

Interim Condensed Consolidated Financial Statements of

ABSOLUTE SOFTWARE CORPORATION

Three and six months ended December 31, 2016 and 2015

(Unaudited)

ABSOLUTE SOFTWARE CORPORATION
Condensed Consolidated Statements of Financial Position
(Expressed in United States dollars) (Unaudited)

| | Notes | December 31, 2016 | June 30, 2016 |
|---------------------------------|-------------|----------------------|-----------------------|
| ASSETS | | | |
| CURRENT | | | |
| Cash and cash equivalents | | \$ 37,066,069 | \$ 23,092,852 |
| Short-term investments | (Note 3) | 636,502 | 11,637,085 |
| Trade and other receivables | (Note 4) | 13,812,180 | 21,138,351 |
| Income taxes receivable | (Note 10) | 1,056,837 | - |
| Prepaid expenses and other | | 2,255,667 | 2,379,234 |
| | | 54,827,255 | 58,247,522 |
| INVESTMENTS | (Note 3) | - | 12,821,302 |
| PROPERTY AND EQUIPMENT | | 6,729,590 | 5,853,222 |
| DEFERRED INCOME TAX ASSETS | (Note 10) | 22,246,391 | 22,353,391 |
| INTANGIBLE ASSETS AND GOODWILL | (Note 5) | 14,783,864 | 15,382,262 |
| | | \$ 98,587,100 | \$ 114,657,699 |
| LIABILITIES | | | |
| CURRENT | | | |
| Trade and other payables | (Note 6) | \$ 14,181,223 | \$ 13,942,922 |
| Income taxes payable | (Note 10) | - | 5,990,927 |
| Accrued warranty | | 490,000 | 460,000 |
| Deferred revenue – current | (Note 7) | 71,130,316 | 72,464,399 |
| | | 85,801,539 | 92,858,248 |
| DEFERRED REVENUE | (Note 7) | 62,592,387 | 65,509,763 |
| | | 148,393,926 | 158,368,011 |
| CONTINGENCIES | (Note 13) | | |
| SHAREHOLDERS' DEFICIENCY | | | |
| Share capital | (Note 9(b)) | 59,721,564 | 58,607,382 |
| Equity reserve | | 38,472,524 | 36,732,175 |
| Treasury shares | (Note 9(j)) | (666,546) | - |
| Deficit | | (147,334,368) | (139,049,869) |
| | | (49,806,826) | (43,710,312) |
| | | \$ 98,587,100 | \$ 114,657,699 |

SUBSEQUENT EVENTS (Note 14)

See accompanying notes to the Condensed Consolidated Financial Statements.

Approved on behalf of the Board on February 6, 2017:

(signed) "Daniel P. Ryan"
Daniel P. Ryan, Director

(signed) "Josef Vejvoda"
Josef Vejvoda, Director

ABSOLUTE SOFTWARE CORPORATION

Condensed Consolidated Statements of Operations and Comprehensive Income

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

| | Notes | Three months ended December 31, | | Six months ended December 31, | |
|--|-------------|------------------------------------|---------------|----------------------------------|---------------|
| | | 2016 | 2015 | 2016 | 2015 |
| REVENUE | | \$ 22,450,143 | \$ 21,142,083 | \$ 44,935,007 | \$ 45,125,164 |
| COST OF REVENUE | | 3,955,548 | 3,220,448 | 7,462,092 | 6,671,346 |
| GROSS MARGIN | | 18,494,595 | 17,921,635 | 37,472,915 | 38,453,818 |
| OPERATING EXPENSES | | | | | |
| Sales and marketing | | 11,056,328 | 11,216,424 | 22,414,917 | 23,008,701 |
| Research and development | | 4,897,163 | 3,078,843 | 9,253,788 | 6,077,135 |
| General and administration | | 3,464,838 | 2,420,579 | 6,425,475 | 5,232,449 |
| Share-based compensation | (Note 9(i)) | 1,219,924 | 959,096 | 2,217,475 | 2,003,966 |
| | | 20,638,253 | 17,674,942 | 40,331,655 | 36,322,251 |
| OPERATING (LOSS) INCOME | | (2,143,658) | 246,693 | (2,838,740) | 2,131,567 |
| OTHER (EXPENSE) INCOME | | | | | |
| Interest income, net | | 5,647 | 82,494 | 47,586 | 179,297 |
| Foreign exchange loss | | (49,735) | (718,714) | (29,245) | (796,062) |
| Gain on disposal of business unit | | - | 14,098,066 | - | 14,098,066 |
| | | (44,088) | 13,461,846 | 18,341 | 13,481,301 |
| NET (LOSS) INCOME BEFORE INCOME TAXES | | (2,187,746) | 13,708,539 | (2,820,399) | 15,612,868 |
| INCOME TAX RECOVERY (EXPENSE) | (Note 10) | 345,000 | (4,960,000) | 188,000 | (5,850,000) |
| NET (LOSS) INCOME AND COMPREHENSIVE (LOSS) INCOME | | \$ (1,842,746) | \$ 8,748,539 | \$ (2,632,399) | \$ 9,762,868 |
| BASIC (LOSS) INCOME PER SHARE | | \$ (0.05) | \$ 0.22 | \$ (0.07) | \$ 0.23 |
| DILUTED (LOSS) INCOME PER SHARE | | \$ (0.05) | \$ 0.21 | \$ (0.07) | \$ 0.22 |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING, BASIC | (Note 9(k)) | 39,019,022 | 39,975,241 | 38,992,040 | 42,219,971 |

See accompanying notes to the Condensed Consolidated Financial Statements.

