



**Absolute**Software

Redefining endpoint  
security  
and management

Annual Report 2011

# Absolute<sup>®</sup>Software

Letter to Shareholders	1
Management’s Discussion and Analysis	2
Independent Auditor’s Report	44
Consolidated Financial Statements	45
Notes to Consolidated Financial Statements	49

## Forward-Looking Statements

This report contains forward-looking statements that involve risks and uncertainties. These forward-looking statements relate to, among other things, the expected performance, functionality and availability of our services and products, and other expectations, intentions and plans contained in this report that are not historical fact. When used in this report, the words “plan,” “expect,” “believe,” and similar expressions generally identify forward-looking statements. These statements reflect our current expectations. They are subject to a number of risks and uncertainties, including, but not limited to, changes in technology and general market conditions. In light of the many risks and uncertainties you should understand that we cannot assure you that the forward-looking statements contained in this report will be realized.

## Letter to Shareholders

Fiscal 2011 was a year of robust growth for Absolute. We increased sales contracts 20 percent in constant currency to \$79.1 million; we nearly doubled cash from operating activities to \$12.5 million; and we generated record adjusted operating income<sup>1</sup> of \$9.4 million. Overall, a very solid performance, and we achieved these results while holding the line on costs.

We have clearly established Absolute as the leader in both the anti-theft and computer theft recovery markets, and we plan to continue to aggressively grow this core business. Today, we have well over 5.0 million subscriptions under management and have a proven track record of more than 20,000 successful computer recoveries. We have helped our customers remedy countless internal threats, significantly reduce loss rates and prevent data breaches.

Throughout the year, we made significant strides, transforming Absolute into a broader, more relevant solutions provider. We believe the endpoint security and client lifecycle management markets are converging. Organizations are realizing they cannot secure what they cannot manage. The growth of corporate tablets, smartphones and employees bringing their own devices into the workplace are all accelerating concern and device management complexity. Accordingly, we enhanced Absolute Manage, adding support for Apple iOS devices and integrating our Computrace persistence technology to create the world's only persistent lifecycle management solution. Subsequent to year-end, we released Absolute Manage 6.0, which uniquely positions Absolute to offer a lifecycle management platform that natively manages PCs, Macs, Android and iOS devices through the same console. This release also included AbsoluteSafe, an industry breakthrough solution for document control on iOS devices that gives organizations an innovative "app" to deliver, lock down, protect and control sensitive data on iOS devices.

In fiscal 2011, we continued to enhance our Computrace line of business. We improved reporting and added functionality including remote file retrieval, data delete upgrades and Computrace Mobile support for the Android platform. In addition, we expanded our unique persistence capability. We added BIOS support for Windows-based tablets, won our first Android persistence position with the Lenovo ThinkPad Tablet, which launched subsequent to year end, and we continued to diversify, enhance and globalize our LoJack for laptops consumer business.

We also launched Absolute Secure Drive, which helps organizations protect data on the end-point via managing newly introduced self-encrypting drives (SED). The SED market is currently in its infancy. However, analysts are predicting that SED capability will be in more than 80 percent of Solid State Drives by 2013<sup>2</sup>. We are excited to be making inroads with early adopters in this evolving security space, and expect to see our first sales for Absolute Secure Drive in fiscal 2012.

Looking forward, in fiscal 2012, we will focus on driving long-term growth and profitability by executing on the following key strategies: continuing to deliver must-have, cost effective, easy-to-use, reliable, unified, analyst recognized solutions that help customers secure and manage their data and diverse endpoint devices; further improving internal sales enablement and go-to-market strategies with existing OEM partners; broadening our firmware persistence support to more computer product lines and mobile form factors; enhancing existing customer relationships through broader offerings, improved service, increased license renewals and deployment expansions; and accelerating our growth in Europe, Asia-Pacific and Latin America.

To conclude, Absolute has significantly evolved over the past two years and now competes in a much larger, \$4.0 billion plus, growth market. Today we have a world-class, robust suite of offerings and we believe with our strategy, strong balance sheet, competitive advantages and fantastic team we will become the recognized leader in this market.

Finally, I would like to thank our employees for another year of hard work, our Board of Directors for their thoughtful guidance, and you, our shareholders, for your continued support.

Sincerely,



John Livingston  
Chairman and Chief Executive Officer

<sup>1</sup> See MD&A for the period ended June 30, 2011 dated August 18, 2011 on [www.sedar.com](http://www.sedar.com) for complete definitions

<sup>2</sup> New Industry Forecast Projects Dramatic Shift to Self-Encrypting Hard Disk and Solid State Drives by 2017 with More than 80 Percent of HDDS to be SEDS in Next Two Years, September 21, 2011

**ABSOLUTE SOFTWARE CORPORATION (TSX: ABT)**  
**Fiscal 2011 Management's Discussion and Analysis**  
**For the years ended June 30, 2011 and 2010**  
**Dated: August 18, 2011**

*The following Management's Discussion and Analysis ("MD&A") is prepared in accordance with National Instrument 51-102F1, and should be read in conjunction with the Company's Fiscal 2011 Consolidated Financial Statements and accompanying notes. These documents, along with additional information about the Company, including the Annual Report and Annual Information Form, are available at [www.absolute.com](http://www.absolute.com) and [www.sedar.com](http://www.sedar.com).*

*This MD&A contains certain forward-looking statements, which relate to future events or the Company's future performance, that include terms such as "will", "intend", "anticipate", "could", "should", "may", "might", "expect", "estimate", "forecast", "plan", "potential", "project", "assume", "contemplate", "believe", "shall", "scheduled", and similar terms. These statements involve known and unknown risks, uncertainties and other factors that are beyond the Company's control, which may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes the expectations reflected in these forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this MD&A should not be unduly relied upon. These statements speak only as of the date of this MD&A or as of the date specified in the documents incorporated by reference into this MD&A.*

*This MD&A, and the documents incorporated by reference, contain forward-looking statements pertaining to expectations which include, but are not limited to: (a) a continuing need for laptop data protection, theft recovery services and computer lifecycle management solutions in difficult economic times; (b) the successful integration of acquired products and technologies; (c) a continuation in computer refresh/replacement cycles; (d) the attainment of certain sales and cash flow targets and company performance; (e) increased adoption, or attach, rates of the Company's lifecycle management, computer tracking, and computer theft recovery solutions; (f) the ability of the Company to successfully execute on its growth strategies, including attracting new distribution partners and successfully launching new products or features and adapting solutions to new platforms; (g) the ability of the Company to successfully compete in an increasingly competitive landscape; (h) continuation of embedded firmware support from its current and anticipated PC OEM partners; (i) the demand for its products continuing to increase; (j) stable currency valuations and a sufficiently stable and healthy global economic and business environment; (k) the ability of the Company to access and gain traction in international markets and that such markets are growing as anticipated; (l) increasing market demand for self-encrypting hard drives based on OPAL specifications; and (m) other expectations, intentions and plans contained in this document that are not historical fact.*

*The key assumptions underlying the aforementioned forward-looking statements are that: (a) the data security and endpoint lifecycle management markets are converging, and the Company will be able to capitalize on this convergence as a result of an expanded product and feature set; (b) worldwide computer and mobile device shipments will continue to grow, and the Company will benefit from this trend through increased sales as a result of its investments in global sales and marketing and PC OEM partnerships; (c) the Company's investments in future growth of the business will generate returns as the worldwide computer and mobile device markets grow; (d) the Company will be able to continue to add new products and features on a global scale; (e) self-encrypting hard drives will become a popular form of encryption and the OPAL specifications will become a popular standard for self-encrypting drives; and (f) the Company will expand and be able to benefit from its portfolio of intellectual property, including patents. Certain or all of the forgoing assumptions may prove to be incorrect which could negatively impact the Company's business and the anticipated results discussed herein.*

*The Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of substantial known and unknown risks and uncertainties, certain of which are beyond the Company's control. Such risks and uncertainties include, without limitation: risks associated with increased competition from other producers; the impact of general, economic conditions in Canada, the United States and overseas; industry conditions, changes in technology, changes in laws and regulations (including the new intellectual property and privacy and data collection laws and regulations) and changes in how they are interpreted and enforced; changes in federal and provincial tax laws and legislation; the lack of availability of qualified personnel or management; fluctuations in foreign exchange or interest rates; stock market volatility and market valuations of companies with respect to announced transactions and the final valuations thereof; and obtaining required approvals of regulatory authorities. Readers are cautioned that the foregoing list of risks to the Company's performance is not exhaustive and reference is made to the items under "Risk Factors" in this MD&A and the Company's Annual Information Form for the year ended June 30, 2011. All subsequent forward-looking statements, whether written or oral, attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by these cautionary statements. Furthermore, the forward-looking statements contained in this MD&A are made as at the date hereof and the Company does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.*

**Selected Annual Information**  
(in millions, except percent and per share data)

	<b>Fiscal 2011</b>	Fiscal 2010	Fiscal 2009
Sales Contracts <sup>(1)</sup>	<b>\$ 79.1</b>	\$ 69.7	\$ 71.9
% increase (decrease)	<b>14%</b>	(3%)	(1%)
Sales Contracts in constant currency <sup>(1)</sup>	<b>\$ 83.4</b>	\$ 69.7	\$ 65.5
% increase (decrease)	<b>20%</b>	7%	(13%)
Cash from Operating Activities <sup>(1)</sup>	<b>\$ 12.5</b>	<b>\$ 6.4</b>	<b>\$ 17.6</b>
Per Share (basic) <sup>(1)(2)</sup>	<b>\$ 0.28</b>	\$ 0.14	\$ 0.37
Per Share (diluted) <sup>(1)(2)</sup>	<b>\$ 0.28</b>	\$ 0.14	\$ 0.36
Revenue	<b>\$ 72.2</b>	\$ 64.1	\$ 53.2
% increase	<b>13%</b>	20%	41%
Adjusted Operating Income (Loss) <sup>(1)</sup>	<b>\$ 9.4</b>	\$ 0.4	\$ (0.6)
% increase	<b>2,177%</b>	<i>Nm</i>	<i>Nm</i>
Net loss	<b>\$ (1.1)</b>	\$ (8.2)	\$ (2.3)
Per share (basic and diluted) <sup>(2)</sup>	<b>\$ (0.03)</b>	\$ (0.18)	\$ (0.05)
Total assets	<b>\$ 116.7</b>	\$ 124.3	\$ 117.3
Cash, cash equivalents, and investments	<b>\$ 53.8</b>	\$ 58.0	\$ 68.9
Deferred Revenue	<b>\$ 109.4</b>	\$ 102.8	\$ 95.9

(1) Throughout this document, “Cash from Operating Activities”, “Adjusted Operating Income”, and “Basic or Diluted Cash from Operating Activities per Share” are used as a profitability measures. “Sales Contracts” (invoiced sales) and Sales Contracts in “constant currency” are used as measures of sales performance and as indicators of future cash flows and revenue. Please refer to the “Non-GAAP Measures” and “Subscription Business Model” sections of this MD&A for further discussion on these measures.

(2) Per share figures for F2011 and F2010 reflect a reduced number of outstanding shares following the Company’s purchase and retirement of 238,000 common shares in fiscal 2010 and 3,797,020 common shares in fiscal 2011 under annual Normal Course Issuer Bids that commenced in November 2009 and 2010.

The words “we”, “our”, “us”, “Company”, and “Absolute” refer to Absolute Software Corporation and/or the management and employees of the Company.

All dollar figures are stated in Canadian dollars unless otherwise indicated.

## **BUSINESS OVERVIEW:**

### **Background**

Absolute® Software Corporation (“Absolute”, the “Company”, or “we”) and its subsidiaries is a provider of firmware-embedded endpoint security and management solutions that reduce IT costs, prove regulatory compliance, respond to computer theft, and optimize productivity. Absolute was founded in 1993 based upon the idea that individuals and businesses should be able to manage, track, and protect their mobile computers regardless of their physical location. Today, our solutions manage, track, and protect more than 5.8 million computers worldwide and our customers include corporations, educational institutions, healthcare and government organizations, and individual consumers.

Our most popular offering is Computrace®, which provides commercial customers with the ability to track and manage their computer and mobile device inventories on or off the corporate network, prove regulatory compliance and protect data through functions such as locating devices, remotely locking devices, deleting sensitive information, and recovering stolen devices. Our consumer version of this product is called Computrace LoJack® for Laptops.

In December 2009, we expanded our commercial offering with the purchase of Absolute Manage® (formerly LANrev). Absolute Manage is an endpoint lifecycle management product that enables IT administrators to perform application and license management, automated patch management, asset inventory and similar essential systems management functions for their PC and Mac computers as well as iOS-4 devices (iPhone and iPad) from a single platform.

The market opportunity for our products is driven largely by the increased adoption of mobile computers and ultra-portable devices such as tablet computers and smart phones (collectively, “mobile devices”). This opportunity arises in part from the fact that these devices are susceptible to loss or theft, and enterprises and consumers are concerned with the protection of sensitive or confidential data resident on those devices. They are also concerned about the recovery of the devices and the identification of individuals responsible for a theft so they can be prosecuted.

In addition, the increased adoption of mobile computing and the concurrent diversification of mobile device types and computing platforms within organizations have resulted in increased costs and management challenges for corporate IT departments. This has led to an opportunity for endpoint lifecycle management and tracking solutions designed to track and manage multiple mobile devices and platforms from a single management console.

The core software for our technology is firmware-embedded in laptop, netbook, desktop and tablet computers from leading PC manufacturers (“PC OEMs”, see Partner Ecosystem below) to make Absolute’s Computrace and Absolute Manage products more highly tamper-resistant, or “persistent”. This means that these solutions are able to self-heal in the event that the software agent is disrupted. This is a key competitive advantage for mobile computing, as devices without the ability to self-heal are virtually impossible to track when the software agent is disrupted. With sensitive or confidential

data at risk on these devices and the stringent data privacy regulations with which organizations must comply, we believe that our products have a distinct competitive advantage in the marketplace.

We also provide emergency response services that are unique in the market, enabling customers to take immediate action whenever they lose control of a device. These services are Absolute's flagship data and device security services, which are a significant part of our core value proposition and competitive advantage, and include: data delete, device freeze, persistent device messaging, investigative services, file retrieval, location identification and theft recovery. Importantly, the location and theft recovery services are managed by our recovery team, which includes former law enforcement professionals, who work in concert with current law enforcement personnel. We believe our approach is the only viable way to provide such services while also ensuring that privacy rights are protected.

In February 2011 we announced the general availability of Absolute Secure Drive to manage self-encrypting hard drives. We believe that an emerging market opportunity exists for the management of self-encrypting drives and that our persistent technology and PC OEM relationships will provide us with a competitive advantage. Self-encrypting drives are a relatively new technology, and therefore our success in this market will be dependent on the general market adoption of self-encrypting drives as a security solution, among other factors.

## **Globalization**

In developing the market for our solutions, we have focused primarily on North America from where we have historically generated the majority of our annual sales. However, we believe that extending our market reach globally offers significant long-term growth opportunities, especially since international computer shipments are expected to grow at much faster rates than those in North America. As a result, we are continuing to invest in our overseas operations.

We currently have offices in Vancouver, Canada; Austin, USA; Reading, UK; and Nuremburg, Germany. We also service additional geographies through our remote sales force and through our partner network. Our products and customer support services are available in 13 languages. We currently have sales distribution agreements with nine PC OEMs and a number of other in-country resellers in Europe ("EMEA"), Asia-Pacific and Latin America.

In fiscal 2011 ("F2011"), sales outside of North America grew 93% in constant currency, and represented 10% of our total sales, compared to 6% in fiscal 2010 ("F2010"). While our investments in our overseas operations have begun to drive growth, we are still in the formative stages of our international expansion.

## Partner Ecosystem

Our partner ecosystem is an essential component of our business strategy. Our primary partners are PC OEMs who are both key collaborative technology partners and key distribution partners. We generate approximately 85% of our total sales through our PC OEM partners using various sales and marketing programs combined with co-engagement from our direct sales force to help identify and close sales opportunities.

We also have relationships with leading market influencers including infrastructure partners (for example, Intel®, Qualcomm®, and Microsoft®), telecom service providers, and other software vendors and resellers to complement our PC OEM efforts.

From a technology perspective, our PC OEM partners have adopted our Computrace technology as a standard and have embedded it in the firmware of laptop, netbook, desktop and tablet computers. This is an important collaboration for us, as the embedded support enhances the persistence (ability to survive unauthorized or unintentional removal attempts) of our software. This is a key value proposition and differentiator for Absolute.

Every year, our software ships embedded in the firmware of millions of computers worldwide. The following table lists the PC OEMs who are currently providing embedded support for Computrace:

Acer (since 2009)	Intel (Classmate Computer) (since 2009)
ASUS (since 2009)	Lenovo (since 2005)*
Dell (since 2005)	Motion Computing (since 2006)
Fujitsu (since 2006)*	NEC Personal Products (since 2010)
GammaTech (since 2008)	OQO, Inc. (since 2007)
General Dynamics Itronix (since 2008)	Panasonic (since 2006)
Getac (since 2008)	Toshiba (since 2006)
HP (since 2005)*	Xplore Technologies (since 2008)
IEI Technology (since 2009)	

\* includes tablet computers

Our consumer solutions are also distributed through retail and online partners, such as; Best Buy™, Staples™, and TigerDirect™; and via our website: [www.lojackforlaptops.com](http://www.lojackforlaptops.com).

## Solutions and Technology

### Computrace

Our Computrace solutions allow customers to centrally secure and track their IT assets within a single web-based interface, the Absolute Customer Center. These solutions incorporate the Computrace Agent, which is a small software client that is embedded into the firmware of many computers at the factory by our OEM partners or can be installed on the hard drive of the computer or device by the manufacturer or end customer. Once activated, the Agent maintains daily contact with the Absolute Monitoring Center (hosted by Absolute), providing detailed data from each device. By logging into the Absolute Customer Center, IT administrators can monitor their devices (on or off the network), knowing where they are, who is using them, and what types of software and other applications reside on them. They can also perform security and

event management (“SIEM”) functions, such as managing device security settings and establishing alerts for events when a corporate security policy is compromised. In the event of an emergency situation, customers can take protective measures, such as locating the device, remotely locking the device, deleting sensitive information, retrieving important files and supporting the recovery of stolen devices. Computrace is offered in several variations (for example, with or without managed theft recovery) and is available for laptop and desktop PCs and Macs, and for mobile devices (BlackBerry, Symbian, Android, and Windows Mobile). Our consumer version of this product is branded as Computrace LoJack for Laptops, which was awarded Editor’s Choice honors by PC Magazine in August 2011.

### ***Absolute Manage***

Absolute Manage is our computer configuration lifecycle management technology. It allows IT administrators to manage their PC, Mac, and Apple iOS-4 (iPhone or iPad) devices from within a single console. Absolute Manage includes an administrator server and individual agents that are installed onto each device. Agent calls occur throughout the day and provide data from each computer. IT administrators use this data to monitor and manage their computer inventories. They can implement actions directly from the administrator server interface to remotely perform actions such as locating, terminating, removing, or installing applications, licenses, patches and computer images, as well as other management functions such as power management and asset inventory.

### ***Absolute Secure Drive***

On February 10, 2011, we announced the general availability of Absolute Secure Drive to manage self-encrypting hard drives. Absolute Secure Drive manages the self-encrypting drives that meet OPAL (an industry standard released in 2009 by the Trusted Computing Group) and Drive Trust (a standard released by Seagate) specifications. With Absolute Secure Drive, IT administrators can easily set up and administer self-encrypting drives on each computer in their deployment from a single united console.

### ***Future Products***

In the coming year, we expect to continue adding new product features, particularly in the areas of endpoint lifecycle management, data protection, and mobile device support on a global scale. We also intend to advance the integration of our Computrace and Absolute Manage products to create a single management console from which our customers can view data and initiate actions from either system.

