

PhotoChannel Networks Inc.

**Unaudited Interim Consolidated Financial Statements
For the period ended June 30, 2008**

PhotoChannel Networks Inc.

Consolidated Balance Sheets

Unaudited – Prepared by Management

(expressed in Canadian dollars)

	<u>June 30, 2008</u>	<u>September 30, 2007</u>
Assets		
Current assets		
Cash and cash equivalents	\$ 1,997,135	\$ 7,405,034
Accounts receivable (note 9)	4,437,166	4,045,035
Prepaid expenses and other current assets	543,122	523,356
	<u>6,977,423</u>	<u>11,973,425</u>
Property and equipment	6,440,746	2,760,545
Deferred expenses	39,289	89,804
Intangible assets	4,378,951	6,067,614
Goodwill	4,838,867	4,867,231
	<u>\$ 22,675,276</u>	<u>\$ 25,758,619</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	\$ 7,675,434	\$ 7,510,751
Current portion of deferred revenue	678,950	344,833
Current portion of capital lease obligations (note 14)	490,074	-
	<u>8,844,458</u>	<u>7,855,584</u>
Deferred revenue	574,966	171,210
Long-term portion of capital lease obligations (note 14)	520,646	-
Asset retirement obligations	23,023	120,699
	<u>9,963,093</u>	<u>8,147,493</u>
Shareholders' Equity (note 10)		
Share capital	\$ 65,554,107	\$ 65,293,214
Warrants	4,961,826	4,961,826
Contributed surplus	11,189,821	10,215,777
	<u>81,705,754</u>	<u>80,470,817</u>
Deficit	(68,052,564)	(62,050,122)
Accumulated other comprehensive loss (note 10)	(941,007)	(809,569)
	<u>(68,993,571)</u>	<u>(62,859,691)</u>
	12,712,183	17,611,126
	<u>\$ 22,675,276</u>	<u>\$ 25,758,619</u>

Approved by the Board of Directors

“Cory Kent” Director

“Peter Fitzgerald” Director

The accompanying notes are an integral part of these consolidated financial statements

PhotoChannel Networks Inc.

Consolidated Statements of Loss and Comprehensive Loss

Unaudited – Prepared by Management

(expressed in Canadian dollars)

	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Revenue	\$ 4,217,992	\$ 1,272,962	\$ 11,776,085	\$ 4,112,147
Expenses				
Network delivery	1,986,924	306,763	5,454,718	1,078,671
Research and development	1,902,773	699,530	5,219,847	2,024,256
General and administration	1,353,583	446,619	3,312,233	1,384,193
Sales and marketing	322,128	150,662	944,108	519,438
Amortization	1,081,368	128,465	2,969,986	361,162
	6,646,776	1,732,039	17,900,892	5,367,720
Net loss before the undernoted	(2,428,784)	(459,077)	(6,124,807)	(1,255,573)
Foreign exchange gain (loss)	38,144	(1,369,179)	(107,530)	(1,371,158)
Interest income	6,655	188,605	117,783	232,345
Gain on disposal of property, plant & equipment	-	-	25,741	-
Gain on settlement of asset retirement obligation (note 6)	86,371	-	86,371	-
	131,170	(1,180,574)	122,365	(1,138,813)
Net loss	(2,297,614)	(1,639,651)	(6,002,442)	(2,394,386)
Other comprehensive loss:				
Unrealized foreign exchange loss on translation of self sustaining foreign operations (note 10)	(161,213)	-	(131,438)	-
Comprehensive loss	\$ (2,458,827)	\$ (1,639,651)	\$ (6,133,880)	\$ (2,394,386)
Basic and fully diluted net loss per share	\$ (0.07)	\$ (0.05)	\$ (0.18)	\$ (0.08)
Weighted average number of common shares outstanding	33,403,690	32,404,197	33,361,427	28,721,894

The accompanying notes are an integral part of these consolidated financial statements

PhotoChannel Networks Inc.

Consolidated Statements of Deficit Unaudited – Prepared by Management (expressed in Canadian dollars)

	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Balance, beginning of period	\$ (65,754,950)	\$ (56,732,621)	\$ (62,050,122)	\$ (55,977,886)
Net loss for the period	(2,297,614)	(1,639,651)	(6,002,442)	(2,394,386)
Balance, end of the period	<u>\$ (68,052,564)</u>	<u>\$ (58,372,272)</u>	<u>\$ (68,052,564)</u>	<u>\$ (58,372,272)</u>

The accompanying notes are an integral part of these consolidated financial statements

PhotoChannel Networks Inc.

Consolidated Statements of Cash Flows

Unaudited – Prepared by Management

(expressed in Canadian dollars)