ABSOLUTE SOFTWARE CORPORATION

Condensed Consolidated Statement of Changes in Shareholders' Deficiency

(Expressed in United States dollars) (Unaudited)

| | Share Capital | | | | | Total |
|---|-------------------------------|----------------------|----------------------|---------------------|-------------------------|------------------------|
| | Number of Common shares | Amount | Equity reserve | Treasury Shares | Deficit | |
| BALANCE, JUNE 30, 2015 | 44,862,344 | \$ 59,607,392 | \$ 35,322,483 | \$ - | \$ (108,066,367) | \$ (13,136,492) |
| Shares issued on options exercised | 454,675 | 2,738,242 | (930,618) | - | - | 1,807,624 |
| Shares issued under Employee Share Purchase Plan | 67,411 | 359,596 | - | - | - | 359,596 |
| Shares issued under Performance Share Unit Plan | 10,000 | - | - | - | - | - |
| Shares repurchased and cancelled under the Normal Course Issuer Bid | (678,700) | (53,474) | - | - | (168,796) | (222,270) |
| Shares repurchased and cancelled under the Substantial Issuer Bid | (6,250,000) | (7,685,894) | - | - | (30,603,647) | (38,289,541) |
| Share-based compensation | - | - | 1,761,133 | - | - | 1,761,133 |
| Dividends paid | - | - | - | - | (4,667,691) | (4,667,691) |
| Net income and total comprehensive income | - | - | - | - | 9,762,868 | 9,762,868 |
| BALANCE, DECEMBER 31, 2015 | 38,465,730 | \$ 54,965,862 | \$ 36,152,998 | \$ - | \$ (133,743,633) | \$ (42,624,773) |
| Shares issued on options exercised | 429,375 | 2,231,597 | (821,366) | - | - | 1,410,231 |
| Shares issued under Employee Share Purchase Plan | 58,450 | 262,284 | - | - | - | 262,284 |
| Shares issued under Phantom Share Unit plan | 150,552 | 1,516,167 | (1,100,692) | - | - | 415,475 |
| Shares repurchased and cancelled under the Normal Course Issuer Bid | (222,800) | (368,528) | - | - | (678,537) | (1,047,065) |
| Share-based compensation | - | - | 2,501,235 | - | - | 2,501,235 |
| Dividends paid | - | - | - | - | (4,593,513) | (4,593,513) |
| Net income and total comprehensive income | - | - | - | - | (34,186) | (34,186) |
| BALANCE, JUNE 30, 2016 | 38,881,307 | \$ 58,607,382 | \$ 36,732,175 | \$ - | \$ (139,049,869) | \$ (43,710,312) |
| Shares issued on options exercised | 225,925 | 1,290,359 | (430,275) | - | - | 860,084 |
| Shares issued under Employee Share Purchase Plan | 42,126 | 190,610 | - | - | - | 190,610 |
| Shares issued under Phantom Share Unit Plan | 6,844 | 46,851 | (46,851) | - | - | - |
| Shares repurchased and cancelled under the Normal Course Issuer Bid | (132,400) | (195,522) | - | - | (416,520) | (612,042) |
| Shares committed to be repurchased under the Normal Course Issuer Bid | - | (218,116) | - | - | (486,702) | (704,818) |
| Treasury shares repurchased under the Normal Course Issuer Bid | - | - | - | (666,546) | - | (666,546) |
| Share-based compensation | - | - | 2,217,475 | - | - | 2,217,475 |
| Dividends paid | - | - | - | - | (4,748,878) | (4,748,878) |
| Net loss and total comprehensive loss | - | - | - | - | (2,632,399) | (2,632,399) |
| BALANCE, DECEMBER 31, 2016 | 39,023,802 | \$ 59,721,564 | \$ 38,472,524 | \$ (666,546) | \$ (147,334,368) | \$ (49,806,826) |

See accompanying notes to the Condensed Consolidated Financial Statements.

ABSOLUTE SOFTWARE CORPORATION

Condensed Consolidated Statements of Cash Flows

Three and six months ended December 31, 2016 and 2015
(Expressed in United States dollars) (Unaudited)