### ***Deployment Models***

Our Computrace and LoJack for Laptops products are primarily delivered in a Software as a Service (“SaaS”) model. The customer activates Computrace in the firmware or as software, and can immediately begin realizing the benefits. Our Absolute Manage product is an on-premise client-server solution that is designed for minimal server infrastructure requirements. Additionally, a small number of Computrace customers, whose internal policies prohibit their computers from accessing third-party servers, have purchased our Computrace product using an on-premise server model.

## **Patent Portfolio**

We have a portfolio of 21 issued patents, and currently have 86 new patent applications in process. Several potential competitors have taken licenses to our patent portfolio to enable them to participate in the computer theft recovery space. The royalty revenue from these licensees is currently not material.

Due to the nature of our patent portfolio, from time to time the Company is involved in assertions and claims of patent infringement as both the initiating party and, from time to time, as a respondent to such claims. Currently, the company is party to the following material patent-related matter:

Absolute Software Corporation and Absolute Software, Inc. v. Stealth Signal, Inc., and Computer Security Products, Inc. in the United States District Court for the Southern District of Texas, Case No. H-05-1416. On July 21, 2010 the claim of patent infringement made against Stealth Signal, Inc. by the Company was dismissed and the counterclaim against the Company for patent infringement was also dismissed. Subsequently, both parties filed notices to appeal the dismissal of their respective claim and counterclaim. Both parties filed with the United States Court of Appeals for the Federal Circuit, briefs supporting their respective claims. On July 5, 2011, the Court of Appeals for the Federal Circuit conducted an oral hearing, addressing the parties' respective positions. The Company is awaiting a decision from the Court of Appeals for the Federal Circuit.

In order to establish and defend its proprietary rights and patent portfolio, the Company is also the initiating party in two patent-related matters. The Company's management believes Absolute will prevail in these cases, however, the potential outcome, timing, and impact on the Company's business and patent portfolio is not determinable at this time.

## **Competition**

We have historically had few direct competitors in our services for mobile device protection and computer theft recovery. Most competitors have been small operators with limited resources to widely commercialize their offerings. However, concurrent with the increased proliferation and adoption of smart phones over the past two years, we have recently seen increased competition, primarily in the consumer market for mobile devices. Based on our proprietary technology, patent protection, managed theft recovery approach and PC OEM relationships, we believe that our products maintain a competitive advantage in the market place. Several competitors have taken licenses to our patents and now pay us royalties on their sales; have ceased offering the potentially infringing offerings; or have abandoned their own applications and become resellers or referral partners of our solutions.

In the data and device security market, we also compete indirectly with data security companies that offer encryption solutions such as Safeboot (from McAfee), Utimaco (from Sophos), Checkpoint and Symantec, among others. Our Computrace solutions are generally purchased as a complement to all these solutions.

Our endpoint lifecycle management solution, Absolute Manage, competes in a market where there is a greater level of established competition. In this market, we compete

with products such as Altiris (from Symantec), LANdesk, Kace (from Dell), and BigFix (from IBM), among others. The primary advantages of our solution include our firmware persistent technology, cross-platform capability (PC, Mac, and Apple iOS-4 support), and lower deployment and ongoing administrative and infrastructure costs as compared to solutions offered by our primary competitors.

In addition, there is another subset of competitors with Absolute Manage Mobile Device Management (“MDM”), our solution to allow organizations to manage their iOS4 devices. Competitors in this area include Good Technology and Mobile Iron. The primary advantage of our solution is that we allow organizations to manage desktops, laptops, and ultra-portable devices from a single console.

With the recent launch of Absolute Secure Drive, we have entered the market for the management of self-encrypting hard drives. This is a relatively new and emerging market with few established competitors. We currently view Wave and WinMagic as competitors in this market, and expect other entrants to this market in the future.

### **Subscription Business Model**

We sell the majority of our solutions under a subscription model in which customers acquire subscriptions to software-based services for a limited license term. From a financial perspective, this subscription model improves the predictability and visibility of revenue streams, enables recurring cash flows and is expected to maximize profitability over time.

However, the accounting treatment for the subscription model results in a significant deferral of revenue and profitability generated from pre-paid subscriptions, despite the cash flow it generates in the current reporting period. As a result, we believe that cash flow from operations is an important indicator of profitability and performance.

Subscriptions to Absolute’s solutions are fully invoiced up-front for the purchase term (which varies from one to five years) on ordinary invoice and payment terms. Once received, payments are normally non-refundable. The amount invoiced is recorded at the foreign exchange rate in effect at the time of sale in deferred revenue on the balance sheet, and is recognized ratably over the contract term.

We also sell a portion of our Absolute Manage licenses on a perpetual license basis. In these scenarios, customers are invoiced up-front for the cost of the license as well as an annual maintenance and support services fee. From an accounting perspective, perpetual licenses are generally recognized at the time of delivery (assuming other criteria are met), while annual maintenance and support fees are accounted for in the same manner as subscription license fees. During F2012, the perpetual licenses were not a significant portion of our overall sales; however we expect that the proportion of perpetual licenses may increase over time as sales of the Absolute Manage product increase.

We refer to our total invoiced sales in a period as our total “Sales Contracts”.

As our term Sales Contracts have traditionally averaged approximately 27 months in term, there is a significant lag between revenue recognition and the timing of the Sales Contract and our receipt of non-refundable cash flows. In general, only 15-20% of total Sales Contracts reported for any given fiscal year are also recognized as revenue in the

same fiscal year. Conversely, a majority of our operating expenses in each fiscal period are incurred to generate Sales Contracts for that period. As a result, in times of rapid growth in the business, GAAP earnings will often decrease or losses increase, while operating cash flow accelerates. Accordingly, we focus on Cash from Operating Activities as the key profitability metric for the Company. We believe this metric provides a meaningful evaluation of the future of the business, while revenue and operating income (loss) provide a lagging indication of performance.

### **Non-GAAP Measures**

Throughout this MD&A, we refer to a number of measures which we believe are meaningful in the assessment of the Company's performance. All these metrics are non-standard measures under Canadian Generally Accepted Accounting Principles ("GAAP"), and are unlikely to be comparable to similarly titled measures reported by other companies. Readers are cautioned that the disclosure of these items is meant to add to, and not replace, the discussion of financial results or cash flows from operations as determined in accordance with GAAP.

The purpose of these non-GAAP measures is to provide supplemental information that may prove useful to investors who wish to consider the impact of certain non-cash or uncontrollable items on the Company's operating performance. Non-cash stock-based compensation and amortization of acquired intangible assets are being excluded from the Company's operating expenses because the decisions which gave rise to these expenses were not made to increase Sales Contracts in a particular period, but were made for the Company's long-term benefit over multiple periods. While strategic decisions, such as those to issue stock-based awards or to acquire intangible assets, are made to further the Company's long-term strategic objectives and do impact the Company's earnings under GAAP, these items affect multiple periods and management is not able to change or affect these items within any particular period. As such, supplementing GAAP disclosure with non-GAAP disclosure using the non-GAAP measures outlined below provides management with an additional view of operational performance by excluding expenses that are not directly related to performance in any particular period, and management uses both GAAP and non-GAAP measures when planning, monitoring, and evaluating the company's performance.

These measures, as well as their method of calculation or reconciliation to GAAP measures, are as follows:

#### *a) Basic and diluted Cash from Operating Activities per share*

As a result of the nature of our revenues (please refer to "Subscription Business Model" in this MD&A), we believe Cash from Operating Activities per share is a meaningful indicator of profitability per share. Cash from Operating Activities per share is calculated by dividing Cash from Operating Activities by the average number of shares outstanding for the period (basic), or the fully diluted number of shares using the treasury stock method (diluted).

*b) Sales Contracts*

See the “Subscription Business Model” section of this MD&A for a detailed discussion of why we believe Sales Contracts (also known as “bookings”) provide a meaningful performance metric. Sales Contracts are a component of deferred revenue (see Note 10 of the Notes to the Consolidated Financial Statements), and result from invoiced sales of our products and services.

*c) Sales Contracts in constant currency*

Approximately 95% of our Sales Contracts are denominated in U.S. dollars, and we believe this is important to consider when evaluating underlying sales performance. Sales Contracts in “constant currency” refers to the Canadian dollar sales that would have been reported had the average U.S. dollar foreign exchange rate been unchanged from the rate in fiscal 2010, and is calculated by applying the appropriate U.S. dollar foreign exchange rate from the prior year to the current year sales denominated in U.S. dollars.

The average U.S. dollar to Canadian dollar exchange rate on sales was \$1.001 in F2011 compared to \$1.055 in F2010.

*d) Adjusted Operating Expenses*

A number of significant non-cash expenses are reported in our Cost of Revenue and Operating Expenses. Management believes that analyzing these expenses exclusive of these non-cash items provides a useful measure of the cash invested in operating the business. Most significantly, these non-cash items include stock-based compensation and amortization of acquired intangible assets.

Specifically, management adjusts for the following items in computing its Adjusted Operating Expenses:

- 1) *Stock-based compensation:* Our compensation strategy includes the use of stock-based awards to attract and retain key employees and executives. It is principally aimed at aligning their interests with those of our shareholders and at long-term employee retention, rather than to motivate or reward operational performance for any particular period. Thus, stock-based compensation expense varies for reasons that are generally unrelated to operational decisions and performance in any particular period.
- 2) *Amortization of Acquired Intangible Assets:* We believe that amortization of acquisition-related intangible assets, such as the amortization of acquired technology and customer relationships, relate to items arising from pre-acquisition activities. These are costs that are determined at the time of an acquisition. While it is continually reviewed for potential impairment, amortization of the cost is a static expense, one that is typically not affected by operations during any particular period.

Please see the following for a reconciliation of our GAAP Cost of Revenue and Operating Expenses to the Adjusted Operating Expenses:

(in millions)	Year ended					
	June 30, 2011			June 30, 2010		
	Per consolidated financial statements	Adjustments	Adjusted	Per consolidated financial statements	Adjustments	Adjusted
Cost of Revenue ("COR")	\$ 18.9	\$ (5.5) <sup>(1)</sup>	\$ 13.4	\$ 14.9	\$ (2.7) <sup>(1)</sup>	\$ 12.2
Total Operating Expenses per Statement of Operations	52.2	(2.8) <sup>(2)</sup>	49.4	53.6	(2.1) <sup>(2)</sup>	51.5
Total COR and Operating Expenses	\$ 71.1	\$ (8.3)	\$ 62.8	\$ 68.5	\$ (4.8)	\$ 63.7

**Notes:**

- (1) Amortization of intangible assets per the Statement of Cash Flows in the Consolidated Financial Statements.
- (2) Stock-based compensation per the Statement of Operations and Comprehensive Loss.

*e) Adjusted Operating Income*

Management believes that analyzing operating results exclusive of the significant non-cash items noted above provides a useful measure of the Company's performance. The non-cash items excluded in the determination of Adjusted Operating Income include stock-based compensation and amortization of acquired intangible assets. See point (d) above for a discussion of these items.

The following tables provide a reconciliation of our GAAP Operating Income (Loss) to the Adjusted Operating Income:

(in millions)	Year ended					
	June 30, 2011			June 30, 2010		
	Per consolidated financial statements	Adjustments	Adjusted	Per consolidated financial statements	Adjustments	Adjusted
Operating Income (Loss)	\$ 1.1	\$ 8.3 <sup>(1)(2)</sup>	\$ 9.4	\$ (4.4)	\$ 4.8 <sup>(1)(2)</sup>	\$ 0.4

**Notes:**

- (1) Amortization of intangible assets per the Statement of Cash Flows in the Consolidated Financial Statements.
- (2) Stock-based compensation per the Statement of Operations and Comprehensive Loss.

## FINANCIAL PERFORMANCE REVIEW AND ANALYSIS

### Performance Overview

During F2011, we continued to focus on our corporate and consumer sales execution in North America and internationally and to broaden our product offerings targeted to the endpoint management and security market.

Operational highlights for F2011 included:

- Sales Contracts invoiced were \$79.1 million (\$83.4 million in constant currency), representing a 14% increase (20% in constant currency) compared to \$69.7 million in F2010 (\$69.7 million in constant currency).
- Cash from operating activities was \$12.5 million, representing an increase of 94% compared to \$6.4 million in F2010.
- Adjusted Operating Income was \$9.4 million, representing an increase of 2,177% over \$0.4 million in F2010.
- International sales increased 84% to 10% of total Sales Contracts, compared to 6% in F2010.
- Launched Computrace® Mobile for the Android platform, and Absolute Manage Mobile Device Management for Apple® iOS 4 devices (iPhone®, iPad™ and iPod touch®).
- Introduced Remote File Retrieval, a data leakage prevention feature, for Computrace®.
- Integrated Computrace® persistence technology with Absolute Manage to create a unique self-healing lifecycle management solution.
- Extended data and device protection capabilities with the launch of Absolute Secure Drive to manage self-encrypted drives.
- Repurchased 3,797,020 shares in the year under the Company's Normal Course Issuer Bids for a total cost of \$14.2 million.

We believe that our improved financial performance in F2011 reflects a combination of successful execution of our sales and product strategy, improved general economic conditions, and our continuing efforts to improve internal productivity and to optimize our corporate cost structure.

## Sales Contracts

In fiscal 2011, Sales Contracts were \$79.1 million (\$83.4 million in constant currency), up 14% (20% in constant currency) from \$69.7 million in F2010. The increase from F2010 reflects a 12% increase in commercial sales (18% in constant currency) and a 21% increase in consumer sales (28% in constant currency).

The following table shows Sales Contracts by commercial and consumer customers:

(in Millions)	Fiscal 2011	Fiscal 2011 Constant Currency	Fiscal 2010
Commercial Customers			
Theft recovery products <sup>(1)</sup>	\$53.8	\$56.8	\$49.0
Non-theft recovery products <sup>(2)</sup>	\$14.4	\$15.2	\$11.7
Total Commercial Customers	\$ 68.2	\$ 72.0	\$ 60.7
Consumer Customers	\$ 10.9	\$ 11.4	\$ 9.0
Total Sales Contracts	\$ 79.1	\$ 83.4	\$ 69.7

(1) “**Theft recovery products**” are defined as Computrace products that include a theft recovery component.

(2) “**Non-theft recovery products**” are defined as our Absolute Manage and Absolute Secure Drive products, as well as Computrace products that do not include a theft recovery component (for example, Absolute Track and Computrace Data Delete).

### *Commercial Customer Sales Performance:*

Our commercial business consists of sales of our Computrace, Absolute Manage and Absolute Secure Drive product suites. We sell these products and related services into four primary market verticals: corporate, education, government, and health care. Our primary sales channels for this business are our PC OEM partners, as well as a number of distributors and value-added resellers.

In constant currency, invoiced sales to commercial customers increased 18% in F2011 compared to F2010. This growth is a result of three main factors: a) our sales to existing customers have increased; b) we have experienced sales productivity gains as we begin to realize the benefits from the expansion of our sales and marketing teams over the past two years; and c) we have broadened our product portfolio which has increased our product appeal and addressable market.

In F2011, commercial Sales Contracts from our theft recovery product line grew 16% in constant currency over F2010, as theft recovery services continue to be valued in the market. Commercial Sales Contracts from our non-theft recovery products grew 31% in constant currency over F2010, as we continued to expand our product portfolio in both management and security. For F2011, our non-theft recovery products represented 21% of commercial Sales Contracts.

Sales Contracts from existing commercial customers were \$56.5 million in F2011, an increase from \$51.0 million in F2010, and represented 83% of total commercial sales,

consistent with F2010 at 84% and our historical average of 80-85%. In F2011, we maintained a high customer retention rate and continued to expand our footprint within our existing customer base. We also continued to add new customers, which we expect will generate continued growth as we further develop our relationships with these new customers.

We have historically used additional metrics as indicators of the performance of our commercial business; however, as the business has evolved and expanded, we feel that these metrics are no longer reliable indicators of our performance.

The Expiring Subscription Ratio has historically been used as a proxy for the level of product renewal and expansion achieved within our existing Computrace customer base. In F2011, 1,027,000 commercial subscriptions expired and 1,599,000 subscriptions were sold to existing customers, representing an Expiring Subscription Ratio of 1.6:1 compared to 1.7:1 in the prior year when 661,000 subscriptions expired and 1,107,000 subscriptions were sold to existing customers. The Expiring Subscription Ratio has decreased over time as our customer base has grown, and has fluctuated over the short-term due to economic conditions and customers' buying patterns. As we have expanded the size of our business and have added multiple product lines, we believe that the expiring subscription ratio has become a less accurate proxy for the level of expansion and renewal within our customer base and therefore no longer provides a useful measure of our current or future performance.

The average selling price for existing customer sales in U.S. dollars was \$35.35 in F2011, which was lower than the \$43.61 experienced in F2010. The year over year decline in average selling price is a reflection of the expansion of our product portfolio in order to expand our addressable market and to maximize our revenue opportunity per customer. We believe that, with the expansion of our product portfolio into multiple product lines with different selling prices, the average selling price is no longer a meaningful metric from which to measure the current or future performance of the company.

For the reasons outlined above, we will not be publishing expiring subscriptions, the expiring subscription ratio and the average selling price in future quarters. However, we will publish metrics that we believe are more meaningful to assessing the performance and future prospects of our business. These relevant metrics focus on product diversification (breakdown of commercial Sales Contracts between those that include a theft recovery component and those that do not), geographic expansion (breakdown of Sales Contracts between those originating from within North America those originating internationally), as well as additional commentary on vertical performance, new customer acquisitions, and customer retention.

#### *Consumer Sales Performance:*

Our consumer business consists of sales of our consumer-branded product suite, Computrace LoJack for Laptops. Our primary sales channels for these products include our PC OEM partners, as well as other distribution channels such as online and traditional retailers. Some of our PC OEM partners bundle our solutions with new PC purchases, which has formed the largest portion of our consumer product sales in prior years and which we expect will become a less significant portion of our business as we continue to diversify into other retail channels. These bundled sales are typically lower priced and are

for a shorter term than our commercial business. Most renewal business is completed directly with our end customers.

Consumer sales in F2011 increased 21% (28% in constant currency) from F2010. Our online and retail strategies continue to produce increasing levels of non-bundled PC OEM sales, which is reflected in our year to date non-bundled sales performance which has increased 36% (43% in constant currency) to \$6.3 million from \$4.6 million in F2010.

## Revenue

Revenue for F2011 increased 13% to \$72.2 million, compared to \$64.1 million in the prior year. A majority of our revenue is derived from the amortization of Sales Contracts through the prior year's deferred revenue balance. As the average contract life of Sales Contracts averages approximately 27 months, typically only 15-20% of new and renewal Sales Contracts reported for any given fiscal year are included in revenue for that particular year. The remainder is included in deferred revenue on the balance sheet. As we increase the relative proportion of perpetual versus term license sales with our Absolute Manage product, we expect that a greater portion of Sales Contracts will be recognized as revenue in the same year as the year the Sales Contract is concluded. See the "Subscription Business Model" section of this MD&A for further discussion, and the table below for a breakdown of the revenue components:

(in millions)	Fiscal 2011	Fiscal 2010
Revenue recognized from:		
Prior year Deferred Revenue	\$ 55.6	\$ 50.5
Current year Sales Contracts	16.6	13.6
Total	\$ 72.2	\$ 64.1
Percent of revenue from current year Sales Contracts	21%	19%

## Adjusted Operating Expenses<sup>(1)</sup>

(Millions of dollars)	Fiscal 2011	Fiscal 2010	Percentage increase (decrease)
Cost of revenue ("COR") <sup>(1)</sup>	\$ 13.4	\$ 12.2	9%
Sales and marketing ("S&M")	33.0	34.7	(5%)
Research and development ("R&D")	11.6	10.4	12%
General and administration ("G&A")	8.0	7.7	4%
Investment tax credits ("ITC")	(3.2)	(1.3)	156%
<b>Total Adjusted Operating Expenses<sup>(1)</sup></b>	<b>\$ 62.8</b>	<b>\$ 63.7</b>	<b>(1%)</b>
Number of employees at June 30	337	350	(4%)

### ADJUSTMENTS:

- (1) Please refer to the Non-GAAP Measures section of this MD&A for a reconciliation of these adjusted expenses to those in the Consolidated Financial Statements.

