending facilities and other sources as required. As at October 31, 2011, the Company has operating credit facilities of \$32,000 that have been approved but not drawn upon except for the guarantee letters described in note 10(a).

The table below summarizes the maturity profile of the Company's financial liabilities based on contractual undiscounted payments.

	On Demand	< 3 Months	3 to 12 Months	1 to 5 Years	Total
October 31, 2011					
Loans and interest payable	\$ -	\$ 2,714	\$ 7,153	\$ 16,404	\$ 26,271
Income taxes payable	-	162	140	-	302
Accounts payable and accrued liabilities	3,549	16,802	6,022	930	27,303
Total	<u>\$ 3,549</u>	<u>\$ 19,678</u>	<u>\$ 13,315</u>	<u>\$ 17,334</u>	<u>\$ 53,876</u>
October 31, 2010					
Loans and interest payable	\$ -	\$ 1,667	\$ 5,076	\$ 11,600	\$ 18,343
Accounts payable and accrued liabilities	3,535	18,434	5,959	968	28,896
Total	<u>\$ 3,535</u>	<u>\$ 20,101</u>	<u>\$ 11,035</u>	<u>\$ 12,568</u>	<u>\$ 47,239</u>

## 11. Capital Management

The primary objectives of the Company's capital management are:

- to ensure that it maintains strong credit ratings and exceeds its borrowing covenants in order to support its business and maximize shareholder value, and
- to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk undertaken.

The Company monitors capital on a basis consistent with others in the industry based on total debt to shareholders' equity. Capital is defined as shareholders' equity as presented on the balance sheet excluding AOCL and total debt is defined as the sum of short-term and long-term interest-bearing debt. The Company uses the percentage of total debt to total capital to monitor the capitalization of the Company. The Company is not subject to any capital requirements imposed by a regulator.

## 12. Share Capital and Earnings Per Share

### a) Issued Capital

The Company has authorized an unlimited number of preferred shares of which there are none outstanding. The Company has authorized an unlimited number of common shares

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with no par value. The following details the changes in issued and outstanding common shares for the two years ended October 31, 2011:

	Common Shares	
	Number	Dollar Value
Balance, October 31, 2009	76,100,289	\$345,885
Shares issued through employee plan (ii)	55,838	183
Balance, October 31, 2010	76,156,127	\$346,068
Issuance of common shares (i)	252,500	741
Shares issued through employee plan (ii)	58,908	130
Repurchased and cancelled common shares (iii)	(280,500)	(1,273)
Balance, October 31, 2011	76,187,035	\$345,666

- i. During the year ended October 31, 2011, the Company issued 252,500 common shares to satisfy the equivalent number of stock options exercised of which all of the options represent options issued after November 1, 2003 (nil in 2010). The value of the stock options exercised transferred from contributed surplus was \$227 (nil in 2010).
- ii. On February 28, 2011 the Company issued 58,908 (55,838 in 2010) common shares under the ESOP. The value of the shares issued through the employee plan transferred from contributed surplus was \$130 (\$183 in 2010).
- iii. On March 18, 2011, the Company announced acceptance by the Toronto Stock Exchange ("TSX") of the Company's Notice of Intention to make a Normal Course Issuer Bid (the "Notice") through the facilities of the TSX. Pursuant to the Notice, the Company proposed to repurchase up to an aggregate of 6,631,947 common shares during the 12 month period commencing March 21, 2011 and ending March 20, 2012. The Company shall make available a maximum of \$10,000 to fund the repurchase of common shares during this period. The Company will determine the number of common shares to be repurchased and the timing of such purchases subject to the normal course issuer bid policy of the TSX. All common shares repurchased by the Company during this period will be cancelled.

During the year ended October 31, 2011, the Company repurchased and cancelled 280,500 common shares with an average book value of \$1,273. The difference between the cost of the shares repurchased and the average book value is \$759. This amount is included in contributed surplus.

The maximum number of shares outstanding if all options were exercised and ESOP shares were issued is 77,239,135.

