Annual Report // 2002

SERVICES & SOFTWARE
FOR COMPUTER SECURITY
& ASSET MANAGEMENT

AbsoluteSoftware

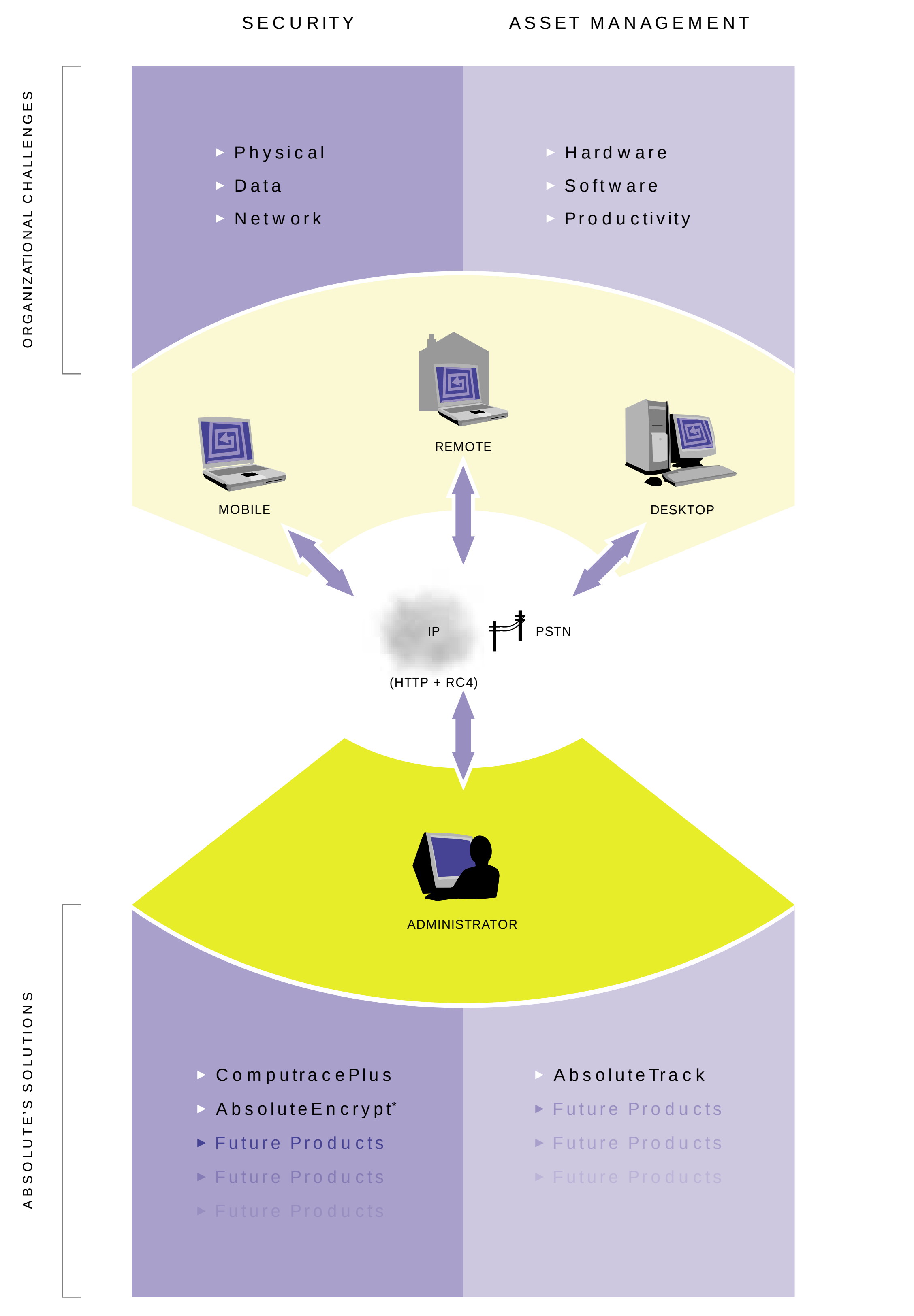
// Contents

// Welcome

Absolute Software helps organizations overcome the security risks and asset management challenges associated with their PCs – remote, mobile and local. Absolute's software offerings can be easily implemented as an enterprise system, or delivered as a managed service over the Internet. Over 2000 customers, including Fortune 1000 companies, government agencies, small and medium businesses, and educational institutions rely on Absolute every day to secure and manage the investment in their PC population.

// Introduction to the Company

ABSOLUTE SOFTWARE'S SOLUTIONS
SERVICES & SOFTWARE FOR COMPUTER SECURITY & ASSET MANAGEMENT



* Scheduled for release in early 2003

Dear Shareholders:
Absolute reported many achievements during the year and we believe the Company is poised for a tremendous future. The new customers earned, the new services and software offered, and the expanded channel relationships all represent essential strides Absolute has made towards evolving from a point service provider to an enterprise-wide solutions provider.

With Computrace®Plus and our new managed service AbsoluteTrack, we broadened our customer base to over 2,000 corporate accounts and grew subscriptions 40% over fiscal 2001. We also sold and delivered our first customer-hosted enterprise software solution. We managed key product and development initiatives that will allow us to release our third and fourth managed services in fiscal 2003. And very importantly, we continued to expand our relationships with Dell and IBM.

Looking toward fiscal 2003, we are confident, engaged and excited about the opportunities before us! The PC – remote, mobile and desktop – remains a fundamental business tool for organizations of all sizes in diverse industries. And, with our growing suite of services and software, Absolute is well positioned to help companies address the security and asset management challenges their mobile and LAN-based PC populations represent.

Customers
Companies today are placing emphasis on solutions that provide tangible operating efficiencies and swift payback on technology investments. Absolute delivered this business value to customers in fiscal 2002 and earned another year of revenue growth. Sales contracts of $6.28 million were 9% higher than the prior year.

In addition, Absolute added over 115,000 new subscriptions compared with 82,000 in fiscal 2001, and the average subscription term increased by 16% to 29 months. We remain the market-leader with ComputracePlus in the growing PC tracking and loss control segment. Industry statistics show that computer theft is continuing unabated and the financial toll to organizations is mounting. In fact, the average loss due to 1 laptop theft alone is estimated at US$89,000[1], which represents hardware, software and productivity loss across the organization.

Also, we gained significant traction with existing customers for AbsoluteTrack and are pleased with our win rate to date in the more competitive asset tracking and inventory management space. Overall, we've attracted more medium to large prospects than in previous years, and made encouraging inroads with the education and government segments.

Services & Software
Launching our new AbsoluteTrack service this year was a major achievement. AbsoluteTrack not only added a new revenue stream to the business, but also demonstrated how we can deliver new managed services based on the Computrace technology platform.

As Absolute expands its managed service portfolio, striking alliances with technology leaders will significantly accelerate the time-to-market for selected offerings. In April of this year, Absolute announced the first of these new relationships. By working with PC Dynamics, Absolute will be able to release a new managed encryption service early in the new calendar year.

This year, we not only leveraged our Computrace technology platform to deliver a new service, but also invested in expanding our implementation options. In addition to the Managed Service Provider (MSP) delivery model, we will be able to deploy both existing and new services via an enterprise software delivery model in fiscal 2003. Flexible implementation methods will better meet market needs, while providing Absolute with an additional revenue opportunity to complement MSP sales.

These accomplishments demonstrate our evolution toward being an enterprise-wide solutions company with a flexible services and software suite. Importantly, we're getting there by leveraging the unique core technology we've always had – the Computrace technology platform.

Strategic Alliances
Absolute's strategic alliances expand our international reach, market opportunity and add to our base of experience and expertise. These relationships are also instrumental for building greater operating leverage within our business model.

With 49% of sales generated through the reseller channel in fiscal 2002, Absolute is pleased with the growing contribution from OEM and value-added resellers. We expect revenue from the channel to increase in fiscal 2003 and average in excess of 60% of total sales contracts.

Dell continued to generate a significant portion of sales, averaging 29% for the year, which is up slightly from last year's average of 28%. The distribution relationship was expanded this year to include AbsoluteTrack, which is gaining momentum within Dell. Absolute also developed a new relationship with IBM to resell ComputracePlus to small to medium enterprises and the government sector in the US.

Other notable achievements this year include signing New York-based reseller ICP and advancing international relationships formed in late fiscal 2001. Absolute also tightened its objectives for reseller sales and streamlined its existing reseller base to preserve only the highest quality relationships. We are encouraged at the potential pipeline for new resellers and expect to form additional relationships in fiscal 2003.

Looking Forward
The opportunities available to us are sizeable. The PC market itself is enormous – and all of these PCs need to be secured and the investment they represent needs to be managed.

A demonstrated market need clearly exists, and Absolute is well positioned to win many of the opportunities that computer security and asset management requirements present. Our services and software, Computrace technology platform, flexible implementation methods and expanding reseller network give us a unique advantage in this large, growing market.