| | Notes | Three months ended December 31, | | Six months ended December 31, | |
|--|-------------|------------------------------------|----------------------|----------------------------------|----------------------|
| | | 2016 | 2015 | 2016 | 2015 |
| OPERATING ACTIVITIES | | | | | |
| Net (loss) income | | \$ (1,842,746) | \$ 8,748,539 | \$ (2,632,399) | \$ 9,762,868 |
| Items not involving cash | | | | | |
| Amortization of property and equipment | | 717,321 | 533,413 | 1,399,769 | 1,059,516 |
| Amortization of acquired intangible assets | (Note 5) | 34,333 | 263,723 | 84,409 | 379,599 |
| Amortization of intangible assets – contract costs and brand | (Note 5) | 2,237,148 | 1,852,157 | 4,485,758 | 3,746,948 |
| Share-based compensation | (Note 9(i)) | 1,215,437 | 875,414 | 2,212,988 | 1,761,133 |
| Deferred income taxes | (Note 10) | 226,000 | (594,000) | 107,000 | (1,131,000) |
| Gain on disposal of business unit | | - | (14,098,066) | - | (14,098,066) |
| Transaction fees on disposal of business unit | | - | (1,257,910) | - | (1,257,910) |
| Non-cash interest and amortization of investment premium | | 513,236 | 266,999 | 466,885 | 367,406 |
| Change in non-cash working capital | | | | | |
| Trade and other receivables | | (1,453,667) | 770,281 | 7,326,171 | 9,194,214 |
| Prepaid expenses and other | | 554,603 | 149,748 | 123,567 | 116,975 |
| Intangible assets – contract costs and brand additions | (Note 5) | (2,158,577) | (2,052,074) | (4,032,572) | (4,660,152) |
| Trade and other payables | | 1,463,039 | 2,714,727 | (203,268) | 1,451,141 |
| Income taxes payable | | (1,212,616) | 5,344,420 | (4,423,874) | 4,429,828 |
| Accrued warranty | | - | (90,000) | 30,000 | (50,000) |
| Deferred revenue | | (1,480,486) | (2,074,444) | (4,251,459) | (4,740,569) |
| CASH (USED IN) FROM OPERATING ACTIVITIES | | (1,186,975) | 1,352,927 | 692,975 | 6,331,931 |
| INVESTING ACTIVITIES | | | | | |
| Purchase of property and equipment | | (1,041,818) | (413,198) | (3,082,984) | (860,342) |
| Purchase of intangible assets | | - | (225,000) | - | (225,000) |
| Proceeds from disposal of business unit | | - | 11,046,737 | - | 11,046,737 |
| Income taxes paid on disposal of business unit | | - | - | (2,623,890) | - |
| Proceeds from investments | | 23,355,000 | 3,700,000 | 23,355,000 | 3,700,000 |
| Purchase of investments | | - | (201,124) | - | (201,124) |
| CASH FROM INVESTING ACTIVITIES | | 22,313,182 | 13,907,415 | 17,648,126 | 13,460,271 |
| FINANCING ACTIVITIES | | | | | |
| Repurchase of common shares for cancellation | (Note 9(b)) | (612,040) | (38,105,614) | (612,040) | (42,454,880) |
| Dividends paid | (Note 9(h)) | (2,316,379) | (2,290,909) | (4,748,878) | (4,667,691) |
| Issuance of common shares | (Note 9(b)) | 451,026 | 1,685,313 | 973,048 | 2,067,684 |
| CASH USED IN FINANCING ACTIVITIES | | (2,477,393) | (38,711,210) | (4,387,870) | (45,054,887) |
| FOREIGN EXCHANGE EFFECT ON CASH | | (45,866) | (589,900) | 19,986 | (750,800) |
| INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | | 18,602,948 | (24,040,768) | 13,973,217 | (26,013,485) |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | | 18,463,121 | 42,132,833 | 23,092,852 | 44,105,550 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | | \$ 37,066,069 | \$ 18,092,065 | \$ 37,066,069 | \$ 18,092,065 |

SUPPLEMENTAL CASH FLOW INFORMATION (NOTE 11)

See accompanying notes to the Condensed Consolidated Financial Statements.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

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 endpoint security and data risk management solutions for computing devices such as desktops, laptops, tablets and smartphones. The Company’s solutions include remote data and device security, powered by its proprietary and patented Persistence technology. The Company markets its solutions through computer original equipment manufacturers (“OEMs”), distributors, value added resellers, and directly to its customers, which includes 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 and Latin American regions, the majority of its sales are generated in North America. The Company’s head office, principal address and registered office is Suite 1400, 1055 Dunsmuir Street, Vancouver, British Columbia, Canada, V7X 1K8. The Company trades on the TSX under the symbol ABT.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) *Basis of presentation*

These unaudited interim condensed consolidated financial statements are prepared in accordance with International Financial Reporting Standards applicable to interim financial information, as outlined in International Accounting Standard (“IAS”) 34, *Interim Financial Reporting*, and using the accounting policies consistent with those in the audited consolidated financial statements as at and for the year ended June 30, 2016.

These unaudited interim condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries; however, they do not include all disclosures normally provided in annual consolidated financial statements and should be read in conjunction with the annual consolidated financial statements as at and for the year ended June 30, 2016. Interim results are not necessarily indicative of the results expected for the fiscal year.

(b) *Significant accounting judgment*

The critical judgment that the Company’s management has made in the process of applying the Company’s accounting policies, apart from those involving estimations (Note 2(c)), that has the most significant effect on the amounts recognized in the Company’s consolidated financial statements, is related to the determination of the functional currency for the Company and its subsidiaries.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) *Key sources of estimation uncertainty*

The preparation of these interim consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from these estimates. The interim consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the interim consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the date of the statement of financial position, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, include, but are not limited to, the following:

- the assessment of the carrying values of allowances for unrecoverable accounts receivable and assets;
- the inputs used in accounting for share-based compensation in the statement of operations; and
- the recognition and recoverability of the Company's deferred tax assets.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

3. SHORT-TERM INVESTMENTS AND INVESTMENTS

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

| | <u>December 31, 2016</u> | <u>June 30, 2016</u> |
|-----------------------------|--------------------------|----------------------|
| Term deposits | \$ 636,502 | \$ 650,975 |
| Investment grade securities | - | 10,986,110 |
| | <u>\$ 636,502</u> | <u>\$ 11,637,085</u> |

At June 30, 2016, the Company's long-term investments are comprised entirely of investment grade securities. All investments are classified as held to maturity.