**b) Stock Based Compensation**

The Company employs a fair value based method of accounting for all options issued to employees or directors. The Company recognizes compensation cost for all stock options granted to employees and directors under its stock option plan. The option exercise price is the market value of the Company's common shares at the date of the grant. During 2011 the Company granted 366,614 options (434,644 in 2010).

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Options granted vest over three years, and vested options can be exercised over a five-year period from the date of issue. The maximum number of shares authorized for grant under the option plan is 9.4% of the outstanding shares issued or 7,161,581.

The fair value of options issued was estimated at the date of grant, using the Black-Scholes Option Model with the following weighted average assumptions:

	For the year ended October 31, 2011	For the year ended October 31, 2010
Risk-free interest rate	2.23%	2.23%
Dividend yield	0.00%	0.00%
Volatility	44.6%	48.0%
Expected life of options	5 years	5 years
Weighted average fair value of options granted	\$0.98	\$0.86
Weighted average exercise price of options granted	\$2.36	\$1.95

The estimated fair value of the options is amortized to expense over the vesting period of the options. In the year, compensation expense of \$234 (\$207 in 2010) was recognized. This amount was added to contributed surplus.

A summary of option activity for the years ended October 31 is as follows:

	Number	2011 Weighted Average Exercise Price	Number	2010 Weighted Average Exercise Price
Balance as at October 31,	1,782,810	\$3.29	1,664,339	\$3.56
Granted	366,614	\$2.36	434,644	\$1.95
Exercised	(252,500)	\$2.03	-	-
Expired	(1,022,120)	\$3.99	(88,030)	\$3.77
Forfeited	-	-	(228,143)	\$2.54
Balance as at October 31,	874,804	\$2.43	1,782,810	\$3.29

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The outstanding options are summarized as follows:

	Options Outstanding			Options Vested	
	Number Outstanding at October 31, 2011	Weighted Average Remaining Life in Years	Weighted Average Exercise Price	Number Outstanding at October 31, 2011	Weighted Average Exercise Price
Range of Exercise Prices					
\$1.89 – 2.84	673,939	4.15	\$ 2.16	126,349	\$ 1.93
\$2.85 – 3.78	200,865	2.67	3.35	136,541	3.34
\$1.89 – 3.78	<u>874,804</u>			<u>262,890</u>	

**c) Employee Share Ownership Plan**

The value of Employee Stock Ownership Plan shares amortized to compensation expense but not yet issued at year-end was \$222 (\$198 in 2010). This amount is included in contributed surplus. The estimated number of shares, if all outstanding ESOP shares were issued, is 177,296.

**d) Long Term Incentive Plan**

The following details the RSUs and PSUs for the year ended October 31:

	2011		2010	
	RSUs	PSUs	RSUs	PSUs
Balance as at October 31,	1,002,191	554,238	635,103	151,589
Granted	288,155	232,668	370,156	416,187
Forfeited	-	(37,420)	(3,068)	(13,538)
Balance as at October 31,	<u>1,290,346</u>	<u>749,486</u>	<u>1,002,191</u>	<u>554,238</u>
Aggregate fair value of units granted as at October 31,	<u>\$3,244</u>	<u>\$1,889</u>	<u>\$2,566</u>	<u>\$1,345</u>
Weighted average fair value of units granted in the year	<u>\$2.35</u>	<u>\$2.34</u>	<u>\$1.91</u>	<u>\$2.03</u>

In the year ended October 31, 2011, compensation expense of \$1,323 (\$1,086 in 2010) was recognized. These amounts were added to contributed surplus.