	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Cash flows from operating activities				
Net loss for the period	\$ (2,297,614)	\$ (1,639,651)	\$ (6,002,442)	\$ (2,394,386)
Items not affecting cash				
Amortization	1,081,368	128,465	2,969,986	361,162
Stock-based compensation expense	653,001	167,964	1,065,920	488,633
Unrealized foreign exchange (gain) loss	(63,135)	1,369,179	72,550	1,371,158
Gain on disposal of property, plant & equipment	-	-	(25,741)	-
Gain on settlement of asset retirement obligations	(86,371)	-	(86,371)	-
Accretion expense	337	-	4,700	-
	(712,414)	25,957	(2,001,398)	(173,433)
Net change in non-cash working capital				
Items (note 15)	1,661,930	(1,635,040)	328,445	(17,272)
Payments made to settle asset retirement obligations	(36,418)	-	(36,418)	-
	913,098	(1,609,083)	(1,709,371)	(190,705)
Cash flows from investing activities				
Purchase of property and equipment	(279,557)	(125,806)	(3,538,716)	(735,941)
Proceeds on disposal of property, plant & equipment	-	-	25,741	-
Cash held in trust	-	17,402,679	-	(53,838)
Deferred charges	-	(319,844)	-	(477,177)
	(279,557)	16,957,029	(3,512,975)	(1,266,956)
Cash flows from financing activities				
Proceeds on exercise of options and warrants	75,251	2,382,558	169,017	4,221,743
Issuance of common shares and warrants – net proceeds	-	-	-	16,185,674
Repayment of capital lease obligations	(237,744)	-	(237,744)	-
	(162,493)	2,382,558	(68,727)	20,407,417
Effect of changes in foreign exchange rates on cash and cash equivalents	4,208	(1,392,104)	(116,826)	(1,387,237)
Increase (Decrease) in cash and cash equivalents during the period	475,256	16,338,400	(5,407,899)	17,562,519
Cash and cash equivalents - beginning of period	1,521,879	3,246,134	7,405,034	2,022,015
Cash and cash equivalents - end of period	\$ 1,997,135	\$ 19,584,534	\$ 1,997,135	\$ 19,584,534

The accompanying notes are an integral part of these consolidated financial statements

PhotoChannel Networks Inc.

Notes to Consolidated Financial Statements

Unaudited – Prepared by Management

(expressed in Canadian dollars)

1. Nature of operations

PhotoChannel Networks Inc. (the “Company”) offers the photofinishing retailer and its customers an online and in-store solution for producing prints and gifting products from their digital images. The Company’s online platform electronically connects the photofinishing retailer and its customers through the internet and provides digital image delivery, hosting, transaction processing and storage. The Company, through its wholly-owned subsidiary, Pixology Limited, provides the photofinishing retailer with kiosk software which allows consumers to offload digital images from their digital media and order prints and gifting products within the retailer’s locations. The kiosk software is also connected to the Company’s online platform permitting customers in-store to order gifting products from the kiosk, which are then transmitted from the kiosk to a remote fulfillment facility.

2. Summary of significant accounting policies

General

These unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) in Canada, using the same accounting policies as outlined in Note 2 to the most recent audited consolidated financial statements for the year ended September 30, 2007. These unaudited interim consolidated financial statements do not include all disclosures required for annual financial statements and should be read in conjunction with the audited consolidated financial statements for the year ended September 30, 2007.

In the opinion of management, all adjustments (which include reclassifications and normal recurring adjustments) necessary to present fairly the consolidated financial position, consolidated loss and comprehensive loss, and consolidated cash flows as at June 30, 2008 and for all periods presented, have been made. All amounts herein are expressed in Canadian dollars unless otherwise noted.

Basis of consolidation

These consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada, and include the accounts of the Company and each of its wholly-owned subsidiaries, PhotoChannel Capital Inc., PhotoChannel Management Inc., Pixology Limited, Pixology Software Limited and Pixology Incorporated.

All material intercompany balances and transactions are eliminated upon consolidation.

PhotoChannel Networks Inc.
Notes to Consolidated Financial Statements
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(expressed in Canadian dollars)

Reporting currency and foreign currency translation

These consolidated financial statements are reported in Canadian dollars. Foreign currency denominated revenues and expenses are translated using average rates of exchange during the period. Foreign currency denominated assets and liabilities are translated at the rate of exchange in effect at the balance sheet date.

The Company translates the assets and liabilities of self-sustaining foreign operations to Canadian dollars at the rate of exchange prevailing at the balance sheet dates and revenues and expenses of those operations are translated using the average rates of exchange during the period. Gains and losses resulting from these translation adjustments for the self-sustaining foreign operations are recorded in accumulated other comprehensive loss, a component of shareholders' equity, until there is a realized reduction in the net investment in the foreign operation.

Changes in accounting policies

(a) Capital Disclosures

Effective October 1, 2007, the Company adopted the recommendations included in the Canadian Institute of Chartered Accountants ("CICA") handbook, section 1535, Capital Disclosures. The new standard requires disclosure of qualitative and quantitative information that enables users of financial statements to evaluate the Company's objectives, policies and processes for managing capital. The additional disclosures, required as a result of the adoption of these standards, have been included in Note 8, Capital management.

(b) Financial Instruments

On October 1, 2007, the Company adopted CICA Handbook Section 3862, Financial Instruments – Disclosures and section 3863, Financial Instruments - Presentation.

Section 3862 requires disclosure about the significance of financial instruments for an entity's financial position, the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks.

Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives.

Sections 3862 and 3863 replace Section 3861, Financial Instruments – Disclosure and Presentation.

PhotoChannel Networks Inc.
Notes to Consolidated Financial Statements
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(c) Accounting Changes

On October 1, 2007, the Company adopted the recommendations of CICA Section 1506 Accounting Changes. This Handbook section provides for expanded disclosures to be made relating to changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retrospectively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in accounting policy are made only when required by a primary source of GAAP or the change results in more relevant and reliable information. The Company has not had any such changes which impact the interim financial statements.

