

Financial Statements of

**INTERNATIONAL WATER-GUARD
INDUSTRIES INC.**

Years ended September 30, 2009 and 2008



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AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the balance sheets of International Water-Guard Industries Inc. as at September 30, 2009 and 2008 and the statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP (signed)

Chartered Accountants

Vancouver, Canada
November 13, 2009

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Balance Sheets

September 30, 2009 and 2008

	2009	2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,362,363	\$ 940,302
Accounts receivable	672,010	710,770
Inventory (note 3)	577,993	496,335
Prepaid expenses	42,807	65,407
Future income tax asset (note 9)	86,000	-
	<u>2,741,173</u>	<u>2,212,814</u>
Furniture and equipment (note 4)	229,135	250,607
Future income tax assets (note 9)	279,000	478,000
	<u>\$ 3,249,308</u>	<u>\$ 2,941,421</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 449,413	\$ 449,247
Current portion of capital lease obligations and loan payable (note 6)	25,757	40,593
	<u>475,170</u>	<u>489,840</u>
Capital lease obligations and loan payable (note 6)	18,101	45,206
	<u>493,271</u>	<u>535,046</u>
Shareholders' equity:		
Share capital (note 7)	8,111,487	8,108,202
Contributed surplus (note 7(c))	200,164	165,803
Deficit	(5,555,614)	(5,867,630)
	<u>2,756,037</u>	<u>2,406,375</u>
Contingencies and commitments (note 8)		
	<u>\$ 3,249,308</u>	<u>\$ 2,941,421</u>

See accompanying notes to financial statements.

Approved on behalf of the Board:

"David C. Fox" Director

"Bruce W. Gowan" Director

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Statements of Operations and Deficit

Years ended September 30, 2009 and 2008

	2009	2008
Sales	\$ 4,898,157	\$ 4,156,469
Cost of goods sold	1,827,070	1,922,205
Gross profit	3,071,087	2,234,264
Expenses:		
Selling expenses	427,924	328,773
Engineering and product development	875,219	772,194
General, administrative and occupancy	1,266,085	1,204,850
Amortization	60,389	64,758
Interest	16,454	11,733
	2,646,071	2,382,308
Income (loss) before taxes	425,016	(148,044)
Future income tax recovery (expense) (note 9)	(113,000)	51,000
Net income (loss) and comprehensive income (loss)	312,016	(97,044)
Deficit, beginning of year	(5,867,630)	(5,770,586)
Deficit, end of year	\$ (5,555,614)	\$ (5,867,630)
Income (loss) per share amounts:		
Basic	\$ 0.007	\$ (0.003)
Diluted	0.007	(0.003)
Weighted average shares outstanding:		
Basic	39,340,283	34,647,428
Diluted	39,340,283	34,647,428

See accompanying notes to financial statements.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Statements of Cash Flows

Years ended September 30, 2009 and 2008

	2009	2008
Cash flows from (used by):		
Operations:		
Net income (loss)	\$ 312,016	\$ (97,044)
Items not involving cash:		
Future income tax expense (recovery)	113,000	(51,000)
Amortization	60,388	64,758
Change in value in forward contract	(47,688)	(6,500)
Stock based compensation	35,396	18,408
	473,112	(71,378)
Changes in non-cash operating working capital:		
Accounts receivable	86,448	17,008
Inventory	(81,658)	145,897
Prepaid expenses	22,600	(27,438)
Accounts payable and accrued liabilities	166	24,175
	500,668	88,264
Financing:		
Repayment of capital lease obligations	(37,795)	(29,654)
Repayment of loan payable	(4,146)	(4,147)
Issuance of capital stock	2,250	494,080
	(39,691)	460,279
Investments:		
Purchase of furniture and equipment	(38,916)	(47,173)
Increase in cash and cash equivalents	422,061	501,370
Cash and cash equivalents, beginning of year	940,302	438,932
Cash and cash equivalents, end of year	\$ 1,362,363	\$ 940,302
Supplementary information:		
Interest paid	\$ 16,454	\$ 11,733
Non-cash transactions:		
Furniture and equipment purchased using capital lease obligations	-	48,902

See accompanying notes to financial statements.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

1. Operations:

The Company is incorporated under the Business Corporations Act (British Columbia). The Company's principal business operations relate to the development, manufacture and sale of aircraft water treatment equipment and water systems.