In closing, I would like to thank our customers, employees, directors and shareholders for their ongoing commitment to Absolute. We are looking forward to fiscal 2003 and are striving to make it one of the most pivotal years in the company's history.

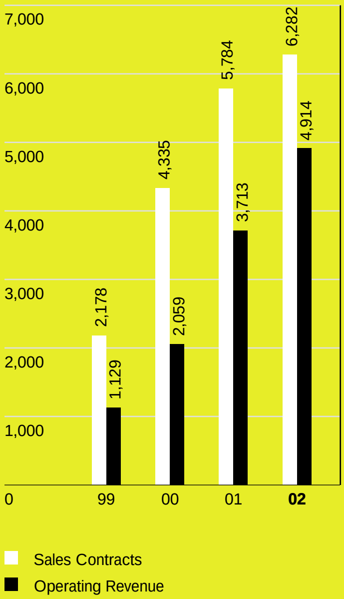
Sincerely,

John Livingston
President & Chief Executive Officer

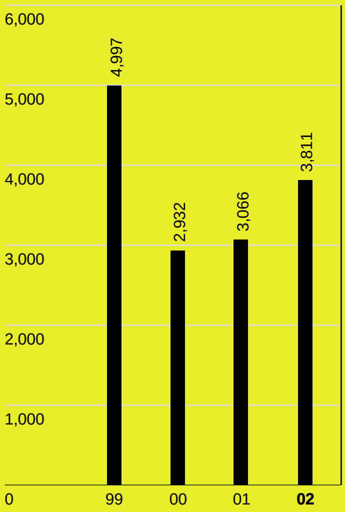
[1] Computer Security Institute/Federal Bureau of Investigation (CSI/FBI) 2002 Survey

// Financial Highlights

CONSOLIDATED OPERATIONAL DATA ($000s)



CONSOLIDATED CASH USED IN OPERATIONS ($000s)



Unless otherwise stated, all dollar amounts are in Canadian Dollars. In thousands. Years ended June 30.

CONSOLIDATED OPERATIONAL DATA (IN 000s EXCEPT PER SHARE DATA) FOR THE YEARS ENDED JUNE 30

	2002	2001	2000	1999
Sales contracts	**$6,282**	$5,784	$4,335	$2,178
Operating revenue	**$4,914**	$3,713	$2,059	$1,129
Loss for the period	**$5,608**	$5,126	$6,661	$5,825
– Per share	**$0.28**	$0.25	$0.56	$0.75
Cash used for operating activities	**$3,811**	$3,066	$2,932	$4,997
– Per share	**$0.19**	$0.15	$0.25	$0.64
Weighted average shares outstanding	**19,895**	20,311	11,849	7,809

CONSOLIDATED BALANCE SHEET DATA (000s) AS AT JUNE 30

	2002	2001	2000	1999
Cash and short-term investments	**$12,088**	$16,778	$20,282	$4,210
Long-term debt and convertible preferred shares	**—**	—	—	$8,875
Deferred revenue	**$7,375**	$6,215	$4,081	$1,806
Working capital	**$9,185**	$14,058	$18,691	$3,249
Liquidity ratio	**2.9 : 1**	4.2 : 1	7.0 : 1	2.7 : 1

// Operating Highlights

Evolving to an enterprise-wide solutions company

- Absolute launched a new managed service called **AbsoluteTrack** for secure asset tracking and inventory management.
- Absolute formed a licensing agreement with PC Dynamics for its Safehouse encryption product to deliver a **new managed encryption service.**
- Absolute announced its first sales contract, and largest win ever, for an **enterprise version of ComputracePlus.**

Broadening our distribution network

- Absolute's reseller channel accounted for **49%** of sales contracts for fiscal 2002.
- **Dell** remained Absolute's most important alliance this year, contributing 29% of sales contracts.
- Absolute announced a new relationship with **IBM** that significantly expands market reach for ComputracePlus.
- Both Dell and IBM launched **major marketing initiatives** that included Absolute services.
- Absolute announced a new relationship with nationally ranked integrator **ICP** to resell both AbsoluteTrack and ComputracePlus to its extensive client base.
- Absolute announced an alliance with **The St. Paul Companies** aimed at decreasing computer losses and related insurance claims.

Expanding our customer base

- Absolute sold **115,000** new subscriptions this year, compared to 82,000 new subscriptions in fiscal 2001.
- Absolute signed new **AbsoluteTrack** customers and expanded existing ComputracePlus relationships to include AbsoluteTrack.
- Absolute's overall sales pipeline includes the highest number of **medium to large prospects** than in any prior year.
- Over **2,000** customers, including Fortune 1000 companies, government agencies, small and medium businesses, and educational institutions, now rely on Absolute to secure and manage the investment in their PC population.

Recovering stolen computers

- Absolute has been able to recover over **90%** of the stolen PCs that contact the Absolute Monitoring Center.
- Absolute's fastest recovery ever: **20** minutes!
- Absolute's U.K. reseller Eurotechnix recovered **5** laptops stolen from a storage facility in Newbury, Berkshire.
- Absolute has secured over **50** case studies and testimonials.
- Absolute's success rate in enabling search warrants and subpoenas to be granted is **100%.**
- On average, ComputracePlus customers have seen internal theft rates drop to **0.5%** (with some as low as **0%!**), far below the industry average forecast of **3-5%.**

SERVICES & SOFTWARE FOR COMPUTER SECURITY & ASSET MANAGEMENT

Whether used in corporate headquarters or remote offices, by telecommuters or mobile employees, corporate PCs simultaneously represent a security risk and an asset management challenge. On one hand, organizations face risks associated with securing the physical device, the data on that device, and the device's network connection. On the other hand, organizations must manage the financial investment in their PC population, which is comprised of hardware, software and the productivity associated with employees using the PC as their primary business tool.

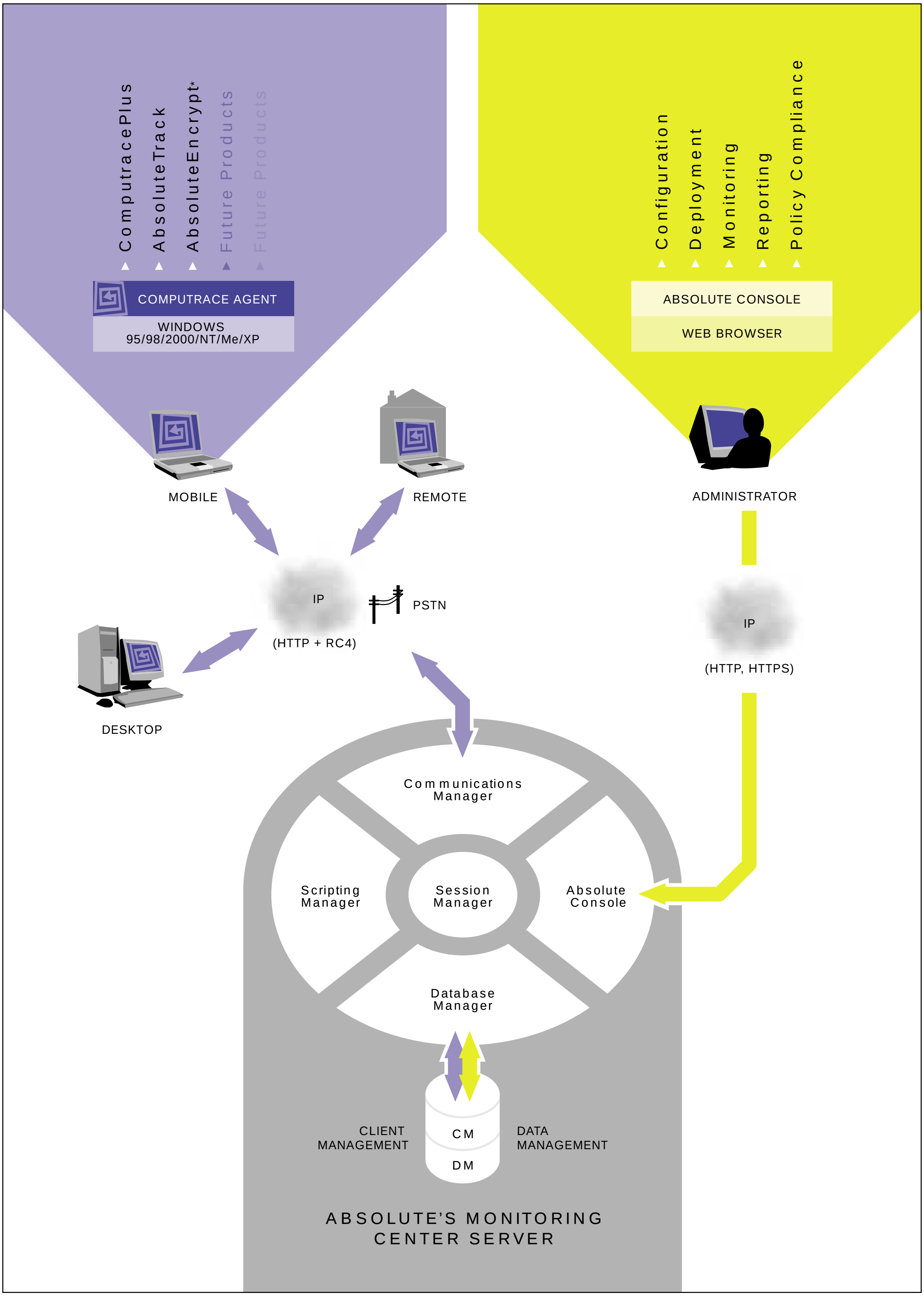
With its Computrace technology platform, Absolute is building upon its theft recovery success to date to help companies address both PC security and asset management needs. In fiscal 2002, Absolute broadened the capabilities of its market-leading PC tracking and loss control service ComputracePlus. Absolute also launched a new secure asset tracking and inventory management service known as AbsoluteTrack. The introduction of AbsoluteTrack diversified Absolute's market offerings, added a new revenue stream to the business, and moved Absolute into the asset tracking space.