(d) Determining whether a contract is routinely denominated in a single currency

Effective January 1, 2008, the Company adopted CICA Emerging Issues Committee (EIC) 169, Determining whether a contract is routinely denominated in a single currency. EIC 169 provides guidance on how to interpret one particular requirement of CICA Handbook Section 3855, Financial Instruments – Recognition and Measurement relating to the accounting for contracts entered into which are denominated in a foreign currency. The adoption of this EIC had no impact on the Company's consolidated financial statements.

(e) Inventories

Effective January 1, 2008, the Company adopted CICA Handbook Section 3031, Inventories, which has replaced Section 3030 with the same title. This Section aligns Canadian GAAP with International Financial Reporting Standards and establishes four basic principles: Inventory should be measured at the lower of cost and net realizable value; the cost of inventory includes costs directly attributable to its acquisition as well as an appropriate portion of fixed and variable production overheads; if the units in inventory are interchangeable, their cost should be determined using either a first-in first-out or weighted average cost formula; and write-downs of inventory to its net realizable value should be reversed if the value subsequently recovers. The adoption of this Handbook Section had no impact on the Company's consolidated financial statements.

3. Recently issued accounting standards

CICA Handbook Section 1400, Going Concern

In June 2007, the CICA amended Handbook Section 1400, Going Concern, to include additional requirements to assess and disclose an entity's ability to continue as a going concern. Section 1400 is effective for interim and annual reporting periods beginning on or after January 1, 2008. The adoption of this standard will have no impact on the Company's operating results or financial position and management expects that there will be no material impact on the Company's financial statement disclosure.

PhotoChannel Networks Inc.

Notes to Consolidated Financial Statements

Unaudited – Prepared by Management

(expressed in Canadian dollars)

CICA Handbook Section 3064, Goodwill and Intangible Assets

In February 2008, the CICA issued Handbook Section 3064, Goodwill and Intangible Assets which will replace Handbook Section 3062, Goodwill and Other Intangible Assets and Section 3450, Research and Development Costs. This revision aligns Canadian GAAP with International Financial Reporting Standards and establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This section applies to fiscal years beginning October 1, 2008 and will be adopted by the Company on that date. Management is currently in the process of determining the impact of this standard on the Company's consolidated financial statements.

4. Seasonality of operations

Demand for photofinishing products is highly seasonal, with a significant proportion of recurring revenues being generated during the Company's first fiscal (fourth calendar) quarter. The Company's limited operating history, coupled with its rapid growth may have overshadowed seasonal or cyclical factors which might have influenced business to date. Due to the seasonal nature of our business, the results of operations for any interim period are not necessarily indicative of the results of operations to be expected for the fiscal year.

5. Acquisition of Pixology PLC

On July 2, 2007, the Company acquired all of the outstanding shares of Pixology PLC ("Pixology"), a company incorporated in England and Wales and a provider of software and online solutions for the digital photography industry. The Company paid cash of \$18,657,729 including transaction costs of \$1,170,442.

The acquisition of Pixology gives the Company global reach and an international presence in the delivery of solutions for online printing. In addition, it expands the Company's product offerings into the important kiosk software market providing access to well established market-proven technology that could otherwise take up to two years to develop at an estimated cost of \$2,000,000.

The preliminary purchase price allocation summarizing the estimated fair value of the assets acquired and liabilities assumed at the date of the acquisition is as follows:

Cash and cash equivalents	\$	8,146,421
Other current assets		4,055,407
Property and equipment		462,104
Intangible assets		6,942,165
Goodwill		5,135,490
Current liabilities		(5,959,518)
Asset retirement obligations		(124,340)
Net identifiable assets and liabilities acquired for cash	\$	18,657,729

The factors that contributed to the recognition of goodwill included securing access to development synergies, cost saving opportunities, access to additional markets around the world and the acquisition of a talented workforce.

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This preliminary purchase price allocation is based on initial calculations by management of the fair value of assets and liabilities as of July 2, 2007. The final purchase price allocation is dependent on the finalization of valuations of certain intangible assets acquired. Management expects to complete these valuations during the fourth quarter of fiscal 2008.

Any final adjustment may change the purchase price allocation, which could materially affect the residual value attributed to goodwill. None of the goodwill arising on the acquisition of Pixology is deductible for tax purposes.

6. Asset retirement obligation

The following table summarizes the changes in the balance of asset retirement obligation during the period ended June 30, 2008:

Balance, March 31, 2008	\$	125,642
Payments made to settle asset retirement obligations		(36,418)
Recognition of gain on settlement of asset retirement obligation		(86,371)
Liability incurred during the period		22,684
Accretion expense included in general and administration expenses		335
Impact of foreign currency translation		(2,849)
Balance, June 30, 2008	\$	23,023

During the three month period ended June 30, 2008, the Company's property lease which previously gave rise to an asset retirement obligation was terminated. Costs incurred to restore the leased premises to their original condition upon termination of the lease totalled \$36,418. As a result of settling the liability for less than originally anticipated, a gain of \$86,371 has been recognised during the quarter.

During the three month period ended June 30, 2008, the Company entered into a lease agreement for new premises. The lease agreement entered into, which has a term of 5 years, requires the Company to restore the leased premises to their original condition at the end of the lease term. Accordingly, an asset retirement obligation relating to this requirement has been calculated. At June 30, 2008, the total undiscounted cash flows which are estimated to be required to settle the asset retirement obligation are \$35,512 and the credit-adjusted risk free interest rate at which the estimated cash flows have been discounted is 9%.

