

Synodon Inc.
Interim Financial Statements
For the Third Quarter Ended July 31, 2008 and 2007
Unaudited

Notice: These management prepared, unaudited interim financial statements have not been reviewed by the Company's auditors

Synodon Inc.
(a development stage enterprise)
BALANCE SHEETS
(see note 1 – going concern uncertainty)
(unaudited)

As at	<u>July 31,</u> 2008	<u>October 31,</u> 2007
	\$	\$
ASSETS		
Current		
Cash	754	4,943
Accounts receivable	117,206	114,827
Prepaid expenses and deposits	27,113	10,697
	145,073	130,467
Property and equipment <i>[note 3]</i>	14,052	15,970
Long-term deposits	19,666	18,786
	178,791	165,223
LIABILITIES AND SHAREHOLDERS' DEFICIENCY		
Current		
Accounts payable and accrued liabilities	1,327,537	725,837
Government assistance <i>[note 9]</i>	—	11,790
Notes payable <i>[note 4]</i>	29,000	5,000
Loans from directors <i>[note 5]</i>	130,100	28,000
Current portion of obligations under capital lease <i>[note 6]</i>	32,822	30,569
Deposit on distribution rights	65,875	65,875
Deposit on share subscriptions	238,500	—
	1,823,834	867,071
Obligations under capital lease <i>[note 6]</i>	8,104	17,064
	1,831,938	884,135
Shareholders' deficiency		
Share capital <i>[note 7]</i>	4,320,814	4,239,464
Warrants on issue of units	256,634	256,634
Contributed surplus <i>[note 8]</i>	642,091	538,248
Deficit	(6,872,686)	(5,753,258)
	(1,653,147)	(718,912)
	178,791	165,223

See accompanying notes

On behalf of the Board:

(signed) "Adrian Banica"

Adrian Banica, President and Chief
Executive Officer

(signed) "Nimal Rodrigo"

Nimal Rodrigo, Chief Financial
Officer

Synodon Inc.**(a development stage enterprise)****STATEMENTS OF LOSS AND COMPREHENSIVE LOSS AND DEFICIT**

(unaudited)

	Three months ended		Nine months ended	
	July 31,		July 31	
	2008	2007	2008	2007
	\$	\$	\$	\$
REVENUE	—	—	—	—
EXPENSES				
Research and development costs, net of government assistance <i>[note 10]</i>	107,239	455,241	421,772	842,893
Amortization	1,374	1,315	4,195	4,487
Financing charges and interest	22,512	5,003	59,584	15,927
Foreign exchange (gains) losses	4,430	(2,643)	40,421	2,795
Stock-based compensation	46,292	22,049	103,843	109,570
Sales and marketing	29,511	1,800	34,760	3,000
Office and general administrative	180,259	144,264	454,853	481,247
	391,617	627,029	1,119,428	1,459,918
Loss from operations	(391,617)	(627,029)	(1,119,428)	(1,459,918)
Other income	—	5,375	—	22,064
NET LOSS AND COMPREHENSIVE				
LOSS FOR THE PERIOD	(391,617)	(621,654)	(1,119,428)	(1,437,854)
Deficit, beginning of the period	(6,481,069)	(4,763,270)	(5,753,258)	(3,947,070)
Deficit, end of the period	(6,872,686)	(5,384,924)	(6,872,686)	(5,384,924)
Loss per share				
- Basic and diluted	(0.02)	(0.03)	(0.05)	(0.07)
Weighted-average number of shares outstanding	20,872,712	20,249,023	20,820,102	19,590,737

See accompanying notes

Synodon Inc.
(a development stage enterprise)
STATEMENTS OF CASH FLOWS
(unaudited)