AbsoluteTrack has given the Company an important foothold in the asset management market, a segment which is expected to grow to US$4.9 billion by 2003 according to GartnerGroup. This will be an area of significant opportunity moving forward and Absolute expects to deliver key capabilities to the asset management market in fiscal 2003.

On the security front, thanks to ongoing research and development investment throughout fiscal 2002, Absolute is expecting to launch its third service, a managed encryption service addressing the universal problem of data security. The encryption service will give organizations the ability to easily resolve vulnerabilities associated with sensitive data falling into unauthorized hands. Adopting the service will be trouble-free for customers because it is delivered via the Computrace Agent, which is easier to install, configure and manage than typical encryption products.

COMPUTRACE TECHNOLOGY PLATFORM

CLIENT/SERVER ARCHITECTURE THAT DELIVERS ABSOLUTE'S PRODUCTS AS MANAGED SERVICES OR ENTERPRISE SOFTWARE SYSTEMS INSTALLED AT THE CUSTOMER'S SITE



* Scheduled for release in early 2003

CORE TECHNOLOGY: POWERED BY COMPUTRACE

Computrace Technology Platform

The Computrace technology platform powers the Company's managed services for computer security and asset tracking, and has been at the heart of Absolute's business since inception. Extending this core technology is fundamental to broadening the Company's managed service portfolio, and to implementing the same computer security and asset management solutions as stand-alone enterprise systems.

The Computrace technology platform is comprised of the patented Computrace Agent and the Monitoring Center. The Computrace Agent is a secure software client that resides on the hard drive of host PCs and enables the hands-free, auto-discovery of PC location information and asset data. The Agent contacts the Monitoring Center via a secure connection on a regular basis and transmits different auto-discovered data points, depending on the service(s) purchased.

Benefits of the Computrace Agent

The Computrace Agent offers customers many advantages over conventional computer tracking mechanisms and larger enterprise asset management applications:

1. **Secure, Persistent & Reliable:** The Agent is the only low-level software client on the market today. The Agent runs silently and automatically and is very difficult to accidentally or deliberately delete because it is not visible in file directories. It survives most hard drive reformatting or repartitioning, and an F-disk command. In addition, because it initiates the connection to the Monitoring Center, the Agent is inherently more secure than conventional auto-discovery mechanisms that rely on an open and listening port, potentially vulnerable to hackers. The Agent also encrypts the communication of asset data.

2. **Small Footprint & Low Bandwidth:** The Agent itself occupies only 8K of memory when idle and 27K when it places a call. When the Agent transmits asset data, it uses tiny data packets typically between 500B and 2KB. The demand on customers' networks is therefore very low in contrast with larger, bandwidth-intensive applications.

3. **Easy Installation:** The Agent can be installed seamlessly on a corporate image, centrally deployed over a LAN, or even pre-installed at the factory by Dell. Once installed, the Agent simply needs an Internet or phone connection to gather asset data regularly from the PC. Most competitive products deploy an executable requiring user intervention and/or need out-of-office devices to be connected to the corporate network before they can be tracked.

4. **Frequent & Regular Calling:** The Agent calls frequently and on a scheduled basis over IP and dial-up connections. This means customers have accurate, up-to-date information at their fingertips and can monitor changes to their PC population (including remote and mobile computers) as they unfold. Because the Agent requires zero action from the PC user, it is always "on", collecting and transmitting asset data.

5. **Flexibility:** The Agent is "programmable", which means that the same software client can be used to deploy multiple software offerings. This flexibility results in minimal lead times for bringing new capabilities to market, and allows existing customers to easily add and apply new offerings to their PC population. In addition, thanks to the flexibility of the Computrace technology platform itself, Absolute can deliver computer security and asset management solutions to customers as managed services or as enterprise systems.

Absolute relies on a combination of copyright, trade secret and trademark laws, confidentiality procedures, contractual provisions and other similar measures to protect the Computrace Agent and its proprietary information.

FLEXIBLE IMPLEMENTATION MODELS

Absolute announced its largest single sales contract in fiscal 2002. Dubbed "Guardian", this was also the Company's first contract for an enterprise-style system. By leveraging the work completed with international partners, Absolute expedited its time-to-market for a generic enterprise system, and anticipates an official launch of what is now termed the Enterprise Delivery Model in the second quarter of fiscal 2003.

The Enterprise Delivery Model is aimed at medium to large organizations that want to manage Absolute's software offerings in-house. Enterprise customers typically want greater control over the IT/security environment as they have internal IT departments with a sophisticated knowledge of system infrastructure and maintenance. Additionally, some customers require local storage of all PC location and asset data collected by the Computrace Agent. For larger installations, this model also provides customers with greater cost savings by owning and operating the infrastructure and services on their own.

STRATEGIC ALLIANCES

Absolute's strategic alliances include top OEM organizations, high caliber value-added resellers, and leading technology companies.

OEM Relationships

Absolute's services are well-suited to be sold by computer manufacturers who are aggressively pursuing value-added strategies that differentiate their PC hardware from the competition.

Dell continues to be Absolute's most successful distribution channel to date. In fiscal 2002, Absolute expanded the relationship with Dell to include support for AbsoluteTrack as well as ComputracePlus. In fiscal 2002, Absolute also signed an agreement with IBM to resell ComputracePlus to the small to medium sized enterprise market and government sector.

At both Dell & IBM, Absolute has been recently featured in major marketing initiatives that we believe will help contribute to fiscal 2003 revenue growth. From an awareness perspective, these programs afford Absolute a tremendous amount of widespread coverage that the Company would not have the resources to lead on its own. In addition, these programs are evidence that visibility with key OEM resellers is increasing.

Reseller Relationships

In June 2002, Absolute announced that New York-based ICP has agreed to resell both AbsoluteTrack and ComputracePlus to its client base which features the Fortune 1000, growing medium sized companies, government agencies, and leaders in the computing industry. A nationally ranked integrator, ICP is a strong reselling partner with the methodology, resources and experience to manage engagements of all sizes and complexity.

Absolute also installed equipment and completed ComputracePlus training with international partners in the U.K. and South Africa. The first recovery successes have already been achieved in the U.K. In addition, both resellers are also now marketing AbsoluteTrack.

Technology Companies

The next service on Absolute's product roadmap is an encryption service that lets administrators seamlessly encrypt information on the desktop, and attempt to encrypt sensitive data after a security incident, such as a lost or stolen computer. To this end, Absolute formed a licensing agreement with PC Dynamics to integrate the virtual disk components of its Safehouse encryption product within the framework of Absolute's security service suite.

As with AbsoluteTrack and ComputracePlus, the encryption service will be delivered via the Computrace Agent, which should make it easier to install, configure and manage than typical encryption products. Future integrated technologies will be similarly powered by the Agent, and also offered in the enterprise model.

HISTORY IN PC SECURITY

Absolute has been tracking PCs – remote, mobile, and desktop – in a managed service provider model since 1996. In 1997, Absolute made history with Computrace when it became the world's first software-driven solution to help recover a stolen computer. Today, Absolute draws on years of experience and the same core technology to help organizations overcome not only the security risks associated with corporate PCs, but also the asset management challenges they pose.

Absolute has earned an enviable reputation in the PC security space with its market-leading PC tracking and loss control service ComputracePlus, and has made significant inroads in the PC inventory arena with its recently launched secure asset tracking and inventory management service AbsoluteTrack. With planned future offerings that will be based on the same core Computrace technology platform, Absolute is moving more aggressively than ever before toward its vision of being a leading provider of enterprise-wide services and software for computer security and asset management.

The following discussion and analysis should be read in conjunction with the Company's 2002 Consolidated Financial Statements and accompanying notes beginning on page 15 of this Annual Report. Certain statements in this Annual Report constitute forward-looking statements that involve risks and uncertainties. These forward-looking statements relate to, among other things, plans and timing for the introduction or enhancement of Absolute's services and products, and other expectations, intentions and plans contained in this analysis that are not historical fact. When used in this Annual Report, the words "plan," "expect," "believe," and similar expressions generally identify forward-looking statements. These statements reflect 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 readers should understand that Absolute cannot offer assurance that the forward-looking statements contained in this analysis will be realized.