7. Financial instruments

The Company is exposed to a number of risks related to changes in foreign currency exchange rates, interest rates, collection of accounts receivable, settlement of liabilities and management of cash and cash equivalents.

The Company has established policies and procedures to manage these risks, with the objective of minimising any adverse effects that changes in these variables could have on the consolidated financial statements.

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(expressed in Canadian dollars)

Classification of financial instruments

The Company has made the following classifications for its financial instruments:

- Cash and cash equivalents are classified as "Assets held for trading" and are measured at fair value at the end of each period with any resulting gains or losses recognized in operations;
- Accounts receivable are classified as "Loans and receivables" and are recorded at cost. Subsequent measurement of trade receivables is at cost, less an allowance for doubtful accounts; and
- Accounts payable and accrued liabilities are classified as "Other financial liabilities" and are measured at cost.

Credit risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist of cash and cash equivalents and accounts receivable. The Company maintains cash and cash equivalents with various high credit quality financial institutions located in Canada and the United Kingdom. The Company's cash equivalents consist primarily of deposit investments with commercial banks in the United Kingdom. Of the amounts held with financial institutions on deposit, \$700,844 is covered by either the Financial Services Compensation Scheme in the United Kingdom or the Canada Deposit Insurance Corporation, leaving \$1,296,291 at risk should the financial institutions with which the deposits are held cease trading. The Company considers the likelihood of this happening to be remote.

The Company's accounts receivable are all from large, well-known retailers located in Canada, the United States and the United Kingdom. Credit risk from accounts receivable encompasses the default risk of retail customers. Prior to accepting new customers, the Company assesses the risk of default associated with a particular company. In addition, on an ongoing basis, management monitor the level of accounts receivable attributable to each customer and the length of time taken for amounts to be settled and where necessary, takes appropriate action to follow up on those balances considered overdue.

Management does not believe that there is significant credit risk arising from any of the Company's customers; however, should one of the Company's main customers be unable to settle amounts due, the impact on the Company could be significant. The maximum exposure to loss arising from accounts receivable is equal to their total carrying amounts. At June 30, 2008, three customers each account for 10% or more of total accounts receivable (September 30, 2007 – four customers).

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Financial assets past due

At June 30, 2008, the Company does not consider any of its financial assets to be impaired.

The following table provides information regarding the ageing of financial assets that are past due but which are not impaired.

At June 30, 2008

	Financial assets that are past due but not impaired				Carrying value on the balance sheet \$
	Neither past due nor impaired	31 – 60 days	61 – 90 days	91 days +	
Accounts receivable	68%	4%	14%	14%	4,184,042

The definition of items that are past due is determined by reference to terms agreed with individual customers. Of the 91 days+ balance at June 30, 2008, 21% has been subsequently collected. None of the amounts outstanding have been challenged by the respective customer(s) and the Company continues to conduct business with them on an ongoing basis. Accordingly, management has no reason to believe that this balance is not fully collectable in the future.

The Company reviews financial assets past due on an ongoing basis with the objective of identifying potential matters which could delay the collection of funds at an early stage. Once items are identified as being past due, contact is made with the respective company to determine the reason for the delay in payment and to establish an agreement to rectify the breach of contractual terms.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach is to ensure that it has sufficient liquidity to meet its liabilities when due.

The Company does not have any borrowing or debt facilities and settles its financial obligations out of cash and cash equivalents as they fall due. The ability to do this relies on the Company collecting its accounts receivables in a timely manner and by maintaining sufficient cash on hand.

The Company manages liquidity risk through ongoing review of accounts receivable balances and the following up of amounts past due and the management of its cash and cash equivalents and their allocation between cash on hand and short-term deposit.

At June 30, 2008, the Company's accounts payable and accrued liabilities were \$7,675,434 all of which fall due for payment within twelve months of the balance sheet date.

PhotoChannel Networks Inc.

Notes to Consolidated Financial Statements

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(expressed in Canadian dollars)

Market risk

Market risk is the risk to the Company of adverse financial impact due to changes in the fair value or future cash flows of financial instruments as a result of fluctuations in interest rates and foreign currency exchange rates. Market risk arises as a result of the Company generating revenues and incurring expenses in foreign currencies, holding cash and cash equivalents which earn interest and having operations based in the United Kingdom in the form of its wholly owned subsidiary, Pixology.

Interest rate risk

The only financial instruments that expose the Company to interest rate risk are its cash and cash equivalents. The Company's objectives of managing its cash and cash equivalents are to ensure sufficient funds are maintained on hand at all times to meet day to day requirements and to place any amounts which are considered in excess of day to day requirements on short-term deposit with the Company's banks so that they earn interest. When placing amounts of cash and cash equivalents on short-term deposit, the Company only uses high quality commercial banks and ensures that access to the amounts placed can be obtained on short-notice.

Currency risk

The Company generates revenues and incurs expenses and expenditures primarily in Canada, the United States and the United Kingdom and is exposed to risk from changes in foreign currency rates. In addition, the Company holds financial assets and liabilities in foreign currencies that expose the Company to foreign exchange risks. The Company does not utilise any financial instruments or cash management policies to mitigate the risks arising from changes in foreign currency rates.

At June 30, 2008, through its wholly owned subsidiary, the Company had cash and cash equivalents of \$1,903,160, accounts receivable of \$1,369,279 and accounts payable of \$4,754,658 which were denominated in UK £. In addition, at June 30, 2008, the Company had cash and cash equivalents of US\$27,171, accounts receivable of US\$1,536,528 and accounts payable of US\$413,773.