2. Significant accounting policies:

(a) Basis of presentation and operations:

The Company's financial statements are prepared in accordance with Canadian generally accepted accounting principles and, except where otherwise indicated, are expressed in Canadian dollars. These principles require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenue and expenses during the reporting period. Significant estimates used in the preparation of these financial statements primarily relate to the assessment of the valuation of accounts receivable, the net realizable value of inventory, and the realizability of future income tax assets. Actual results could differ from these estimates.

(b) Cash and cash equivalents:

Cash equivalents are highly liquid investments, such as term deposits with major financial institutions, having a term to maturity of three months or less at acquisition that are readily convertible to specified amounts of cash.

(c) Inventory:

Inventory is valued at the lower of cost (determined on a first-in, first-out basis) and net realizable value. Raw materials inventory includes parts to be used in the manufacturing process. Work-in-process and finished goods inventory includes the cost of raw materials, direct labour, freight and other direct manufacturing costs as well as an allocation of indirect overhead costs and depreciation. A provision is recognized to the extent that cost of inventory exceeds its net realizable value. Such provisions are reversed in subsequent periods if the net realizable value increases.

(d) Furniture and equipment:

Furniture and equipment is stated at cost. Amortization using the declining-balance method on tooling and equipment is provided at a rate of 20% per annum and on computer equipment at 25% per annum. Leasehold improvements are amortized over the term of the lease on a straight-line basis.

(e) Impairment of long-lived assets:

The Company tests long-lived assets, such as furniture and equipment, for impairment when events or circumstances indicate that impairment may exist. Long-lived assets are impaired if the undiscounted cash flows expected to be earned from their use is less than their carrying amount, at which time, long-lived assets are written down to their fair value.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

2. Significant accounting policies (continued):

(f) Revenue recognition:

Revenue is recognized when persuasive evidence of a contractual arrangement exists, the products and services have been delivered to the customer and there are no significant vendor obligations remaining, the price is fixed or determinable, and collectibility is reasonably assured. Amounts received from customers in advance of satisfying all revenue recognition criteria are deferred.

(g) Government assistance:

The Company receives payments from time to time under various government assistance programs. These payments are recorded in the period during which the amounts are received or receivable. Payments received in respect of operating expenditures are deducted from expenses and in respect of capital expenditures are applied to reduce the cost of such additions. Under certain government assistance programs, the Company is required to pay future royalties to the government as a condition of receiving the grant (note 8(a)). Royalty payments are recognized and expensed when incurred.

(h) Engineering and product development:

Engineering costs are expensed as incurred. Product development costs are expensed as incurred unless certain specified criteria for deferral have been met. The Company applies a stringent interpretation of these criteria, with the result that only costs associated with completing specific technologically feasible product applications having a continuing identifiable market with best estimates of net cash flows in excess of the carrying value of the costs incurred are deferred. Routine alterations to existing products are expensed as incurred.

(i) Income taxes:

Income taxes are accounted for using the liability method. Future income tax assets and liabilities are determined based on temporary differences between the accounting and tax bases of existing assets and liabilities, and are measured using the tax rates expected to apply when these differences reverse. A valuation allowance is recorded against any future tax asset when such benefits are not expected to be realized.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

2. Significant accounting policies (continued):

(j) Stock-based compensation:

The Company has a stock-based compensation plan, which is described in note 7(c).

The Company recognizes stock-based compensation related to stock options granted to employees and directors based on the fair value of the options on the grant date and recognizes such stock-based compensation in results from operations over the vesting period. Options granted to consultants are measured at fair value and the related compensation is recognized over the period that the services are delivered. The measurement date for options granted to consultants is the date on which the services are substantially completed and changes in fair value between the grant date and measurement date are recognized in stock-based compensation during the period.

(k) Income (loss) per share:

Income (loss) per share amounts have been calculated based on the weighted average number of shares outstanding. Fully diluted per share amounts have been calculated using the treasury stock method, which takes into account the dilutive effect of outstanding warrants and options. Securities such as stock options and warrants are included in the calculation of diluted per share amounts only if the market price of the underlying common shares exceeds the exercise price. All of the Company's outstanding options were excluded from the calculation of diluted earnings per share for the years ended September 30, 2009 and 2008 as they were anti-dilutive.