Total Adjusted Operating Expenses decreased 1% in F2011 compared to F2010, as a result of the slight contraction of the employee base during the year, increased investment tax credits from our development efforts, and reduced spending in certain sales and marketing activities.

### **Adjusted Operating Expenses as a Percentage of Sales Contracts<sup>(1)</sup>**

As discussed in the “Subscription Business Model” section of this MD&A, a large percentage of total adjusted operating expenses costs relate to efforts to generate Sales Contracts in the same and future periods. Therefore, management focuses on Adjusted Operating Expenses to measure the Company’s operating efficiency and effectiveness. In F2011, Adjusted Operating Expenses were 79% of Sales Contracts, representing a decrease from 91% in F2010.

(percentage of Sales Contracts)	<b>Fiscal 2011</b>	Fiscal 2010
Cost of revenue (“COR”) <sup>(1)</sup>	<b>17%</b>	17%
Sales and marketing (“S&M”)	<b>42%</b>	50%
Research and development (“R&D”)	<b>15%</b>	15%
General and administration (“G&A”)	<b>10%</b>	11%
Investment tax credits (“ITC”)	<b>(4%)</b>	(2%)
<b>Total COR and operating expenses<sup>(1)</sup></b>	<b>79%</b>	<b>91%</b>

#### **ADJUSTMENTS:**

- (1) Please refer to the Non-GAAP Measures section of this MD&A for a reconciliation of these adjusted expenses to those in the Interim Consolidated Financial Statements.

#### *Cost of Revenue and Gross Margin*

Cost of revenue is comprised of customer support, training and theft recovery activities as well as product packaging, shipping and service guarantee costs. These costs increased year over year primarily as a result of amortization of acquired intangible assets and increases in average headcount in these areas. Amortization of intangible assets increased to \$5.6 million compared to \$2.7 million in F2010 due to assets acquired from the acquisitions of LANrev and FailSafe® and Phoenix® Freeze™ part way through F2010. We exited F2011 with a headcount of 82 in these areas, as compared to 88 at June 30, 2010 and 74 at June 30, 2009. A majority of the reduction in headcount occurred in the second half of F2011, and therefore, did not impact operating expenses significantly in the current year.

Gross margin in F2011 was 74% compared to 77% in the prior year. The decrease was primarily the result of the amortization of the intangible assets acquired as part of the LANrev and Failsafe acquisitions, which occurred in F2010. Not including these charges, gross margin in F2011 would have been 82%, slightly improved from 81% in F2010.

### *Sales and Marketing*

The decrease in sales and marketing expenses reflect reductions in certain marketing initiatives in the current year. S&M expenses decreased in the year by 5% to \$33.0 million from \$34.7 million in F2010. As a percent of Sales Contracts, S&M expenses were 42% for F2011, as compared to 50% F2010. This decrease is primarily a result of the contraction of certain partner and organic marketing programs during the year, offset by increased headcount related costs in our direct sales force. During F2010, we added to our sales headcount, as we increased the number of sales regions in the U.S. market and also increased the number of salespeople serving each region. Accordingly, F2011 includes the impact of a full year of salaries for employees who were hired over the course of F2010 as well as additional employees who were hired during F2011. In addition, we expensed higher sales commissions in F2011 as compared to F2010, as the amortization of previously deferred sales commissions has increased in line with our increase in revenue. We exited F2011 with a headcount of 140 in sales and marketing, as compared to 138 at June 30, 2010 and 125 at June 30, 2009.

We undertake a number of general sales and marketing initiatives, including: participation in tradeshow and partner events; market development programs with partners; public and industry analyst relations; and advertising expenditures. These expenditures are incurred to increase awareness with both partners and customers, drive coverage with industry analysts and establish Absolute's leadership position globally.

### *Research and Development*

Research and development expenditures increased 12% from last year to \$11.6 million, as compared to \$10.4 million in F2010. R&D expenses remained consistent as a percentage of Sales Contracts at 15% in both F2011 and F2010. As compared to F2010, we operated most of F2011 with expanded headcount commensurate with our expanded product offering, however, headcount levels were reduced during the third and fourth quarters. In addition, employee bonus accruals were higher in F2011 as compared to F2010 due to improved corporate financial performance. We exited F2011 with a headcount of 84 in research and development, as compared to 95 at June 30, 2010 and 73 at June 30, 2009.

### *General and Administration*

General and administration expenses increased 4% from the prior year, to \$8.0 million from \$7.7 million in F2010. This increase is primarily due to increases in legal fees and bad debt expenses. The increase in legal fees was due primarily to patent creation and patent defense. We exited F2011 with a headcount of 31 in general and administration, as compared to 29 at June 30, 2010 and 29 at June 30, 2009.

### *Investment Tax Credits*

ITCs consist of amounts credited to the Company in respect of eligible Canadian Scientific Research and Development expenditures. ITC recovery amounted to \$3.2 million in F2011, which included an amount of \$1.6 million recorded on acceptance of certain of our historical claims which remained outstanding in prior periods. Overall, ITC recovery increased 156% from \$1.3 million in F2010.

## **Operating Income (Loss)**

Absolute generated Adjusted Operating Income of \$9.4 million in F2011 as compared to \$0.4 million in F2010. The improved adjusted operating results in F2011 are the result of an increase in revenues of \$8.1 million, offset by smaller increases in adjusted operating costs, and the impact of the large ITC recovery recorded in the current year.

Absolute generated GAAP operating income of \$1.1 million in F2011, compared to an operating loss of \$4.4 million in F2010. A majority of the improvement in operating income F2011 relates to increased revenues as compared with F2010, offset primarily by the increase in the amortization of acquired intangible assets.

## **Other Income and Expenses**

Absolute earns interest income on its cash resources beyond immediate operating requirements. These cash balances are primarily invested in money market funds and investment grade bonds. In F2011, interest income was higher than F2010 at \$743,000 as compared to \$699,000, as a result of higher interest earned on cash equivalent balances due to increased risk-free interest rates.

Other expenses also include foreign exchange gains and losses incurred primarily on the translation of U.S. dollar cash, receivable and liability balances. U.S. denominated assets normally exceed liabilities as over 95% of sales are denominated in U.S. dollars, compared to approximately 40% of costs. This generally results in foreign exchange losses (gains) in periods where the U.S. dollar declines (appreciates) relative to the Canadian dollar. In F2011, the foreign exchange loss was \$1.8 million, consistent with the F2010 foreign exchange loss of \$1.8 million. The loss in the current year is primarily a result of the continued appreciation of the Canadian dollar compared to the U.S. dollar.

In F2011, we experienced a gain of \$287,000 on disposal of marketable securities. In F2010, as we were holding these and other securities and investments, we experienced a gain of \$98,000.

## **Income Taxes**

In F2011, we recorded current income tax expense of \$1.6 million and a future income tax recovery of \$0.1 million. In F2010, we recorded a current tax expense of \$1.3 million and a future income tax expense of \$1.5 million. In both years, our current tax expense was largely offset by Scientific Research and Development Investment Tax Credits claimed, which are presented as a reduction of operating expenses. In addition, in F2011, we recorded a reduction in our historical current tax payable upon the resolution of SRED ITC claims from past years. In F2011, our future income tax recovery is primarily attributable to the benefit of tax loss carryforwards, offset by the effect of the USD/CAD foreign exchange rate on our USD denominated future income tax assets. In F2010, our future income tax expense was primarily attributable to the effect of the USD/CAD foreign exchange rate on our USD denominated future income tax assets.

## **Net Income (Loss)**

The Company experienced a net loss in F2011 of \$1.1 million, as compared to a net loss of \$8.2 million in F2010. The improvement in net loss reflects the net impact of those factors discussed above with the changes in the operating and other income, and income tax expense.

The Company earned net income adjusted for Adjusted Operating Expenses of \$7.2 million in F2011, compared to a net loss adjusted for Adjusted Operating Expenses of \$3.3 million in F2010. The primary reason for this improvement is the improvement in the adjusted operating loss as noted above, the favorable variance in our investment gains and losses, and the changes in our net income tax expense and recovery.

## **Cash from Operating Activities**

In F2011, we recorded Cash from Operating Activities of \$12.5 million, an increase of 94% from \$6.4 million in F2010. The improved performance in the current year is the result of increases in Sales Contracts recorded in the current year while Adjusted Operating Expenses have not changed significantly from the prior year.

## **Liquidity and Capital Resources**

Absolute is in a strong financial position, with no debt and the financial resources necessary to fund its operating and capital requirements and to execute on its growth strategies. At June 30, 2011, Absolute's cash, cash equivalents and investments were \$53.8 million, compared to \$58.0 million at June 30, 2010. The Company's cash and investment position has changed as a result of contributions from positive operating cash flows and proceeds from stock option exercises and our employee share purchase plan, less our cash outlay of \$14.2 million related to our share buyback in F2011. Based on current sales and investment plans, management believes that the Company has sufficient capital resources to meet its growth and operating requirements.

The Company has no material individual capital expenditure commitments for fiscal 2011. Given our strong cash and investment balances and operating cash flow, at this time management does not believe we require any additional capital resources.

### *Accounts receivable*

Accounts receivable balances increased to \$15.6 million at June 30, 2011 (71% of Q4-F2011 Sales Contracts) from \$13.9 million at June 30, 2010 (72% of Q4-F2010 Sales Contracts). This increase is primarily due to higher Sales Contracts recorded in Q4-F2011 as compared to Q4-F2010, as a result of improved sales performance in the current year.

At June 30, 2011, 20% of the Company's accounts receivable balance was aged over 90 days as compared to 18% at June 30, 2010. At June 30, 2011, accounts receivable included two PC OEM partners that represented more than 10% of receivables, with one at 18% and the other at 29%. At June 30, 2010, the same two partners comprised 27% and 20%, respectively, of our total accounts receivable.

### *Accrued warranty*

Accrued warranty is related to a service guarantee with certain of our products. The accrued warranty decreased to \$8.7 million (8% of deferred Sales Contract revenue) at June 30, 2011, compared to \$9.2 million (9% of deferred Sales Contract revenue) at June 30, 2010. The reduction relative to F2010 as a percent of deferred revenue reflects warranty experience gains. Each period, management evaluates its guarantee payment experience and considers whether changes are required to the estimated warranty provision. In F2011, we determined that an adjustment of \$2.3 million was required in order to bring our warranty accrual in line with our estimates for future payments, as compared to a similar adjustment in F2010 of \$3.7 million.

### *Deferred revenue*

Deferred revenue was \$109.4 million at June 30, 2011, compared to \$102.8 million at June 30, 2010. Deferred revenue is comprised of the unamortized portion of deferred revenue from Sales Contracts, less the deferred portion of accrued warranty liabilities relating to the Sales Contracts. The deferred revenue balance is amortized to revenue, while the deferred warranty cost is amortized to cost of sales.

The deferred Sales Contract revenue component of deferred revenue increased to \$115.1 million at June 30, 2011, up 6% from \$108.5 million at June 30, 2010.

The scheduled recognition of deferred revenue is as follows:

(in millions)	<b>F2012</b>	<b>F2013</b>	<b>F2014</b>	<b>F2015</b>	<b>F2016</b>	<b>Total</b>
Revenue to be recognized	\$58.6	\$35.0	\$16.4	\$4.0	\$1.1	\$115.1
Subscriptions expiring	2.9	1.3	1.3	0.3	0.0	5.8

### *Future income tax assets and current taxes payable*

At June 30, 2011, we had no current taxes payable as our current tax expense is wholly offset by our expected claims for Scientific Research and Expenditure Investment Tax Credits ("ITC"s).

At June 30, 2011, we had total future income tax assets of \$20.4 million, which are primarily attributable to the future benefit of deferred revenue balances and operating loss carryforwards in our U.S. operations. Management believes these future income tax assets are more likely than not to be realized.

The Company operates in various tax jurisdictions, and accordingly, the Company's income is subject to varying rates of tax. Losses incurred in one jurisdiction cannot be used to offset income taxes payable in another. The Company's ability to use income tax losses and future income tax deductions is dependent upon the profitable operations of the Company in the tax jurisdictions in which such losses or deductions arise.

In assessing the valuation of future income tax assets, management considers whether it is more likely than not that some portion or all of the future income tax assets will be realized. The ultimate realization of future income tax assets is dependent upon the generation of future taxable income during the years in which the temporary differences are deductible. To the extent that management believes that the realization

of the future income tax assets does not meet the more likely than not realization criteria, a valuation allowance is recorded against the future tax assets.

## Accounting Changes adopted in F2011

*None.*

## Quarterly Operating Data

(in millions except per share data)	Q4-11	Q3-11	Q2-11	Q1-11	Q4-10	Q3-10	Q2-10	Q1-10
Sales Contracts <sup>(1)</sup>	\$22.1	\$17.2	\$17.9	\$21.9	\$19.3	\$15.0	\$16.1	\$19.2
Revenue	18.9	18.0	17.9	17.3	16.6	16.6	15.8	15.0
Adjusted Operating Income (Loss) <sup>(2)</sup>	4.0	3.4 <sup>(3)</sup>	1.7	0.3	(0.8)	1.9 <sup>(5)</sup>	(0.6)	(0.1)
Net Income (Loss)	0.5	1.1	(1.5)	(1.3)	(3.8) <sup>(4)</sup>	(0.0)	(2.3)	(2.0)
Basic and diluted income (loss) per share	0.01	0.03	(0.03)	(0.03)	(0.08)	(0.00)	(0.05)	(0.04)
Cash from Operating Activities	3.0	2.9	3.3	3.3	0.2	0.7	(5.6)	11.2
Operating cash per share (basic)	0.07	0.06	0.07	0.07	0.00	0.01	(0.12)	0.24

(1) Please refer to "Seasonality" section of this MD&A.

(2) Please refer to the "Non-GAAP Measures" section of this MD&A.

(3) Q3-11 results included the impact of a \$1.6 million ITC recovery.

(4) Q4-10 results included the impact of a \$2.1 million income tax expense.

(5) Q3-10 results included the impact of a \$1.1 million positive adjustment to warranty accrual.

## Fourth Quarter 2011 Performance Analysis

Absolute's strongest quarters tend to be the first and fourth quarter of each fiscal year, primarily due to strong activity in the education vertical during those quarters. The first fiscal quarter also benefits from increased consumer market activity related to students returning to school.

This seasonality trend continued in the fourth quarter of Fiscal 2011 ("Q4-F2011") relative to the third quarter, with Q4 Sales Contracts increasing 28% (30% in constant currency) to \$22.1 million.

Compared to the prior year, Sales Contracts for Q4-F2011 were up 14% from Q4-F2010, and were up 21% in constant currency. Consistent with the first three quarters of the fiscal year, the year over year increase reflects steady growth in our Computrace theft recovery products and accelerated growth in our non-theft recovery products, particularly Absolute Manage.

Q4-F2011 revenue of \$18.9 million increased 14% over \$16.6 million in Q4-F2010 and 5% over Q3-F2011, as a result of historical Sales Contracts and deferred revenue balances. Gross margin of 77% in Q4-F2011 was higher than the 73% gross margin in Q4-F2010 due primarily to the increased revenue as the cost of revenue in Q4-F2011 was consistent with the cost of revenue in Q4-F2010.

Absolute generated Adjusted Operating Income of \$4.0 million in Q4-F2011 as compared to an Adjusted Operating Loss of \$0.8 million in Q4-F2010. The improved adjusted operating results in F2011 are the result of a combination of increased revenue and lower Adjusted Operating Expenses.

In Q4-F2011, Absolute generated GAAP operating income of \$2.1 million, compared to an operating loss of \$2.7 million in Q4-F2010. The increased income compared to Q4-F2010 is due to the increased gross margin, as well as a significant decrease in sales and marketing expenses, largely due to the contraction of specific marketing programs in our consumer business.

The Company reported net income of \$0.5 million in Q4-F2011 (\$0.01 per share) compared to a net loss of \$3.8 million (\$0.08 per share) in Q4-F2010. The primary reason for this improvement is the increase in operating income as noted above, offset by a foreign exchange loss as compared to a foreign exchange gain in Q4-F2010, and the changes in our net income tax expense and recovery.

The Company reported positive Cash from Operating Activities of \$3.0 million, compared to \$0.2 million in Q4-F2010. The increase was expected due to increases in Sales Contracts while Adjusted Operating Expenses have been reduced.

### **Shareholders' Deficiency and Outstanding Share Data**

At June 30, 2011, Absolute had a shareholders' deficiency of \$13.2 million. In evaluating shareholders' deficiency, management believes it is important to consider the \$109.4 million of deferred revenue carried on the balance sheet. This amount represents prepaid (or due to be paid in full on payment terms) and non-refundable revenue, on which management expects to generate high margins when recognized in income, as much of the associated contract costs are already included in the operating deficit.

The Company's common shares trade on the TSX (TSX: ABT), and at June 30, 2011 the Company had 43,680,498 (August 18, 2011 – 43,337,300) fully issued and outstanding common shares. The following rights to receive common shares are issued and outstanding at June 30, 2011:

- Employee Share Option Plan: 4,725,951 (August 18, 2011 – 4,725,951) common stock options granted and outstanding. The options have a weighted average exercise price of \$4.55 per share, and a weighted average term to expiry of 2.9 years. In F2011, 1,249,300 employee stock options were granted at an average strike price of \$3.85.
- Employee Share Purchase Plan: Under the Plan, employees may purchase treasury shares at a 15% discount from market during two discrete six month offering periods each year. A total of two million shares have been reserved for grant under the Plan, of which 900,166 have been issued as at June 30, 2011 (August 18, 2011 – 993,668).
- Acquisition of LANrev: Pursuant to the terms of the LANrev purchase agreement, 333,334 common shares are to be issued to the selling shareholders prior to June 30, 2013.

## **Corporate Developments**

In F2011, Errol Olsen joined the Company as Chief Financial Officer, and Rob Chase transitioned to the role of Chief Operating Officer.

In addition, our Board of Directors welcomed Dan Ryan as a Board Member. Mr. Ryan is a seasoned executive with more than 25 years experience in the endpoint security and management industries. In order to enhance our corporate governance, the Board of Directors also appointed Ian Reid as Lead Director.

## **Critical Accounting Policies and Estimates**

Management considers the Company's accounting for Sales Contracts, deferred contract costs, warranty accruals and future tax assets to be critical accounting policies. An understanding of the accounting policies for these items is important for meaningful analysis of Absolute's business.

Sales Contracts represent invoiced sales for subscriptions to Absolute's services and software that are included in deferred revenue and amortized to revenue ratably over the contract term, commencing in the month after sale. A majority of Absolute's Sales Contracts are transacted via channel partners who purchase from Absolute in order to resell to their customers. While Absolute's services are provided directly to the end user customer, the orders come in various forms from reseller partners. Absolute ships the software if applicable, commences the subscription term, and invoices the reseller and reports this as a Sales Contract for the applicable period. Accordingly, Absolute relies upon the reseller partner to have sufficiently concluded the sales process with the end user customer to ensure that the order is valid and the risk of returns and/or reversals is kept to a minimum. These Sales Contracts are recorded as a receivable and deferred revenue item at period end (and not included in revenue at the time), and no estimates for returns, bad debts and reversals are made until such time as subsequent evidence suggests such an estimate is required.