Sensitivity analysis

The Company has completed a sensitivity analysis to estimate the impact on net for the period which a change in foreign exchange rates during the period ended June 30, 2008 would have had.

This sensitivity analysis includes the following assumptions:

- Changes in individual foreign exchange rates do not cause foreign exchange rates in other countries to alter
- Changes in market interest rates do not cause a change in foreign exchange rates

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The results of the sensitivity analysis can be seen in the following table:

	Impact on net loss
	\$
Change of +/- 10% in US\$ foreign exchange rate	+/- 143,100
Change of +/- 7% in UK£ foreign exchange rate	+/- 432,667

The above results arise primarily as a result of the Company having US\$ denominated trade accounts receivable balances, trade accounts payable balances and bank account balances as well as a UK£ denominated payable balance.

Limitations of sensitivity analysis

The above table demonstrates the effect of either a change in foreign exchange rates or interest rates in isolation. In reality, there is a correlation between the two factors.

Additionally, the financial position of the Company may vary at the time that a change in either of these factors occurs, causing the impact on the Company's results to differ from that shown above.

8. Capital management

The Company considers its share capital, warrants, contributed surplus and capital lease obligations, as capital, which at June 30, 2008 totalled \$82,716,474.

The Company manages its capital structure in order to ensure sufficient resources are available to meet day to day operating requirements; to allow it to enhance existing product offerings as well as develop new ones and to have the financial ability to expand the size of its operations by taking on new customers. In managing its capital structure, the Company takes into consideration various factors, including the seasonality of the market in which it operates, the growth of its business and related infrastructure and the upfront cost of taking on new clients.

The Company's Officers and senior management take full responsibility for managing the Company's capital and do so through quarterly meetings and regular review of financial information. The Company's Board of Directors are responsible for overseeing this process.

Methods used by the Company to manage its capital include the issuance of new share capital and warrants which has historically been done through private placements primarily with institutional investors.

The Company is not subject to any externally imposed capital requirements.

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9. Accounts receivable

	As at June 30, 2008	As at September 30, 2007
Trade accounts receivable	\$ 4,184,042	\$ 3,927,420
Goods and services tax recoverable	181,921	45,443
Other	71,203	72,172
Total	\$ 4,437,166	\$ 4,045,035

10. Share capital, stock options and loans receivable

a) Consolidated statement of shareholders' equity

	Capital stock		Other capital accounts				
	Number of Common Shares	Amount	Contributed surplus	Warrants	Deficit	Accumulated other comprehensive loss	Total shareholders' equity
Balance - September 30, 2007	33,315,536	\$ 65,293,214	\$ 10,215,777	\$ 4,961,826	\$ (62,050,122)	\$ (809,569)	\$ 17,611,126
Issuance of shares on exercise of options	19,702	40,123	(11,357)	-	-	-	28,766
Stock-based compensation recorded in net loss	-	-	175,460	-	-	-	175,460
Loss for the period	-	-	-	-	(1,082,600)	-	(1,082,600)
Other comprehensive loss	-	-	-	-	-	(496,001)	(496,001)
Balance December 31, 2007	33,335,238	\$ 65,333,337	\$ 10,379,880	\$ 4,961,826	\$ (63,132,722)	\$ (1,305,570)	\$ 16,236,751
Issuance of shares on exercise of options	49,500	111,781	(46,780)	-	-	-	65,001
Stock-based compensation recorded in net loss	-	-	237,459	-	-	-	237,459
Loss for the period	-	-	-	-	(2,622,228)	-	(2,622,228)
Other comprehensive gain	-	-	-	-	-	525,776	525,776
Balance March 31, 2008	33,384,738	\$ 65,445,118	\$ 10,570,559	\$ 4,961,826	\$ (65,754,950)	\$ (779,794)	14,442,759
Issuance of shares on exercise of options	55,694	108,989	(33,739)	-	-	-	75,250
Stock-based compensation recorded in net loss	-	-	653,001	-	-	-	653,001
Loss for the period	-	-	-	-	(2,297,614)	-	(2,297,614)
Other comprehensive loss	-	-	-	-	-	(161,213)	(161,213)
Balance June 30, 2008	33,440,432	\$ 65,554,107	\$ 11,189,821	\$ 4,961,826	(68,052,564)	(941,007)	12,712,183

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b) Options

The Company has a stock option plan (the “Plan”) which is described in note 11(e) to the most recent audited consolidated financial statements for the year ended September 30, 2007. The Plan grants to directors, employees and consultants of the Company the option to purchase common shares of the Company. The Plan allows for a maximum of 10% of the Company’s issued and outstanding common shares be reserved for issuance, less any previously granted and outstanding options. As at June 30, 2008, the Company has reserved 2,915,869 common shares. The exercise price of each option is determined by the market price of the Company’s stock on the date of the grant and an options’ maximum term is five years as determined by the rules of the TSX Venture Exchange. Options vest over eighteen (18) months.

During the nine months ended June 30, 2008, 1,465,300 options (Nine months ended June 30, 2007 – 745,000) were granted to directors, officers and employees of the Company. These options have an exercise price of \$3.35, a term of 5 years and vest in equal amounts over 18 months. The weighted average fair value of each option issued was estimated at \$1.98 at the grant date using the Black-Scholes option-pricing model. The option valuation was based on an average expected option life of 4 years, a risk-free interest rate of 3.35%, a dividend yield of nil% and an expected volatility of 77%.