4. TRADE AND OTHER RECEIVABLES

The Company's trade and other receivables are comprised of the following:

| | <u>December 31, 2016</u> | <u>June 30, 2016</u> |
|---------------------------------|--------------------------|----------------------|
| Trade receivables | \$ 13,915,276 | \$ 21,207,490 |
| Other receivables | 178,465 | 196,527 |
| Allowance for doubtful accounts | (281,561) | (265,666) |
| | <u>\$ 13,812,180</u> | <u>\$ 21,138,351</u> |

At December 31, 2016, 3% of the Company's accounts receivable balance is over 90 days past due (June 30, 2016 – 2%). As at December 31, 2016, 23%, 21%, 18%, and 15%, (June 30, 2016 - 15%, 30%, 26%, and 13%) of the receivable balances are owing from four OEM and distributor partners.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

5. INTANGIBLE ASSETS AND GOODWILL

The following tables summarize intangible asset activity for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, 2016 | | | |
|-----------------------|------------------------------------|---------------------|-----------------------|--------------------------|
| | Carrying amount - opening | Additions | Amortization | Carrying amount - ending |
| Contract costs | \$ 13,923,735 | \$ 3,907,327 | \$ (4,382,942) | \$ 13,448,120 |
| Patents and other | 164,327 | - | (145,212) | 19,115 |
| Brand rights – LoJack | 194,200 | 125,245 | (102,816) | 216,629 |
| Goodwill | 1,100,000 | - | - | 1,100,000 |
| | \$ 15,382,262 | \$ 4,032,572 | \$ (4,630,970) | \$ 14,783,864 |

| | Six months ended December 31, 2015 | | | | |
|-----------------------------------|------------------------------------|---------------------|-----------------------|---------------------|--------------------------|
| | Carrying amount - opening | Additions | Amortization | Disposals | Carrying amount - ending |
| Contract costs | \$ 12,323,146 | \$ 4,611,029 | \$ (3,703,558) | \$ (753,397) | \$ 12,477,220 |
| Software – Palisade | 133,333 | - | (91,667) | - | 41,666 |
| Customer relationships – Palisade | 91,666 | - | (20,831) | - | 70,835 |
| Patents and other | 572,748 | 225,000 | (204,344) | - | 593,404 |
| Brand rights – LoJack | 81,479 | 49,123 | (43,390) | - | 87,212 |
| Goodwill | 1,100,000 | - | - | - | 1,100,000 |
| | \$ 14,302,372 | \$ 4,885,152 | \$ (4,063,790) | \$ (753,397) | \$ 14,370,337 |

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

Three and six months ended December 31, 2016 and 2015

(Expressed in United States dollars) (Unaudited)

6. TRADE AND OTHER PAYABLES

The Company's trade and other payables are comprised of the following:

| | <u>December 31, 2016</u> | <u>June 30, 2016</u> |
|-------------------------------|--------------------------|----------------------|
| Trade payables | \$ 5,488,984 | \$ 6,533,633 |
| Payroll and employee benefits | 4,535,143 | 5,484,393 |
| Lease inducements | 1,234,909 | 19,980 |
| Accrued liabilities | 1,217,932 | 1,595,187 |
| Share repurchase accrual | 704,818 | - |
| Treasury share accrual | 666,546 | - |
| Sales taxes payable | 332,891 | 309,729 |
| | <u>\$ 14,181,223</u> | <u>\$ 13,942,922</u> |

7. DEFERRED REVENUE

The following table provides a reconciliation of deferred revenue balances on billings to invoiced billings, revenue, and other adjustments, for each of our Data and Device Security segment and our historical Endpoint and Service Management segment:

| Data and Device Security | Six months ended December 31, | |
|---------------------------------|--------------------------------------|----------------------|
| | <u>2016</u> | <u>2015</u> |
| Balance, beginning of period | \$ 137,974,162 | \$ 135,316,725 |
| Billings | 40,683,857 | 38,436,614 |
| Revenue recognized | (44,935,007) | (42,246,973) |
| Other adjustments | (309) | 473 |
| Balance, end of period | <u>133,722,703</u> | <u>131,506,839</u> |
| Less: current portion | <u>(71,130,316)</u> | <u>(68,187,611)</u> |
| | <u>\$ 62,592,387</u> | <u>\$ 63,319,228</u> |

| Endpoint and Service Management | Six months ended December 31, | |
|--|--------------------------------------|--------------|
| | <u>2016</u> | <u>2015</u> |
| Balance, beginning of period | \$ - | \$ 9,394,624 |
| Billings | - | 2,030,656 |
| Revenue recognized | - | (2,961,339) |
| Divested | - | (8,463,941) |
| Balance, end of period | <u>\$ -</u> | <u>\$ -</u> |

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

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(Expressed in United States dollars) (Unaudited)

8. POST-RETIREMENT BENEFITS AND REORGANIZATION CHARGES

During the three months ended December 31, 2016, under the terms of an agreement with a former senior officer, the Company incurred post-retirement benefits in the amount of \$638,000. In addition, during the six months ended December 31, 2016, the Company reorganized certain functional departments to optimize internal resources. Pursuant to the reorganization, the Company incurred termination benefits amounting to \$2,121,148 (2015 - \$753,726).

These post-retirement benefits and reorganization charges were attributable to the following areas for the three and six months ended December 31, 2016 and 2015:

| | Three months ended December 31, | | Six months ended December 31, | |
|----------------------------|------------------------------------|-------------|----------------------------------|-------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Research and development | \$ 756,800 | \$ - | \$ 1,058,774 | - |
| Sales and marketing | 366,300 | - | 773,780 | \$ 753,726 |
| Cost of revenue | 427,408 | - | 535,240 | - |
| General and administration | 352,358 | - | 391,354 | - |
| | <u>\$ 1,902,866</u> | <u>\$ -</u> | <u>\$ 2,759,148</u> | <u>\$ 753,726</u> |

9. 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 six months ended December 31, 2016, the Company issued 225,925 common shares on exercise of employee stock options for total proceeds of \$860,084. An amount of \$430,275 related to the original fair value of the options was transferred from equity reserve to common shares upon exercise.

During the six months ended December 31, 2016, the Company issued 42,126 common shares pursuant to its employee share purchase plan for total proceeds of \$190,610.

