

**ID WATCHDOG, INC.**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**SECOND QUARTER 2008**

**ID WATCHDOG, INC.**

**CONSOLIDATED FINANCIAL STATEMENTS**

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**ID WATCHDOG, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(Unaudited)  
(Expressed in U.S. Dollars)

	<b>June 30, 2008</b>	<b>December 31, 2007</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 1,334,376	\$ 631,665
Accounts receivable .....	23,412	8,083
Prepaid expenses and other .....	10,328	66,098
Total current assets .....	1,368,116	705,846
Furniture and equipment, net (Note 3) .....	378,712	212,429
Debt offering costs, net (Note 5) .....	323,441	486,810
Deferred equity offering costs .....	396,632	—
Intangible assets, net .....	3,135	3,300
Total assets .....	\$ 2,470,036	\$ 1,408,385
<b>LIABILITIES</b>		
Current liabilities:		
Accounts payable .....	\$ 466,414	\$ 204,823
Accrued liabilities .....	363,164	256,955
Current portion of capital lease obligation (Note 5) .....	2,290	2,290
Total current liabilities .....	831,868	464,068
Convertible debentures, net of unamortized discount of \$175,775 and \$269,155 at June 30, 2008 and December 31, 2007, respectively (Note 5) .....	3,474,516	3,456,136
Capital lease obligation, net of current portion (Note 5) .....	9,100	10,289
Total liabilities .....	4,315,484	3,930,493
Commitments and Contingencies (Note 6) .....		
Series A redeemable convertible preferred shares; \$2.00 stated value; 1,750,000 shares authorized, issued and outstanding at June 30, 2008; no shares authorized, issued and outstanding at December 31, 2007; liquidation preference of \$3,500,000 at June 30, 2008; plus accrued and unpaid dividends of \$176,919 and net of unamortized discount of \$623,222 (Note 7) .....	3,053,697	—
Series B redeemable convertible preferred shares; \$2.00 stated value; 500,000 shares authorized, 497,500 issued and outstanding at June 30, 2008; no shares authorized, issued and outstanding at December 31, 2007; liquidation preference of \$995,000 at June 30, 2008; plus accrued and unpaid dividends of \$9,169 and net of unamortized discount of \$775,882 (Note 7) .....	228,287	—
<b>SHAREHOLDERS' DEFICIT</b> (Note 8):		
Preferred shares; no par value; 450,000,000 shares authorized, 1,750,000 Series A and 497,500 Series B redeemable convertible shares issued and outstanding at June 30, 2008 (see above) .....	—	—
Ordinary shares; no par value; 450,000,000 shares authorized, 21,337,442 and 19,912,408 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively .....	5,363,472	2,188,756
Accumulated deficit .....	(10,490,904)	(4,710,864)
Total shareholders' deficit .....	(5,127,432)	(2,522,108)
Total liabilities and shareholders' deficit .....	\$ 2,470,036	\$ 1,408,385

See notes to unaudited consolidated financial statements

**ID WATCHDOG, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)  
(Expressed in U.S. Dollars)

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30, 2008</b>	<b>June 30, 2007</b>	<b>June 30, 2008</b>	<b>June 30, 2007</b>
Revenue.....	\$ 1,104,374	\$ 5,357	\$ 1,995,700	\$ 7,212
Cost of revenue.....	216,937	5,066	443,912	7,395
Gross (loss) profit.....	<u>887,437</u>	<u>291</u>	<u>1,551,788</u>	<u>(183)</u>
Operating expense:				
Marketing expense.....	2,514,032	65,147	4,335,445	101,742
General and administrative expense .....	751,531	250,764	1,313,817	549,299
Research and development expense.....	—	18,317	—	32,912
	<u>3,265,563</u>	<u>334,228</u>	<u>5,649,262</u>	<u>683,953</u>
Operating loss.....	<u>(2,378,126)</u>	<u>(333,937)</u>	<u>(4,097,474)</u>	<u>(684,136)</u>
Other income (expense):				
Interest income.....	8,039	2,884	26,382	2,884
Interest expense .....	(213,649)	(27,914)	(424,146)	(34,706)
Loss on sale of equipment .....	—	—	(502)	—
	<u>(205,610)</u>	<u>(25,030)</u>	<u>(398,266)</u>	<u>(31,822)</u>
Net loss .....	<u>(2,583,736)</u>	<u>(358,967)</u>	<u>(4,495,740)</u>	<u>(715,958)</u>
Dividends on redeemable convertible preferred shares .....	(113,595)	—	(186,088)	—
Deemed dividends on redeemable convertible preferred shares .....	(364,481)	—	(872,657)	—
Accretion of discount related to redeemable convertible preferred shares .....	(78,675)	—	(225,555)	—
Net loss applicable to ordinary shares .....	<u>\$ (3,140,487)</u>	<u>\$ (358,967)</u>	<u>\$ (5,780,040)</u>	<u>\$ (715,958)</u>
Basic and diluted net loss per share.....	<u>\$ (0.16)</u>	<u>\$ (0.02)</u>	<u>\$ (0.29)</u>	<u>\$ (0.04)</u>
Weighted average number of shares outstanding-basic and diluted.....	<u>20,163,974</u>	<u>18,140,933</u>	<u>20,087,294</u>	<u>17,810,083</u>