COMPARISON OF OPERATING RESULTS FOR THE YEARS ENDED JUNE 30, 2002, 2001 AND 2000

Overview

The past three years have been foundation-building years that have set the stage for executing Absolute's future growth strategies. Following the March 28, 2000 initial public offering ("IPO") through which Absolute raised $19.88 million, the Company has expanded its infrastructure, channel network and development, sales and marketing teams. During this period, the Company grew from 49 employees at June 30, 2000 to 74 at June 30, 2001 and then to 79 at June 30, 2002.

Expansion efforts have enabled Absolute to build a team appropriate for its planned growth, to optimize the Computrace technology platform, to expand Absolute's suite of services, and to increase market awareness and sales contracts for those services. With most of the building blocks now in place, Absolute is poised to capitalize on its unique technology platform and further solidify its position in the PC security and asset management market.

During fiscal 2002 Absolute sold its first enterprise contract. The enterprise solution broadens Absolute's market by allowing customers to bring Absolute's managed services in-house. In this configuration, the customer will manage the communications and database functions. This first contract was primarily a custom solution sale and as a result had a long sales lead time. Absolute's R&D team is currently developing a non-custom enterprise software solution that will shorten the lead time on enterprise sales by providing an off-the-shelf customer installable version of Absolute's services.

The Company continued to build on its Managed Service Provider ("MSP") model in fiscal 2002. Specifically Absolute was able to:

- Release its second service, AbsoluteTrack, in October 2001 which has increased awareness in Absolute and its services due to broadened market appeal;
- Dedicate additional resources to improving Absolute's reseller channels; and
- Release of a number of value-added enhancements to Absolute's services.

SALES CONTRACTS AND OPERATING REVENUE

	2002 [millions]	2001 [millions]	2000 [millions]
Sales Contracts	**$6.28**	$5.78	$4.34
% change	**9%**	33%	99%
Operating Revenue	**$4.91**	$3.71	$2.06
% change	**32%**	80%	82%

Sales contracts and operating revenue are key measures for Absolute. Sales contracts are a non-GAAP measure and do not have a standardized meaning prescribed by GAAP. A reconciliation of sales contracts to GAAP measures appears with the deferred revenue discussion on page 13. While operating revenue is ultimately used to measure the profitability of the Company, sales contracts provide a measure of the volume of business. Much of the costs associated with sales contracts are incurred at the beginning of the contract term, including sales commissions, customer support, training, and technical support.

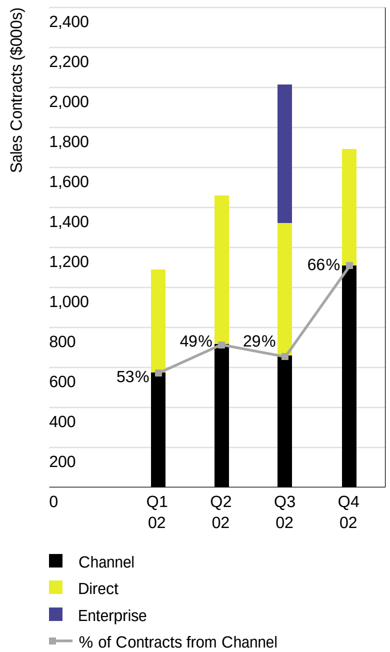
On a cash basis, these up-front costs approximately match the timing of cash flows from sales contracts since the contracts are invoiced and receivable at the beginning of their term. Conversely, the revenue from sales contracts is recognized on a straight-line basis over the contract term (generally 12, 24, 36 or 48 months). Accordingly, the rate of growth in operating revenue will not necessarily match the rate of growth in sales contracts.

For fiscal 2002, operating revenue increased 32% compared to 80% in fiscal 2001, while sales contracts grew 9% in fiscal 2002 and 33% in fiscal 2001. The rate of growth in operating revenue decreased between fiscal years as a result of the drop in the growth rate in sales contracts over the same period.

Given the difficult economic times, fiscal 2002 sales contracts growth of 9% is encouraging evidence that Absolute's services are continuing to gain market acceptance. Absolute's first enterprise sales contract in Q3'02, which accounted for 11% of sales contracts for fiscal 2002, also contributed to the year's growth in sales contracts.

In addition to the sales contract growth, the average contract term has grown from 25 months in fiscal 2001 to 29 months in fiscal 2002. This increase is important as it has come without a change in Absolute's pricing model.

QUARTERLY SALES CONTRACTS BY SOURCE FOR FISCAL 2002



The above graph illustrates Absolute's quarterly sales contracts by source for fiscal 2002. The custom enterprise sales contract, while a direct sale, has been shown separately due to its significance. With both Q3'02 and Q4'02 improving over the first half of the year as illustrated in the above graph, Absolute believes its markets have started to rebound. On this basis, Absolute has issued guidance for fiscal 2003 sales contract growth in the range of 35% to 50% over fiscal 2002.

This growth is expected to come from a combination of increased sales through reseller channels and additional opportunities from new services and enterprise solutions. Over the course of the year, channel generated sales have ranged from 29% to 66% of total quarterly sales contracts, averaging 49% for the year. This compares to an average of 45% in fiscal 2001 and 48% in fiscal 2000. Dell continued to be Absolute's most successful channel reseller, contributing 29% of sales contracts in fiscal 2002, compared to 28% in fiscal 2001 and 27% in fiscal 2000. Absolute is focusing on the reseller channel as a critical success factor for growth and is expecting channel sales to generate over 60% of sales contracts in fiscal 2003.

COST OF GOODS SOLD AND GROSS MARGIN

Cost of goods sold is comprised of two components: monitoring, support and recovery; and technical support and product maintenance. The first component is primarily fixed costs associated with operations infrastructure and customer support. The second component is primarily an allocation of research and development time spent on non-development projects such as product maintenance and customer-specific issue resolution. Monitoring, support and recovery costs have increased 28% to $0.97 million in fiscal 2002 from $0.76 million in fiscal 2001 and $0.45 million in fiscal 2000. The increases are primarily due to increased payroll costs, as staff grew to 15 from 10 in fiscal 2001 and 7 in fiscal 2000 in support of increased sales volume. In addition, the support team undertook additional travel to assist in the sales process, focus on customer satisfaction, and provide installation and training support.

Fiscal 2002 technical support and product maintenance costs increased 62% to $0.98 million from $0.61 million in fiscal 2001 and $0.32 million in fiscal 2000. The year over year increases reflect increased volume, maintenance releases of the ComputracePlus and AbsoluteTrack services and infrastructure building efforts. During fiscal 2002, these efforts focused on integration of back-end systems to better streamline Absolute's delivery platform, re-design of Absolute's Customer Center and configuration and implementation of a customer relationship management system. Maintenance efforts were carried out on AbsoluteTrack during fiscal 2002 to incorporate customer feedback and significantly improve the ability of customers to track their software assets.

Despite cost of goods sold increases, the gross margin has remained relatively constant at 60% in fiscal 2002, 63% in fiscal 2001 and 62% in fiscal 2000, as operating revenue has increased sufficiently to absorb most of the cost increases.

OPERATING EXPENSES

Selling and marketing

Selling and marketing expenses were up slightly at $4.60 million in fiscal 2002, compared to $4.51 million in fiscal 2001 and $3.51 million in fiscal 2000. The selling and marketing teams have undergone considerable rebuilding over the fiscal year and payroll costs, including severance costs in fiscal 2002, have remained relatively constant from fiscal 2001 to fiscal 2002. Conversely, payroll costs were largely responsible for the cost increase from 2000 to 2001 as staff increased from 24 to 35 employees over that period. During fiscal 2002, cost savings gained through a reduction in general marketing related expenditures, were offset by increases in travel and marketing development funds with key resellers.

While the staff complement is expected to expand only marginally in fiscal 2003, selling and marketing costs are expected to increase as Absolute plans to increase sales related travel and the amount of market development funds to be made available to key resellers.

Research and development ("R&D")

R&D expenses increased 9% to $2.20 million in fiscal 2002 from $2.00 million in fiscal 2001, which was 78% higher than fiscal 2000 at $1.12 million. However, a portion of the cost increase has been offset by increases in the allocation of R&D costs to technical support and product maintenance. When the allocated costs are included, overall costs related to the R&D team as a whole increased 21% and 80% in fiscal 2002 and 2001 respectively. A majority of the cost increase in fiscal 2002 and 2001 relates to new hires, as the headcount grew to 25 in fiscal 2002 from 17 and 11 in fiscal 2001 and 2000 respectively. The remainder of the cost increases in both years primarily relate to consulting expenses.

The R&D new hire and consulting expenditures in the past two years have been essential to build upon Absolute's technology platform and develop new services. Much of the foundation has now been laid and Absolute expects fewer new hires during fiscal 2003. Consulting expenses however are anticipated to continue to increase as Absolute utilizes the services of specialists in new service areas. In addition, R&D cost allocation to technical support and product maintenance is expected to decline due to the focus on new services.