During the six months ended December 31, 2016, the Company issued 6,844 common shares pursuant to its Phantom Share Unit Plan.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

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(Expressed in United States dollars) (Unaudited)

9. SHARE CAPITAL (Continued)

During the six months ended December 31, 2015, the Company issued 454,675 common shares on exercise of employee stock options for total proceeds of \$1,807,624. An amount of \$930,618 related to the original fair value of the options was transferred from equity reserve to common shares upon exercise.

During the six months ended December 31, 2015, the Company issued 67,411 common shares pursuant to its employee share purchase plan for total proceeds of \$359,596.

During the six months ended December 31, 2015, the Company issued 10,000 common shares pursuant to the Phantom Share Unit Plan.

On August 23, 2016, the Company received approval from the TSX to commence a Normal Course Issuer Bid (the "Bid") on August 29, 2016 that enables the Company to purchase and cancel up to 2,643,256 of its common shares or return such shares to treasury. The Bid allows for the purchase of up to 19,864 common shares on a daily basis until August 28, 2017, except where purchases are made in accordance with "block purchases" exemptions under applicable TSX policies. Prior to August 29, 2016, the Company purchased and cancelled shares under previously approved Normal Course Issuer Bids (together, the "Bids").

Under the Bids, during the six months ended December 31, 2016, the Company repurchased and cancelled 132,400 common shares for a total cost of \$612,042. On cancellation of the common shares, the difference between the purchase price and the average book value of the common shares is recorded in deficit, which amounted to \$416,520.

(c) *Stock Option Plan*

The Company's share-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, 2009, and 2015). Under the Option Plan, the maximum number of common shares reserved for issuance is limited to 12% of the number of common shares outstanding, less the amount that are issuable under the Phantom Share Unit Plan and Performance and Restricted Share Unit Plan. On this basis, at December 31, 2016, the maximum number of common shares available under the Option Plan was 3,691,730 (June 30, 2016 – 3,904,973), of which 197,835 remained available for grant thereunder.

ABSOLUTE SOFTWARE CORPORATION

Notes to the Condensed Consolidated Financial Statements

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(Expressed in United States dollars) (Unaudited)

9. SHARE CAPITAL (Continued)

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 7 years from the date of grant of the option, and are generally granted with a four year vesting period (25% vesting on each anniversary date).

The following table summarizes activity under the Option Plan for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, | | | |
|----------------------------------|-------------------------------|---------------------------------------|-------------------|---------------------------------------|
| | 2016 | | 2015 | |
| | Number of options | Weighted average exercise price (CAD) | Number of options | Weighted average exercise price (CAD) |
| Outstanding, beginning of period | 3,718,950 | \$ 7.13 | 4,202,925 | \$ 6.63 |
| Granted | 122,720 | 7.31 | 182,500 | 8.09 |
| Exercised | (225,925) | 5.03 | (454,675) | 5.09 |
| Forfeited | (95,475) | 8.52 | (106,125) | 5.25 |
| Expired | (26,375) | 8.15 | (22,775) | 8.69 |
| Outstanding, end of period | 3,493,895 | \$ 7.22 | 3,801,850 | \$ 6.91 |

Fair values – Option Plan

The total fair value of options granted under the Option Plan in the six months ended December 31, 2016 was \$112,108 (2015 - \$184,288). The weighted average grant date fair value of options granted during the six months ended December 31, 2016 was \$0.91 (2015 - \$1.01).

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:

| | Six months ended December 31, | |
|--------------------------|-------------------------------|------|
| | 2016 | 2015 |
| Risk-free interest rate | 0.8% | 0.6% |
| Dividend yield | 4.4% | 4.0% |
| Expected life (in years) | 4.0 | 3.8 |
| Volatility | 31% | 31% |

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(Expressed in United States dollars) (Unaudited)

9. SHARE CAPITAL (Continued)

(d) Phantom Share Unit Plan

The Company's share-based compensation plans also include a Phantom Share Unit ("PhSU") Plan.

In 2015, the Company's shareholders ratified the PhSU Plan. Under the PhSU Plan, the maximum number of common shares reserved for issuance is limited to 12% of the number of common shares outstanding, less the amount that are issuable under the Option Plan, the Performance and Restricted Share Unit Plan, and the Employee Share Purchase Plan. At December 31, 2016, the Company had exceeded this limit by 83,995 PhSUs, which is permissible under certain conditions.

Terms and conditions of PhSUs granted are determined pursuant to the PhSU Plan. Under the PhSU Plan, PhSUs are issued to eligible persons and generally vest over a two or three year period (50% or 33.3%, respectively, vesting on each anniversary date). PhSUs may be settled, at the Company's sole discretion, in common shares, cash, or a combination thereof. If settled in cash, the amount paid is based on the volume weighted average daily price for the five days preceding the payment.

The following table summarizes activity under the PhSU Plan for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, | | | |
|----------------------------------|-------------------------------|-----------------------|-----------------|-----------------------|
| | 2016 | | 2015 | |
| | Number of units | Grant date fair value | Number of units | Grant date fair value |
| Outstanding, beginning of period | 439,558 | \$ 7.51 | 516,365 | \$ 7.60 |
| Granted | 4,503 | 7.52 | 71,078 | 6.32 |
| Released | (5,990) | 6.89 | (10,000) | 6.99 |
| Forfeited | (2,008) | 6.99 | (12,765) | 6.99 |
| Outstanding, end of period | 436,063 | \$ 7.52 | 564,678 | \$ 7.45 |

The total fair value of PhSUs granted under the PhSU Plan in the six months ended December 31, 2016 was \$33,841 (2015 - \$449,213). The weighted average grant date fair value of PhSUs granted during the six months ended December 31, 2016 was \$7.52 (2015 - \$6.33). At December 31, 2016, 115,361 the outstanding PhSUs had vested.