Deferred contract costs represent expenses that are generated or incurred at the start of each service subscription (or Sales Contract) and are primarily comprised of prepaid employee sales commissions. These items are capitalized on the balance sheet as deferred contract costs, and are recognized as expense ratably over the contract term. Management estimates the benefit period of deferred costs to be equivalent to the contract term of the Sales Contract to which the expense relates. If management's estimate of the future value of such costs should change it could result in a significant write-down in the value of this deferred asset.

Warranty accruals require management estimates of the amount of warranty claims that will be paid over the life of each Sales Contract. The value of the accrued warranty estimate is capitalized as an offset to deferred revenue and is charged to cost of sales ratably over the contract term. Accrual estimates are established based on Absolute's experience with loss and recovery rates and are reviewed for reasonableness based on actual experience on a regular basis. However, actual experience will likely vary and may require a change in the estimated liability. Should these estimates change, they may require changes to the amount of warranty expense in future periods, in addition to a

change in the warranty accrual.

The Company has recognized future tax assets on the balance sheet. Each reporting period, management assesses the likelihood of realizing future tax assets. Where management considers that it is more likely than not that some portion or all of the future tax assets will be realized, the estimated realizable value of the future tax asset is recognized on the balance sheet. The net income or loss after income taxes can vary widely in periods where tax assets are recognized, and such variances could lead to a material write-down or increase in the estimated value of the Company's tax assets.

### **Contractual Commitments**

The Company's maintains operating leases for premises, and also has commitments under equipment and business service agreements, and a branding agreement. At June 30, 2011, the minimum payments under these commitments are as follows:

2012	\$ 1,783,773
2013	1,969,359
2014	1,761,837
2015	906,486
2016 and thereafter	186,267
	<u>\$ 6,607,722</u>

### **Off Balance Sheet Arrangements**

The Company has not entered into any off balance sheet arrangements other than standard office lease agreements.

### **Related Party Transactions**

None.

### **Subsequent Events**

Subsequent to June 30, 2011, through August 18, 2011, the Company has repurchased an additional 436,700 common shares under its Normal Course Issuer Bid for a total cost of \$1,726,290.

On July 18, 2011, 93,502 common shares were issued pursuant to the Purchase Plan.

### **Recent Canadian Accounting Pronouncements**

#### *Business Combinations*

In January 2009, the CICA issued Section 1582, "Business Combinations", Section 1601, "Consolidated Financial Statements", and Section 1602, "Non-controlling Interests". Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International

Financial Reporting Standards. Section 1582 is applicable for any business combinations with acquisition dates on or after July 1, 2011. Early adoption of this Section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company's interim and annual consolidated financial statements for its fiscal year beginning July 1, 2011. Early adoption of this Section is permitted. If the Company chooses to early adopt any one of these Sections, the other two sections must also be adopted at the same time. The Company does not expect the adoption of these standards will have a material impact on its consolidated financial statements.

#### *Multiple Deliverable Revenue Arrangements*

In December 2009, the CICA issued Emerging Issues Committee Abstract ("EIC") 175, "Multiple Deliverable Revenue Arrangements", replacing EIC 142, "Revenue Arrangements with Multiple Deliverables". This abstract was amended to (1) exclude from the application of the updated guidance those arrangements that would be accounted for in accordance with ASC 985-605 (formerly Financial Accounting Standards Board Statement of Position 97-2), "Software Revenue Recognition" as amended by Accounting Standards Update 2009-14; (2) provide updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and the consideration allocated; (3) require in situations where a vendor does not have vendor-specific objective evidence or third-party evidence of selling price, that the entity allocate revenue in an arrangement using estimated selling prices of deliverables; (4) eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method; and (5) require expanded qualitative and quantitative disclosures regarding significant judgments made in applying this guidance.

The accounting changes summarized in EIC 175 are effective for fiscal years beginning on or after January 1, 2011, with early adoption permitted. Adoption may either be on a prospective basis or by retrospective application. The Company does not believe the adoption of this standard will have a material impact on its consolidated financial statements.

#### *Adoption of International Financial Reporting Standards ("IFRS")*

The CICA plans has converged Canadian GAAP with IFRS , effective for fiscal years beginning on or after January 1, 2011. Our first annual financial statements required to be filed using IFRS are for the year ended June 30, 2012 (with comparative financial statements for fiscal 2011), and the Company's first interim financial statements filed under IFRS will be for the three months ended September 30, 2011. The International Accounting Standards Board continues to evolve IFRS, and as a result, the Company's accounting policies may change over time. The Company has substantially completed its assessment of the future impact of these existing standards on its consolidated financial statements, as outlined below under "Convergence with International Financial Reporting Standards".

## **Convergence with International Financial Reporting Standards**

In order to progress the key activities and meet the milestones necessary to convert from Canadian GAAP to IFRS, we developed a four-phase approach to transitioning to IFRS:

*Phase 1 – Initial assessment*

*Phase 2 – Detailed assessment*

*Phase 3 – Design*

*Phase 4 – Implementation*

Our preliminary assessment was completed during the year ended June 30, 2010, and consisted of identifying internal resources to complete IFRS conversion, ensuring the appropriate external resources were available, and completing a preliminary assessment of likely areas in which differences from Canadian GAAP will arise. Phase 2, *Detailed Assessment*, was substantially completed in the first half of F2011, and we now have an evaluation of and recommendations for appropriate accounting policy choices, and an evaluation of accounting changes required and opening balance sheet adjustments that will be required upon IFRS adoption.

In our MD&A for the year ended June 30, 2009, we presented a table summarizing the key activities and milestones required to convert to IFRS by July 1, 2011. We also provided a detailed discussion of our implementation plan and progress towards convergence with IFRS in our MD&A for the year ended June 30, 2010 and in our MD&A for each interim quarterly report of F2011. In our MD&A for the three and nine months ended March 31, 2011, we also discussed specific differences we had identified (which are also presented below). These documents are available at [www.sedar.com](http://www.sedar.com).

We are nearing completion of our IFRS transition project. The majority of the work identified in our implementation plan is complete, although work will continue throughout F2012 as we begin reporting our unaudited consolidated interim financial results for the year. We expect that we will have prepared preliminary comparative interim financial results for F2011 in accordance with IFRS by November 30, 2011. By that time, we expect our Audit Committee and our external auditors will review these comparative interim results and reconciliations to Canadian GAAP, together with the policy choices and elections that we have made as part of our convergence project.

Phase 2 – *Detailed Assessment* and Phase 3 – *Design* of our IFRS transition plan have helped us identify those areas that will be most significantly affected by our transition to IFRS. This assessment is based on currently enacted standards, available information and expectations as of the date of this MD&A. Accordingly, this should not be regarded as a complete list of changes that will result from our transition to IFRS. Rather, it is intended to highlight the areas we believe to be the most significant in respect of our consolidated financial statements. As we finalize the transition project, we will confirm additional changes.

As such, we have identified the following areas where IFRS adoption will significantly alter the Company's accounting policies and methodologies and the resulting form of its consolidated financial statements under IFRS:

- 1) **Share-based payments:** IFRS 2, "*Share-based Payments*", requires that each tranche of vesting stock options be valued separately using dissimilar assumptions in the Black-Scholes Option Pricing model, and further requires that each tranche is expensed over its vesting period. Currently, the Company values all options in a grant using the same set of Black-Scholes assumptions, and expenses the entire fair value over the vesting period of the options.

Upon adoption, the Company expects to claim the exemption available under IFRS 1, "*First Time Adoption of IFRS*", which will allow the Company to not revalue any stock options which were fully vested prior to the date of IFRS implementation.

We expect that upon IFRS adoption, we will be required to make an adjustment to account for the differences noted above. The effect of this adjustment will be increase our deficit and our contributed surplus, as previously unrecognized stock-based compensation will be required to be recognized. We expect the magnitude of this adjustment to be approximately \$5.5 million.

- 2) **The Effects of Changes in Foreign Exchange Rates:** IAS 21, "*The Effects of Changes in Foreign Exchange Rates*", prescribes accounting guidance surrounding transactions in foreign currencies, and how to include the results of foreign operations in an entity's financial statements.

In regards to foreign exchange translation of subsidiaries, Canadian GAAP requires an assessment of whether or not a subsidiary is integrated, or self-sustaining. IAS 21 does not include this type of assessment, rather, it requires the assessment of each entity's functional currency based on certain indicators.

Based on our preliminary evaluation, we expect that most of the companies in our group will be assessed as having the US dollar as their functional currency. Currently, our foreign exchange translations are performed in a method that would infer that the Canadian dollar is the functional currency of the entire group.

Based on this preliminary assessment, as we will be required to account for the majority of our entities using the US dollar as their functional currency, we expect that upon IFRS adoption we will begin to report our financial position and our results from operations using the US dollar as the reporting currency.

We are currently working through detailed calculations in order to determine the impact this change will have on our opening balance sheet as at the date of adoption of IFRS. We expect that we will provide an update as this assessment is completed prior to September 30, 2011.

- 3) **Income Taxes:** IAS 12, "*Income Taxes*", prescribes how to account for current and future income taxes.

IAS 12 requires that all deferred income tax assets are to be shown as long-term assets. Currently, we present a portion of our future income tax assets as current.

- 4) **Deferred Contract Costs:** IAS 38, "*Intangible Assets*", prescribes the definition of and method for accounting for intangible assets.

IAS 38 requires that assets qualify as intangible assets only if they are separable (capable of being separated from the entity and sold, transferred, or disposed of) or if they arise from contractual or legal rights.

Based on our evaluation, we do not believe that the deferred contract costs meet this definition. As such, we expect that upon IFRS adoption, we will be required to make an adjustment to remove these deferred contract costs. The effect of this adjustment will be to reduce the balance of the deferred contract costs and to increase our deficit. The amount of deferred contract costs to be removed at the date of adoption is \$7.8 million.

As noted above, we have substantially completed our accounting policy choices. Based on our assessment, we do not believe that any other exemption provisions available under IFRS 1 will be applicable to the Company.

As our policies and accounting methodologies have now been substantially finalized, we will develop the form of IFRS financial statements, to help ensure that data required to comply with the more extensive disclosures under IFRS will be adequately captured by our systems.

We have not yet prepared the 2010 comparative results for the full year under IFRS. This work will be completed prior to November 30, 2011, and may result in additional adjustments that have not been anticipated above. In addition, the IASB continues to update International Financial Reporting Standards. If any standards change prior to June 30, 2012, we will likely be required to apply such changes retrospectively to the date of transition (July 1, 2011), and any such changes may have a material impact on our financial statements. Although we have engaged our external auditors to review the preliminary comparative financial results under IFRS, a review does not involve the same level of analysis as an audit, and as such cannot be expected to identify all matters that may need to be addressed in order to fully comply with IFRS as enacted at June 30, 2011.

Other than the impact on our financial statements, the most significant aspect of the changeover to IFRS that we have identified is the need for significantly enhanced disclosure in the notes to the financial statements. Developing the form of the IFRS financial statements, as noted above, will help ensure that our accounting systems and procedures have been adequately modified to capture the incremental data required to be disclosed under IFRS.

Increased disclosure is not expected to have any material impact on our operations, but can reasonably be expected to impact our internal controls over financial reporting ("ICFR"), which we consider to include disclosure controls and procedures ("DCP"). Over the coming months, we may implement modifications to existing controls, as appropriate, to address the transition to IFRS. We expect to complete the

implementation and review of our ICFR under IFRS prior to issuing our first quarter financial results for F2012. Nevertheless, we may need to continue to review, modify and test our ICFR throughout F2012 as we complete the convergence project. We do not yet know whether such changes to our ICFR or DCP will constitute material changes under National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings.

We do not expect that our conversion to IFRS will materially impact our business activities, including our key performance metrics and compensation arrangements. As a large percentage of our variable compensation is related to Sales Contracts (as opposed to criteria measured under GAAP), we do not expect any changes in variable compensation arrangements to be substantive in nature. We will set our compensation targets during Q1-F2012 as a part of F2012 compensation planning and continued development of our internal performance objectives.

We have also considered the impact of the transition on our financial expertise. We designed and implemented training programs for our accounting staff, senior management and Audit Committee in order to ensure that we have appropriate financial reporting expertise for the preparation and review of financial statements under IFRS.

We expect the implementation phase of our conversion project to continue through F2012, although the majority of the work will be completed prior to the issuance of our consolidated interim financial results for the first quarter of 2011. We expect to meet all milestones in our project plan as we complete our conversion effort.

This information is provided to allow investors and others to obtain a better understanding of our IFRS changeover plan and the resulting possible effects on our financial statements and operations. Readers are cautioned, however, that it may not be appropriate to use such information for any other purpose. This information also 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.

## **Evaluation of Disclosure Controls and Internal Controls over Financial Reporting**

### *Disclosure controls and procedures*

The Company has disclosure controls and procedures in place that are designed to provide reasonable assurance that material information relating to Absolute is disclosed on a timely basis. Management has reviewed the Company's disclosure controls and concluded that they were effective during the reporting period.

The Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) have evaluated the effectiveness of the Company's disclosure controls and procedures related to the preparation of Management's discussion and analysis and the consolidated financial statements. They have concluded that the Company's disclosure controls and procedures were effective, at a reasonable assurance level, to ensure that material information relating to the Company and its consolidated subsidiaries would be made known to them by others within those entities, particularly during the period in which the Management's discussion and analysis and the consolidated financial statements contained in this report were being prepared.

### *Internal control over financial reporting*

The Company has also designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. Absolute's CEO and CFO have assessed the effectiveness of the Company's internal control over financial reporting as at June 30, 2011 in accordance with *Internal Control – Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, Absolute's CEO and CFO have determined that the Company's internal control over financial reporting is effective as at June 30, 2011 and expect to certify Absolute's annual filings with the Canadian securities regulatory authorities.

### *Changes in internal control over financial reporting*

There were no changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## Risks and Uncertainties

The Company is selling and developing products and services for new and emerging markets and, as a result, faces a number of risks, many of which are outlined below.

**Economic Uncertainty** - Many of Absolute's customers are being affected by economic conditions affecting the broader market. Current and future conditions in the domestic and global economies remain uncertain. As a result, it is difficult to estimate the level of growth or contraction for the economy as a whole. It is even more difficult to estimate growth or contraction in various parts, sectors and regions of the economy, including the markets in which the Company participates. Because all components of the Company's budgeting and forecasting are dependent upon estimates of growth or contraction in the markets it serves and demand for its products and services, the prevailing economic uncertainties render estimates of future income and expenditures very difficult to make. Adverse changes may occur as a result of soft economic conditions, wavering consumer confidence, unemployment, declines in stock markets, contraction of credit availability, declines in real estate values, or other factors affecting economic conditions generally. These changes may negatively affect the sales of the Company's products and services, including its ability to meet its internal targets for Cash from Operating Activities and Sales Contracts, and affect the Company's ability to retain key employees, or increase the exposure to losses from investments and bad debts.

**Ability to Predict Rate of Growth and Profitability** – Absolute focuses on sales growth and Cash from Operating Activities as its key performance metrics, and management believes that revenue and GAAP profitability will approach the Company's Cash Margins as the rate of growth slows. However, due to the evolving SaaS business model and the unpredictability of our emerging category of security, Absolute may not be able to accurately forecast the rate of adoption of its services and hence its sales growth. Absolute bases its current and future expense levels and its investment plans on estimates of future sales growth. Absolute may not be able to adjust its spending quickly enough if the rate of new or renewed subscriptions falls short of its expectations. As a result, Absolute's operating results may fluctuate significantly on a quarterly basis. In addition, Absolute's historic Sales Contract, revenue and cash flow growth rates may not be sustainable and may decline in the future. Accordingly, period-to-period comparisons of our operating results may not necessarily be a meaningful indicator of future performance.

**Dependence on Distribution Channels** – Absolute generates a substantial portion of its revenue through PC OEM channels and its sales strategy is built upon Absolute's ability to continue to maintain its BIOS position with these partners and grow its reseller channels. If unable to access end customers through its reseller channels, Absolute will have to change its sales strategy and may not be able to maintain sales or grow at the rates anticipated.

**Microsoft Operating Systems** – Absolute has designed the majority of its services to operate on certain generations of Microsoft Windows operating systems. The development by Microsoft of new versions of Windows and or upgrades or updates to Windows or other operating systems and or the market adoption of these or other operating systems developed by other vendors may have an adverse effect on Absolute's

business if the Company is not able to adapt its technology to be compatible with these new operating systems.

**Customer Subscription Renewal Rates** – Absolute generates more than 50% of its annual sales through purchases and subscription renewals from existing customers. Our customers’ renewal rates may decline or fluctuate as a result of a number of factors, including their level of satisfaction with the services and their ability to continue their operations and spending levels. If our customers do not renew their service subscriptions, our revenue will decline and our business will suffer.

**Foreign Exchange** – The Company’s reporting and functional currency is the Canadian dollar. However, substantially all the Company’s sales are denominated in U.S. dollars while a significant portion of operating expenses are denominated in Canadian dollars. As a result, the Company is exposed to fluctuations in the Canadian and U.S. dollar exchange rate for which it has not entered into foreign exchange hedges. Should the Canadian dollar significantly appreciate relative to the U.S. dollar, then it could impede Absolute’s ability to meet its internal Canadian dollar Sales Contract and Cash from Operating Activities growth and margin targets. The Company expects to begin reporting in U.S. dollars in F2012. See item 2, “The Effects of Changes in Foreign Exchange Rates” in the “*Convergence with International Financial Reporting Standards*” section of this MD&A.

**Breach of Security Measures and Unauthorized Access** – The Company’s service involves the storage and transmission of certain customer information, and security breaches could expose the Company to a risk of loss of this information, litigation and possible liability. Absolute’s technology and security measures have been designed and implemented in order to mitigate risks of this nature. However, if our security measures are breached as a result of third-party action, employee error, malfeasance or otherwise, during transfer of data to additional data centers or at any time, and, as a result, someone obtains unauthorized access to our data or our customers’ data, our reputation could be damaged, our business may suffer and Absolute could incur significant liability. The Company may be unable to anticipate new attack techniques or may not have sufficient time to implement adequate preventative measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and Absolute could lose sales and customers. In addition, our customers may authorize third party service providers to access their customer data. Because the control of these third-party service providers is undertaken by our customers, Absolute cannot ensure the complete integrity or security of such transmissions or processing.

**Intellectual Property Licensing and or Enforcement** – Absolute’s revenue, cost of sales, and expenses may suffer if it cannot continue to license or enforce our intellectual property rights or if third parties assert that Absolute violates their intellectual property rights. The Company relies upon patent, copyright, trademark and trade secret laws in the United States and similar laws in other countries, and agreements with employees, customers, suppliers and other parties, to establish and maintain intellectual property rights in its Computrace and Absolute Manage technology platforms. However, the industry in which the Company competes may include new or existing entrants that own, or claim to own, intellectual property, and the Company has received, and may receive in the future, assertions and claims from third parties that the Company’s products infringe

on their patents or other intellectual property rights (see “Patent Portfolio”). Litigation has been and will likely continue to be necessary to determine the scope, enforceability and validity of third-party proprietary rights or to establish the Company’s proprietary rights. Any of the Company’s direct or indirect intellectual property rights could be challenged, invalidated or circumvented, or such intellectual property rights may not be sufficient to permit Absolute to take advantage of current market trends or otherwise to provide competitive advantages, which could result in costly or delayed product redesign efforts, discontinuance of certain product offerings or other competitive harm. Further, the laws of certain countries do not protect proprietary rights to the same extent as the laws of the United States. Therefore, in certain jurisdictions Absolute may be unable to protect its proprietary technology adequately against unauthorized third-party copying or use, which could adversely affect its competitive position. Third parties also may claim that Absolute or customers or partners indemnified by Absolute are infringing upon their intellectual property rights. In recent years, individuals and groups have begun purchasing intellectual property assets for the sole purpose of making claims of infringement and attempting to extract settlements from established companies. Even if management believes that the claims are without merit, the claims can be time-consuming and costly to defend and divert management’s attention and resources away from the business. Claims of intellectual property infringement also might require Absolute to redesign affected products, enter into costly settlement or license agreements (if such licenses can be obtained on commercially reasonable terms, or at all) or pay costly damage awards, or face a temporary or permanent injunction prohibiting the marketing or selling certain of our products, which could result in the Company’s business, operating results and financial condition being materially adversely affected.