Stock-based compensation expense of \$1,065,920 was recorded for the nine month period ended June 30, 2008 in respect of all outstanding options.

11. Segment information

The Company has a single reportable segment based on the manner in which the Company has organized its operations and provision of financial information to senior management.

The Company’s sales by geographical area are as follows:

Description	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Canada	\$ 972,770	\$ 907,006	\$ 3,024,062	\$ 3,085,672
United States	1,258,267	361,086	2,402,226	1,011,824
United Kingdom	1,953,037	-	6,310,336	-
Other	33,918	4,870	39,461	14,651
Total	\$ 4,217,992	\$ 1,272,962	\$ 11,776,085	\$ 4,112,147

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Revenue is attributable to the geographic location of the Company's customer. As at June 30, 2008 and September 30, 2007, the Company's assets by geographical location are as follows:

	Canada	United Kingdom	Total
June 30, 2008			
Property and equipment	\$ 6,079,063	\$ 361,683	\$ 6,440,746
Goodwill and intangible assets	\$ -	\$ 9,217,818	\$ 9,217,818
September 30, 2007			
Property and equipment	\$ 2,354,737	\$ 405,808	\$ 2,760,545
Goodwill and intangible assets	\$ -	\$ 10,934,845	\$ 10,934,845

Major customers representing 10% or more of the Company's sales for the period are as follows:

Description	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Customer A	\$ 1,049,525	\$ 655,394	\$ 3,413,141	\$ 2,211,793
Customer B	\$ 813,173	\$ -	\$ 2,594,115	\$ -
Customer C	\$ 399,505	\$ 292,623	\$ 1,280,024	\$ 837,937
Customer D	\$ 682,871	\$ 187,315	\$ 1,205,522	\$ 611,054

12. Related Party Transactions

During the nine month period ended June 30, 2008, the Company advanced loans to officers of the Company in the amount of \$68,000 with interest payable at a rate of 7% per annum. Included in accounts receivable at June 30, 2008 is \$71,203, comprising the principal amount and accrued interest. These loans fall due for repayment within one year from the date of issue. At September 30, 2007, an amount of \$48,615 was due from an officer of the Company. This amount was repaid in full on October 25, 2007.

During the nine month period ended June 30, 2008, the Company incurred legal fees of \$105,632 (period ended June 30, 2007 - \$224,832) for services provided by a law firm of which a director of the Company is a partner. Accounts payable and accrued liabilities at June 30, 2008 included \$19,826 (September 30, 2007 \$47,334) related to these services.

During the nine month period ended June 30, 2008, the Company incurred expenses in relation to setting up e-mail marketing campaigns on behalf of a number of our retail customers of \$61,310 (Period ending June 30, 2007 - \$6,030) with a company of which a director of the Company is Chairman and Chief Executive Officer. Accounts payable and accrued liabilities at June 30, 2008 included \$12,600 (September 30, 2007 - \$nil) related to these services. The amounts charged were recorded at their exchange amount, which is the amount of consideration established and agreed to by the related parties and having normal trade terms.

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13. Revenue

Description	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Transaction fees	\$ 2,806,146	\$ 809,469	\$ 7,729,447	\$ 2,571,253
Installation fees	1,002,267	151,752	2,960,402	574,871
Membership fees	235,961	199,395	561,649	667,037
Professional fees	127,266	97,342	383,837	253,975
Archive fees	46,352	15,004	140,750	45,011
Total	<u>\$ 4,217,992</u>	<u>\$ 1,272,962</u>	<u>\$ 11,776,085</u>	<u>\$ 4,112,147</u>

14. Capital lease obligations

On March 19, 2008, the Company entered into a capital lease to acquire certain items of computer equipment. The amount outstanding under this capital lease at the period end is as follows:

	As at June 30, 2008	As at September 30, 2007
Computer equipment under capital lease, bearing interest at 20.51% per annum	<u>\$ 1,010,720</u>	<u>\$ -</u>

Minimum payments

Future minimum lease payments at June 30 are as follows:

	June 30, 2008
Remainder of fiscal 2008	\$ 122,518
2009	490,072
2010	490,072
2011	245,036
	<u>1,347,698</u>
Less: Amounts representing interest	(336,978)
Present value of lease obligation	<u>1,010,720</u>
Less: Current portion	(490,074)
Long-term portion of lease obligation	<u>\$ 520,646</u>

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15. Supplementary cash flow information

Net change in non-cash working capital items

	Three months ended		Nine months ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Accounts receivable	\$ (1,249,562)	\$ (403,050)	\$ (427,182)	\$ 153,904
Prepaid expenses and other current assets	(70,299)	(121,504)	(21,846)	(188,320)
Accounts payable and accrued liabilities	2,347,549	(1,003,662)	(9,656)	217,739
Changes in deferred expenses	16,838	(94,113)	50,515	(165,785)
Changes in deferred revenue	617,404	(12,711)	736,614	(34,810)
	<u>\$ 1,661,930</u>	<u>\$ (1,635,040)</u>	<u>\$ 328,445</u>	<u>\$ (17,272)</u>

16. Commitments

At June 30, 2008, the Company was committed to purchasing items of equipment with a cost of \$881,493.

17. Reconciliation to accounting principles generally accepted in the United States of America

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”), which differ in certain material respects from those principles and practices that the Company would have followed had its financial statements been prepared in accordance with accounting principles and practices generally accepted in the United States (“US GAAP”).