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9. SHARE CAPITAL (Continued)

(e) Performance and Restricted Share Unit Plan

The Company's share-based compensation plans also include a Performance and Restricted Share Unit ("PRSU") Plan. Under the PRSU Plan, the Company may issue Performance Share Units ("PSU"s) and Restricted Share Units ("RSU"s).

In the year ended June 30, 2016, the Company's shareholders ratified the PRSU Plan. Under the PRSU Plan, the maximum number of common shares reserved for issuance is limited to 12% of the number of common shares outstanding, less the amount that are issuable under the Option Plan and the PhSU Plan. On this basis, at December 31, 2016, 197,835 common shares were eligible for grant under the PRSU Plan.

In addition, in the six months ended December 31, 2016, the Company instituted a Market-based PRSU Plan ("Market PRSU Plan"). Shares issued pursuant to the Market PRSU Plan will be acquired, at the Company's election, under the terms of permissible share buyback mechanisms, including the Company's Normal Course Issuer Bid, and will not be issued from treasury.

Terms and conditions of PSUs and RSUs granted are determined by the Board of Directors.

Performance Share Units

Under the PRSU Plan, PSUs are issued to eligible persons and generally vest after a three year period (100% cliff vesting on the third anniversary date). The number of PSUs that ultimately vest is based on an Adjustment Factor, as determined by the Board of Directors at the date of grant, and can range from 0% to 200% of the number of units initially granted. The term of the PSU grants is three years from the date of grant.

The following table summarizes PSU activity under the PRSU Plan for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, | |
|----------------------------------|----------------------------------|--------------------|
| | 2016 | 2015 |
| | Number of units | Number of units |
| Outstanding, beginning of period | 49,811 | - |
| Granted | 68,359 | - |
| Outstanding, end of period | 118,170 | - |

The outstanding PSUs at December 31, 2016 include 40,000 units that were issued pursuant to the Market PRSU Plan.

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9. SHARE CAPITAL (Continued)

Fair values – Performance Share Units

The total fair value of PSUs granted under the PRSU Plan in the six months ended December 31, 2016 was \$594,606 (2015 - \$nil). The weighted average grant date fair value of PSUs granted during the six months ended December 31, 2016 was \$8.77 (2015 - \$nil). At December 31, 2016, none of the outstanding PSUs had vested.

The Adjustment Factor related to the PSUs granted was related to a market-based performance condition. The fair value of the PSUs granted was estimated on the grant date using a Monte Carlo simulation model, taking into account the fair value of the Company's common shares on the date of grant, potential future dividends accruing to the PSU holder's benefit, and encompassing a wide range of possible future market conditions.

Restricted Share Units

Under the PRSU Plan, RSUs are issued to eligible persons and generally vest over a three year period (33.3% vesting on each anniversary date). The term of the RSU grants is three years from the date of grant.

The following table summarizes RSU activity under the PRSU Plan for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, | |
|----------------------------------|--------------------------------------|----------------------------|
| | 2016 | 2015 |
| | Number of units | Number of units |
| Outstanding, beginning of period | 271,856 | - |
| Granted | 261,538 | - |
| Released | (851) | - |
| Forfeited | (4,083) | - |
| Outstanding, end of period | 528,460 | - |

The outstanding RSUs at December 31, 2016 include 51,567 units that were issued pursuant to the Market PRSU Plan.

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9. SHARE CAPITAL (Continued)

Fair values – Restricted Share Units

The total fair value of RSUs granted under the PRSU Plan in the six months ended December 31, 2016 was \$1,487,051 (2015 - \$nil). The weighted average grant date fair value of RSUs granted during the six months ended December 31, 2016 was \$5.75 (2015 - \$nil). At December 31, 2016, none of the outstanding RSUs had vested.

The fair value of the RSUs granted was estimated on the grant date using the fair value of the Company's common shares on the date of grant and potential future dividends accruing to the RSU holder's benefit.

(f) Deferred Share Unit Plan

The Company's share-based compensation plans also include a Deferred Share Unit ("DSU") Plan. The DSU Plan is a cash-settled share based compensation plan.

In the year ended June 30, 2016, the Company's shareholders ratified the DSU Plan. Terms and conditions of DSUs granted are determined by the Board of Directors.

Under the DSU Plan, DSUs are issued to eligible persons and generally vest over a one year period (25% per three months). DSUs are not eligible for redemption until the unitholder ceases to be an eligible person. The term of the DSU grants is coterminous with the date the unitholder ceases to be an eligible person.

The following table summarizes activity under the DSU Plan for the six months ended December 31, 2016 and 2015:

| | Six months ended December 31, | |
|--|--------------------------------------|------------------------|
| | 2016 | 2015 |
| | Number of units | Number of units |
| Outstanding, beginning and end of period | 104,000 | - |

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9. SHARE CAPITAL (Continued)

Fair values – Deferred Share Units

The total fair value of DSUs granted under the DSU Plan in the six months ended December 31, 2016 was \$nil (2015 - \$nil). The weighted average grant date fair value of DSUs granted during the six months ended December 31, 2016 was \$nil (2015 - \$nil).

(g) Employee Share Purchase Plan

The Company's share-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 six months ended December 31, 2016, 42,126 common shares (2015 – 67,411 common shares) were issued from treasury under the Purchase Plan at a weighted average price of \$4.04 (2015 - \$5.53) per share.

At December 31, 2016, 324,159 common shares remained available for grant under the Purchase Plan.