**Ability to Successfully Integrate Acquisitions** – We expect to continue to evaluate possible acquisitions of, or strategic investments in, businesses, products or technologies that are complementary to our business. In December 2009, we acquired certain assets of Pole Position Software GmbH, and in April 2010, we acquired certain technology assets of Phoenix Technologies Ltd. We may not realize future benefits from any of these past or future acquisitions. If we fail to integrate successfully our past and future acquisitions, or the technologies associated with such acquisitions, the revenue and operating results of the combined company could be adversely affected. Any integration process will require significant time and resources, and we may not be able to manage the process successfully. If our customers are uncertain about our ability to operate on a combined basis, they could delay or cancel orders for our products. We may not successfully evaluate or utilize the acquired technology and accurately forecast the financial impact of an acquisition transaction, including accounting charges. The areas where we may face risks include:

- difficulties in integrating the operations, technologies, products and personnel of the companies we acquire into our operations;
- potential disruption of our on-going business and diversion of management’s attention from normal daily operations of the business;
- insufficient revenues to offset increased expenses associated with acquisitions;
- potential for third party intellectual property infringement claims against the companies we acquire;
- failure to successfully further develop acquired technology, resulting in the

- impairment of amounts capitalized as intangible assets;
- impairment of relationships with customers and partners of the companies we acquire or in which we invest, or with our customers and partners, as a result of the integration of acquired operations;
- impairment of relationships with employees of the acquired companies or our existing employees as a result of integration of new management personnel;
- impact of known potential liabilities or unknown liabilities associated with the companies we acquire; and
- in the case of foreign acquisitions, uncertainty regarding foreign laws and regulations and difficulty integrating operations and systems as a result of cultural, systems and operational differences.

We are likely to experience similar risks in connection with our future acquisitions, if any. Our failure to be successful in addressing these risks or other problems encountered in connection with our past or future acquisitions could cause us to fail to realize the anticipated benefits of such acquisitions, incur unanticipated liabilities and adversely affect our business, operating results or financial condition, or result in significant or material control weaknesses.

Future acquisitions or dispositions could also result in dilutive issuances of our equity securities, a decrease in our cash and cash equivalents and short-term investments, the incurrence of additional expense related to compliance, contingent liabilities or amortization of expenses, or write-offs of goodwill, any of which could harm our financial condition and negatively impact our operating results.

**Competition** – Competition in the sector in which the Company operates is increasing. It is also possible that new competitors will enter the marketplace. Several potential competitors are marketing or have announced the development of computer products in direct competition with Absolute. In addition, as Absolute develops new services, the Company may begin competing against companies with whom it did not previously compete. Such competitors may be able to develop and expand their services more quickly, adapt more swiftly to new or emerging technologies and changes in customer requirements, take advantage of acquisition and other opportunities more readily, and devote greater resources to the marketing and sale of their services and products than Absolute. Accordingly, the entry of new competitors could have a material adverse effect on Absolute’s business, financial condition and results of operations.

**Emerging Products and Technology** – The market for Absolute’s products is still emerging and continued growth and demand for, and acceptance of, these products remains uncertain. In addition, other emerging technology and products may impact the viability of the market for Absolute’s products. Absolute’s continued success will depend upon its ability to keep pace with technological and marketplace change and to introduce, on a timely and cost-effective basis, new and enhanced products that satisfy changing customer requirements and achieve market acceptance. There can be no assurance that Absolute will be able to respond effectively to changes in technology or customer demands. Moreover, there can be no assurance that Absolute’s competitors will not develop competitive products or that any such products will not have an adverse effect upon Absolute’s business, financial condition or results of operations.

**Management of Growth** – In prior fiscal years, Absolute has experienced rapid sales growth and has been focused on continuing this growth trend. This has resulted in increasing headcount and operational costs to generate and support this growing customer base, which has placed, and will continue to place, to the extent that Absolute is able to sustain such growth, a significant strain on management, administrative, operational and financial infrastructure. Absolute anticipates that further growth will be required to address increases in the customer base and further development of the service, as well as expansion into new geographic areas. Further growth will require Absolute to continue to hire, train and manage new employees as needed. If new hires perform poorly, or if Absolute is unsuccessful in hiring, training, managing and integrating these new employees, or if Absolute is not successful in retaining existing employees, our business may be harmed. In addition, we may continue to expand our sales teams in an attempt to increase sales growth. Such sales growth may not match or exceed the increase of operations costs associated with such hiring, training, managing, and integrating of such employees.

**Litigation or Dispute Resolution** - From time to time, we may be subject to litigation or dispute resolution relating to any number or type of claims, including claims for damages related to undetected errors or malfunctions of our services and products, claims related to previously-completed acquisition transactions or claims relating to applicable securities laws. A product liability, patent infringement, acquisition-related or securities class action claim could seriously harm our business because of the costs of defending the lawsuit, diversion of employees' time and attention, and potential damage to our reputation. Further, our services and products are complex and often implemented by our customers to interact with third-party technology. Claims may be made against us for damages properly attributable to those third-party technologies, regardless of our lack of responsibility for any failure resulting in a loss. As a result, we could be required to pay substantial amounts of damages in settlement or upon the determination of any of these types of claims, and incur damage to the reputation of Absolute and our products. The likelihood of such claims and the amount of damages we may be required to pay may increase as our customers increasingly use our services and products. Our insurance may not cover potential claims, or may not be adequate to cover all costs incurred in defense of potential claims or to indemnify us for all liability that may be imposed.

**Cyclical Nature of our Business** - Our business may be impacted from time to time by the general cyclical and seasonal nature of PC and other device purchases by corporate and governmental entities. Factors which may create cyclical fluctuations include the development and adoption of new operating system software, the expiry of leases on devices or the introduction of newer or more advanced devices, legal and regulatory requirements, timing of contract renewals between our partners and their own customers and seasonal-based purchasing for educational institutions. Since some of our revenues from particular products and services are tied to the volume of shipments being processed, adverse fluctuations in the volume of global shipments may adversely affect our revenues. There can be no assurance that declines in shipment volumes in the US or internationally will not have a material adverse effect on our business.

**Volatility in our Share Price** - The trading price of our common shares has in the past been subject to wide fluctuations and may also be subject to fluctuation in the future. This may make it more difficult to resell common shares at times and prices that are attractive. Increases in our common share price may also increase our compensation expense pursuant to our existing director, officer and employee compensation arrangements. Fluctuations in our common share price may be caused by events unrelated to our operating performance and beyond our control. Factors that may contribute to fluctuations include, but are not limited to:

- Revenue or results of operations in any quarter failing to meet the expectations, published or otherwise, of the investment community;
- Changes in recommendations or financial estimates by industry or investment analysts;
- Changes in management or the composition of our board of directors;
- Outcomes of litigation or arbitration proceedings;
- Announcements of technological innovations or acquisitions by us or by our competitors;
- Introduction of new products or significant customer wins or losses by us or by our competitors;
- Developments with respect to our intellectual property rights or those of our competitors;
- Fluctuations in the share prices of other companies in the technology and emerging growth sectors;
- General market conditions; and
- Other risk factors set out in this report.

If the market price of our common shares drops significantly, shareholders could institute securities class action lawsuits against us, regardless of the merits of such claims. Such a lawsuit could cause us to incur substantial costs and could divert the time and attention of our management and other resources from our business.

**Reliance on Key Personnel** – Absolute’s future performance depends in part upon attracting and retaining key technical, sales and management personnel. There can be no assurance that Absolute can retain these personnel and continue to recruit required talent. The loss of the services of Absolute’s key employees could have a material adverse effect on Absolute’s business, operating results and financial condition.

**Efforts to Sell to Larger Enterprise Customers** – As Absolute targets more sales efforts at larger enterprise customers, the Company could face greater costs, longer sales cycles, less predictability in completing some sales and greater fluctuation in sales and cash flow in quarters where these large deals conclude. In this market segment, the customer’s decision to use Absolute’s service or products may be an enterprise-wide decision and, if so, these types of sales may require Absolute to provide greater levels of education regarding the use and benefits of the service, as well as education regarding privacy and data protection laws and regulations to prospective customers with international operations. As a result of these factors, these sales opportunities may require Absolute to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting sales and

professional services resources to a smaller number of larger transactions.

**Foreign Operations** – The Company intends to continue to pursue international market growth opportunities, which could result in international sales accounting for an increasing portion of the Company’s consolidated revenues. The Company intends to commit increased resources to its international operations as well as to related sales and marketing activities. The Company maintains offices in Canada, the U.S., the United Kingdom, and Germany. The Company may not be aware of all the factors that may affect its business in foreign jurisdictions. The Company will be subject to a number of risks associated with international business activities that may increase liability or costs, lengthen sales cycles or require significant management attention. International operations carry certain risks and associated costs, such as: the complexities and expense of administering a business abroad; complications in compliance with, and unexpected changes in legal and regulatory restrictions or requirements; foreign laws, international import and export legislation; language barriers and translation costs; trading and investment policies; foreign currency fluctuations; exchange controls; tariffs and other trade barriers; difficulties in collecting accounts receivable; potential adverse tax consequences; uncertainties of laws and enforcement relating to intellectual property and privacy rights; unauthorized copying of software; difficulty in managing a geographically dispersed workforce in compliance with diverse local laws and customs; difficulty in conducting theft recovery operations in foreign jurisdictions; and other factors depending upon the country involved. There can be no assurance that the Company will not experience these risks in the future. If foreign operations expand to the point where they account for a significant portion of the Company’s consolidated revenues, the presence of such risks could have a material adverse effect on the Company’s business, operating results and financial condition.

**Fluctuation of Quarterly Results and Failure to Meet the Expectations of Analysts or Investors** – Absolute’s quarterly operating results are likely to fluctuate, and if Absolute fails to meet or exceed the expectations of securities analysts or investors, the trading price of its common stock could decline. Moreover, the stock price may be based on expectations of Absolute’s future performance that may be unrealistic or that may not be met. Absolute believes that quarter-to-quarter comparisons of its results should not necessarily be relied upon as a reliable indicator of future performance.

**The Effect of Amortization of Revenue Over the Term of the Subscription** – Absolute generally recognizes revenue from customer subscriptions ratably over the terms of the Sales Contracts. The average term is approximately 27 months, although terms can range from one year to as much as five years. As a result, most of the revenue the Company reports in each quarter results from the recognition of deferred revenue relating to Sales Contracts entered into during previous periods. Consequently, a decline in new or renewal subscriptions in any one quarter will not necessarily be fully reflected in the revenue in that quarter but will negatively affect revenue in future quarters. In addition, Absolute may be unable to adjust its cost structure to reflect the changes in Sales Contracts. Accordingly, the effect of significant downturns in sales and market acceptance of the Company’s service or products may not be fully reflected in Absolute’s results of operations until future periods. The Company’s subscription model also makes it difficult to rapidly increase revenue through additional sales in any period, as revenue

from new customers must be deferred and recognized over the applicable subscription term.

**Sales Contracts** – Management considers Sales Contracts to be one of the key financial performance indicators for the Company. Most Sales Contracts (greater than 90%) are conducted via channel partners who purchase from Absolute in order to resell to their customers. While Absolute’s services are provided directly to the end user customer, the orders, which include ship dates, customer name, product, pricing and volume, come in various forms from the reseller partner (sales reports, purchase orders, shipping reports, royalty reports, etc.). Absolute ships the software, commences the subscription term, and invoices the reseller (and receives payment from the reseller) based on receipt of, or ship dates contained in, these forms of evidence of the end customer purchase, and reports this as a Sales Contract for the applicable period. Accordingly, Absolute is relying upon the reseller partner to have sufficiently concluded the sales process with the end user customer to ensure that the order is valid and the risk of returns is kept to a minimum. Historically, Absolute’s experience with returns has corroborated that this reliance is justified. However, it is possible that a reseller may order from us and subsequently return the product in accordance with generally accepted industry return practices. In such cases, if a sale had been reported in a prior period, it would have to be subsequently reversed, impacting future Sales Contracts and revenue performance. However, Absolute does not make a provision against Sales Contracts for potential returns for the following reasons: revenue recognition from Sales Contracts does not commence until the month after sale so there would be no income statement impact as a result of such provision; and the revenue recognition term averages approximately 27 months compared to industry standard return policies which are generally less than 90 days, so any returns are generally accounted for prior to any material recognition of revenue. Accordingly, the effect of any customer returns may not be fully reflected in Sales Contracts and deferred revenue figures until a future period.

**Product Errors and Third-Party Mischief** – The software technology enabling Absolute’s software services is complex and the related application software may contain errors or defects, especially when first introduced or when new versions are released. Any errors that are discovered after commercial release could result in loss of revenues or delay in market acceptance, diversion of development resources, damage to Absolute’s reputation, increased service and warranty costs and liability claims. In addition, it is possible that the Company’s product may become the subject of a third party attack or disruption, whether malicious or otherwise. This could detrimentally affect the persistence of the Company’s technology, which could have a material adverse effect on its business.

**Trends in Theft Rates and Theft Recovery Rates** – Absolute incurs significantly higher costs to service devices that are lost or stolen than to service devices that are merely tracked. When a tracked device is stolen, Absolute incurs additional costs to conduct a theft recovery operation. Some of our products include a service guarantee, where Absolute pays a portion of the original purchase price for the stolen device if a stolen device is not successfully recovered. If a theft recovery operation is not successful for a device with a service guarantee, we incur additional costs to pay out service guarantees to our customers.

Our pricing model depends on averaging our higher costs for stolen devices, and for the payment of service guarantees, across the entire population of devices tracked by Absolute. Absolute bases our estimates of theft and recovery rates on our historical performance. There can be no assurance that future theft and recovery rates will reflect historical theft and recovery rates, or that the theft and recovery rates in jurisdictions where we are expanding will be the same as the rates in the jurisdictions where we historically operated. If a larger percentage of tracked devices is stolen, our average cost per tracked device may increase and our profitability decline. Likewise, if a smaller percentage of devices tracked by Absolute is stolen, our average cost may decrease and our profitability increase.

**Operating Environment** – The Computrace software that enables Absolute’s product operates in a potentially hostile environment. In addition, Absolute’s Computrace services rely upon connection to the Absolute Monitoring Center. If the computer is prevented from making, or is not able to make, a connection, Absolute will not have an opportunity to assist in recovering the stolen computer. If Absolute is unable to successfully demonstrate to customers that the Computrace Agent will call in, it may affect Absolute’s ability to sell the its Computrace line of products.

**Interruptions or Delays in Service From Our Third-Party Hosting Facilities** – Absolute currently serves its customers from facilities that include a third-party hosting facilities located on the west coast of Canada and the U.S. Damage to, or failure of, our systems generally could result in interruptions in our service. Interruptions in our service may reduce our revenue, cause us to issue credits or pay penalties, cause customers to terminate their subscriptions and adversely affect our renewal rates and our ability to attract new customers. Our business will also be harmed if our customers and potential customers believe our service is unreliable.

As part of our current disaster recovery arrangements, redundant hardware is deployed where appropriate in production customer environments. Production data is backed up onto encrypted media and taken off-site. The recovery procedures and encryption keys are held remotely by Absolute employees, so that the systems can be restored in the event of a site-wide disaster. Other than contractual assurances and agreed-to controls, Absolute does not control the operation of any of these facilities, and they are vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunications failures and similar events. They may also be subject to break-ins, sabotage, intentional acts of vandalism and similar misconduct. Despite precautions taken at these facilities, the occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems at these facilities could result in lengthy interruptions in our service. Even with the disaster recovery arrangements, our service could be interrupted.

**Consumer Product Liability** – With the expansion of its consumer business, as with all manufacturers of products and services designed for use by consumers, the Company may be subject to claims related to product liability and consumer protection legislation, particularly in the U.S. Although the Company is insured for claims relating to product liability, no assurance can be given that a judgment will not be rendered against it in an amount exceeding the amount of insurance coverage or in respect of a claim for which the Company is not insured.

**Additional Patent Applications** – The Company’s commercial success depends upon its ability to develop new or improved technologies and products, and to successfully obtain patent or other proprietary or statutory protection for these technologies and products in Canada, the United States and other countries. The Company seeks to patent concepts, components, protocols and other inventions that are considered to have commercial value or that will likely yield a technological advantage. The Company owns rights to patented and patent pending technologies in the United States, Canada and other countries. However, the Company may not be able to develop new technology that is patentable, new patents may not be issued in connection with the Company’s pending applications and allowed claims may not be sufficient to protect the Company’s new technology. Furthermore, any patents issued could be challenged, invalidated or circumvented and may not provide proprietary protection or a competitive advantage. New entrants to the field may have been issued patents, and may have filed patent applications or may obtain additional patents and proprietary rights, for technologies similar to those that the Company has made or may make in the future. Since patent applications filed before November 29, 2000 in the United States are maintained in secrecy until issued as patents, and since publication or public awareness of new technologies often lags behind actual discoveries, the Company cannot be absolutely certain that it was the first to develop the technology covered by its pending patent applications or that it was the first to file patent applications for the technology. In addition, the disclosure in the Company’s new patent applications, particularly in respect of the utility of its claimed inventions, may not be sufficient to meet the statutory requirements for patentability in all cases. As a result, there can be no assurance that the Company’s new patent applications will result in enforceable patents, nor can the breadth of allowed claims in the Company’s patents, and their enforceability, be predicted. Even if the Company’s patents are held to be enforceable, others may be able to design around these patents or develop products similar to the Company’s products that are not within the scope of these patents, or the Company may lack the resources required to enforce its patents.

**Other Proprietary Rights** – In addition to patents, the Company relies on, among other things, copyrights, trademarks, trade secrets, confidentiality procedures and contractual provisions to protect its proprietary rights. While the Company enters into confidentiality and non-disclosure agreements with its employees, consultants, business partners, customers, potential customers and other third parties having access to proprietary and confidential information, it is possible that the following may occur: some or all of its confidentiality agreements will not be honored; third parties will independently develop equivalent technology or misappropriate the Company’s technology and/or designs; disputes will arise with the Company’s strategic partners, customers or others concerning the ownership of intellectual property; there may occur an unauthorized disclosure of source code, know-how or trade secrets, or contractual provisions may not be enforced in foreign jurisdictions. There can be no assurance that the Company will be successful in protecting its proprietary rights.

**Privacy Law Concerns** – Absolute’s customers use our service to transmit, receive and store identifying information regarding their mobile computing devices, including location information. Our products and monitoring systems are developed to ensure that components or tools that enable personal information to be obtained from host

computers are not resident in the products during normal use, and are only implemented by Absolute's trained experts in the case of emergency and on the instructions of our customers. While information obtained in normal usage is generally not of a personally identifiable nature, advances in location and tracking technology may evolve such that certain types of information collected in the tracking process could be considered to be personally identifiable information. Federal, provincial, state and foreign government bodies and agencies have adopted or are considering adopting laws and regulations regarding the collection, use and disclosure of personal information obtained from consumers and individuals and in certain jurisdictions, such laws may prohibit the use of our product in whole or in part. If our understanding of how such privacy laws apply to our business and that of our customers is incorrect, we may inadvertently breach those laws and negatively impact our business. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to the businesses of our customers may limit the use and adoption of our service and reduce overall demand for it. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our service in certain industries and jurisdictions.