(l) Foreign exchange translation:

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rates of exchange in effect at the balance sheet date. Revenue and expenses are translated into Canadian dollars at the rates of exchange in effect at the dates of the transactions. Gains or losses arising from foreign exchange translation are included in the results of operations. For the year ended September 30, 2009, foreign exchange loss included in net earnings totaled \$54,755 (2008 - \$88,837 gain) which are included in sales in the statement of operations.

(m) Comprehensive income (loss):

Comprehensive income (loss), comprising net income and other comprehensive income, is defined as the change in shareholders' equity from transactions and other events from non-owner sources. Cumulative changes in other comprehensive income (loss) are included in accumulated other comprehensive income which is presented as a separate component in shareholders' equity. For all periods presented, net earnings (loss) are equal to comprehensive income (loss). Accordingly, no amounts are required to be recognized as a separate component of shareholders' equity.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

2. Significant accounting policies (continued):

(n) Financial instruments:

Financial assets and liabilities are initially recognized and subsequently measured based on their classification as held-for-trading, available for sale, held-to-maturity, loans and receivables, or other financial liabilities.

The Company classifies cash and cash equivalents as "held-for-trading", measured at fair value. Accounts receivable are classified as "loans and receivables", and measured at amortized cost.

Accounts payable and accrued liabilities, capital lease obligations and loan payable are classified as other financial liabilities and are measured at amortized cost.

The Company enters into foreign currency forward contracts from time to time to protect itself against fluctuations in the U.S. dollar exchange rate. The Company does not use hedge accounting. Accordingly, the foreign currency forward contracts are recognized at fair value on the balance sheet and changes in fair value are recognized in sales in the statement of operations.

(o) Adoption of new accounting standards:

(i) Inventory:

In June 2007, the Canadian Institute of Chartered Accountants (CICA) issued Section 3031 of the CICA Handbook, *Inventories*, which establishes new standards for the determination of inventory cost and its subsequent recognition as an expense, including any write-down to net realizable value and to conform to IFRS. In certain circumstances, the new section will also permit the reversal of previous write-downs. This Section was effective for the Company on October 1, 2008 but had no material impact on the financial statements.

(ii) Goodwill and intangible assets:

In February 2008, the CICA issued Section 3064, *Goodwill and Intangible Assets*, which replaces Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and the recognition, measurement and presentation of intangible assets. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. This Section was effective for the Company on October 1, 2008 and did not have a material impact on the financial statements.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

2. Significant accounting policies (continued):

(p) Future accounting changes:

(i) International Financial Reporting Standards:

In February 2008, the CICA's Accounting Standards Board (AcSB) confirmed that publicly accountable enterprises would be required to adopt International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board for fiscal years beginning on or after January 1, 2011. The Company will be required to report under IFRS effective for interim and annual financial statements relating to its fiscal year beginning on October 1, 2011.

Adoption of IFRS will impact many areas of financial accounting and reporting. The Company is in the process of assessing the impacts of the Canadian convergence initiative and is developing a conversion plan.

3. Inventory:

	2009	2008
Raw materials and work-in-process	\$ 443,505	\$ 350,665
Finished goods	134,488	145,670
	\$ 577,993	\$ 496,335

4. Furniture and equipment:

	2009	2008
Tooling	\$ 7,779	\$ 3,877
Manufacturing and distribution equipment	95,278	87,193
Furniture and office equipment	397,429	370,499
Leasehold improvements	101,072	101,073
	601,558	562,642
Accumulated amortization	(372,423)	(312,035)
Net book value	\$ 229,135	\$ 250,607

Four capital lease agreements ended during the fiscal year, and the buy-out options were exercised. As at September 30, 2009, furniture and equipment with a cost of \$92,831 (2008 - \$131,434) and a net book value of \$50,495 (2008 - \$85,333) is held under capital lease.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

5. Bank credit lines:

The Company has a \$500,000 operating loan credit facility with The Toronto-Dominion Bank. Amounts drawn on the facility bear interest at bank prime rate plus 1.5% and are secured by a general security agreement on the Company's assets with normal covenants and margin requirements. At September 30, 2009, no amounts have been drawn on this facility.