	Three months ended		Nine months ended	
	July 31,		July 31	
	2008	2007	2008	2007
	\$	\$	\$	\$
OPERATING ACTIVITIES				
Loss for the period	(391,617)	(621,654)	(1,119,428)	(1,437,854)
Add charges to operations not requiring a current cash payment:				
Stock-based compensation	46,292	22,049	103,843	109,570
Non-cash payment for services	—	—	50,000	—
Amortization	1,374	1,315	4,195	4,487
Research and development costs, financed by lease financing capital	—	87,858	—	87,858
	(343,951)	(510,432)	(961,390)	(1,235,939)
Net change in non-cash working capital balances related to operations:				
Accounts receivable	2,593	34,814	(2,379)	8,862
Investment tax credits recoverable	—	174,471	—	353,342
Contract deposit	—	27,598	—	(21,100)
Prepaid expenses	(12,190)	(13,516)	(16,416)	(16,184)
Accounts payable and accrued liabilities	98,745	173,353	601,700	(243,853)
Government assistance advance	—	45,610	(11,790)	(96,780)
Cash provided by operating activities	(254,803)	(68,102)	(390,275)	(1,251,652)
INVESTING ACTIVITIES				
Purchase of property, plant and equipment	—	(2,605)	(2,277)	(4,275)
Cash used in investing activities	—	(2,605)	(2,277)	(4,275)
FINANCING ACTIVITIES				
Repayment of obligations under capital lease	(3,882)	(8,546)	(6,707)	(8,546)
Long-term deposits	(132)	—	(880)	—
Proceeds on disposal of assets	—	—	—	1,650
Repayment of notes payable	—	—	—	(8,000)
Deposit on share subscriptions	238,500	—	238,500	—
Issuance of notes payable	21,100	—	126,100	12,000
Issuance of shares	—	300	32,100	1,436,560
Share issuance costs	—	—	(750)	(158,304)
Cash provided by (used in) financing activities	255,586	(8,246)	388,363	1,275,360
Net increase (decrease) in cash during the period	783	(78,953)	(4,189)	19,433
Cash, beginning of period	(29)	98,691	4,943	305
Cash, end of period	754	19,738	754	19,738
Supplemental cash flow information				
Interest paid	44,571	2,072	49,727	3,384

See accompanying notes

Synodon Inc.
(a development stage enterprise)
NOTES TO FINANCIAL STATEMENTS
Interim Financial Statements as at July 31, 2008
(unaudited)

1. GOING CONCERN UNCERTAINTY AND NATURE OF BUSINESS

Going Concern Uncertainty

These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles on a going concern basis which presumes the realization of assets and discharge of liabilities in the normal course of business for the foreseeable future.

The Company has incurred significant losses since incorporation and as at July 31, 2008, the Company has an accumulated deficit of \$6,872,686. At present, the Corporation does not have sufficient cash to continue its activities in the normal course of business. The Company's ability to continue as a going concern is dependant upon achieving profitable operations, the continued financial support of its lenders and the ability to obtain additional debt or equity financing. The outcome of these matters cannot be predicted at this time. These financial statements do not include any adjustment to the amounts and classification of assets and liabilities that might be necessary should the Company be unable to continue in business. Such adjustments could be material.

Nature of Business

The Company is an advanced remote sensing technology company which has developed a proprietary platform technology called realSens™ that has been proven to be capable of measuring small ground-level gas concentrations from an aircraft flying up to 300 metres in altitude. The Company is in the final stages of completing the prototype manufacturing of the realSens™ instrument and developing its plan for commercialization and as such considered a development stage company.

2. SIGNIFICANT ACCOUNTING POLICIES

These unaudited interim financial statements should be read in conjunction with the October 31, 2007 annual financial statements as disclosures provided in the interim financial statements do not conform in all respects to the requirements of GAAP for annual financial statements. In management's opinion, the interim financial statements include all adjustments necessary to present fairly such interim financial statements. The same accounting policies and methods are used as in the 2007 financial statements except for new accounting standards adopted during the quarter.

CHANGES IN ACCOUNTING POLICIES

Effective November 1, 2007, the Company adopted the following new accounting policies:

CICA 1506 – Accounting Changes

This new standard allows an entity to change an accounting policy only if the change is required by a primary source of GAAP or if the new policy results in more reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, financial performance or cash flows. This standard is effective for interim and annual periods related to fiscal years beginning on or after January 1, 2007. The adoption of this standard did not have any effect on the Company.

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CICA 1535 – Capital Disclosures

This new standard requires an entity to provide disclosures related to its capital and how it is managed. The standard is effective for interim and annual periods related to fiscal years beginning on or after October 1, 2007.

The Company's objective in managing its capital is to ensure that it has appropriate financial resources to continue to further its technology toward commercialization. The Company has been primarily dependent upon the issue of common shares and units comprising common shares and a portion of a common share purchase warrant as sources of capital as market conditions and the stage of the Company's technology development have allowed. During certain times when market conditions have not been suitable for issuing units or common shares, the Company has accessed lease financing and issued notes payable as short to medium term sources of capital.

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

The Company does not have sufficient capital to fund operations, as such it is in the process of raising equity (note 13).

CICA 3862 – Financial Instruments – Disclosure

This new standard establishes standards for disclosure about financial instruments and non-financial derivatives. The standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007.