**Development of Brand** – Absolute believes that developing and maintaining awareness of its proprietary and licensed brands in a cost-effective manner is critical to achieving widespread acceptance of its existing and future services and is an important element in attracting new customers. Furthermore, Absolute believes that the importance of brand recognition will increase if competition in our market develops or intensifies. Successful promotion of our brands will depend largely on the effectiveness of our marketing efforts and on our ability to provide reliable secure and useful services at competitive prices. If Absolute fails to successfully promote and maintain its brands, or incurs substantial expenses in an unsuccessful attempt to promote and maintain its brands, Absolute may fail to attract enough new customers or retain existing customers to the extent necessary to realize a sufficient return on brand-building efforts. Absolute also licenses the rights to use the name “LoJack” for our consumer products, and there is no assurance that we will continue to be able to do so on the same terms, or at all.

**Income Taxes** – Significant judgment is required in determining our provision for income taxes. Various internal and external factors may have favourable or unfavourable effects on our future provision for income taxes, income taxes payable, and/or effective income tax rate. These factors include, but are not limited to: changes in tax laws, regulations and/or rates; results of audits by tax authorities; changing interpretations of existing tax laws or regulations; changes in estimates of prior years' items; future levels of R&D spending; changes in the overall mix of income among the different jurisdictions in which we operate; and changes in overall levels of income before taxes. To the extent that the taxation authorities do not agree with our tax positions, we may not be able to realize all or a portion of the tax benefits recognized. Furthermore, new accounting pronouncements or new interpretations of existing accounting pronouncements (such as those described in “Recent Canadian Accounting Pronouncements” in this MD&A) can have a material impact on our effective income tax rate.

The Company and its subsidiaries file income tax returns and pay income taxes in jurisdictions where we believe we are subject to tax. In jurisdictions in which the Company and its subsidiaries do not believe we are subject to tax and therefore do not

file income tax returns, we can provide no certainty that tax authorities in those jurisdictions will not subject one or more tax years (since inception of the Company or its subsidiaries) to examination. Tax examinations are often complex as tax authorities may disagree with the treatment of items reported by the Company, the result of which could have a material adverse effect on our financial condition and results of operations.

**Securities Analysts** - The trading market for Absolute's common stock is in part affected by the research and reports that independent industry or financial analysts publish about Absolute or its business. Absolute does not control these analysts. If one or more of the analysts who publish reports on Absolute were to downgrade Absolute's stock or lower future stock price targets or estimates of operating results, Absolute's stock price could be adversely affected. Furthermore, if one or more of these analysts cease coverage of Absolute, Absolute could lose visibility in the market, which in turn could cause Absolute's stock price to decline.

# Independent Auditor's Report

To the Shareholders of Absolute Software Corporation

We have audited the accompanying consolidated financial statements of Absolute Software Corporation, which comprise the consolidated balance sheets as at June 30, 2011 and 2010 and the consolidated statements of operations and comprehensive loss, changes in shareholders' deficiency, 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.

## Auditor's 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 auditor's 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 auditor considers 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 Absolute Software Corporation as at June 30, 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.

*(signed)* "Deloitte & Touche, LLP"

Chartered Accountants  
Vancouver, British Columbia  
August 18, 2011

# ABSOLUTE SOFTWARE CORPORATION

## Consolidated Balance Sheets

June 30, 2011 and 2010

(Expressed in Canadian dollars)

	Notes	June 30, 2011	June 30, 2010
<b>ASSETS</b>			
<b>CURRENT</b>			
Cash and cash equivalents		<b>\$ 28,805,213</b>	\$ 28,078,851
Short-term investments	(Note 5)	<b>6,717,387</b>	6,420,210
Accounts receivable, net of allowance for doubtful accounts of \$1,409,000 (2010 - \$1,935,000)		<b>15,599,349</b>	13,888,239
Prepaid expenses and other		<b>1,541,225</b>	1,149,428
Current portion of deferred contract costs	(Note 6)	<b>4,392,364</b>	4,038,159
Current portion of future income tax assets	(Note 12)	<b>9,973,479</b>	9,904,709
		<b>67,029,017</b>	63,479,596
INVESTMENTS	(Note 5)	<b>18,234,407</b>	23,527,677
DEFERRED CONTRACT COSTS	(Note 6)	<b>3,840,284</b>	3,744,051
PROPERTY AND EQUIPMENT	(Note 7)	<b>2,114,704</b>	2,754,271
FUTURE INCOME TAX ASSETS	(Note 12)	<b>10,387,213</b>	10,308,983
INTANGIBLE ASSETS	(Note 8)	<b>15,061,026</b>	20,477,801
		<b>\$ 116,666,651</b>	<b>\$ 124,292,379</b>
<b>LIABILITIES</b>			
<b>CURRENT</b>			
Accounts payable and accrued liabilities		<b>\$ 8,456,941</b>	\$ 8,183,219
Income tax payable	(Note 12)	-	1,575,000
Current portion of acquisition payable	(Note 3)	<b>1,666,916</b>	1,728,607
Current portion of accrued warranty	(Note 9)	<b>4,457,446</b>	4,702,888
Current portion of deferred revenue, net	(Note 10)	<b>55,355,122</b>	52,411,595
		<b>69,936,425</b>	68,601,309
ACQUISITION PAYABLE	(Note 3)	<b>1,677,698</b>	3,457,214
ACCRUED WARRANTY	(Note 9)	<b>4,282,644</b>	4,518,461
DEFERRED REVENUE, NET	(Note 10)	<b>53,995,248</b>	50,346,988
		<b>129,892,015</b>	126,923,972
<b>COMMITMENTS</b>	(Note 17)		
<b>CONTINGENCIES</b>	(Note 18)		
<b>SHAREHOLDERS' DEFICIENCY</b>			
Share Capital	(Note 11(b))	<b>45,245,075</b>	44,888,407
Contributed Surplus		<b>30,925,971</b>	28,393,491
Deficit		<b>(89,396,410)</b>	(75,913,491)
		<b>(13,225,364)</b>	(2,631,593)
		<b>\$ 116,666,651</b>	<b>\$ 124,292,379</b>

See accompanying notes to the Consolidated Financial Statements.

Approved on behalf of the Board:

(signed) "John Livingston"  
John Livingston, Director

(signed) "J. Ian Giffen"  
J. Ian Giffen, Director

# ABSOLUTE SOFTWARE CORPORATION

## Consolidated Statements of Operations and Comprehensive Loss

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

	Notes	2011	2010
<b>REVENUE</b>		<b>\$ 72,198,733</b>	\$ 64,075,789
<b>COST OF REVENUE</b>		<b>18,891,474</b>	14,903,452
<b>GROSS MARGIN</b>		<b>53,307,259</b>	49,172,337
<b>OPERATING EXPENSES</b>			
Sales and marketing		<b>33,044,846</b>	34,669,371
Research and development		<b>11,641,015</b>	10,374,545
General and administration		<b>7,980,932</b>	7,707,016
Investment tax credits		<b>(3,208,000)</b>	(1,255,000)
Stock-based compensation	(Note 11)	<b>2,783,899</b>	2,085,977
		<b>52,242,692</b>	53,581,909
<b>OPERATING INCOME (LOSS)</b>		<b>1,064,567</b>	(4,409,572)
<b>OTHER EXPENSE</b>			
Interest income, net		<b>742,573</b>	699,239
Foreign exchange loss		<b>(1,756,078)</b>	(1,772,780)
Gain on investments	(Note 5)	<b>287,499</b>	98,134
		<b>(726,006)</b>	(975,407)
<b>NET INCOME (LOSS) BEFORE INCOME TAXES</b>		<b>338,561</b>	(5,384,979)
<b>INCOME TAX EXPENSE</b>	(Note 12)	<b>(1,486,000)</b>	(2,768,902)
<b>NET LOSS AND COMPREHENSIVE LOSS</b>		<b>\$ (1,147,439)</b>	\$ (8,153,881)
<b>BASIC AND DILUTED LOSS PER SHARE</b>		<b>\$ (0.03)</b>	\$ (0.18)
<b>WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING, BASIC AND DILUTED</b>	(Note 11(h))	<b>44,983,784</b>	46,346,964

See accompanying notes to the Consolidated Financial Statements.

# ABSOLUTE SOFTWARE CORPORATION

## Consolidated Statements of Changes in Shareholders' Deficiency

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

	Share Capital				Total
	Number of Common shares	Amount	Contributed Surplus	Deficit	
<b>BALANCE, JUNE 30, 2009</b>	<b>45,694,350</b>	<b>\$ 41,988,977</b>	<b>\$ 26,822,975</b>	<b>\$ (66,952,469)</b>	<b>\$ 1,859,483</b>
Shares issued on options exercised	741,552	1,659,071	(259,911)	-	1,399,160
Shares issued under Employee Share Purchase Plan	231,188	786,895	-	-	786,895
Shares repurchased and cancelled under the Normal Course Issuer Bid	(238,000)	(202,086)	-	(807,141)	(1,009,227)
Shares issued on warrants exercised	400,000	655,550	(255,550)	-	400,000
Stock-based compensation expense	-	-	2,085,977	-	2,085,977
Net loss	-	-	-	(8,153,881)	(8,153,881)
<b>BALANCE, JUNE 30, 2010</b>	<b>46,829,090</b>	<b>\$ 44,888,407</b>	<b>\$ 28,393,491</b>	<b>\$ (75,913,491)</b>	<b>\$ (2,631,593)</b>
Shares issued on options exercised	296,775	715,889	(251,419)	-	464,470
Shares issued under Employee Share Purchase Plan	184,987	619,934	-	-	619,934
Shares repurchased and cancelled under the Normal Course Issuer Bid	(3,797,020)	(1,855,822)	-	(12,335,480)	(14,191,302)
Shares issued on acquisition	166,667	876,667	-	-	876,667
Stock-based compensation expense	-	-	2,783,899	-	2,783,899
Net loss	-	-	-	(1,147,439)	(1,147,439)
<b>BALANCE, JUNE 30, 2011</b>	<b>43,680,498</b>	<b>\$ 45,245,075</b>	<b>\$ 30,925,971</b>	<b>\$ (89,396,410)</b>	<b>\$ (13,225,364)</b>

See accompanying Notes to the Consolidated Financial Statements.

# ABSOLUTE SOFTWARE CORPORATION

## Consolidated Statements of Cash Flows

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

	Notes	2011	2010
<b>OPERATING ACTIVITIES</b>			
Net loss		\$ (1,147,439)	\$ (8,153,881)
Items not involving cash			
Amortization of property and equipment		1,668,617	1,366,800
Amortization of intangible assets		5,579,118	2,737,602
Stock-based compensation	(Note 11)	2,783,899	2,085,977
Future income taxes	(Note 12)	(147,000)	1,513,902
Gain on investments	(Note 5)	(287,499)	(98,134)
Unrealized foreign exchange gain		(135,137)	-
Non-cash interest and amortization of investment premium		519,551	(670,295)
Change in non-cash working capital			
Accounts receivable		(819,407)	2,114,406
Prepaid expenses and other		(391,797)	(174,864)
Deferred contract costs		(450,438)	(406,549)
Accounts payable and accrued liabilities		808,181	1,636,073
Income tax payable	(Note 12)	(1,575,000)	-
Accrued warranty		(481,259)	(2,030,821)
Deferred revenue		6,591,789	6,521,658
<b>CASH FROM OPERATING ACTIVITIES</b>		<b>12,516,179</b>	<b>6,441,874</b>
<b>INVESTING ACTIVITIES</b>			
Purchase of property and equipment		(1,082,123)	(1,388,566)
Acquisition of LANrev	(Note 3)	(872,333)	(10,288,400)
Purchase of intangible assets	(Note 4)	(162,342)	(7,223,287)
Proceeds from maturities of short-term investments		6,428,986	8,685,644
Purchase of short-term investments		(712,708)	(5,468,009)
Proceeds from maturities of investments	(Note 5)	-	1,304,228
Purchase of investments		(909,306)	(20,881,249)
<b>CASH FROM (USED IN) INVESTING ACTIVITIES</b>		<b>2,690,174</b>	<b>(35,259,639)</b>
<b>FINANCING ACTIVITIES</b>			
Repurchase of common shares for cancellation	(Note 11(b))	(14,226,844)	(1,009,227)
Issuance of common shares	(Note 11(b))	1,084,405	2,586,055
<b>CASH (USED IN) FROM FINANCING ACTIVITIES</b>		<b>(13,142,439)</b>	<b>1,576,828</b>
FOREIGN EXCHANGE EFFECT ON CASH		(1,337,552)	(758,216)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		726,362	(27,999,153)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR		28,078,851	56,078,004
CASH AND CASH EQUIVALENTS, END OF YEAR		\$ 28,805,213	\$ 28,078,851

### SUPPLEMENTAL CASH FLOW INFORMATION (NOTE 14)

See accompanying notes to the Consolidated Financial Statements.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 1. NATURE OF OPERATIONS

Absolute Software Corporation (the “Company”) was incorporated under the Company Act (British Columbia) on November 24, 1993. The Company’s principal business activities are the development, marketing, and support of computer security and end-point management services and products. All of the Company’s services and products are powered by its proprietary and patented Computrace and Absolute Manage software systems. The Company markets its services and products through computer original equipment manufacturers (“OEMs”), distributors, value added resellers, and directly to its customers, who include corporations, government entities, educational institutions, and consumers. While the Company’s products are available internationally through resellers in Europe, Australia, South Africa, South America, and the Asia Pacific region, the majority of its sales are generated in North America. The Company trades on the TSX under the symbol ABT.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### (a) *Basis of presentation*

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). The consolidated financial statements include the accounts of Absolute Software Corporation and its wholly owned subsidiaries, Absolute Software Inc. (U.S.), Absolute Software EMEA Ltd. (U.K.), Absolute Technology GmbH (Germany), Absolute Software K.K. (Japan), Absolute Software (Asia) Pte. Ltd. (Singapore), Computer Recovery, Inc. (U.S.), and 609713 B.C. Limited. All intercompany balances and transactions have been eliminated upon consolidation.

#### (b) *Significant Accounting Policies*

##### *Use of estimates*

The preparation of financial statements in conformity with GAAP requires the Company’s management to make estimates and assumptions that affect the amounts reported in the financial statements and related notes to the financial statements. Significant estimates are used in determining, but are not limited to, the assessment of the carrying values of allowances for unrecoverable accounts receivable and long-lived assets, and the valuation of stock-based compensation, warrants, accrued warranty liabilities, future income tax assets, and the fair value of assets and liabilities acquired in business combinations and asset acquisitions. Actual results could differ from those estimates.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### *Foreign currency transactions and translation*

The Company's functional currency is the Canadian dollar. Transaction amounts denominated in foreign currencies are translated into Canadian dollars at exchange rates prevailing at the time of the transaction. Carrying values of monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rate of exchange in effect at the balance sheet date with any resulting gain or loss being reflected in the statement of operations.

The operations of integrated subsidiaries not reporting in Canadian dollars are translated into Canadian dollars using the temporal method. Under this method, monetary assets and liabilities of foreign subsidiaries are translated at exchange rates in effect at the end of each period and non-monetary assets and liabilities are translated using historical exchange rates. Revenues and expenses are translated at the average exchange rate for the period, which approximates rates in effect on the date of the transaction. Foreign currency translation gains and losses are included in the statement of operations.

#### *Financial Instruments*

The Company's classification and measurement basis of its financial instruments are as follows:

<b>Instrument</b>	<b>Classification</b>	<b>Measurement Basis</b>
Cash and cash equivalents	Held for trading	Fair value
Short-term investments – <i>interest-bearing securities</i>	Held to maturity	Amortized cost
Short-term investments – <i>marketable securities</i>	Held for trading	Fair value
Accounts receivable	Loans and receivables	Amortized cost
Investments – <i>interest-bearing securities</i>	Held to maturity	Amortized cost
Investments – <i>Replacement Notes</i>	Held for trading	Fair value
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Acquisition payable	Other liabilities	Amortized cost
Accrued warranty	Other liabilities	Amortized cost

Changes in items carried at fair value are recorded in the statement of operations. All amounts carried at amortized cost are calculated using the effective interest rate method.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Company assesses declines in the value of individual held-to-maturity investments for impairment to determine whether the decline is other-than-temporary, in which case the investment is written down and the resulting loss recorded in the statement of operations.

The Company classifies and discloses fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 – Valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 – Valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

#### *Cash and cash equivalents*

Cash and cash equivalents consist of cash on deposit and highly liquid short-term interest-bearing securities with maturities at the date of purchase of three months or less.

#### *Short-term investments and investments*

Short-term investments consist of highly liquid short-term interest bearing securities with maturities at the date of purchase of greater than three months, but less than one year, and of other marketable securities.

Investments consist of highly liquid interest bearing securities with maturities at the date of purchase of greater than one year and of long-term notes (“Replacement Notes”) issued in exchange for illiquid non-bank Asset Backed Commercial Paper.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### *Deferred contract costs*

The Company sells fixed-length service contracts (“Sales Contracts”) with monitoring and theft recovery terms ranging from one to five years. Sales commissions directly associated with Sales Contracts are deferred and amortized ratably to sales and marketing over the contract term in the statement of operations.

#### *Property and equipment*

Property and equipment are carried at cost less accumulated amortization. Amortization is calculated using the straight line method from the month of purchase over the following estimated useful lives:

<b>Asset</b>	
Computer equipment	3 years
Furniture and equipment	5 years
Computer software	1 year
Office equipment	3 years
Trade show equipment	2 years
Leasehold improvements	Term of the lease

Property and equipment are reviewed for impairment when events or changes in circumstances indicate that their carrying value may not be recovered. If estimates of future cash flows expected to result from the use of the asset are less than the carrying value, then the carrying value is written down to its fair value, based on the related estimated discounted future cash flows. No impairments have been recognized to date.

#### *Intangible assets*

Intangible assets acquired in business combinations and pursuant to asset purchases are recorded at their fair values. Intangible assets related to brand acquisition rights are recorded at fair values, based on the Black-Scholes fair value attributable to common share purchase warrants issued in order to acquire the asset. All the Company’s intangible assets have finite useful lives and are amortized using the straight line method over the following estimated useful lives:

<b>Asset</b>	
Acquired software – LANrev (Note 3)	5 years
Customer relationships – LANrev (Note 3)	5 years
Acquired software – FailSafe and Freeze (Note 4)	3 years
Acquired brand – LoJack warrants	5 years

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Intangible assets are reviewed for impairment when events or changes in circumstances indicate that their carrying value may not be recovered. If estimates of future cash flows expected to result from the use of the asset are less than the carrying value, then the carrying value is written down to its fair value, based on the related estimated discounted future cash flows. No impairments have been recognized to date.

#### *Future income tax assets and income taxes*

The Company follows the asset and liability method for accounting for income taxes. Under this method, future income taxes are recognized for the future income tax consequences attributable to loss carryforwards and to differences between the financial statement carrying values of existing assets and liabilities and their respective income tax bases (temporary differences). Changes in the net future tax asset or liability are included in the statement of operations.

Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in tax rates is included in income in the period that includes the substantive enactment date. Future income tax assets are periodically evaluated and if realization is not considered more likely than not, a valuation allowance is provided for all or a portion of the value.

#### *Revenue recognition*

The Company sells services and products including computer theft recovery, secure asset tracking, and end-point management. Revenues are recognized when a contractual arrangement is in place, the fee is fixed and determinable, the services and products have been delivered, and collectability is reasonably assured. Amounts invoiced but not yet earned are recorded as deferred revenue.