6. Capital lease obligations and loan payable:

	2009	2008
Obligations under capital leases	\$ 31,420	\$ 69,216
Loan payable	12,438	16,583
	43,858	85,799
Current portion	25,757	40,593
	\$ 18,101	\$ 45,206

The Company has entered into several capital lease agreements for equipment. These lease obligations have terms from 10 to 30 months, with interest rates ranging from 2.3% to 10.5% and averaging 6.1%. Each lease includes a purchase option approximating 10% of the equipment cost exercisable prior to the completion of the lease period. The present value of the lease obligations are recorded as a liability, with the current portion included in current liabilities.

The capital lease obligations require the following minimum annual payments during respective fiscal years:

2010	\$ 23,070
2011	11,271
	34,341
Less: amount representing interest	2,921
Principal amount of capital lease obligation	\$ 31,420

During 2002, the Company received funds from Industry Canada's Industrial Technology Office (ITO). The loan outstanding is non-interest bearing, repayable in equal annual installments until December 2011. Interest at ITO's prescribed rates plus 300 basis points is charged on late payments.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

7. Share capital:

(a) Authorized:

Unlimited number of common shares without par value

Unlimited number of preference shares without par value

(b) Issued common shares:

Common shares	2009		2008	
	Shares	Amount	Shares	Amount
Balance at beginning of year	39,310,694	\$ 8,108,202	34,108,694	\$ 7,607,553
Issued for cash in private placement of common shares, net of issue costs	-	-	5,000,000	476,100
Issued for cash on exercise of options	30,000	3,285	202,000	24,549
Balance at end of year	39,340,694	\$ 8,111,487	39,310,694	\$ 8,108,202

(c) Stock options:

The Company, from time to time, grants stock options to employees, directors, officers and certain consultants under the Company's stock option plan. The maximum amount of options available for issue is 3,503,000 common shares. These stock options are granted at the discretion of, and have terms and conditions as directed by, the Board of Directors. Stock options generally vest over a period of eighteen months following the date of grant.

A summary of the status of the Company's stock option plan as at September 30, 2009 and 2008 and changes during the years ending on those dates is presented below:

	2009		2008	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding, beginning of year	2,197,500	\$ 0.14	2,162,500	\$ 0.14
Granted	767,000	0.10	670,000	0.13
Exercised	(30,000)	(0.08)	(202,000)	(0.09)
Cancelled or expired	(352,000)	(0.11)	(433,000)	(0.13)
Outstanding, end of year	2,582,500	0.13	2,197,500	\$ 0.14
Options exercisable, end of year	2,131,500	\$ 0.14	1,605,500	\$ 0.14

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

7. Share capital (continued);

(c) Stock options:

Stock options outstanding and exercisable at September 30, 2009:

Number of stock options outstanding	Options exercisable	Exercise price	Weighted average remaining contractual life
580,000	580,000	\$ 0.21	31.7 months
190,000	190,000	0.15	28.3 months
320,000	320,000	0.13	39.9 months
280,000	280,000	0.12	22.6 months
1,032,500	581,500	0.10	35.8 months
180,000	180,000	0.09	2.5 months
2,582,500	2,131,500		30.7 months

During the year ended September 30, 2009, the Company recognized \$35,396 (2008 - \$18,408) in stock-based compensation related to options granted.

The fair value of options granted during the year ended September 30, 2009 was calculated using the Black-Scholes option pricing model assuming a weighted average risk-free interest rate of 1.62% (2008 - 3.35%), a dividend yield of 0.0%, a weighted average expected volatility of 53.1% (2008 - 48.7%) and expected life of stock options of 4 years (2008 - 3.5 years). The weighted average grant date fair value of options granted during the year ended September 30, 2009 was \$0.04 (2008 - \$0.05).