(h) Dividends

In the six months ended December 31, 2016, the Company declared two quarterly dividends of CAD\$0.08 per share on its common shares. The dividends were paid in cash to shareholders of record at the close of business on August 5, 2016 (CAD\$0.08 per common share) and November 25, 2016 (CAD\$0.08 per common share).

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9. SHARE CAPITAL (Continued)

(i) Share-based compensation

The Company's share-based compensation for the three and six months ended December 31, 2016 and 2015 was comprised as follows:

| | Three months ended December 31, | | Six months ended December 31, | |
|------------------------------|------------------------------------|-------------------|----------------------------------|---------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Restricted share units | \$ 576,657 | \$ - | \$ 803,366 | \$ - |
| Phantom share unit plan | 300,227 | 498,440 | 604,623 | 1,069,210 |
| Stock option plan | 249,043 | 435,761 | 516,935 | 875,149 |
| Performance share units | 116,716 | - | 178,762 | - |
| Employee share purchase plan | 15,622 | 24,895 | 32,350 | 59,607 |
| Deferred share unit plan | (38,341) | - | 81,439 | - |
| | \$ 1,219,924 | \$ 959,096 | \$ 2,217,475 | \$ 2,003,966 |

The Company's share-based compensation was attributable to the following areas for the three and six months ended December 31, 2016 and 2015:

| | Three months ended December 31, | | Six months ended December 31, | |
|----------------------------|------------------------------------|-------------------|----------------------------------|---------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Cost of revenue | \$ 27,687 | \$ 69,519 | \$ 32,953 | \$ 126,336 |
| Sales and marketing | 444,328 | 94,431 | 730,865 | 356,474 |
| Research and development | 295,747 | 357,814 | 514,763 | 621,556 |
| General and administration | 452,162 | 437,332 | 938,894 | 899,600 |
| | \$ 1,219,924 | \$ 959,096 | \$ 2,217,475 | \$ 2,003,966 |

(j) Treasury shares

During the six months ended December 31, 2016, the Company acquired 104,000 treasury shares for a total cost of \$666,546 (2015 - \$nil). As the repurchase of the treasury shares was settled subsequent to December 31, 2016, this amount has been recorded in accrued liabilities. The treasury shares are presented as a deduction from shareholder's deficiency. The treasury shares were purchased in order to fund the Company's Market based PRSU Plan (note 9(e)).

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9. SHARE CAPITAL (Continued)

(k) *Potentially dilutive securities and diluted number of shares outstanding*

For the three and six months ended December 31, 2016, the basic and diluted weighted average number of common shares outstanding was the same. For the three and six months ended December 31, 2016, there were 1,011,751 and 1,060,791 potentially dilutive securities, respectively. For the three and six months ended December 31, 2015, the diluted weighted average number of common shares was 41,142,893 and 43,412,887, respectively.

10. INCOME TAXES

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 deferred income tax deductions is dependent upon the profitable operations of the Company in the tax jurisdictions in which such losses or deductions arise. The Company's interim tax provisions are estimated based on the expected effective tax rates applicable to the Company's operations for the year ended June 30, 2016.

The Company's income tax expense was comprised as follows:

| | Three months ended December 31, | | Six months ended December 31, | |
|---|------------------------------------|-----------------------|----------------------------------|-----------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Current income tax recovery (expense) | \$ 739,000 | \$ (5,693,000) | \$ 671,000 | \$ (7,194,000) |
| Deferred income tax (expense) recovery | (394,000) | 733,000 | (483,000) | 1,344,000 |
| | <u>\$ 345,000</u> | <u>\$ (4,960,000)</u> | <u>\$ 188,000</u> | <u>\$ (5,850,000)</u> |

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10. INCOME TAXES (Continued)

Income tax expense for the three and six months ended December 31, 2016 and 2015 differs from that calculated by applying statutory rates for the following reasons:

| | Three months ended | | Six months ended | |
|--|--------------------|----------------|------------------|----------------|
| | December 31, | | December 31, | |
| | 2016 | 2015 | 2016 | 2015 |
| Income before income taxes | \$ (2,187,529) | \$ 13,708,539 | \$ (2,820,182) | \$ 15,612,868 |
| Combined Federal and Provincial income tax rate | 26.00% | 26.00% | 26.00% | 26.00% |
| Tax recovery (expense) at statutory rate | 568,758 | (3,564,220) | 733,248 | (4,059,346) |
| Permanent differences | (149,487) | (198,324) | (318,992) | (384,137) |
| Foreign losses (income) tax effected at higher rates | 111,397 | (1,328,473) | 47,088 | (1,538,549) |
| Use of previously unrecognized tax losses | - | 147,891 | - | 148,906 |
| Losses and temporary differences for which no deferred asset has been recognized | (185,668) | (16,874) | (273,344) | (16,874) |
| Total income tax recovery (expense) | \$ 345,000 | \$ (4,960,000) | \$ 188,000 | \$ (5,850,000) |

At December 31, 2016, the Company had total net deferred tax assets of \$22.2 million (June 30, 2016 - \$22.4 million), primarily related to deferred revenue balances, and current income taxes receivable of \$810,521 (June 30, 2016 – Income taxes payable of \$5,990,927). In the three and six months ended December 31, 2016 and 2015, the Company's current tax payable is partially offset by estimated investment tax credit ("ITC") receivable balances. The ITCs were credited against research and development expenses, as the credit is generated by certain eligible scientific research and development expenditures ("SRED").

The ultimate realization of deferred 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 carry-forward periods. Management considers the scheduled reversal of deferred tax assets and liabilities, projected future taxable income, and tax planning strategies in making this assessment. The amount of the deferred tax asset considered realizable could change materially in the near term based on future taxable income during the carry-forward period.