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(a) The reconciliation between Canadian GAAP and US GAAP of the net loss for the period is as follows:

	Three Months Ended		Nine Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Net loss for the period under Canadian GAAP	\$ (2,297,614)	\$ (1,639,651)	\$ (6,002,442)	\$ (2,394,386)
Change in fair value of embedded foreign currency derivatives relating to warrants	(1,607,055)	1,572,245	1,859,785	(3,439,236)
Net profit (loss) for the period under U.S. GAAP	(3,904,669)	(67,406)	(4,142,657)	(5,833,622)
Other comprehensive gain:				
Unrealized foreign exchange loss on translation of self-sustaining foreign operations	(161,213)	-	(131,438)	-
Comprehensive (loss) under U.S. GAAP	\$ (4,065,882)	\$ (67,406)	\$ (4,274,095)	\$ (5,833,622)
Basic and fully diluted loss per share under U.S. GAAP	\$ (0.12)	\$ (0.00)	\$ (0.12)	\$ (0.20)

(b) The reconciliation of the balance sheet between Canadian GAAP and U.S. GAAP is as follows:

	June 30, 2008		September 30, 2007	
	Canadian GAAP	U.S. GAAP	Canadian GAAP	U.S. GAAP
ASSETS				
Current assets	\$ 6,977,423	\$ 6,977,423	\$ 11,973,425	\$ 11,973,425
Intangible assets	4,378,951	4,378,951	6,067,614	6,067,614
Goodwill (note f)	4,838,867	11,349,930	4,867,231	11,378,294
Other long-term assets	6,480,035	6,480,035	2,850,349	2,850,349
Total assets	\$ 22,675,276	\$ 29,186,339	\$ 25,758,619	\$ 32,269,682
LIABILITIES & SHAREHOLDERS' EQUITY				
Current liabilities	\$ 8,844,458	\$ 8,844,458	\$ 7,855,584	\$ 7,855,584
Warrants liability (note d)	-	2,833,952	-	4,693,737
Long-term liabilities	1,118,635	1,118,635	291,909	291,909
SHAREHOLDER'S EQUITY				
Share capital	65,554,107	65,445,947	65,293,214	65,185,054
Warrants (note d)	4,961,826	-	4,961,826	-
Contributed surplus (note d)	11,189,821	13,547,822	10,215,777	12,573,778
Deficit (note d, f)	(68,052,564)	(61,663,468)	(62,050,122)	(57,520,811)
Accumulated other comprehensive loss	(941,007)	(941,007)	(809,569)	(809,569)
	\$ 22,675,276	\$ 29,186,339	\$ 25,758,619	\$ 32,269,682

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(c) Stock-based compensation

Effective October 1, 2004, the Company adopted FAS No. 123, Accounting for Stock-Based Compensation, as subsequently revised by FAS No. 123(R) (“FAS 123(R)”), Share-Based Payment, effective October 1, 2006. The adoption of FAS 123(R), effective October 1, 2006 under the modified prospective method, had no material impact on the Company’s financial position or results of operations. Under US GAAP, the Company recognizes the grant-date fair value of stock-based compensation awards granted to employees and directors over the requisite service period for all awards granted, modified, repurchased or cancelled after October 1, 2004 and the unvested portions of outstanding awards as at October 1, 2004. The Company also adopted CICA Handbook Section 3870, Stock-Based Compensation and Other Stock-Based Payments effective October 1, 2004 for awards granted on or after October 1, 2002.

As a result of these new accounting standards in Canada and the United States, there are no material GAAP differences related to the Company’s stock-based compensation awards during the period ended June 30, 2008 and 2007.

At June 30, 2008, the total compensation cost related to non-vested awards not yet recognized was \$2,261,571, which will be recognized over the remaining vesting period of 14 months.

(d) Warrant Liability

Under US GAAP, the Securities Exchange Commission (“SEC”) determined that it is not possible to treat as equity, warrants whose exercise price currency denomination is different from the functional currency of the entity. The SEC generally views such instruments as derivative liabilities. Therefore, the Company applied FAS No. 133, “Accounting for Derivative Instruments and Hedging Activities”, and allocated the fair value of warrants issued whose exercise price currency denomination is different than the Company’s functional currency as a liability, to be carried at fair value, with changes in fair value to be recorded in operations. The change in fair value of these warrants for the nine month period ended June 30, 2008 was \$1,859,785 and was recognised through the income statement.

(e) Cash flow statements

The Canadian accounting standard for the preparation of cash flow statements is consistent with the guidance provided by International Accounting Standard (IAS) 7, and accordingly, the cash flow statements presented herein have not been reconciled to US GAAP under the accommodation provided by the SEC.

(f) Redemption of Limited Partnership units

During the year ended September 30, 2004, the Company redeemed limited partnership units and recorded the cost as a charge to deficit for Canadian GAAP purposes. Under US GAAP, the Company applied SFAS No. 141, “Business Combinations”, and allocated the cost of issuing the

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common shares and share purchase warrants to goodwill, after first considering any allocation to tangible and intangible assets acquired. This resulted in an increase of \$6,511,063 in goodwill and shareholders' equity. The Company applies SFAS No. 142, "Goodwill and Other Intangible Assets", in determining if there is any impairment in value. As at June 30, 2008, no impairment in value has been recorded to date.

(g) Accounts receivable

No allowance for doubtful accounts has been included against accounts receivable during the nine month period ended June 30, 2008 (June 30, 2007: \$Nil).