Changes in contributed surplus related to stock-based compensation are as follows:

Contributed surplus	2009	2008
Balance at beginning of year	\$ 165,803	\$ 153,964
Stock-based compensation reclassified to share capital on exercise of options	(1,035)	(6,569)
Stock-based compensation recognized	35,396	18,408
Balance at end of year	\$ 200,164	\$ 165,803

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

8. Contingencies and commitments:

- (a) The Company entered into an agreement with the National Research Council of Canada (NRC/IRAP) in 2002, whereby NRC/IRAP assisted in the funding to further develop the Company's potable water systems for certain aircraft (C-PWSTM) in the amount of \$495,000. As a condition of this agreement, the Company agreed to pay NRC/IRAP a royalty of 2% of the Company's gross revenue earned each quarter from April 1, 2005 to June 30, 2005, from April 1, 2007 through September 30, 2007 and then from January 1, 2009 for every quarter thereafter through December 31, 2014. Royalty payments have been made as required with accumulated royalties paid or payable to September 30, 2009 totaling \$151,956 (2008 - \$77,428).
- (b) The Company entered into a long-term operating lease for premises expiring November 30, 2010. The future annual lease payments, exclusive of property taxes and expenses directly payable by the Company, are:

2010	\$ 105,300
2011	17,550
	<u>\$ 122,850</u>

9. Income taxes:

Income tax expense, or recovery attributable to utilization of prior year losses, differs from the amounts computed by applying the combined Canadian federal and provincial income tax rate of 30.25% (2008 - 31.78%) to earnings before income taxes as follows:

	2009	2008
Earnings (loss) before income taxes	\$ 425,016	\$ (148,044)
Expected income tax recovery (expense)	\$ (128,567)	\$ 47,048
Tax effect of:		
Change in valuation allowance	271,342	105,528
Change in tax rate	(47,576)	(100,844)
Expired tax losses	(199,119)	-
Other	(9,080)	(732)
Income tax recovery (expense)	\$ (113,000)	\$ 51,000

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

9. Income taxes (continued):

The tax effects of temporary differences that give rise to future tax assets are presented below:

	2009	2008
Future income tax assets:		
Non-capital losses carried forward	\$ 660,731	\$ 1,021,843
Furniture and equipment	88,816	89,538
Scientific research and development expenditures	90,788	94,420
Share issue costs	7,171	10,398
Total gross future income tax assets	847,506	1,216,199
Valuation allowance	(466,857)	(738,199)
	380,649	478,000
Future income tax liabilities:		
Forward contracts	(15,649)	-
Net future income tax assets	\$ 365,000	\$ 478,000

Future income tax assets are classified on the balance sheet as follows:

	2009	2008
As current asset	\$ 86,000	\$ -
As long-term asset	279,000	478,000
	\$ 365,000	\$ 478,000

In assessing the ability to realize future income tax assets, management considers whether it is more likely than not that some or all of the future tax assets will be realized. The ultimate realization of the future tax assets is dependent on the generation of taxable income during periods in which the temporary differences reverse. As at September 30, 2009, evidence does not yet exist to support a conclusion that it is more likely than not that all future income tax assets will be realized. Accordingly, a valuation allowance has been recorded against those future tax assets which are not expected to be realized. In its determination of the valuation allowance, the Company considered forecasted future earnings and taxable income in the period during which losses are expected to expire or other temporary differences are expected to reverse.

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

9. Income taxes (continued):

The Company has non-capital loss carry forwards of approximately \$2,366,000 which will expire as follows:

2010	\$ 1,269,000
2014	991,000
2028	106,000

The Company also has Scientific Research and Development expenditures of approximately \$363,000 which are available to offset taxable income indefinitely.

10. Financial instruments:

(a) Foreign currency risk:

A foreign currency risk will exist where the future cash flows of financial instruments will fluctuate because of changes in foreign currency exchange rates. The Company conducts a significant portion of its business activities in United States dollars (U.S.). Cash and cash equivalents, accounts receivable and accounts payable that are denominated in U.S. dollars will be affected by changes in the exchange rate between the Canadian dollar and the U.S. dollar.