General and administration ("G&A")

In total, G&A expenses increased 17% in fiscal 2002 to $2.39 million compared to fiscal 2001 and 2000, which were relatively constant at $2.04 million and $1.95 million respectively. In fiscal 2001, cost savings associated with relocating the Company head office from Bellevue, Washington to Vancouver, BC were offset by increased professional, legal and consulting expenditures associated with increased investor relations and public reporting requirements, as well as recruiting costs for new hires as the Company grew from 49 to 74 employees.

The G&A cost increase in fiscal 2002 relates to a non-cash employee loan write-down of $0.40 million and increased salary and amortization expense. Salary has increased due to an increased US dollar exchange rate and changes to the administrative team. Amortization expense increased by $0.18 million over fiscal 2001 with the purchase of new customer relationship management and accounting systems. These increases have been offset by savings in professional and recruiting fees.

The employee loan was written down as a result of the decline in the value of the Company's shares, which are held as security for the loan. The loan has not been forgiven and the Company anticipates extending the loan maturity date (currently October 7, 2002) in order to increase the likelihood of recovery. Accordingly, any future recovery of the loan beyond the written-down value will result in income in the period in which it is recovered.

OTHER INCOME (EXPENSE)

Interest income

The Company raised $19.88 million, after issue expenses, through an IPO on March 28, 2000 and has been investing all amounts beyond immediate operating requirements in treasury bills, bankers' acceptances and investment grade bonds. Following the IPO, interest income increased from $0.40 million in fiscal 2000 to $1.11 million in fiscal 2001, before declining 46% to $0.59 million in fiscal 2002. The decline in fiscal 2002 is a result of both the reduced average cash balance as the Company used cash for operations and the decline in interest rates during the year. Interest income is expected to decrease again in fiscal 2003 as the Company expects to continue to use cash in operations.

Interest expense and bank charges

Following the IPO in fiscal 2000, the Company extinguished all debt and, as a result, only bank credit card charges associated with increased transaction volumes continue to be incurred. Accordingly, interest expense and bank charges have decreased from $0.08 million in fiscal 2000 to $0.03 million in fiscal 2001 and $0.02 million in fiscal 2002.

Foreign exchange gains and losses

A majority of the Company's sales contracts and deferred revenue balances are generated through its wholly owned US subsidiary. Accordingly, Absolute is exposed to foreign exchange fluctuations both from consolidating the US subsidiary and transferring funds between the Canadian and US operations.

Due to the growing deferred revenue balances in the US subsidiary, during periods of a weakening Canadian dollar relative to the US dollar, Absolute will generally incur foreign exchange losses on consolidation. These losses are often offset by gains on transfer of excess US funds to Canadian dollars. As a result, foreign exchange gains and losses have not been significant year over year, fluctuating from losses in fiscal 2001 of $0.01 million, compared to gains in fiscal 2000 and 2002 of $0.01 million and $0.03 million respectively. The Company has not entered into any foreign exchange contracts to mitigate this exposure as management does not consider it to be significant since a majority of the costs associated with fulfilling US sales contracts are incurred in Canadian dollars, while US contracts are generally paid at the beginning of the sales contract.

Taxes

The Company has not generated taxable income in Canada or the United States since inception and accordingly has not been subject to income taxes. The Company has approximately $16.7 million of Canadian tax losses, and $2.5 million of US tax losses that can be used to reduce taxable income of future years. Absolute does not expect to be profitable in fiscal 2003 and as a result, $1.1 million of the Canadian tax losses will expire.

Loss for the year

The Company recorded a loss of $5.61 million ($0.28 per share) in fiscal 2002, $5.13 million ($0.25 per share) in fiscal 2001, and $6.66 million ($0.56 per share) in fiscal 2000. The decreased loss per share from fiscal 2000 to fiscal 2001 partly relates to the increased average shares outstanding from the issuance of additional shares on the March 2000 IPO.

A majority of the increased loss in fiscal 2002 over fiscal 2001 relates to a one-time charge to income of $0.40 million for write-down of an employee loan. Similarly, fiscal 2000 included a non-cash charge of $1.71 million for share-based compensation, which explains a majority of the reduction in the loss for fiscal 2001.

LIQUIDITY AND FINANCIAL RESOURCES

Cash used in operations

Cash used in operations increased to $3.81 million in fiscal 2002 compared to $3.07 million in fiscal 2001, and $2.93 million in fiscal 2000. Fiscal 2001 and 2000 remained relatively constant as infrastructure cost increases in 2001 were nearly offset by a 33% increase in sales contracts and a $0.70 million increase in interest income. Conversely, the reduction in interest income in fiscal 2002, coupled with a 9% growth in sales contracts, was not sufficient to offset increased costs and resulted in increased cash used in operations.

The Company is expecting further investment in personnel and new services in fiscal 2003, which is expected to increase costs by 5% to 10% overall, compared to expected increases in sales contracts of 35% to 50%. Accordingly, cash used for operating activities is expected to improve in fiscal 2003.

Cash position

The Company continues to maintain a strong financial position and at June 30, 2002 held $12.09 million ($0.62 per share) in cash and short-term investments, down from $16.78 million ($0.83 per share) at June 30, 2001 and $20.28 million ($1.00 per share) at June 30, 2000. Cash is held in general operating bank accounts, while cash equivalents and short-term investments are held in treasury bills, bankers' acceptances and investment grade bonds.

Accounts receivable
Consistent with increases in sales contract volume, trade accounts receivable have increased to $1.71 million at June 30, 2002 from $1.55 million at June 30, 2001 and $1.42 million at June 30, 2000. In general, payment for sales contracts is due upon invoicing regardless of the contract service term. However, collection of sales contracts generated through resellers tends to extend beyond sixty days as collection occurs first by the reseller and then by the Company from the reseller.

At June 30, 2002, 30% of receivables were greater than 60 days, compared to 15% at June 30, 2001 and 68% at June 30, 2000. The improvement over fiscal 2000 was achieved through improving credit check and collection processes, coupled by a solid collection campaign during the final quarter of both fiscal 2001 and 2002. The increase in accounts over 60 days in fiscal 2002 over fiscal 2001 relates primarily to one account that represented 20% of receivable balances at June 30, 2002 and was collected subsequent to year end.

At June 30, 2002, four customers (11%, 14%, 15% and 20%) had receivable balances representing more than 10% of total receivables, compared to no customers at June 30, 2001 and one customer (17%) at June 30, 2000. The June 30, 2000 account was subsequently collected and collection is expected for all four June 30, 2002 accounts, the majority of which had been collected by August 2002.

Capital assets
Capital additions were $0.59 million, $0.34 million, and $0.1 million for fiscal 2002, 2001 and 2000 respectively. The additions for fiscal 2002 relate to purchase of a new customer relationship management system, a new accounting system and leasehold improvements at the Company's new leased offices in Vancouver. In April of 2002, the Company moved its offices to improve the operating space and consolidate staff on one floor.

Fiscal 2001 expenditures related to expanding the office space and purchasing new workstations and computers to accommodate increased staff levels, while expenditures were lower in fiscal 2000 corresponding to the level of new hires for that period.

Deferred revenue
Deferred revenue represents sales contracts invoiced and/or paid, but not yet earned. The rate of increase in deferred revenue will differ from the rate of increase in sales contracts and monitoring revenue due to the interaction between the value and term of new sales contracts, the amount of revenue recognizable in the period and the term remaining for contracts from prior periods. In addition, US dollar sales contracts will be subject to foreign exchange translation adjustments over the deferral term.

Deferred revenue balances (current and long-term) increased 19% to $7.37 million at June 30, 2002, from $6.21 million at June 30, 2001 and $4.08 million at June 30, 2000. The increase in each period primarily represents the amount by which new sales contracts exceed operating revenue recognized. The remaining differences are due to receivable balances offset against deferred revenue and foreign exchange gains and losses on translation of US dollar deferred revenue balances as shown in the following table.

	2002 [millions]	2001 [millions]	2000 [millions]
Open deferred revenue	**$6.21**	$4.08	$1.81
New sales contracts	**$6.28**	$5.78	$4.34
Operating revenue recognized	**($4.91)**	($3.71)	($2.06)
Other adjustments	**($0.21)**	$0.06	($0.01)
Closing deferred revenue	**$7.37**	$6.21	$4.08

Normal course issuer bid
On June 18, 2001, the Company received approval from the Canadian Venture Exchange (now the TSX Venture Exchange) to purchase up to 1,369,884 shares of Absolute on the open market. Absolute was successful at purchasing and canceling 689,000 shares at an average price of $0.41. Management believes that the Company's shares continue to be undervalued and on August 20, 2002 obtained approval from the TSX Venture Exchange to purchase up to an additional 1,314,487 shares. Under the bid, Absolute is permitted to purchase shares at the going market rate until the earlier of August 20, 2003 and the date at which the maximum number of shares are purchased.

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.