(h) Income taxes

The Company follows the liability method with respect to accounting for income taxes. Deferred tax assets and liabilities are determined based on temporary differences between the carrying amounts and the tax basis of assets and liabilities. Deferred income tax assets and liabilities are measured using enacted tax rates that will be in effect when these differences are expected to reverse. Deferred income tax assets are reduced by a valuation allowance, if based on the weight of available evidence; it is more likely than not that some portion or all of the deferred tax assets will not be realized.

In July 2006, the Financial Accounting Standards Board (the "FASB") issued Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes, or "FIN 48", which clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. Additionally, FIN 48 provides guidance on the de-recognition, classification, interest and penalties, accounting in interim periods, and disclosure requirements for uncertain tax positions. The Company adopted the provisions of FIN 48 beginning October 1, 2007.

We file income tax returns in the U.S., Canada and the United Kingdom. We are subject to income tax examination by tax authorities in all jurisdictions from our inception to date. Our policy is to recognize interest expense and penalties related to income tax matters as tax expense. At June 30, 2008, we do not have any significant accruals for interest related to unrecognized tax benefits or tax penalties. Based on the Company's evaluation, there are no significant uncertain tax positions requiring recognition in accordance with FIN 48.

(i) Payments under operating leases:

During the nine month period ended June 30, 2008, the Company incurred operating lease expenses of \$1,292,735 (Period ended June 30, 2007 - \$256,748).

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(j) Recent U.S. announcements

FASB 157 – Fair Value Measurement

FAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. These definitions would be applied effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently assessing the impact of this statement.

FASB 159 – The Fair Value for Financial Assets and Financial Liabilities

In February 2007, the FASB issued FAS No. 159, The Fair Value for Financial Assets and Financial Liabilities ("FAS No. 159"). FAS No. 159 permits entities to choose to measure financial assets and liabilities, with certain exceptions, at fair value at specified election dates. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. FAS No. 159 is effective for the Company in fiscal years beginning October 1, 2008. The Company is currently evaluating the impact of FAS No. 159 on its consolidated financial position and results of operations.

FASB 141(R) – Business Combinations

In December 2007, the FASB issued FAS No. 141(R), Business Combinations ("FAS 141(R)"). FAS 141(R) establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree. FAS 141(R) also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. FAS 141(R) is effective for the Company in fiscal years beginning October 1, 2009. This standard will only be applicable to acquisitions after October 1, 2009. While the Company has not yet evaluated this statement for the future impact of FAS 141(R), the Company does not expect FAS 141(R) to have any impact on its consolidated financial position and results of operations related to its current businesses.

FASB 160 – Non-controlling Interests in Consolidated Financial Statements

In December 2007, the FASB issued FAS No. 160, Non-controlling Interests in Consolidated Financial Statements. FAS 160 requires ownership interests in subsidiaries held by other parties to be classified as equity in the consolidated financial statements and changes in ownership interests in a subsidiary to be accounted for as equity transactions. Deconsolidation of a subsidiary is to be accounted for at fair value. FAS 160 is applicable for fiscal years beginning on or after December 15, 2008 on a prospective basis, except for the presentation and disclosure requirements which are to be applied to all periods presented. The Company does not currently have any partially owned

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subsidiaries and does not expect, based on its current structure, the adoption to have any significant impact.

FASB 162 – The Hierarchy of Generally Accepted Accounting Principles

In May 2008, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 162, The Hierarchy of Generally Accepted Accounting Principles (“FAS 162”). The new standard is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with U.S. generally accepted accounting principles (GAAP) for non-governmental entities. For non-governmental entities, the guidance in FAS 162 replaces that prescribed in Statement on Auditing Standards (SAS) No. 69, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles and becomes effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board Auditing amendments to AU Section 411, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles. The Company does not expect the adoption of FAS No. 162 to have a significant impact on its consolidated financial position and results of operations

FASB Staff Position 142-3, Determination of the Useful Life of Intangible Assets

This FASB Staff Position (FSP) amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, Goodwill and Other Intangible Assets. The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset under Statement 142 and the period of expected cash flows used to measure the fair value of the asset under FASB Statement No. 141 (revised 2007), Business Combinations, and other U.S. generally accepted accounting principles (GAAP).

This FSP shall be effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. The guidance for determining the useful life of a recognized intangible asset in paragraphs 7–11 of this FSP shall be applied prospectively to intangible assets acquired after the effective date. The disclosure requirements in paragraphs 13–15 shall be applied prospectively to all intangible assets recognized as of, and subsequent to, the effective date.

FASB Staff Position 157-1, Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13

Issued in February 2008, this FASB Staff Position (FSP) amends FASB Statement No. 157, Fair Value Measurements, to exclude FASB Statement No. 13, Accounting for Leases, and other accounting pronouncements that address fair value measurements for purposes of lease classification or measurement under Statement 13. However, this scope exception does not apply to assets acquired and liabilities assumed in a business combination that are required to be measured at fair value under FASB Statement No. 141, Business Combinations, or No. 141 (revised 2007), Business Combinations, regardless of whether those assets and liabilities are related to leases. The Company

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is currently evaluating the impact of FSP FAS No. 157-1 on its consolidated financial position and results of operations

FASB Staff Position 157-2, Effective Date of FASB Statement No. 157

Issued in February 2008, this FASB Staff Position (FSP) delays the effective date of FASB Statement No. 157, Fair Value Measurements, for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years.