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**e) Earnings Per Share**

The following table sets forth the computation of basic and diluted earnings per share for the comparable reporting periods:

	<b>2011</b>	<b>2010</b>
Numerator for basic and diluted earnings per share available to common shareholders		
Net income attributable to common stockholders	\$13,606	\$2,694
Denominator for basic earnings per share- weighted average number of shares outstanding	76,394,409	76,137,922
Effect of dilutive securities		
Employee stock options	-	97,221
ESOP	66,426	47,666
Potential dilutive common shares	66,426	144,887
Denominator for diluted earnings per share – adjusted weighted average shares and assumed conversions	76,460,835	76,282,809
Basic and diluted earnings per share	\$0.18	\$0.04

**13. Commitments and Contingencies**

**a) General**

The preparation of these consolidated financial statements requires management's best estimate related to events whose outcome will not be fully resolved until future periods. The Company's revenue is derived primarily from long term fixed price contracts, some of which are subject to significant technology risk. The preparation of these consolidated financial statements is based on management estimates of revenue and the required costs to complete the projects. Revisions to the estimates used in preparation of the consolidated financial statements could have a material impact on financial results of future periods. Revenue under such contracts may include incentive payments for specified performance and costs may include performance related penalties.

**b) Lease Commitments**

The Company is committed to various operating leases, primarily related to buildings and computers. Future minimum lease payments under the operating leases for the following fiscal years are approximately as follows:

Year ending October 31,	
2012	\$2,238
2013	906
2014	304
2015	69
2016	50

**c) Claims or Legal Actions**

In the normal course of business, the Company is involved on an ongoing basis in various legal actions, the outcome of which is indeterminable. In management's opinion, the

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resolution of such actions will not have a material adverse effect on the financial condition of the Company.

**d) Tax Audits**

In a recent audit by the Canada Revenue Agency (“CRA”), an assessment was received in the second quarter of 2011 indicating the Company failed to make required withholdings on payments made to certain vendors from 2006 to 2010. Management does not agree with several of the findings and has accordingly filed a Notice of Objection for items that total approximately \$2,600. The Company is currently unable to determine the likelihood of success of its objection to the proposed assessments. Any amount of tax liability arising from these assessments will be recorded when the probable amounts can be determined. The Company provided the CRA a letter of credit as security for any tax liability arising from these assessments.

In a prior year, the Canada Revenue Agency and the Ontario Ministry of Finance completed tax audits. As a result of the audits, prior year tax returns have been reassessed for capital taxes and corporate minimum taxes. The Company opposes several matters on the basis of interpretation of the tax rules and has appealed to the tax authorities on this basis. The Company is currently unable to determine the likelihood of success of its Appeal to the reassessments. The disputed tax and accumulated interest amounts, including estimates for un-assessed years subsequent to the audit period, total \$3,296 which is included in income taxes recoverable. The Company will continue to provide information to the tax authorities and attempt to resolve these issues favourably. Any amount of tax liability arising from these matters will be recorded when the probable amounts can be determined. As part of the objection process, the Company, as required, paid the full amount of the taxes in dispute.

**14. Other Expense (Income)**

	<u>2011</u>	<u>2010</u>
Restructuring	\$ 2,194	\$ 3,307
Routes – acquisition costs (note 6(a))	-	170
Routes – gain on purchase (note 6(a))	-	(670)
Other expense	815	625
Total other expense	<u>\$ 3,009</u>	<u>\$ 3,432</u>

Included in 2011 is a charge of \$2,194 (\$3,307 in 2010) related to a reduction in work force as part of the Company’s internal restructuring.

**15. Segment and Geographic Information**

The Company has two reportable business segments, the Space Segment and the Data Services Segment. Each reportable segment offers different products and services and requires different technology and marketing.

The Space Segment is a leading global designer and manufacturer of space hardware subsystems. With facilities in Canada, the United Kingdom, and the United States, the Space

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Segment designs and manufactures advanced products and subsystems that are sold to the major satellite prime contractors for use in communications, space science, remote sensing and military markets.

The Data Services Segment is actively commercializing a new maritime tracking service know as Satellite Automatic Identification System, or S-AIS. The Data Services Segment offers data services to customers worldwide.

Management assesses segment performance based on income before financing expense and income taxes.

Segment reporting is based on the two business segments, the Space Segment and the Data Services Segment with intra-segment transactions and balances eliminated. The Company accounts for intra-segment transactions at current market rates, negotiated between segments.

**Geographic Information**

Revenue by customer is based on where the customer is located.