The Company's principal source of revenue results from Sales Contracts for the above services, with subscription terms ranging from one to five years. The full value of each Sales Contract is invoiced and receivable upon execution of the contract, delivery of the products and initiation of the services. Typically, Sales Contracts are comprised of multiple elements, including software, monitoring, theft recovery, and maintenance and support services over the term, which are not separable for accounting purposes. As a result, revenue from Sales Contracts is recognized ratably over the subscription term. Direct costs associated with Sales Contracts are deferred and amortized over the same period (see "Deferred Contract Costs" above).

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Company obtains the majority of its Sales Contracts through OEM and reseller partners, the majority of which are in North America. All Sales Contracts are recorded at the net sale amount received by Absolute from the reseller, provided that all significant contractual obligations have been satisfied and collection is reasonably assured. For direct sales, the Sales Contract is recorded at the sale amount received from the customer.

Deferred revenue is comprised of the remaining unamortized balance of Sales Contracts sold, net of the related deferred warranty costs (see “Accrued Warranty and Guarantee” below).

#### *Accrued warranty and guarantee*

The Company provides a service guarantee, or warranty, on certain of its theft recovery offerings. The warranty is not separately sold, nor charged, but forms part of the product offering to which it is attached, and accordingly has a term matching that of the product offering. If a computer equipped with a product that includes the recovery guarantee is stolen, and the Company is unable to either recover the stolen computer, or delete data on it, then the customer may be eligible for a guarantee payment of up to \$1,000. In order to qualify for the warranty, the customer must comply with the Company’s terms and conditions included in its End User Service Agreement, including the filing of a police report amongst other criteria. The amount of the eligible warranty payment decreases in each year of the service contract and is also limited by the value of the stolen computer.

This service guarantee is accounted for as a warranty liability, and is recorded at the time the related Sales Contract is signed based on the amount of estimated costs that will be incurred under the guarantee. The warranty liability is estimated based on a number of factors, including historical warranty experience, and computer theft and theft recovery rates. The liability balance is drawn down by service guarantee payments issued, and is adjusted on a periodic basis for changes in future estimated warranty payment rates and actual historic experience.

The initial warranty expense is deferred and offset against deferred revenue and is amortized ratably to cost of sales over the contract term in the statement of operations. Periodic adjustments related to unamortized warranty costs are recorded in deferred revenue, with the remainder recorded directly in cost of sales.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### *Research and development costs*

Research and development activities are separated into a research phase and a development phase when feasible. Research costs are charged to operations when they are incurred. Development costs are capitalized as intangible assets when the Company can demonstrate that the technical feasibility of the project has been established; the Company intends to complete the asset for use or sale and has the ability to do so; the asset can generate probable future economic benefits; that technical and financial resources are available to complete the development; and the Company can reliably measure the expenditure attributable to the intangible asset during its development. At June 30, 2011, the Company has not capitalized any development costs.

#### *Stock-based compensation plans*

The Company has a stock option plan and an employee share purchase plan, which are described in Notes 11(c) and 11(d). When stock or stock options are issued to employees, the Company records the estimated fair value of the stock-based awards as compensation expense over the vesting period with a corresponding credit to contributed surplus. Upon exercise of stock options or purchase of common shares, any consideration paid by employees, together with the amount previously recorded in contributed surplus, is credited to share capital.

Under the employee share purchase plan, the stock-based compensation charge is determined by the difference between the share purchase price and market price at the start of each purchase period.

#### *Loss per share*

Basic loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period. Diluted loss per share is equal to basic loss per share. Diluted earnings per share is calculated using the treasury stock method, which assumes that cash that would be received on the exercise of stock options or warrants is applied to purchase shares at the average price during the year. The difference between the shares issued on the exercise of the stock options or warrants and the number of shares purchased under this computation, on a weighted average basis, is added to the number of shares outstanding. Anti-dilutive stock options are not considered in computing diluted earnings per share. Stock options and warrants are typically dilutive when the Company has income for the year and the average market price of the common shares during the year exceeds the exercise price of the options and warrants.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) *Comparative financial information*

Certain costs previously allocated to cost of revenue and sales and marketing are now reported in research and development. This reclassification had the following impact:

	<u>Year ended June 30, 2010</u>
<b>Cost of revenue</b>	
As originally reported	\$ 15,709,686
As recast	\$ 14,903,452
<b>Sales and marketing</b>	
As originally reported	\$ 36,205,179
As recast	\$ 34,669,371
<b>Research and development</b>	
As originally reported	\$ 8,032,503
As recast	\$ 10,374,545

In addition, the Company has reclassified immaterial errors in its consolidated statements of cash flows for the year ended June 30, 2010, related to the classification of the effect of foreign exchange rate changes on non-cash working capital, and cash and cash equivalents. The reclassification moved the foreign exchange impact from affected non-cash working capital balances to be presented as "Foreign Exchange Effect on Cash". In addition, certain immaterial non-cash investing activities (Note 14) have been reclassified in the consolidated statement of cash flows. As a result of these reclassifications, there was no impact on the previously reported net change in cash and cash equivalents, net loss, net loss per common share, or financial position for the year ended June 30, 2010. These reclassifications had the following impact:

	<u>Year ended June 30, 2010</u>
<b>Cash from operating activities</b>	
As originally reported	\$ 6,425,183
As recast	\$ 6,441,874
<b>Cash used in investing activities</b>	
As originally reported	\$ (36,001,164)
As recast	\$ (35,259,639)

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### (d) *Adoption of Future Accounting Standards*

In January 2009, the CICA issued Section 1582, “*Business Combinations*”, Section 1601, “*Consolidated Financial Statements*”, and Section 1602, “*Non-controlling Interests*”. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International Financial Reporting Standards. Section 1582 is applicable for any business combinations with acquisition dates on or after July 1, 2011. Early adoption of this Section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company’s interim and annual consolidated financial statements for its fiscal year beginning July 1, 2011. Early adoption of this Section is permitted. If the Company chooses to early adopt any one of these Sections, the other two sections must also be adopted at the same time. The Company does not expect the adoption of these standards will have a material impact on its consolidated financial statements.

In December 2009, the CICA issued Emerging Issues Committee Abstract (“EIC”) 175, “*Multiple Deliverable Revenue Arrangements*”, replacing EIC 142, “*Revenue Arrangements with Multiple Deliverables*”. This abstract was amended to (1) exclude from the application of the updated guidance those arrangements that would be accounted for in accordance with ASC 985-605 (formerly Financial Accounting Standards Board Statement of Position 97-2), “*Software Revenue Recognition*” as amended by Accounting Standards Update 2009-14; (2) provide updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and the consideration allocated; (3) require in situations where a vendor does not have vendor-specific objective evidence or third-party evidence of selling price, that the entity allocate revenue in an arrangement using estimated selling prices of deliverables; (4) eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method; and (5) require expanded qualitative and quantitative disclosures regarding significant judgments made in applying this guidance.

The accounting changes summarized in EIC 175 are effective for fiscal years beginning on or after January 1, 2011, with early adoption permitted. Adoption may either be on a prospective basis or by retrospective application. The Company does not believe the adoption of this standard will have a material impact on its consolidated financial statements.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 3. ACQUISITION OF LANREV

On December 2, 2009, the Company acquired certain assets and operations of Pole Position Software GmbH, a software company specializing in end-point and systems management software. Pole Position's sole product was LANrev ("LANrev"), a comprehensive, cross-platform end-point and computer asset management software solution.

The purchase of the assets was accounted for as a business combination, with the Company being identified as the acquirer. The results of the acquired LANrev business were included in the Company's results of operations from the purchase date of December 2, 2009.

The aggregate purchase price of \$15,474,221 was comprised of cash and 500,000 common shares of the Company, as follows:

Cash	\$ 12,624,043
Common shares	2,630,000
Acquisition costs	<u>220,178</u>
	<u>\$ 15,474,221</u>

Of the above, \$2,555,821 (USD \$2,500,000) and the 500,000 common shares were deferred consideration, with each amount payable in equal one-third installments annually on the first three anniversary dates of the acquisition. The fair value of the common shares to be issued of \$5.26 was determined based on the average closing price of the Company's common shares for a reasonable period prior to and following the acquisition date of December 2, 2009. The deferred amount payable in cash was discounted to present value using a discounted cash flow model.

The total purchase consideration was allocated to the fair values of the assets acquired and liabilities assumed based on management's best estimates and taking into account all available information at the time of the acquisition. The purchase consideration was allocated to the net assets acquired as follows:

Property and equipment	\$ 16,998
Intangible assets	15,864,341
Accrued liabilities	(26,801)
Deferred revenue	<u>(380,317)</u>
	<u>\$ 15,474,221</u>

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 3. ACQUISITION OF LANREV (Continued)

Details of the acquired intangible assets are as follows:

Acquired software	\$ 15,370,880
Customer relationships	493,461
	<u>\$ 15,864,341</u>

These intangible assets were each determined to have a useful life of 5 years.

The Company's Acquisition Payable is comprised of:

Amount payable in cash	\$ 1,607,501
Amount payable in common shares	1,753,334
	<u>3,360,835</u>
Amount representing interest at 1.4%	16,221
	<u>3,344,614</u>
Less: current portion	(1,666,916)
	<u>\$ 1,677,698</u>

### 4. ASSET ACQUISITION

On April 7, 2010, the Company acquired the technology assets of the FailSafe® and Phoenix Freeze™ products from Phoenix Technologies Ltd. Under the terms of the asset purchase agreement, the Company paid \$6,894,250 (US\$6,875,000) in cash for the acquired assets.

The aggregate purchase consideration of \$7,223,287 was comprised of the following:

Cash	\$ 6,894,250
Acquisition costs	329,037
	<u>\$ 7,223,287</u>

The total purchase consideration has been allocated to the fair value of the intangible assets acquired, which consist of acquired software, based on management's best estimates and taking into account all available information at the time of the acquisition.

These intangible assets were determined to have a useful life of 3 years.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 5. SHORT-TERM INVESTMENTS AND INVESTMENTS

The Company's short-term investments are comprised of the following:

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Term deposits	\$ 675,979	\$ 5,367,315
Investment grade securities	6,041,408	129,726
Marketable securities	-	923,169
	<u>\$ 6,717,387</u>	<u>\$ 6,420,210</u>

During 2011, the Company disposed of its marketable securities for total proceeds of \$1,183,631. At the date of disposal, these marketable securities had a cost of \$2,434,037, offset by an unrealized loss of \$1,537,340 (June 30, 2010 - \$1,510,868), for a net amount of \$896,697 (June 30, 2010 - \$923,169).

At June 30, 2011 and 2010, the Company's long-term investments are comprised entirely of investment grade securities.

The Company's gain on investments is comprised of the following:

	<u>2011</u>	<u>2010</u>
Realized gain on marketable securities	\$ 286,934	\$ -
Realized gain on Replacement Notes	-	320,114
Unrealized gain (loss) on marketable securities	565	(221,980)
	<u>\$ 287,499</u>	<u>\$ 98,134</u>

### 6. DEFERRED CONTRACT COSTS

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Sales commissions	8,093,592	\$ 7,618,590
Other prepaid contract costs	139,056	163,620
	<u>8,232,648</u>	<u>7,782,210</u>
Less: current portion	(4,392,364)	(4,038,159)
	<u>\$ 3,840,284</u>	<u>\$ 3,744,051</u>

**ABSOLUTE SOFTWARE CORPORATION**  
**Notes to the Consolidated Financial Statements**

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

**7. PROPERTY AND EQUIPMENT**

	<b>June 30, 2011</b>		
	Cost	Accumulated Amortization	Net Book Value
Computer equipment	\$ 5,309,343	\$ 4,258,302	\$ 1,051,041
Furniture and equipment	1,321,343	1,023,171	298,172
Computer software	1,964,955	1,869,386	95,569
Office equipment	1,655,612	1,137,729	517,883
Trade show equipment	94,566	94,247	319
Leasehold improvements	600,999	449,279	151,720
	<b>\$ 10,946,818</b>	<b>\$ 8,832,114</b>	<b>\$ 2,114,704</b>

  

	June 30, 2010		
	Cost	Accumulated Amortization	Net Book Value
Computer equipment	\$ 4,677,327	\$ 3,235,675	\$ 1,441,652
Furniture and equipment	1,318,194	896,910	421,284
Computer software	1,803,621	1,739,553	64,068
Office equipment	1,316,380	731,003	585,377
Trade show equipment	94,566	86,786	7,780
Leasehold improvements	600,999	366,889	234,110
	<b>\$ 9,811,087</b>	<b>\$ 7,056,816</b>	<b>\$ 2,754,271</b>

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

### 8. INTANGIBLE ASSETS

During 2006, the Company acquired the worldwide rights to brand its consumer offering “LoJack for Laptops” for a 10 year period ending June 30, 2015. In addition to an annual and per unit royalty, the Company issued 1,000,000 common share purchase warrants to LoJack Operating Company L.P. The fair value of the warrants was calculated using the Black-Scholes option pricing model in the amount of \$638,873, and accordingly, this amount was recorded as an intangible asset (Note 11(g)). In addition, in 2011, the Company acquired certain patents for a total cost of \$162,342.

The Company’s other intangible assets relate to the acquisitions of LANrev (Note 3) and FailSafe® and Phoenix Freeze™ (Note 4).

	<b>June 30, 2011</b>		
	Cost	Accumulated Amortization	Net Book Value
Acquired software – LANrev	\$ 15,371,104	\$ 5,002,455	\$ 10,368,649
Customer relationships – LANrev	493,238	143,387	349,851
Acquired software – FailSafe and Freeze	7,223,287	3,015,536	4,207,751
Acquired patents	162,342	27,567	134,775
Acquired brand rights – LoJack warrants	638,873	638,873	-
	<b>\$ 23,888,844</b>	<b>\$ 8,827,818</b>	<b>\$ 15,061,026</b>

	<b>June 30, 2010</b>		
	Cost	Accumulated Amortization	Net Book Value
Acquired software – LANrev	\$ 15,370,880	\$ 1,967,728	\$ 13,403,152
Customer relationships – LANrev	493,461	40,992	452,469
Acquired software – FailSafe and Freeze	7,223,287	601,107	6,622,180
Acquired brand rights – LoJack warrants	638,873	638,873	-
	<b>\$ 23,726,501</b>	<b>\$ 3,248,700</b>	<b>\$ 20,477,801</b>

During 2011, the Company recorded amortization of intangible assets of \$5,579,118 (2010 - \$2,737,602).

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 9. ACCRUED WARRANTY AND GUARANTEE

The following table summarizes changes in the accrued warranty for the years ended June 30, 2011 and 2010:

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Balance, beginning of year	\$ 9,221,349	\$ 11,252,170
Warranty accrual on new sales contracts	4,003,611	4,038,686
Changes in previous estimates	(2,299,542)	(3,748,796)
Guarantee payments	(2,185,328)	(2,320,711)
Balance, end of year	<u>8,740,090</u>	<u>9,221,349</u>
Less: current portion	(4,457,446)	(4,702,888)
	<u>\$ 4,282,644</u>	<u>\$ 4,518,461</u>

### 10. DEFERRED REVENUE

The following table provides a reconciliation of deferred revenue balances on sales contracts to invoiced Sales Contracts, revenue, and other adjustments:

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Balance, beginning of year	\$ 108,458,988	\$ 103,210,166
Sales contracts	79,128,643	69,682,056
Acquired from LANrev (note 3)	-	380,317
Revenue recognized	(72,198,733)	(64,075,789)
Other adjustments	(324,598)	(737,762)
Balance, end of year	<u>\$ 115,064,300</u>	<u>\$ 108,458,988</u>

The following table provides a breakdown of the net deferred revenue balances at June 30, 2011 and 2010:

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Deferred revenue	\$ 115,064,300	\$ 108,458,988
Deferred warranty costs	(5,713,930)	(5,700,405)
	<u>109,350,370</u>	<u>102,758,583</u>
Less: current portion	(55,355,122)	(52,411,595)
	<u>\$ 53,995,248</u>	<u>\$ 50,346,988</u>

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 11. SHARE CAPITAL

#### (a) Authorized

100,000,000 common shares, no par value  
20,000,000 preferred shares, Series A, voting, convertible, redeemable

#### (b) Issued and outstanding

During the year ended June 30, 2011, the Company issued 296,775 common shares on exercise of employee stock options for total proceeds of \$464,470. An amount of \$251,419 related to the original fair value of the options was transferred from contributed surplus to common shares upon exercise.

During the year ended June 30, 2011, the Company issued 184,987 common shares pursuant to its employee share purchase plan for total proceeds of \$619,934.

During the year ended June 30, 2011, the Company issued 166,667 common shares pursuant to its acquisition of LANrev (Note 3). The fair value of these common shares, measured at the date of the acquisition, was \$876,667.

During the year ended June 30, 2010, the Company issued 741,552 common shares on exercise of employee stock options for total proceeds of \$1,399,160. An amount of \$259,911 related to the original fair value of the options was transferred from contributed surplus to common shares upon exercise.

During the year ended June 30, 2010, the Company issued 231,188 common shares pursuant to its employee share purchase plan for total proceeds of \$786,895.

During the year ended June 30, 2010, the Company issued 400,000 common shares upon exercise of share purchase warrants for total proceeds of \$400,000. An amount of \$255,550 related to the original fair value of the warrants was transferred from contributed surplus to common shares upon exercise.

On November 19, 2010, the Company received approval from the TSX for a Normal Course Issuer Bid that enables the Company to purchase and cancel up to 3,263,702 of its common shares. The Bid allows for the purchase on a daily basis of up to 13,171 common shares until November 18, 2011, except where purchases are made in accordance with "block purchases" exemptions under applicable TSX policies. Prior to November 19, 2010, the Company purchased and cancelled shares under a previously approved Normal Course Issuer Bid (together, the "Bids").

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 11. SHARE CAPITAL (Continued)

Under the Bids, the Company repurchased 3,797,020 common shares for a total cost of \$14,191,302 (2010 – 238,000 common shares for a cost of \$1,009,227). On repurchase of the common shares, the difference between the purchase price and the average book value of the common shares is recorded in accumulated deficit, amounting in 2011 to \$12,335,480 (2010 - \$807,141).

#### (c) Stock Option Plan

The Company's stock-based compensation plans include an Employee Stock Option Plan ("Option Plan").

In 2001, the Company's Board of Directors adopted the Option Plan (as amended in 2007 and 2009), which provided for a maximum of 12% of the number of common shares outstanding to be allocated to Option Plan participants. On this basis, at June 30, 2011, the maximum number of common shares available under the Option Plan was 5,241,660 (2010 - 5,619,490), of which 515,709 remained available for grant thereunder.

Terms and conditions of options granted under the Option Plan are determined solely by the Board of Directors. Under the Option Plan, the exercise price of each option equals the last closing market price of the Company's common shares before the grant date. The term of option grants may not exceed 10 years from the date of grant of the option. Generally, options are granted with a four year vesting period (25% vesting on each anniversary date), with each tranche expiring two years after each vesting date.