See notes to unaudited consolidated financial statements

**ID WATCHDOG, INC.**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT**  
**(Unaudited)**  
**(Expressed in U.S. Dollars)**

	<u>Ordinary Shares</u>	<u>Ordinary Shares</u>	<u>Accumulated Deficit</u>	<u>Total Shareholders' Deficit</u>
Balances, December 31, 2007	19,912,408	\$ 2,188,756	\$ (4,710,864)	\$ (2,522,108)
Stock options exercised .....	55,556	8,333	—	8,333
Ordinary shares issued – private placement .....	1,041,667	453,331	—	453,331
Ordinary shares issued in satisfaction of accrued interest .....	59,954	16,787	—	16,787
Ordinary shares issued upon conversion of convertible debentures .....	267,857	75,000	—	75,000
Warrants issued in connection with Series A and series B redeemable convertible preferred shares ...	—	420,265	—	420,265
Warrants issued in connection with private placement of ordinary shares .....	—	46,669	—	46,669
Share-based compensation expense and stock options issued for services .....	—	160,872	—	160,872
Beneficial conversion feature on Series A and Series B redeemable convertible preferred shares, net of Series B preferred shares issuance costs (Note 7) ...	—	1,993,459	—	1,993,459
Dividends on Series A and Series B redeemable convertible preferred shares .....	—	—	(186,088)	(186,088)
Deemed dividends on series A and series B redeemable convertible preferred shares .....	—	—	(872,657)	(872,657)
Accretion of discount on Series A and series B redeemable convertible preferred shares .....	—	—	(225,555)	(225,555)
Net loss .....	—	—	(4,495,740)	(4,495,740)
Balances, June 30, 2008 .....	<u>21,337,442</u>	<u>\$ 5,363,472</u>	<u>\$ (10,490,904)</u>	<u>\$ (5,127,432)</u>

See notes to unaudited consolidated financial statements

**ID WATCHDOG, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**  
**(Expressed in U.S. Dollars)**

	<b>Six Months Ended</b>	
	<b>June 30,</b>	
	<b>2008</b>	<b>2007</b>
Cash flows from operating activities:		
Net loss .....	\$ (4,495,740)	\$ (715,958)
Adjustment to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization expense .....	59,785	20,572
Amortization of debt offering costs .....	163,369	6,384
Amortization of convertible debenture discount .....	93,380	3,735
Share-based compensation expense to employees, directors and consultants.....	153,934	21,042
Ordinary shares issued in payment of interest .....	16,787	—
Compensation paid by officer/shareholder .....	—	96,850
Loss on sale of equipment .....	502	—
Changes in assets and liabilities:		
Increase in receivables .....	(15,329)	(6,766)
Decrease (increase) in prepaid expenses and other .....	55,770	(151)
Increase in accounts payable .....	261,591	95,051
Increase in accrued liabilities .....	106,209	459
Net cash used in operating activities .....	<u>(3,599,742)</u>	<u>(478,782)</u>
Cash flows from investing activities:		
Capital expenditures .....	(226,405)	—
Net cash used in investing activities .....	<u>(226,405)</u>	<u>—</u>
Cash flows from financing activities:		
Proceeds from convertible debentures and warrants .....	—	2,526,200
Debt offering costs .....	—	(416,572)
Proceeds from redeemable convertible preferred shares and warrants .....	4,495,000	—
Convertible preferred shares issuance costs .....	(83,592)	—
Proceeds from issuance of convertible notes .....	—	391,634
Repayment of convertible debt .....	—	(275,000)
Proceeds from issuance of ordinary shares .....	500,000	—
Proceeds from exercise of stock options .....	8,333	—
Deferred IPO costs .....	(389,694)	—
Repayment of capital lease obligation .....	(1,189)	(580)
Net cash provided by financing activities .....	<u>4,528,858</u>	<u>2,225,682</u>
Net increase in cash .....	\$ 702,711	\$ 1,746,900
Cash and cash equivalents, beginning of period .....	\$ 631,665	\$ 308
Cash and cash equivalents, end of period .....	<u>\$ 1,334,376</u>	<u>\$ 1,747,208</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest .....	\$ 151,181	\$ —
Supplemental disclosure of non-cash investing and financing activities:		
Ordinary shares issued upon conversion of debt .....	\$ 75,000	\$ 225,800
Ordinary shares issued in satisfaction of accrued interest .....	\$ 16,787	\$ —
Fair market value of beneficial conversion feature issued with redeemable convertible preferred shares .....	\$ 2,007,051	\$ —
Fair market value of warrants issued with redeemable convertible preferred shares .....	\$ 420,265	\$ —
Stock options issued for equity issuance costs .....	\$ 6,938	\$ —
Capital lease obligation incurred for new equipment .....	\$ —	\$ 12,179