	2011	2010
Revenue from external customers		
Canada	\$42,209	\$45,153
USA	116,915	120,089
Europe	32,206	40,074
Other	11,865	15,605
	<u>\$203,195</u>	<u>\$220,921</u>

Capital assets are attributed to the country in which they are located and patents and acquired contracts in the country they relate to.

**Capital assets**

Canada	\$56,768	\$53,675
USA	16,815	19,297
United Kingdom	2,618	2,798
	<u>\$76,201</u>	<u>\$75,770</u>

**Intangible assets**

Canada	\$23,889	\$18,729
USA	5,242	9,079
United Kingdom	47	54
	<u>\$29,178</u>	<u>\$27,862</u>

Goodwill of \$2,200 (\$2,252 in 2010) all relates to USA.

Four Space Segment customers comprise 69% of revenue for the year ended October 31, 2011 (five Space Segment customers comprised 75% in 2010).

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Segment Information for the year ended October 31, 2011:

	Space Segment	Data Services Segment	Intra- Segment Eliminations	Total
External revenue	198,435	4,760	-	203,195
Intra-segment revenue	9,059	210	(9,269)	-
Gross margin	50,267	(2,274)	(1,412)	46,581
Gross margin %	24%			23%
Selling expenses	9,213	2,154	-	11,367
General expenses	15,413	2,225	-	17,638
Amortization	10,818	852	-	11,670
Income before financing expense and income taxes	33,638	(7,690)	(1,412)	24,536
Income tax expense	8,170	-	-	8,170
Net income (loss)				
Attributable to non- controlling interest	-	(2,051)	-	(2,051)
Attributable to shareholders	20,558	(5,540)	(1,412)	13,606
Property, plant and equipment additions	2,608	8,200	(1,342)	9,466
Intangible asset additions	5,400	626	(70)	5,956
Segment Assets	210,106	41,248	(1,412)	249,942

Segment Information for the year ended October 31, 2010:

	Space Segment	Data Services Segment	Intra- Segment Eliminations	Total
External revenue	219,036	1,885	-	220,921
Intra-segment revenue	12,952	-	(12,952)	-
Gross margin	49,891	(1,497)	(3,275)	45,119
Gross margin %	22%			20%
Selling expenses	10,533	1,312	-	11,845
General expenses	17,226	3,463	-	20,689
Amortization	11,243	18	-	11,261
Income before financing expense and income taxes	15,316	(6,093)	(3,275)	5,948
Income tax expense	2,115	-	-	2,115
Net income (loss)				
Attributable to non- controlling interest	(21)	(247)	-	(268)
Attributable to shareholders	11,794	(5,825)	(3,275)	2,694
Property, plant and equipment additions	4,449	12,081	(2,681)	13,849

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Intangible asset additions	7,945	3,575	(594)	10,926
Segment Assets	207,634	38,107	(3,275)	242,466

**16. Employee Future Benefit Plans**

The Company provides certain pension and other future employee benefits to eligible participants upon retirement. The Company has obtained full actuarial values for both the pension and other future benefits as of October 31, 2011.

**CDE Pension Benefits**

The Company's UK subsidiary has a defined contribution pension plan for its employees. The Company's contributions, which are based on the contributions by employees, were \$532 (\$442 for 2010) and have been included in General expenses on the Consolidated Statements of Operations.

**CDU Pension Benefits**

The Company's US subsidiary has a defined benefit plan that covers former L-3 Electron Technologies Employees, only.

Management's assumptions used include:

	2011	2010
Accrued benefit obligation		
Discount rate	4.5%	5.3%
Rate of compensation increase	3.0%	3.5%
Net periodic benefit cost		
Discount rate	5.3%	5.5%
Rate of compensation increase	3.5%	3.5%
Expected return on plan assets	8.0%	8.0%
Average remaining service life of employees	7.0	7.7

The year-end balances were valued and measured as of October 31, 2011.