The following table summarizes activity under the Option Plan for the years ended June 30, 2011 and 2010:

	2011		2010	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding, beginning of year	4,707,925	\$ 4.87	4,127,127	\$ 4.57
Granted	1,249,300	3.85	1,910,950	4.70
Exercised	(296,775)	1.56	(741,552)	1.89
Forfeited	(563,088)	5.25	(524,350)	5.57
Expired	(371,411)	7.54	(64,250)	9.36
Outstanding, end of year	<b>4,725,951</b>	<b>\$ 4.55</b>	<b>4,707,925</b>	<b>\$ 4.87</b>

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

### 11. SHARE CAPITAL (Continued)

The following table summarizes information about stock options issued and exercisable at June 30, 2011:

Range of exercise prices	Options Outstanding			Options Exercisable	
	Number of options	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options	Weighted average exercise price
\$1.13 - \$2.28	167,500	0.5	1.45	167,500	1.45
\$2.95 - \$4.28	2,694,375	3.0	3.87	785,749	3.89
\$4.48 - \$6.31	1,551,950	3.2	4.69	396,486	4.70
\$8.01 - \$13.42	312,126	1.4	11.46	244,248	11.28
	<b>4,725,951</b>	<b>2.9</b>	<b>\$ 4.55</b>	<b>1,593,383</b>	<b>\$ 4.97</b>

#### *Fair values – Option Plan*

The total fair value of options granted under the Option Plan in the year ended June 30, 2011 was \$1,961,655 (2010 - \$3,604,859). The weighted average grant date fair value of options granted during the year ended June 30, 2011 was \$1.57 (2010 - \$1.89).

The estimated fair value of each option granted under the Option Plan was estimated on the grant date using the Black-Scholes option pricing model with the following weighted average assumptions:

	2011	2010
Risk-free interest rate	1.2%	0.5%
Dividend yield	0%	0%
Expected life (in years)	3.0	3.0
Volatility	60%	60%

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 11. SHARE CAPITAL (Continued)

#### (d) *Non-standard Options*

On December 15, 2010, the Company's shareholders ratified the grant of an additional 500,000 stock options (the "Non-standard Options") outside of the Option Plan, pursuant to the employment agreements of the selling shareholders of LANrev (note 3). The Non-standard Options were granted effective December 2, 2009, the date of the acquisition, with an exercise price of \$5.15, and vest in equal instalments over a three year period beginning on that date. Each tranche expires two years after each vesting date.

The total fair value of the Non-standard Options was \$1,033,067, with a weighted average grant date fair value of \$2.07. This fair value was measured at the date the employment agreements were entered into, as the terms and conditions of the grants were known at that time. The estimated fair value of the Non-standard Options was estimated by using the Black-Scholes option pricing model assuming no dividend yield, an expected life of three years, volatility of 60%, and a risk-free interest rate of 0.5%. At June 30, 2011, 166,667 Non-standard Options had vested and remained outstanding.

#### (e) *Employee Share Purchase Plan*

The Company's stock-based compensation plans also include an Employee Share Purchase Plan ("Purchase Plan").

The Purchase Plan allows employees to purchase up to 2,000,000 common shares from treasury at a 15% discount from the market price. Each employee may allocate a maximum of \$10,500 per year to the purchase of common shares through two six month offering periods per year. During the year ended June 30, 2011, 184,987 common shares (2010 – 231,188 common shares) were issued from treasury under the Purchase Plan at a weighted average price of \$3.38 (2010 - \$3.43) per share.

At June 30, 2011, 1,099,834 common shares remained available for grant under the Purchase Plan.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

### 11. SHARE CAPITAL (Continued)

#### (f) Stock-based compensation

The Company's stock-based compensation for the years ended June 30, 2011 and 2010 was comprised as follows:

	2011	2010
Stock option plan	\$ 2,129,111	\$ 1,960,901
Non-standard Options	545,230	-
Employee share purchase plan	109,558	125,076
	<b>\$ 2,783,899</b>	<b>\$ 2,085,977</b>

The following table summarizes the allocation of stock-based compensation for the years ended June 30, 2011 and 2010:

	2011	2010
Cost of revenue	\$ 308,197	\$ 325,906
Sales and marketing	1,256,046	923,580
Research and development	886,047	564,260
General and Administration	333,609	272,232
	<b>\$ 2,783,899</b>	<b>\$ 2,085,977</b>

#### (g) Warrants

During 2006, the Company issued 1,000,000 common share purchase warrants in connection with a 10 year branding agreement entered into with LoJack Operating Company L.P. whereby the Company acquired the rights to use the "LoJack®" brand name for its consumer theft recovery products. Each warrant was exercisable for one common share at an exercise price of \$1.00 per share. The warrants vested 20% annually on June 30 of each year from 2006 to 2010. All unexercised warrants expired the earlier of 2 years after the vesting date, June 30, 2011 or on termination of the agreement.

During 2010, the remaining 400,000 warrants were exercised.

The grant date fair value of the warrants was recorded as an intangible asset (Note 8).

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 11. SHARE CAPITAL (Continued)

(h) *Potentially dilutive securities*

For the year ended June 30, 2011, 178,980 share purchase options (2010 - 1,181,275 share purchase options) were excluded from diluted loss per share as their effect would have been anti-dilutive.

### 12. INCOME TAXES

Income tax expense (recovery) for the years ended June 30, 2011 and 2010 differ from that calculated by applying statutory rates for the following reasons:

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Income (loss) before income taxes	\$ 338,561	\$ (5,384,979)
Combined Federal and Provincial income tax rate	<u>27.50%</u>	<u>29.25%</u>
Tax expense (recovery) at statutory rate	93,104	(1,575,106)
Permanent differences	(10,139)	398,682
Foreign losses tax effected at higher rates	(660,886)	(731,138)
Impact on future income tax assets of changes in foreign exchange rates	1,691,140	1,777,255
Changes in statutory tax rates	66,681	546,954
Benefit of previously unrecognized future income tax assets and change in valuation allowance	653,984	865,626
Changes in prior year estimates	(347,884)	1,486,629
Total income tax expense	<u>\$ 1,486,000</u>	<u>\$ 2,768,902</u>
Comprised of:		
Current income tax expense	\$ 1,633,000	\$ 1,255,000
Future income tax (recovery) expense	(147,000)	1,513,902
	<u>\$ 1,486,000</u>	<u>\$ 2,768,902</u>

For the year ended June 30, 2011, the Company recorded a net current income tax payable of \$nil (2010 - \$nil), comprised of a provision for income tax expense of \$1.6 million (2010 - \$1.3 million) offset by a \$1.6 million recovery (2010 - \$1.3 million) for Canadian Investment Tax Credits ("ITCs"). The ITCs were credited against operating expenses, as the credit is generated by certain eligible scientific research and development expenditures ("SRED").

In addition, the Company recorded an additional \$1.6 million reduction in current taxes payable and recovery of ITCs related to historical SRED claims upon their assessment by CRA during the year.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

### 12. INCOME TAXES (Continued)

The tax effect of the significant temporary differences and loss carryforwards that comprise future income tax assets and liabilities at June 30, 2011 and 2010 are as follows:

	<u>2011</u>	<u>2010</u>
Future income tax assets (liabilities):		
Property and equipment	\$ 283,596	\$ 658,271
Intangible assets	(883,079)	(1,382,449)
Deferred revenue	16,936,839	18,313,467
Accrued warranty	756,540	963,330
Operating loss carryforwards	5,048,209	2,514,350
Other	(262,429)	12,349
	<u>21,879,676</u>	<u>21,079,318</u>
Valuation allowance	(1,518,984)	(865,626)
	<u>20,360,692</u>	<u>20,213,692</u>
Less: current portion	(9,973,479)	(9,904,709)
	<u>\$ 10,387,213</u>	<u>\$ 10,308,983</u>

The ultimate realization of future tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible and during the loss carryforward periods. Management considers the scheduled reversal of future tax assets and liabilities, projected future taxable income, and tax planning strategies in making this assessment. The amount of the future tax asset considered realizable could change materially in the near term based on future taxable income during the carryforward period. The Company has estimated operating tax loss carryforwards of \$18,091,175, of which \$4,627,323 expire in 2030 with the balance carrying forward indefinitely.

The Company's operations are conducted in a number of countries with complex tax legislation and regulations pertaining to the Company's activities. Any reassessment of the Company's tax filings by the tax authorities may result in material adjustments to net income or loss, tax assets and operating loss carry-forwards.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 13. CAPITAL RISK MANAGEMENT

The Company's objectives in managing capital are to ensure sufficient liquidity to pursue its strategy of organic growth and strategic acquisitions in order to provide returns to its shareholders, and have not changed since 2010. The Company's capital structure consists of cash and cash equivalents, short-term investments and investments, and shareholders' deficiency, which is comprised of issued capital, contributed surplus, and deficit. The Company does not pay annual dividends and does not hold debt. The Company makes adjustments to its capital structure in light of general economic conditions, the risk characteristics of the underlying assets and the Company's working capital requirements. The Board of Directors reviews and approves any material transactions not in the ordinary course of business, including major investments and share repurchases.

### 14. SUPPLEMENTAL CASH FLOW INFORMATION

#### *Composition of cash and cash equivalents*

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Cash	\$ 28,575,992	\$ 10,667,886
Cash equivalents	229,221	17,410,965
	<u>\$ 28,805,213</u>	<u>\$ 28,078,851</u>

#### *Other cash flow information*

	<u>2011</u>	<u>2010</u>
Cash paid for income taxes	\$ -	\$ 237,367
Cash paid for interest	-	-

#### *Non-cash investing and financing activities*

Accrued purchases of property and equipment	\$ 18,165	\$ 71,231
Common shares issued for Acquisition Payable (Note 3)	867,667	-
Accrued purchase price payable (Note 3)	-	5,185,822

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010  
(Expressed in Canadian dollars)

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### 15. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

#### (a) Overview

The Company is exposed to risks of varying degrees of significance which could affect its ability to achieve its strategic objectives for growth. The main objectives of the Company's risk management process are to ensure that risks are properly identified and that the capital base is adequate in relation to those risks. The principal financial risks to which the Company is exposed are described below.

#### (b) Market risk

Market risk is the risk that changes in market prices, such as fluctuations in the market prices of the Company's publicly traded investments, foreign exchange rates, and interest rates, will affect the Company's income or the value of its financial instruments. The Company does not engage in risk management practices such as hedging, derivatives or short selling with respect to its investments.

The Company operates internationally, primarily in the United States, giving rise to exposure to market risks from foreign exchange rates. The Company maintains a net U.S. dollar asset position, and therefore records gains in periods of rising U.S. dollar exchange rates and losses in periods of declining rates. Operating costs are converted at current exchange rates, while revenue is recorded at historic rates from when the Sales Contracts were recorded into deferred revenue, and therefore the Company's operating loss increases in periods when the U.S. dollar appreciates.

#### *Foreign Currency Sensitivity Analysis*

Sales contracts billed in U.S. dollars by the Company are recorded at the exchange rate in effect at the time of sale, and are collected on standard trade payable terms. Excess U.S. dollar balances are converted to Canadian dollars on a regular basis. The Company typically does not enter foreign currency hedges. Further devaluation in the U.S. dollar relative to the Canadian dollar could impact the Company's ability to continue at current sales growth rates and margins as substantially all Sales Contracts are denominated in U.S. dollars.

The Company is exposed to fluctuations in the U.S. dollar, through U.S. dollar working capital balances and U.S. dollar denominated operating expenses. The Company's sensitivity to a 1% strengthening of the U.S. dollar against the Canadian dollar is an approximate decrease of \$310,000 in operating income and a \$15,000 decrease in net loss. For a 1% weakening of the U.S. dollar against the Canadian dollar, there would be an equal and opposite impact on operating income and net loss.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 15. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (Continued)

#### (c) *Liquidity Risk*

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at excessive cost. The Company mitigates liquidity risk by holding sufficient cash and cash equivalents to meet its financial obligations. The Company's growth is financed through cash on hand and cash flows from operations. The majority of the Company's financial liabilities recorded in accounts payable and accrued liabilities are due within 60 days.

Given the Company's available liquid resources as compared to the timing of the payments of liabilities, management assesses the Company's liquidity risk to be low.

#### (d) *Credit Risk*

Credit risk represents the financial loss that the Company would experience if a counterparty to a financial instrument, in which the Company has an amount owing from the counterparty, failed to meet its obligations in accordance with the terms and conditions of its contracts with the Company. The carrying amount of the Company's financial assets represents the Company's maximum credit exposure.

The Company manages credit risk related to accounts receivable by carrying out credit investigations for new customers and partners, and by maintaining reserves for potential credit losses. The majority of the accounts receivable balance is due from well-capitalized computer manufacturers who have a history of paying on a timely basis. Over half of the Company's bad debt provisions relate to a second tier PC OEM that declared bankruptcy in late 2008. At June 30, 2011, 20% of the Company's accounts receivable balance is over 90 days past due (2010 – 18%). Accounts receivable are net of allowance for doubtful accounts of \$1.4 million (June 30, 2010 - \$1.9 million). As at June 30, 2011, 29% and 18% (June 30, 2010 - 20% and 27%) of the receivable balances are owing from two OEM partners.

The Company manages credit risk related to cash, cash equivalents, and investments by maintaining bank and investment accounts with high credit quality financial institutions, including Schedule 1 banks.

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

### 15. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (Continued)

#### (e) Fair Values of Financial Instruments

The carrying value of cash and cash equivalents, short term investments, accounts receivable, and accounts payable and accrued liabilities approximate their fair values due to the immediate or short-term nature of these instruments. The carrying value of investments is higher than their fair value as the investments generally bear interest at rates higher than market. The carrying value of acquisition payable approximates its fair value as the cash portion of the liability is discounted to present value at an interest rate that approximates market. The carrying value of accrued warranty is higher than its fair value due to the fact that the payments will be made over time and the liability is not discounted to present value.

The carrying value of the marketable securities which are publicly traded (included in short term investments) are determined by the quoted market values for the investment, a Level 1 valuation methodology (Note 5).

### 16. SEGMENTED INFORMATION

The Company carries on business in the computer security monitoring and end-point management industry and all sales are made in this segment. Geographic revenue information is based on the location of the customer invoiced. Long-lived assets include property and equipment and intangible assets.

	<u>2011</u>	<u>2010</u>
<b>Revenue</b>		
United States	\$ 65,587,965	\$ 59,386,340
Canada and rest of world	<u>6,610,768</u>	<u>4,689,449</u>
	<u>\$ 72,198,733</u>	<u>\$ 64,075,789</u>
	<u>June 30, 2011</u>	<u>June 30, 2010</u>
<b>Long-lived assets</b>		
Canada	\$ 16,420,942	\$ 22,459,028
United States and rest of world	<u>754,788</u>	<u>773,044</u>
	<u>\$ 17,175,730</u>	<u>\$ 23,232,072</u>

# ABSOLUTE SOFTWARE CORPORATION

## Notes to the Consolidated Financial Statements

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### 17. COMMITMENTS

The Company's minimum payments required under operating leases for premises, equipment and business service agreements, and a branding agreement (note 8) are as follows as at June 30, 2011:

2012	\$ 1,783,773
2013	1,969,359
2014	1,761,837
2015	906,486
2016 and thereafter	186,267
	<u>\$ 6,607,722</u>

### 18. CONTINGENCIES

Due to the nature of its patent portfolio, from time to time the Company is involved in assertions and claims of patent infringement as both the initiating party and, from time to time, as a respondent to such claims. Currently, the Company is party to the following patent-related matter:

Absolute Software Corporation and Absolute Software, Inc. v. Stealth Signal, Inc., and Computer Security Products, Inc. in the United States District Court for the Southern District of Texas, Case No. H-05-1416. On July 21, 2010 the claim of patent infringement made against Stealth Signal, Inc. by the Company was dismissed and the counterclaim against the Company for patent infringement was also dismissed. Subsequently, both parties filed notices to appeal the dismissal of their respective claim and counterclaim. Both parties filed with the United States Court of Appeals for the Federal Circuit, briefs supporting their respective claims. On July 5, 2011, the Court of Appeals for the Federal Circuit conducted an oral hearing, addressing the parties' respective positions. The Company is awaiting a decision from the Court of Appeals for the Federal Circuit.

In order to establish and defend its proprietary rights and patent portfolio, the Company is also the initiating party in two other patent-related matters. The Company's management believes it will prevail in these cases, however, the potential outcome, timing, and impact on the Company's business and patent portfolio is not determinable at this time.

In addition, due to the nature of the Company's business and products, the Company is involved in other legal matters which arise from time to time in the ordinary course of the Company's business. The Company believes that any such claims currently existing are without merit and intends to vigorously defend any such assertions. At this time, there are no legal matters of this type which are believed to be material to the Company's results of operations, liquidity, or financial condition.

# **ABSOLUTE SOFTWARE CORPORATION**

## **Notes to the Consolidated Financial Statements**

Years ended June 30, 2011 and 2010

(Expressed in Canadian dollars)

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### **19. SUBSEQUENT EVENTS**

Subsequent to June 30, 2011, through August 18, 2011, the Company has repurchased an additional 436,700 common shares under its Normal Course Issuer Bid for a total cost of \$1,726,290.

On July 18, 2011, 93,502 common shares were issued pursuant to the Purchase Plan.

## BOARD OF DIRECTORS

**John Livingston**  
Chairman and Chief Executive Officer  
Vancouver, BC

**Phil Gardner**  
Chief Technology Officer  
Woodbury, Minnesota

**J. Ian Giffen\***  
Toronto, ON

**Terry Libin\*\***  
Calgary, AB

**Ian Reid\*\*\***  
Vancouver, BC

**Daniel P. Ryan**  
Greenwood, MN

## OFFICERS AND SENIOR MANAGEMENT

**John Livingston**  
Chairman and Chief Executive Officer

**Rob Chase**  
Chief Operating Officer

**Errol Olsen**  
Chief Financial Officer

**Phil Gardner**  
Chief Technology Officer

**John Sarantakes**  
Senior Vice President, Sales

**Martin Bestmann**  
Senior Vice President, R&D Lifecycle Management

**Ward Clapham**  
Vice President, Recovery Services

**Leigh Day**  
Vice President, Services

**Peter Frankl**  
Vice President, Lifecycle Management

**Mark Grace**  
Vice President, Global Consumer, APAC & LATAM

**Abigail Maines**  
Vice President, Channel Strategy

**Stephen Midgley**  
Vice President, Global Marketing

**Leah Rubin**  
Vice President, Human Resources

**Klaus Salchner**  
Vice President, Development

\* Chairman of Audit Committee

\*\* Chairman of Strategic Planning Committee & Chairman of Governance and Nominating Committee

\*\*\* Lead Director & Chairman of Compensation Committee

## CORPORATE INFORMATION

### Auditors

**Deloitte & Touche LLP**  
Vancouver, BC

### Transfer Agent and Registrar

**Canadian Stock Transfer Company, Inc.**  
www.canstockta.com  
www.cibcmellon.com  
Vancouver, BC

### Legal Counsel

**McMillan LLP**  
Vancouver, BC

### Common Shares

Absolute Software common shares are traded on the Toronto Stock Exchange (TSX) under the trading symbol "ABT".

## ADDITIONAL INFORMATION

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**TMX Equicom**  
Kristen Dickson  
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kdickson@equicomgroup.com

### Annual General Meeting

4:00 pm (P.T.), Thursday, December 15, 2011  
at Terminal City Club in Vancouver, BC

©2011 Absolute Software Corporation. All rights reserved. Computrace and Absolute are registered trademarks of Absolute Software Corporation. LoJack is a registered trademark of LoJack Corporation, used under license by Absolute Software Corporation. LoJack Corporation is not responsible for any content herein. U.S. patents No. 5,715,174, No. 5,764,892, No. 5,802,280, No. 5,896,497, No. 6,087,937, No. 6,244,758, No. 6,269,392, No. 6,300,863, No. 6,507,914, No. 7,818,557, No. 7,818,803, and No. 7,945,709. Canadian patents No. 2,211,735, No. 2,284,806, and No. 2,205,370. U.K. patents No. EP0793823, No. GB2298302, and No. GB2338101. German patent No. 69512534. Australian patent No. 699045. Japanese patent No. JP4067035. The Toronto Stock Exchange has neither approved nor disapproved of the information contained in this report.

# Absolute<sup>®</sup>Software

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