Credit risk

The Company's accounts receivable as presented on its balance sheet represent its total exposure to credit risk and are comprised primarily of holdbacks related to government assistance programs. These holdbacks are expected to be released upon the Company filing appropriate final reports including external auditors' reports on certain financial information of the related program.(note 9)

Interest rate risk

The Company has fixed repayment terms on its obligations under capital lease and fixed interest rates on its notes payable and, accordingly, is not exposed to interest rate cash flow risk on its interest-bearing obligations. The Company is exposed to interest rate price risk should interest rates fall while the Company is committed to a higher fixed rate.

CICA 3863 – Financial Instruments – Presentation

This new standard supersedes and carries forward unchanged the presentation standards of CICA 3861 Financial Instruments – Presentation and Disclosure. The standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. There was no effect on the Company of adopting this standard.

Other Accounting Policies

In addition to the disclosures in its annual financial statements, the Company is disclosing its accounting policy related to leases which was not previously disclosed.

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Leases

The Company records its lease obligations as either operating or capital. Capital leases are those where the Company is transferred substantially all of the benefits and risks of ownership whereas under operating leases the Company is not transferred substantially all of the benefits and risks of ownership. Capital lease obligations are accounted for as the acquisition of property and equipment or development expenditure and a related obligation measured at the present value of future minimum lease payments. The related assets, if capitalized, are amortized, over their estimated useful lives and imputed interest is recognized as a component of periodic lease payments. Operating leases are expensed as the payments are due.

RECENT ACCOUNTING PRONOUNCEMENTS ISSUED BUT NOT YET ADOPTED

International Financial Reporting Standards

In February 2008, the Canadian Accounting Standards Board confirmed that Canadian public companies will be required to adopt International Financial Reporting Standards for years beginning on or after January 1, 2011. The Company has not yet evaluated the effect of this change in standards on its financial statements.

3. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	July 31, 2008		
	Cost \$	Accumulated amortization \$	Net book value \$
Computer equipment	37,890	33,958	3,932
Computer software	6,866	6,644	222
Laboratory equipment	8,048	3,294	4,754
Furniture and fixtures	12,873	7,729	5,144
	65,677	51,625	14,052

	October 31, 2007		
	Cost \$	Accumulated amortization \$	Net book value \$
Computer equipment	36,735	31,692	5,043
Computer software	6,521	6,321	200
Laboratory equipment	7,271	2,544	4,727
Furniture and fixtures	12,873	6,873	6,000
	63,400	47,430	15,970

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4. NOTES PAYABLE

The notes payable consist of the following:

	<u>July 31,</u> <u>2008</u>	<u>October 31,</u> <u>2007</u>
	\$	\$
Demand promissory notes		
Notes, bearing interest at 8% per annum	<u>29,000</u>	5,000
	<u>29,000</u>	5,000

During the three-month period ended July 31, 2008, the Corporation issued demand promissory notes with a face value of \$10,000.

5. LOANS FROM DIRECTORS

The loans from Directors consist of the following:

	<u>July 31,</u> <u>2008</u>	<u>October 31,</u> <u>2007</u>
	\$	\$
Demand promissory notes		
Notes, bearing interest at 8% per annum	<u>130,100</u>	28,000
	<u>130,100</u>	28,000

During the three-month period ended July 31, 2008, the Corporation issued demand promissory notes with a face value of \$11,100.

6. OBLIGATIONS UNDER CAPITAL LEASE

	<u>July 31,</u> <u>2008</u>	<u>October 31,</u> <u>2007</u>
	\$	\$
Vencore Solutions LLC, at 8.25%		
Lease contract #1, payable \$1,776 monthly, due October 10, 2009	28,422	37,416
Lease contract #2, payable \$526 monthly, due October 25, 2009	8,633	11,365
Lease contract #3, payable \$1,281 monthly, due November 25, 2009	22,483	29,118
	<u>59,538</u>	<u>77,899</u>
Less amounts representing interest and lease arrangement costs	<u>(18,612)</u>	(30,266)
	<u>40,926</u>	<u>47,633</u>
Less current portion of obligations under capital lease	<u>(32,822)</u>	<u>(30,569)</u>
	<u>8,104</u>	<u>17,064</u>

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7. SHARE CAPITAL

	<u>July 31,</u> <u>2008</u>	<u>October 31,</u> <u>2007</u>
	\$	\$
<hr/>		
Authorized		
Unlimited number of Class A voting common shares		
Unlimited number of Class B voting common shares		
Unlimited number of Class C non-voting common shares		
Unlimited number of Class D non-voting common shares		
Unlimited number of Class E non-voting, redeemable, retractable preferred shares		
Issued and outstanding		
20,872,712 Class A common shares	4,320,814	
20,746,571 Class A common shares		4,239,464
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The following table sets out the change in share capital:

	Number of shares	Total \$
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Balance, October 31, 2006	17,255,550	3,285,593
Issued in IPO, net of costs of issuance of \$441,694 and net of fair value of warrants of \$294,787	2,807,500	667,269
Issued in private placement, net of costs of issuance of \$20,070 and net of fair value of warrants of \$51,688	492,271	198,993
Issued for cash on the exercise of warrants	11,250	6,750
Issued for cash from exercise of options	50,000	25,000
Issued on conversion of notes payable and accrued interest	130,000	51,350
Reclassify from contributed surplus on exercise of options	—	4,509
Balance, October 31, 2007	20,746,571	4,239,464
Issued for cash on the exercise of broker warrants	4,000	2,000
Issued for cash on the exercise of warrants	58,038	30,100
Balance, January 31, 2008	20,808,609	4,271,564
<u>Issued on conversion of account payable, net of costs of issuance of \$750</u>	<u>64,103</u>	<u>49,250</u>
Balance, April 30, 2008 and July 31, 2008	20,872,712	4,320,814
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Issuance of common shares for debt

On February 12, 2008, the Company issued 64,103 common shares to a supplier in satisfaction of a liability to that supplier incurred during December, 2007.

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Warrants

At July 31, 2008 the Company had 2,119,665 (October 31, 2007 – 2,795,315) common share purchase warrants outstanding, as follows:

Exercise price \$	Expiry date	Number outstanding and exercisable
0.65	October 15, 2008	281
0.65 US	December 31, 2009	98,500
0.60 – 0.75	December 28, 2008	1,367,000
0.60 – 0.75	December 28, 2008	65,000
0.50	December 28, 2008	276,750
0.65	May 15, 2009	66,000
0.80	September 13, 2009	246,134
		2,119,665

Share options

Under the Company's share option policy, options to purchase common shares may be granted by the Board of Directors to directors, officers and employees. The Company has reserved up to 10% of the outstanding common shares as a pool available for the settlement of options. The exercise price per share and the vesting period shall be determined at the time of grant by the Board. Except for the first grant, which vested when specific performance criteria were met, options granted prior to October 31, 2006 have vested immediately. Options granted subsequent to October 31, 2006 generally vest over a period of three years. The option period for options granted as compensation to directors, officers and employees shall be a period of time fixed by the Board not to exceed five years. The option period for options granted in exchange for services is specified by the Board at the time of grant and ranged from three to ten years for options granted prior to April 30, 2006. After April 30, 2006, the option period for options granted in exchange for services are specified by the Board at the time of grant. If an option has lapsed, the board may grant new options covering the shares not purchased. If a participant ceases to be an employee or provider, the participant has 90 days to exercise his options or they are cancelled.

The following table summarizes information about share options outstanding at July 31, 2008:

Exercise price \$	Year of grant	Number outstanding	Weighted-average remaining contractual life [years]	Weighted-average exercise price \$
0.45	2005	400,000	1.7	0.45
0.40	2006	550,000	1.7	0.40
0.50	2006	100,000	3.1	0.50
0.50	2007	410,000	3.7	0.50
0.78	2008	300,000	4.8	0.78
\$0.40 – 0.78		1,760,000	2.8	0.5051

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The weighted-average fair value of share options is determined at the date of grant using the Black-Scholes option pricing model. For the period ended July 31, 2008, \$46,292 [period ended July 31, 2007 - \$22,049] has been recorded as compensation expense with an equal amount reflected in contributed surplus.

8. CONTRIBUTED SURPLUS

The following table sets out the change in contributed surplus:

	Nine Months	Year ended
	July 31,	October 31,
	2008	2007
	\$	\$
Balance, beginning of period	538,248	322,006
Stock-based compensation	103,843	131,619
Issuance of warrants	—	89,132
Transfer to share capital on exercise of options	—	(4,509)
Balance, end of period	642,091	538,248

9. GOVERNMENT ASSISTANCE

SDTC funding

During fiscal 2006 the Company entered into a funding agreement with Canada Foundation for Sustainable Development Technology (“SDTC”) for the purpose of fostering the development and adoption of technologies that contribute to a sustainable development technology infrastructure in Canada by contributing to the rapid development, demonstration and pre-commercialization of technological solutions which address climate change and air quality. Upon the Company attaining pre-determined milestones, SDTC advances non-repayable funds totalling the lesser of \$650,000 and 24.77% of the eligible project costs, less 10% holdbacks on each advance. As at July 31, 2008, Milestone #1, #2 and #3 were earned and the Corporation received \$585,000 (\$650,000 less 10% holdback) for these milestones.