Information about the Company's defined benefit pension plans is as follows:

	2011	2010
Accrued benefit obligation		
Beginning of year	\$ 12,407	\$ 11,604
Current service	487	485
Interest costs	624	609
Actuarial losses	434	614
Benefits paid	(445)	(218)
Currency translation gains	(275)	(687)
End of year	\$ 13,232	\$ 12,407
Plan assets at fair value		
Beginning of year	\$ 8,652	\$ 7,730
Return on plan assets	(43)	826
Employer contributions	857	779
Benefits paid	(445)	(218)
Currency translation losses	(196)	(465)
End of year	\$ 8,825	\$ 8,652

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Plan deficit	\$ 4,407	\$ 3,755
Unamortized actuarial losses	(4,261)	(3,489)
Accrued benefit liability	<u>\$ 146</u>	<u>\$ 266</u>
Net periodic benefit cost		
Current service	\$ 487	\$ 485
Interest costs	624	609
Amortization of actuarial (gain) loss	(423)	523
	<u>\$ 688</u>	<u>\$ 1,617</u>
Less: return on plan assets	(43)	826
Net periodic benefit cost	<u><u>\$ 731</u></u>	<u><u>\$ 791</u></u>

**CDU Non-Pension Benefits**

The Company provides non-pension retirement benefits including medical and vision benefits for eligible retirees, their spouses and qualified dependents for its US subsidiary on an accrual basis.

In 2011, the Company recorded a curtailment gain of \$307 against non-pension benefits due to the decrease in a significant number of active employees that were part of this plan.

	<u>2011</u>	<u>2010</u>
Management's assumptions used include:		
Discount rate – accrued benefit obligations	4.5%	5.3%
Discount rate – net periodic benefit cost	5.3%	5.3%
Health care cost increase	6.5%	7.0%

Information about the Company's retirement medical benefits plan is as follows:

Accrued benefit obligation		
Beginning of year	\$ 1,634	\$ 1,573
Current service cost	67	80
Interest costs	76	75
Amortization of gain	(4)	(1)
Effect of curtailment	(307)	-
Currency translation	(39)	(93)
End of year	<u>\$ 1,427</u>	<u>\$ 1,634</u>
Plan deficit	\$ 1,427	\$ 1,634
Unamortized actuarial gains	9	10
Accrued benefit liability	<u>\$ 1,436</u>	<u>\$ 1,644</u>
Net periodic benefit cost		
Current service costs	\$ 67	80
Interest costs	76	75
Amortization of gain	(4)	(1)
Effect of curtailment	(307)	-
Net periodic benefit cost	<u><u>\$ (168)</u></u>	<u><u>\$ 153</u></u>

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**Sensitivity to Change In Health Care Trend Rates**

	Trend Minus 1% in every year	Current Trend	Trend Plus 1% in every year
Retirement medical benefit obligation	1,449	1,573	1,710
Difference due to trend change	(125)		136
Percentage difference	(7.9%)		8.7%
Service cost plus interest cost	147	160	174
Difference due to trend change	(13)		14
Percentage difference	(8.1)%		8.9%

**CDU Future Benefit Payments**

	Defined Benefit Pension Plan	Retirement Medical	Total
Expected employer contribution for fiscal year ending October 31, 2012	\$ 997	\$ 24	\$ 1,021
Expected benefit payments			
2012	\$ 347	\$ 24	\$ 371
2013	398	34	432
2014	458	44	502
2015	442	60	502
2016	403	76	479
Thereafter	2,603	457	3,060
	<u>\$ 4,651</u>	<u>\$ 695</u>	<u>\$ 5,346</u>

**CDU Plan Assets**

The weighted-average asset allocation of the Company's defined benefit pension plans at October 31, are as follows:

Asset Category	2011	2010
Equity securities	49.7%	38.8%
Fixed income securities	24.9%	39.6%
Cash and cash equivalents	16.3%	2.3%
Exchange traded index funds	9.1%	19.3%
Total	<u>100.0%</u>	<u>100.0%</u>

The expected rate of return on plan assets was determined by considering the Company's current investment mix, the historic performance of these investment categories and expected future performance of these investment categories.

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**17. Comparative Consolidated Financial Statements**

The comparative consolidated financial statements have been reclassified from financial statements previously presented in order to conform to the presentation of the current year consolidated financial statements.