Dependence on Two Services and Market Acceptance.
Absolute currently has two service offerings, ComputracePlus, a PC tracking and loss control service and AbsoluteTrack, a secure asset tracking and inventory management service. Absolute is developing other service offerings but there can be no assurance that Absolute's current or future service offerings will achieve widespread market acceptance.

Competition. The market for software is intensely competitive, fragmented, and rapidly changing. Several potential competitors are marketing or have announced the development of PC security and asset tracking products in direct competition with ComputracePlus and AbsoluteTrack. In addition, as Absolute develops new services, the Company may begin competing against companies with whom it did not previously compete. It is also possible that new competitors will enter the marketplace.

Given the size of the market opportunity for PC security and asset tracking services, potential competitors may develop new technology that is as cost-effective, or more cost-effective, than the software-based services offered by Absolute. Furthermore, many of Absolute's potential competitors have greater market presence, marketing capabilities and financial, technological and personnel resources than those available to Absolute. As a result, 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. The entry of new competitors could have a material adverse effect on Absolute's business, financial condition and results of operations. As Absolute introduces new products in new markets, the number and type of competitors will change.

Microsoft Operating Systems. Absolute has designed its services to operate on certain generations of Microsoft Windows operating systems. As a result, Absolute's market for its services are customers who have procured their computing systems around these operating systems. Absolute's future financial performance will depend on continued growth and the number of businesses that successfully adopt these operating systems, each of which face increasing competition. If the number of businesses that adopt Microsoft operating systems fails to grow or grows more slowly than the Company expects, or if Microsoft delays a release of new or enhanced products, revenues could be adversely affected.

The development by Microsoft of new versions of Windows or other operating systems, and the wide acceptance by customers of these or other operating systems developed by other vendors, may have an adverse effect on Absolute's business if it is not able to adapt its Computrace technology platform to be compatible with these new operating systems.

Product Errors. Software services as complicated as Absolute's and related application software may contain errors or defects, especially when first introduced or when new versions are released. Absolute's software may not be free from errors after commercial shipments have begun. 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, Absolute relies on other software, such as Microsoft operating systems, which may contain defects or errors. Any defects in these products could adversely affect the operation of and market for Absolute's services, reduce revenues, increase costs and damage Absolute's reputation.

Operating Environment for ComputracePlus. Absolute's PC tracking and loss control service ComputracePlus is reliant upon the Computrace Agent installed on a PC contacting Absolute's Monitoring Center via dial-up modem or Internet connection and providing the location information necessary for Absolute to facilitate recovery of the PC. As such, the Computrace Agent software that enables this service operates in a potentially hostile environment. If the PC 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. Should Absolute become unable to successfully demonstrate to customers that its software agent will call in, it may affect Absolute's ability to sell the theft recovery portion of the services offered to customers.

Reliance on Key Personnel. Absolute's future performance depends in part upon the continued service of its key technical, sales and senior management personnel. Absolute's future success also depends on its continuing ability to attract, train and retain highly qualified technical, sales and managerial personnel. There can be no assurance that Absolute can retain its key technical, sales and managerial personnel in the future and the loss of the services of one or more of Absolute's key employees could have a material adverse effect on Absolute's business, operating results and financial condition.

Emerging Markets. The market for Absolute's services is still emerging and continued growth and demand for and acceptance of these services remains uncertain. Even if the market for these services grows, businesses may purchase the services of our competitors or develop their own services. The strategy of Absolute to expand its service offerings is based upon an assumption of continued use of the Internet by businesses. Absolute is uncertain how businesses will use the Internet as a means of communication and commerce and whether a significant market will develop for Internet-based services. Additional Internet-related risks include the failure of the Internet infrastructure to support demands placed on it by continued growth and a failure of the Internet to establish itself as a viable communications tool due to any number of concerns, including reliability, cost, security, ease of use, accessibility and quality of service.

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 services 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.

Sales Cycle. A decision by an organization to purchase Absolute's services is discretionary, may involve a significant commitment of its resources and is influenced by budget cycles. Absolute expects that these same issues will arise as it begins to market its other PC security and asset tracking services. In order to successfully sell its services, Absolute's sales force must often educate potential customers regarding the use and benefits of the services in general and the solutions offered by Absolute, in particular. This period of education may require significant time and allocation of resources. Consequently, the period between initial contact and the purchase of services for Absolute's products can be long and subject to delays associated with the lengthy budgeting, approval and competitive evaluation processes that typically accompany such expenditures. Absolute's sales cycles are lengthy and variable, typically ranging between weeks to 12 months or more from initial contact. While the establishment of third party distribution channels may assist in accelerating these sales cycles or easing the resource burden placed upon Absolute's sales force, there can be no certainty that these new relationships will result in shorter sales cycles or less resource requirements from Absolute. Sales delays could cause Absolute's operating results to vary.

MANAGEMENT'S STATEMENT OF RESPONSIBILITIES

The management of Absolute Software Corporation is responsible for the preparation of the accompanying consolidated financial statements and the preparation and presentation of all information in the Annual Report. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada, and are considered by management to present fairly the financial position and operating results of the Company.

The Company maintains various systems of internal control to provide reasonable assurance that transactions are appropriately authorized and recorded, that assets are safeguarded, and that financial reports are properly maintained to provide accurate and reliable financial statements.

The Company's audit committee is comprised entirely of non-management directors and is appointed by the Board of Directors annually. The committee meets periodically with the Company's management and independent auditors to review the consolidated financial statements and the independent auditors' report. The audit committee reported its findings to the Board of Directors, who have approved the consolidated financial statements.

The Company's independent auditors, KPMG LLP, have examined the consolidated financial statements and their report follows.

John Livingston
President & Chief Executive Officer
August 9, 2002

Peter Scott
Executive Vice-President & Chief Financial Officer
August 9, 2002

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Absolute Software Corporation as at June 30, 2002 and 2001 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at June 30, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles. As required by the Company Act (British Columbia), we report that, in our opinion, these principles have been applied, after giving retroactive effect to the adoption of the new accounting standard relating to earnings per share explained in **NOTE 2(h)** to the financial statements, on a consistent basis.

KPMG LLP

Chartered Accountants
Vancouver, Canada
August 2, 2002

(Expressed in Canadian Dollars)

As at June 30, 2002 & 2001		2002	2001
Assets			
CURRENT ASSETS:			
Cash and cash equivalents	$	**6,640,302**	6,615,998
Short-term investments		**5,448,176**	10,162,264
Accounts receivable		**1,712,718**	1,553,753
Investment tax credits receivable		**—**	30,000
Prepaid expenses and deposits		**168,489**	108,038
Current portion of loans to directors and employees		**108,571**	—
		14,078,256	18,470,053
Loans to directors and employees **(NOTE 4)**		**497,819**	986,878
Property and equipment **(NOTE 5)**		**915,127**	721,314
	$	**15,491,202**	20,178,245
Liabilities and Shareholders' Equity			
CURRENT LIABILITIES:			
Accounts payable and accrued liabilities	$	**798,720**	752,911
Current portion of deferred revenue		**4,094,080**	3,659,425
		4,892,800	4,412,336
Deferred revenue		**3,280,440**	2,555,330
		8,173,240	6,967,666
SHAREHOLDERS' EQUITY:			
Share capital **(NOTE 6)**		**37,808,075**	39,134,949
Contributed surplus **(NOTE 6(g))**		**1,042,709**	—
Deficit		**(31,532,822)**	(25,924,370)
		7,317,962	13,210,579
	$	**15,491,202**	20,178,245

Commitment **(NOTE 9)**

Subsequent event **(NOTE 6(g))**

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board:

John Livingston
Director

Ian Reid
Director

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001		2002	2001
REVENUE:			
Monitoring revenue	$	**4,794,557**	3,639,449
Installation services, licensing fees and other revenues		**119,330**	73,057
		4,913,887	3,712,506
COST OF GOODS SOLD:			
Monitoring, support and recovery		**973,242**	757,752
Technical support and product maintenance		**983,123**	607,381
		1,956,365	1,365,133
Gross margin		**2,957,522**	2,347,373
EXPENSES:			
Selling and marketing		**4,603,556**	4,508,909
Research and development		**2,167,497**	1,995,853
General and administration		**2,394,038**	2,038,901
		9,165,091	8,543,663
Operating loss		**6,207,569**	6,196,290
OTHER INCOME (EXPENSE):			
Interest and other income		**594,799**	1,105,111
Interest and bank charges		**(23,394)**	(26,861)
Foreign exchange gain (loss)		**27,712**	(7,882)
		599,117	1,070,368
Loss for the year		**5,608,452**	5,125,922
Deficit, beginning of year		**25,924,370**	20,798,448
Deficit, end of year	$	**31,532,822**	25,924,370
Basic and diluted loss per common share **(NOTE 2(h))**	$	**(0.28)**	(0.25)
Weighted average number of common shares outstanding		**19,894,962**	20,311,460

See accompanying notes to consolidated financial statements.