During the three months ended April 30, 2008, the Company applied for incremental funding for both previously unclaimed expenses in Milestone #2 and a new Milestone #4. The amount of funding applied for was \$332,813 (\$299,532 plus 10% holdback). Milestone #4 is expected to conclude by January 31, 2009.

The holdback outstanding is currently \$65,000. The Company expects to receive payment for all holdbacks at the completion of Milestone #4.

IERD

The Company has applied for and received final approval of the IERD project completion and expects to receive the holdback of \$48,413 by September 30, 2008

Investment tax credits

As of December 29, 2006 the Company ceased to be considered a Canadian-Controlled Private Corporation for the purpose of earning refundable Investment Tax Credits (ITC’s). Instead, the Company will file ITC claims on qualified expenditures at a rate of 20% and will apply them in the future towards taxes payable.

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10. RESEARCH AND DEVELOPMENT COSTS

Research and development costs and reductions due to government assistance are summarized as follows:

	Nine months ended <u>July 31,</u> 2008	Nine months ended <u>July 31,</u> 2007
	\$	\$
Research and development expenditures	433,562	1,066,381
Investment tax credit <i>[note 9]</i>	-	(64,658)
SDTC government assistance <i>[note 9]</i>	(11,790)	(158,830)
Research and development costs, net of government assistance	421,772	842,893

11. RELATED PARTY TRANSACTIONS

Officers, directors and shareholders provided promissory notes as well as services to the Company through rental agreements. The related party transactions occurred during the normal course of the Company's operations and are measured at their exchange amounts, which is the consideration amount established and agreed upon with the related parties.

- (a) The Company leased facilities from an officer who is also a shareholder. Total rental payments for the nine-month period ended July 31, 2008 were \$3,000 [nine-month period ended July 31, 2007 - \$4,500].
- (b) The Company incurred interest on promissory notes in the amount of \$6,967 during the nine-month period ended July 31, 2008 [nine-month period ended July, 31, 2007 - \$3,689] of which \$6,280 was payable to directors of the Company.

12. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform with the current period's presentation.

13. SUBSEQUENT EVENTS

Private Placement

On May 7, 2008, the Company announced the commencement of a non-brokered private placement process whereby the Company seeks to issue up to 2,750,000 units at a price of \$0.55 per unit (the "Units") for gross proceeds of \$1,512,500.00. On August 27, 2008 the Company announced an amendment to the private placement. Under the new terms the Company will issue up to 2,750,000 units at a price of \$0.45 per Unit (the "Units") for gross proceeds of \$1,237,500.

The Units will be comprised of one Class A common share and one Class A common share purchase warrant (the "Warrants"). Each Warrant will entitle the holder to purchase one additional Class A common

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share of the Company at a price of \$0.75 per share for a period of two years from the date of issue. The Warrants will have an accelerated exercise provision under which, if the volume weighted average closing price of the Shares, as traded on the Stock Exchange, equals or exceeds \$1.05 per Share, then the warrants must be exercised or will expire 30 calendar days after notice of such event is mailed to the warrant-holders.

The Company will pay, where appropriate, a cash finder's fee of up to 7% in connection with the sale of the Units and issue finder's warrants of up to 7% of the total number of Units issued under this offering, subject to regulatory approval. Each finder's fee warrant will entitle the holder to subscribe for one Class A Common share of the Company at a price of \$0.45 for a period of two years from the date of issue.

During the quarter ended July 31, 2008, the Company received cash of \$238,500 (530,000 units) as part of the private placement.

Proceeds from this offering will be used by the Company for general working capital.

Completion of this placement is subject to the approval of the TSX Venture Exchange.

Issuance of stock options

On August 1, 2008 the Company issues 300,000 options to CHF Investor Relations as per the terms of the agreement announced in the June 8, 2008 press release. The options are exercisable at \$0.75 for a period of 5 years and vest in 4 equal tranches over a period of 12 months (75,000 options every three months).

Government Assistance

On September 8, 2008, the Company signed the SDTC extension contract for \$332,813 (\$299,532 + 10% holdback)

On September 22, 2008, the Company received the IERD holdback of \$60,000 (which included amounts for previously disallowed expenses) and the SDTC funding of \$299,532.