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, deferred tax assets and operating loss carry-forwards.

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11. SUPPLEMENTAL CASH FLOW INFORMATION

Composition of cash and cash equivalents

At December 31 and June 30, 2016, cash and cash equivalents were comprised entirely of cash.

Other cash flow information

| | Three months ended December 31, | | Six months ended December 31, | |
|--|------------------------------------|-------------|----------------------------------|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| <i>Non-cash investing and financing activities</i> | | | | |
| Accrued purchases of property and equipment | \$ (208,305) | \$ (57,904) | \$ 806,847 | \$ (29,435) |

12. SEGMENTED INFORMATION

(a) *Operating Segments*

The Company and its subsidiaries have historically operated primarily in one principal business, that being the development, marketing, and support of endpoint security and data risk management, and endpoint management solutions for computing devices such as desktops, laptops, tablets and smartphones.

On July 1, 2015, the Company reorganized its internal information reported to the chief operating decision maker for the purposes of resource allocation and assessment of operational performance. This reorganization focused on the bifurcation of two markets in which the Company's products participate, namely, a) Data and Device Security and b) Endpoint and Service Management. As a result, the Company operated in these two operating segments.

The divestiture of the Absolute Manage and Absolute Service business unit on October 5, 2015 eliminated the Endpoint and Service Management segment.

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12. SEGMENTED INFORMATION (continued):

The Company operated solely in the Data and Device Security segment for the three and six months ended December 31, 2016. The Company's revenue, results, and other segment information for the three and six months ended December 31, 2015 is as follows:

| | Three months ended December 31, 2015 | | |
|-------------------------------|--------------------------------------|---------------------------------|---------------|
| | Data and Device Security | Endpoint and Service Management | Consolidated |
| Revenue from external sources | \$ 20,951,168 | \$ 190,915 | \$ 21,142,083 |
| Operating expenses | (18,905,230) | (233,928) | (19,139,158) |
| Share-based compensation | (959,096) | - | (959,096) |
| Depreciation and amortization | (797,136) | - | (797,136) |
| Interest income, net | 82,494 | - | 82,494 |
| Foreign exchange loss | (718,714) | - | (718,714) |
| Disposal of business unit | - | 14,098,066 | 14,098,066 |
| Income before income taxes | \$ (346,514) | \$ 14,055,053 | \$ 13,708,539 |
| Provision for income taxes | - | - | (4,960,000) |
| Net income | | | \$ 8,748,539 |

| | Six months ended December 31, 2015 | | |
|-------------------------------|------------------------------------|---------------------------------|---------------|
| | Data and Device Security | Endpoint and Service Management | Consolidated |
| Revenue from external sources | \$ 42,240,727 | \$ 2,884,437 | \$ 45,125,164 |
| Operating expenses | (37,651,854) | (1,898,662) | (39,550,516) |
| Share-based compensation | (2,003,966) | - | (2,003,966) |
| Depreciation and amortization | (1,439,115) | - | (1,439,115) |
| Interest income, net | 179,297 | - | 179,297 |
| Foreign exchange loss | (796,062) | - | (796,062) |
| Disposal of business unit | - | 14,098,066 | 14,098,066 |
| Income before income taxes | \$ 529,027 | \$ 15,083,841 | \$ 15,612,868 |
| Provision for income taxes | - | - | (5,850,000) |
| Net income | | | \$ 9,762,868 |

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12. SEGMENTED INFORMATION (continued):

(b) *Entity wide disclosures*

Geographic revenue information is based on the location of the customer invoiced. Long-lived assets include property and equipment and intangible assets.

| | Three months ended | | Six months ended | |
|----------------|----------------------|----------------------|----------------------|----------------------|
| | December 31, | | December 31, | |
| | 2016 | 2015 | 2016 | 2015 |
| Revenue | | | | |
| United States | \$ 19,653,184 | \$ 18,200,967 | \$ 39,254,544 | \$ 38,675,684 |
| Rest of world | 2,314,836 | 2,333,469 | 4,711,004 | 5,132,886 |
| Canada | 482,123 | 607,647 | 969,458 | 1,316,594 |
| | \$ 22,450,143 | \$ 21,142,083 | \$ 44,935,007 | \$ 45,125,164 |

| | December 31, 2016 | June 30, 2016 |
|---------------------------------|----------------------|----------------------|
| Long-lived assets | | |
| United States and rest of world | \$ 11,789,542 | \$ 12,239,412 |
| Canada | 9,723,912 | 8,996,072 |
| | \$ 21,513,454 | \$ 21,235,484 |

13. CONTINGENCIES

Due to the nature of the Company's business, products, and patent portfolio, 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. 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 financial performance, liquidity, or financial condition.

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

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14. SUBSEQUENT EVENTS

(a) Employee share purchase plan

On January 17, 2017, 42,329 common shares were issued pursuant to the Employee Share Purchase Plan.

(b) Quarterly dividend

On January 20, 2017, the Company declared a quarterly dividend of CAD\$0.08 per share on its common shares, payable in cash on February 24, 2017 to shareholders of record at the close of business on February 3, 2017.

(c) Share repurchase

Pursuant to its Normal Course Issuer Bid, subsequent to December 31, 2016, through February 6, 2017, the Company repurchased and settled payment for 147,700 common shares for a total cost of \$704,818. The difference between the purchase price and the average book value of the common shares was \$486,702. As a result of the Company's agreement with a financial institution to administer these share repurchases, these amounts have been recorded in share capital and deficit and in accrued liabilities.