See notes to unaudited consolidated financial statements

**ID WATCHDOG, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**June 30, 2008**  
**(Unaudited)**  
**(Expressed in U.S. Dollars)**

**1. Organization, Basis of Presentation, and Liquidity, Going Concern and Management's Plans:**

**Organization:**

ID Watchdog, Inc. ("ID Watchdog" or the "Company") provides a variety of identity theft detection, protection and resolution services primarily to individual consumers on a subscription basis, through its wholly owned subsidiary, ID Rehab Corporation ("ID Rehab"). During the quarter ended December 31, 2007, the Company transitioned from a development stage enterprise to an operating company.

ID Watchdog is a limited liability exempted company incorporated on May 13, 2008 under the laws of the Cayman Islands.

The Company was originally formed on July 27, 2005 as ID Rehab, LLC ("LLC"), a Colorado limited liability company. On December 12, 2005, the sole member of LLC formed ID Rehab, a Colorado corporation, and transferred all of the assets, net of certain liabilities (at historical cost) of LLC to ID Rehab and merged LLC into ID Rehab in exchange for 10,000,000 ordinary shares of ID Rehab.

Pursuant an Agreement and Plan of Merger dated as of June 24, 2008 among Identity Rehab, ID Watchdog (then a wholly-owned subsidiary of Identity Rehab) and Mergeco, Inc. (Mergeco") (then a wholly-owned subsidiary of the ID Watchdog), Mergeco merged into Identity Rehab, and Identity Rehab became a wholly-owned subsidiary of ID Watchdog (the "Reorganization"). Upon the completion of the Reorganization on June 25, 2008, former shareholders of Identity Rehab exchanged their securities of Identity Rehab for equivalent securities of ID Watchdog on a one-for-one basis. Convertible Debentures of Identity Rehab remain the obligation of Identity Rehab but will be convertible into ordinary shares of ID Watchdog.

The accompanying consolidated financial statements include the results of operations of LLC from July 27, 2005 through December 12, 2005 and those of ID Rehab subsequent to that date.

**Interim reporting:**

The accompanying consolidated financial statements of the Company are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial statements. Accordingly, they do not necessarily include all the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, the accompanying consolidated financial statements include all adjustments, which are normal and recurring in nature, considered necessary to present fairly the Company's financial position as of June 30, 2008, the results of operations for the three and six months ended June 30, 2008 and 2007, and cash flows for the six months ended June 30, 2008 and 2007. The results of operations for the three and six months ended June 30, 2008 are not necessarily indicative of those to be expected for the entire year. For a more complete understanding of the Company's operations, financial position and accounting policies, these consolidated financial statements and the notes thereto should be read in conjunction with the audited financial statements of ID Rehab for the year ended December 31, 2007.

**Liquidity:**

The Company has incurred significant losses from operations, and has funded its operations primarily through private placements of debt and equity including loans from related parties. The Company also has a limited operating history and has only recently had significant revenue producing operations beginning in the fourth quarter of 2007. The net proceeds from these private placements will provide working capital for use principally in connection with the Company's growth plan and programs during the next six months.

**ID WATCHDOG, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**  
**June 30, 2008**  
**(Unaudited)**  
**(Expressed in U.S. Dollars)**

**2. Summary of Significant Accounting Policies:**

**Use of estimates in the preparation of financial statements:**

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Cash and cash equivalents:**

Cash and cash equivalents are highly liquid investments that consist primarily of short-term money market instruments and overnight deposits with insignificant interest rate risk and original maturities of three months or less at the time of purchase. We utilize and invest with financial institutions that are sound and of high credit quality. Our investments are in low-risk instruments and we limit our credit exposure in any one institution or type of investment instrument based upon criteria including creditworthiness.