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001		2002	2001
Cash provided by (used in):			
OPERATIONS:			
Loss for the year	$	**(5,608,452)**	(5,125,922)
Items not involving cash:			
Amortization		**400,526**	223,971
Common shares issued in settlement of claim		**—**	29,174
Write-down of loans to directors and employees		**401,842**	—
Interest and foreign exchange on loans to directors and employees		**(21,354)**	(61,835)
Changes in non-cash operating working capital:			
Accounts receivable		**(158,965)**	(136,288)
Investment tax credit receivable		**30,000**	(30,000)
Prepaid expenses and deposits		**(60,451)**	12,353
Accounts payable and accrued liabilities		**45,809**	(110,793)
Deferred revenue		**1,159,765**	2,133,287
		(3,811,280)	(3,066,053)
INVESTMENTS:			
Property and equipment purchased		**(594,339)**	(341,445)
Disposition (acquisition) of short-term investments		**4,714,088**	(10,162,264)
		4,119,749	(10,503,709)
FINANCING:			
Loans to directors and employees		**—**	(99,000)
Common shares issued on exercise of options and warrants		**—**	2,637
Common shares repurchased		**(284,165)**	—
		(284,165)	(96,363)
Increase (decrease) in cash and cash equivalents		**24,304**	(13,666,125)
Cash and cash equivalents, beginning of year		**6,615,998**	20,282,123
Cash and cash equivalents, end of year	$	**6,640,302**	6,615,998
SUPPLEMENTARY INFORMATION:			
Cash paid for taxes	$	**29,357**	18,659
Cash paid for interest and bank charges		**23,394**	26,861
Non-cash financing and investing activities:			
Common shares issued in settlement of claim		**—**	29,174

See accompanying notes to consolidated financial statements.

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001

1. ORGANIZATION:

The principal business activities of the Company since incorporation under the Company Act (British Columbia) on November 24, 1993 are the development, marketing and support of computer security, asset tracking and theft monitoring services and products. The Company markets its services and products to original equipment manufacturers, resellers, corporations, governments and educational institutions primarily in North America. The Company completed its initial public offering (“IPO”) in March 2000 and trades on the TSX Venture Exchange under the symbol ABT.

2. SIGNIFICANT ACCOUNTING POLICIES:

(a) Basis of presentation:

The consolidated financial statements include the accounts of Absolute Software Corporation and its wholly owned subsidiaries, Absolute Software Inc. and 609713 B.C. Limited. All intercompany balances and transactions have been eliminated.

(b) Cash and cash equivalents and short-term investments:

Cash equivalents have terms to maturity at the date of acquisition of not more than three months. Short-term investments are recorded at the lower of cost and market value.

(c) Property and equipment:

Property and equipment are carried at cost less accumulated amortization. Amortization is calculated using the declining balance method at the following annual rates:

Asset	Rate
Computer equipment	40%
Computer software	100%
Office equipment	20%
Furniture and equipment	20%
Trade show equipment	30%

Leasehold improvements are amortized over the term of the lease.

(d) Revenue recognition:

The Company recognizes revenue in accordance with the provisions of the Securities and Exchange Commission’s Staff Accounting Bulletin 101 “Revenue Recognition in Financial Statements” and the American Institute of Certified Public Accountants’ Statement of Position 97-2 “Software Revenue Recognition” and specifically as follows:

(i) Revenue is generally recognized at the time of service delivery, provided there are no significant vendor obligations remaining, the fee is fixed or determinable and collection is reasonably assured.

(ii) Revenue from licensing and monitoring fees is deferred and amortized on a straight-line basis over the term of the service contract.

(iii) Revenue from sales of multiple element contracts is recognized separately for each element when vendor specific objective evidence (“VSOE”) exists for each such element. If VSOE cannot be established, revenue is recognized ratably over the last undelivered element.

(iv) Revenue from training, consulting and installation services is recognized upon delivery of the agreed services.

(e) Research and development costs:

Research costs are charged to expense in the year in which they are incurred. Development costs are deferred if they meet specific criteria; otherwise, they are expensed as incurred. At June 30, 2002 and 2001 no development costs have been deferred.

(f) Foreign currency translation:

Monetary assets and liabilities denominated in a foreign currency have been translated into Canadian dollars at rates of exchange in effect at the balance sheet date. Other assets and revenue and expense items are translated at rates prevailing when they were acquired or incurred. Exchange gains and losses arising on translation of assets and liabilities denominated in foreign currencies are included in income.

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001

(g) 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 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 income. Future tax assets and liabilities are measured using 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 evaluated and if realization is not considered “more likely than not”, a valuation allowance is provided.

(h) Loss per share and change in accounting policy:

Basic net loss per share is calculated by dividing net loss available to common shareholders by the weighted average number of common shares outstanding during the period. For all periods presented, net loss available to common shareholders equates to net loss. Diluted earnings per share is calculated by the treasury stock method. Under the treasury stock method, the weighted average number of common shares outstanding assumes that the proceeds to be received on the exercise of dilutive stock options are applied to repurchase common shares at the average market price for the period. This policy was adopted in the year ended June 30, 2002 and has been applied retroactively. There was no impact from the retroactive application on disclosed diluted net loss per share.

The diluted loss per share does not differ from the basic loss per share as outstanding options, warrants and convertible preferred shares are anti-dilutive. At June 30, 2002 there were 625,000 (2001 – 666,000) potentially dilutive stock options and warrants outstanding.

(i) Share-based compensation:

The Company’s share-based compensation plans are described in note 6(c). No compensation expense is recognized when share options are issued to employees. Any consideration paid by employees on exercise of share options or purchase of shares is credited to share capital.

(j) Use of estimates:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent liabilities, and the reported amounts of revenues and expenses during the period. Accounts receivable, loans to employees and refundable investment tax credits are significant areas requiring the use of estimates. Actual results may differ from the estimates used in the preparation of the financial statements.

3. FINANCIAL INSTRUMENTS:

(a) Fair values of financial statements:

The carrying amounts of cash and cash equivalents, short-term investments, accounts receivable, investment tax credits receivable and accounts payable and accrued liabilities approximate their fair values due to their short-term maturity.

The carrying amount of loans to directors and employees approximates their fair value as the interest rate on the loans approximates the prevailing market rate.

(b) Foreign currency risk:

Foreign exchange risk reflects the risk that the Company’s earnings will decline due to fluctuations in exchange rates. Contracts billed in United States dollars by the Company are collected in the short-term and, accordingly, the Company has determined there is no significant exposure to foreign currency fluctuations. However, due to the terms of the sales contracts which range from 12 to 48 months and consistent with the Company’s policy for deferred revenue, the realization of US dollar deferred revenue over the contract period will result in the realization of foreign currency gains and losses. The Company does not have foreign currency hedges.

(c) Credit risk:

Credit risk reflects the risk that the Company may be unable to recover contractual receivables. The Company has a significant number of individual contracts and no one contract represents a concentration of credit risk. The Company employs established credit approval practices to further mitigate this risk.

4. LOANS TO DIRECTORS AND EMPLOYEES:

In fiscal years prior to 2002, the Company provided $864,000 in loans to directors and employees of the Company to exercise share options in the completion of contractual arrangements entered into in fiscal year 2000. No such loans were provided in 2002.

		2002	2001
Loans, beginning of year	$	986,878	826,043
Loans provided		—	99,000
Accrued interest and foreign exchange		21,354	61,835
Valuation adjustment		(401,842)	—
Loans, end of year	$	606,390	986,878

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001

4. LOANS TO DIRECTORS AND EMPLOYEES CONTINUED:

The loans to employees are secured by 836,744 common shares. The market value of the shares held as security for the loans was $368,167 at June 30, 2002 (2001 – $468,577). The Canadian dollar loans totaling $497,819 bear interest at the Bank of Canada's bank rate plus one percent per annum, calculated monthly on the principal balance with the first interest payments due on December 31, 2003 and the principal to be paid in full no later than December 31, 2006. US dollar loans totaling $510,413 (US $336,640) bear interest at the rate of 6.46% per annum, calculated monthly on the principal balance with the full principal and interest payable on October 7, 2002. During the year, the Company ceased recording interest on the US dollar loans and took a valuation adjustment to reduce the carrying value of the US dollar loan to $108,571.