The U.S. dollar carrying amount subject to exposure to such foreign currency risk at September 30, 2009 is as follows (U.S. dollar amounts):

	2009	2008
Cash and cash equivalents	\$ 284,710	\$ 89,888
Accounts receivable	563,320	650,128
Accounts payable	29,328	23,449

The Company periodically uses foreign currency forward contracts to fix the rate of exchange for Canadian dollars at future dates in order to reduce a portion of the Company's exposure to foreign currency fluctuations on US dollar sales. At September 30, 2009, the Company had open forward currency contracts with a total commitment to sell US\$1,400,000 at an average rate of CAD\$1.102 to May 2010.

A 100 basis point change in the foreign exchange rate as at September 30, 2009 would have changed net loss by approximately \$21,926 (2008 - \$9,465).

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

10. Financial instruments (continued):

(b) Credit risk:

The Company's exposure to credit risk will relate to uncertainties as to the timing and collectability of accounts receivable. The Company mitigates credit risk through regular credit assessment and collection policies. The Company reviews its trade receivable accounts regularly and will recognize an allowance for doubtful receivables should it be determined an account is not fully collectable. All amounts due are from long term regular customers who generally pay within agreed payment terms.

The carrying amount of financial assets represented by accounts receivable of \$672,010 (2008 - \$710,770) represents the maximum credit exposure. At September 30, 2009, nine customers (2008 - eight) represented approximately 94% (2008 - 92%) of accounts receivable.

The Company's cash and cash equivalents are held by a Canadian Schedule 1 bank.

(c) Liquidity risk:

Liquidity risk is the risk that the Company would not be able to meet its financial obligations as they fall due. The Company's cash flows have enabled it to satisfy its financial commitments for its current and long term debt, financial and operating leases, royalties and lease commitments. The Company maintains up-to-date budgets and/or forecasts of sales, costs and expenses related to its current and future products and the sales value impacted by fluctuations in the value of the U.S. dollar to enable the Company to manage its future operating cash position.

The following contractual maturities of financial obligations exist as at September 30, 2009.

	Carrying amount	Contractual cash flows	Within 1 year	2 to 4 years	5 years and over
Accounts payable and accrued liabilities	\$ 449,413	\$ 449,247	\$ 449,247	\$ -	\$ -
Loan payable	12,438	12,438	4,146	8,292	-
Obligations under capital leases	31,420	34,341	23,070	11,271	-
Operating lease commitments	-	122,850	105,300	17,550	-
Royalty payments	-	590,544	102,260	426,280	62,004
	<u>\$ 493,271</u>	<u>\$ 1,209,420</u>	<u>\$ 684,023</u>	<u>\$ 463,393</u>	<u>\$ 62,004</u>

INTERNATIONAL WATER-GUARD INDUSTRIES INC.

Notes to Financial Statements

Years ended September 30, 2009 and 2008

10. Financial instruments (continued):

(d) Fair values:

Financial instruments include cash, accounts receivable, accounts payable and accrued liabilities, the carrying values of which are considered by management to approximate their fair values due to their ability for prompt liquidation and short-term to maturity. Financial instruments also includes loan payable and capital lease obligations, the fair value of which is not materially different from its carrying value based on market rates of interest.

The fair value of foreign currency forward contracts was an asset of \$54,188 at September 30, 2009 (2008 - \$6,500). This asset has been included in accrued receivables on the Company's balance sheet.

11. Management of capital:

As at September 30, 2009, the Company's capital is composed of share capital.

The Company's objectives when managing capital are as follows:

- (a) to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- (b) to have sufficient cash, cash equivalents, short-term investments and marketable securities on hand to fund the Company's business plans.

The Company's primary uses of capital are to finance product development, market development, working capital, capital expenditures, and operating losses. The Company currently funds these requirements from internally generated cash flows, amounts drawn against its line of credit and proceeds from the offering of debt or equity securities. There were no changes to the Company's approach to capital management during the year ended September 30, 2008. The Company is not subject to externally imposed capital requirements.

12. Segmented information:

The Company's principal business operations relate to the development, manufacturing and sale of aircraft water treatment equipment and water systems and, accordingly, the Company has only one reportable segment. In 2009, sales to five customers (2008 - six customers) represent approximately 85% (2008 - 82%) of total revenue. All of the Company's furniture and equipment is located in Canada. In 2009, approximately 25% (2008 - 25%) of sales revenue was generated by customers in Canada and 75% (2008 - 75%) by customers in other countries, primarily the United States.