5. PROPERTY AND EQUIPMENT:

2002		**Cost**	**Accumulated amortization**	**Net book value**
RESEARCH AND DEVELOPMENT:				
Computer equipment	$	617,757	486,487	131,270
Computer software		48,007	46,070	1,937
Furniture and equipment		24,330	10,863	13,467
OFFICE:				
Furniture and equipment		592,514	347,857	244,657
Office equipment		305,266	132,667	172,599
Computer equipment		460,425	288,235	172,190
Computer software		289,018	214,702	74,316
Trade show equipment		33,242	20,637	12,605
Leasehold improvements		102,649	7,658	94,991
		2,473,208	1,555,176	918,032
Investment tax credits		(29,313)	(26,408)	(2,905)
	$	2,443,895	1,528,768	915,127

2001		Cost	Accumulated amortization	Net book value
RESEARCH AND DEVELOPMENT:				
Computer equipment	$	550,833	417,020	$133,813
Computer software		43,300	40,508	2,792
Furniture and equipment		24,330	7,496	16,834
OFFICE:				
Furniture and equipment		538,492	294,075	244,417
Office equipment		253,127	98,368	154,759
Computer equipment		366,621	211,678	154,943
Computer software		70,716	69,980	736
Trade show equipment		31,449	15,746	15,703
Leasehold improvements		67,508	66,041	1,467
		1,946,376	1,220,912	725,464
Investment tax credits		(29,313)	(25,163)	(4,150)
	$	1,917,063	1,195,749	721,314

6. SHARE CAPITAL:

(a) Authorized:

50,000,000 common shares, no par value
Unlimited preferred shares, Series A, voting, convertible, redeemable

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001

6. SHARE CAPITAL CONTINUED:

(b) Issued:

	Number of shares	Amount
COMMON SHARES:		
Balance at June 30, 2000	20,295,033	$ 39,103,138
Shares issued in settlement of claim **(NOTE 6(b)(i))**	31,000	29,174
Proceeds for options exercised in prior year	—	2,637
Balance at June 30, 2001	20,326,033	39,134,949
Shares repurchased and cancelled during the year under the Normal Course Issuer Bid **(NOTE 6(g))**	(689,000)	(1,326,874)
Balance at June 30, 2002	19,637,033	$ 37,808,075

(i) On April 27, 1998 the Company was served with a Writ of Claim by a former employee claiming rights to common shares. On December 19, 2000, the Company issued 31,000 common shares in settlement of the claim and recorded a $29,174 increase in share capital based on the average trading value of the Company's common shares at the date of settlement.

(c) Share purchase options:

The 2001 Employee Share Option Plan provides that a maximum of 4,065,206 common shares may be allocated to participants. The exercise price of each option equals the closing market price of the Company's shares on the day before the grant date, or if there is no sale on that date, the average of the closing bid and ask prices. The term of option grants will 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), and expire two years after each vesting date.

	June 30, 2002. Shares	**Weighted average Exercise price**	June 30, 2001. Shares	Weighted average Exercise price
SHARE OPTIONS:				
Outstanding, beginning of year	2,842,670	$ 3.29	2,102,000	$ 4.76
Forfeited	(680,493)	3.46	(306,830)	4.62
Granted during the year	664,500	0.40	1,047,500	0.71
Outstanding, end of year	2,826,677	$ 2.57	2,842,670	$ 3.29

	Options outstanding at June 30, 2002			**Options exercisable at June 30, 2002**	
Exercise prices	Number of stock options outstanding	Weighted average remaining contractual life	Weighted average exercise price	Number of stock options exercisable	Weighted average exercise price
$5.00	1,255,177	1.76	$ 5.00	876,177	$ 5.00
$1.45 to $2.10	234,500	2.55	1.72	81,125	1.65
$0.36 to 0.97	1,337,000	3.72	0.44	170,250	0.48
	2,826,677	2.75	$ 2.57	1,127,552	$ 4.08

(d) Bonus shares:

During the year ended June 30, 2001, the Company cancelled the Share Bonus Plan. No shares were issued under the plan.

(e) During the year, 440,000 share purchase warrants expired unexercised:

At June 30, 2002, 666,666 share purchase warrants with an exercise price of $2.27 (US $1.50) remain outstanding. These warrants expire September 4, 2002.

(f) Escrow agreement:

The Company has nil common shares subject to an escrow agreement.

(Expressed in Canadian Dollars)

Years Ended June 30, 2002 & 2001

(g) Normal course issuer bid:

On June 18, 2001, the Company received approval from the TSX Venture Exchange for a normal course issuer bid. Under the terms of the bid, the Company could buy back up to 1,369,884 common shares from time to time at prevailing market prices during the one-year period ended June 15, 2002. During the year ended June 30, 2002, the Company repurchased 689,000 (2001 – nil) of its common shares for $284,165 (average of $0.41 per share). All shares repurchased were cancelled and returned to the authorized and unissued share capital of the Company. Upon cancellation of the shares, share capital was reduced at the imputed per share value and the difference between the share capital reduction and the actual amount paid was credited to contributed surplus in the amount of $1,042,709.

Subsequent to June 30, 2002, the Company filed an application with the TSX Venture Exchange for a second normal course issuer bid. Under the terms of the application, the Company could buy back up to 1,314,487 common shares from time to time at prevailing market prices during the one-year period commencing on the application approval date.

7. SEGMENTED INFORMATION:

The Company carries on business in the computer security monitoring industry and all sales are made in this segment. Its activities are carried out in the United States, Canada and internationally through resellers in the United Kingdom and South Africa. For the year ended June 30, 2002, monitoring revenues in the United States were $4,091,214 (2001 – $3,062,539) and in Canada were $601,725 (2001 – $576,910). Installation services, licensing fees and other revenues in the United States were $119,330 for the year ended June 30, 2002 (2001 – $73,057).

8. INCOME TAXES:

Income tax expense for the year ended June 30, 2002 differs from that calculated by applying statutory rates for the following reasons:

		2002	2001
Combined Canadian federal and provincial income tax recoveries at expected rate of 42.1% (2001 – 45.11%)	$	**(2,326,076)**	(2,312,303)
Permanent and other differences		**1,262,797**	957,030
Differences due to changes in enacted rates		**93,215**	181,293
Foreign losses tax effected at lower rates		**638,647**	363,333
Losses not tax effected		**331,417**	810,647
	$	**—**	—

The tax effect of the significant temporary differences which would comprise tax assets and liabilities at June 30, 2002 are as follows:

		2002	2001
FUTURE TAX ASSETS (LIABILITIES):			
Property and equipment	$	**348,122**	236,072
Cumulative eligible capital deductions		**10,805**	10,726
Deferred revenue		**1,458,349**	1,227,250
Operating loss carry forwards		**6,806,571**	6,141,968
Share issue costs		**334,505**	449,540
Scientific research and experimental development expenditure carry forwards		**232,121**	230,426
Loans to directors and employees		**(114,689)**	—
Working capital		**(5,784)**	4,518
Total future tax assets		**9,070,000**	8,300,500
Valuation allowance		**(9,070,000)**	(8,300,500)
Net future tax assets	**$**	**—**	—

In assessing the realizability of future tax assets, management considers whether it is more likely than not that some portion or all of the future tax assets will not be realized. 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. Management considers the scheduled reversal of future tax 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 carry forward period.

(Expressed in Canadian Dollars)

8. INCOME TAXES CONTINUED:

The Company has approximately $16,700,000 of non-capital losses available for Canadian income tax purposes to reduce taxable income of future years that expire as follows:

Year ending June 30:

2003	$	1,100,000
2004		2,900,000
2005		3,400,000
2006		3,300,000
2007		2,400,000
2008		2,000,000
2009		1,600,000
	$	16,700,000

The Company also has available unclaimed scientific research and experimental development expenditures of approximately $652,000 which may be carried forward indefinitely and used to reduce future taxable income.

In addition, the Company has approximately $2,500,000 of net operating loss carry forwards available for US income tax purposes to reduce taxable income of future years. These net operating loss carry forwards expire in 2019 to 2022.

9. COMMITMENT:

The Company has future minimum lease payments under an operating lease to May 31, 2006 as follows:

Year ending June 30:

2003	$	214,116
2004		214,116
2005		214,116
2006		196,273
	$	838,621

10. COMPARATIVE FIGURES:

Certain comparative figures have been reclassified to conform to the presentations adopted during the current year.

BOARD OF DIRECTORS

John Livingston
Chairman, President & Chief Executive Officer
Absolute Software
Vancouver, BC

Christian Cotichini
Vancouver, BC

Terry Libin
Calgary, AB

Ian Reid
Vancouver, BC

Peter Scott
Executive Vice President & Chief Financial Officer
Absolute Software
Vancouver, BC

OFFICERS AND SENIOR MANAGEMENT

John Livingston
President & Chief Executive Officer

Peter Scott
Executive Vice President & Chief Financial Officer

Phil Gardner
Chief Technology Officer

Michael Anfield
Vice President, Recovery Services

Rob Chase
Vice President Finance & Corporate Controller

Bob Chow
Vice President Sales

Ben Haidri
Vice President Business Development & Marketing

Don Hughes
Area Vice President Channel Sales

Fred McConnell
Vice President Development & Operations

Mark St. Quintin
Vice President Product Management

Leo Raffin
Corporate Secretary

AUDITORS

KPMG LLP
Vancouver, BC

TRUST AGENT

CIBC Mellon Trust
www.cibcmellon.com

LEGAL COUNSEL

Lang Michener
Vancouver, BC

COMMON SHARES

Absolute Software common shares are traded on the TSX Venture Exchange (TSX-VEN) under the trading symbol ABT.

ADDITIONAL INFORMATION

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Courtney Chauvin, Public Relations
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ANNUAL GENERAL MEETING

Absolute Software's Annual General Meeting will take place at 3:00 pm, Thursday, November 14, 2002 at the Terminal City Club in Vancouver, BC.

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