**Furniture, equipment, leasehold improvements, depreciation and amortization:**

Furniture, equipment, leasehold improvements and computer software are stated at cost and are depreciated and amortized using the straight-line method over the estimated useful lives of the assets ranging from three to five years.

**Debt offering costs:**

Debt offering costs are amortized to interest expense over the life of the related debt instrument using the straight-line method which approximates the effective interest method.

**Intangible assets:**

Intangible assets represent the costs of trademarks and are amortized over the shorter of the lives of the trademarks or the estimated useful lives using the straight-line method, subject to periodic evaluation for possible impairment.

**Long-lived assets:**

Management assesses the carrying values of long-lived assets for impairment when circumstances indicate that such amounts may not be recoverable from future operations. Generally, long-lived assets are considered impaired if the sum of expected undiscounted future cash flows is less than the carrying amount of the asset. At June 30, 2008 and December 31, 2007, management believes that no impairment exists.

**Fair value of financial instruments:**

The fair value of the Company's cash, accounts receivable, accounts payable, accrued liabilities and other current liabilities approximate their carrying amounts due to the short-term nature of these instruments. The Company's 9% convertible debentures and Series A and series B redeemable convertible preferred shares are carried at amortized cost, which approximates fair value. See also Notes 5 and 7.

**ID WATCHDOG, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**  
**June 30, 2008**  
**(Unaudited)**  
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**Convertible securities:**

The Company accounts for conversion options imbedded in its convertible securities in accordance with the Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 133 "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133") and the FASB's Emerging Issues Task Force ("EITF") Issue No. 00-19 "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock" ("EITF 00-19") and related interpretations. SFAS No. 133 generally requires companies to bifurcate conversion options embedded in convertible securities from their host instruments and to account for them as free-standing derivative instruments in accordance with EITF 00-19. SFAS No. 133 provides an exception to this rule when convertible notes, as host instruments, are deemed to be conventional convertible debt as that term is described in the implementation guidance under Appendix A to SFAS No. 133 and further clarified in EITF Issue No. 05-2 "The Meaning of Conventional Convertible Debt Instrument in Issue No. 00-19." SFAS No. 133 also provides an exception to this rule when convertible preferred shares have a mandatory redemption feature. Accordingly, the Company has evaluated its convertible securities and has determined that bifurcation is not required.

The Company also accounts for its convertible securities in accordance with the provisions of EITF Issue No. 98-5 "Accounting for Convertible Securities with Beneficial Conversion Features" ("EITF 98-5") and EITF Issue No. 00-27 "Application of EITF 98-5 to Certain Convertible Instruments" (EITF 00-27"). Accordingly, the Company records, as a discount to convertible securities, the intrinsic value of such beneficial conversion features based upon the differences between the fair value of the underlying ordinary shares at the commitment date of the security transaction and the effective conversion price embedded in the instrument. Discounts under these arrangements are amortized over the expected term to the redemption date of the related security.

**Revenue recognition:**

The Company recognizes revenue on identity theft detection and resolution services. The Company's services are offered to consumers principally on a monthly subscription basis or to consumers as the service is delivered, such as the Company's identity resolution product. Subscription fees are generally billed directly to the subscriber's credit card or demand deposit account. At times, as a means of allowing customers to become familiar with the Company's services, the Company offers free trial or guaranteed refund periods. No revenue is recognized until these applicable periods are completed.

The point in time at which the Company recognizes revenue from services is determined in accordance with the Securities and Exchange Commission's Staff Accounting Bulletin ("SAB") No. 101 "Revenue Recognition in Financial Statements," as amended by SAB No. 104 "Revenue Recognition." Consistent with the requirements of these SABs: a.) persuasive evidence of arrangement exists, b.) delivery has occurred once the product is transmitted, c.) the seller's price to the buyer is fixed, as sales are generally based on contract or list prices, and d.) collectibility is reasonably assured, as individual customers pay by credit card which has limited the Company's risk of non-collection. Revenue for monthly subscriptions is recognized in the month the subscription fee is earned.

Revenue for annual subscription fees is deferred if the subscriber has the right to cancel the service. Annual subscriptions include subscribers with full refund provisions at any time during the subscription period and pro-rata refund provisions. Revenue related to annual subscriptions with full refund provisions is recognized on the expiration of these refund provisions. Revenue related to annual subscribers with pro-rata provisions is recognized based on a pro-rata share of revenue earned. An allowance for subscription refunds is established based on actual refund experience for estimated future charge-backs and refunds applicable to previously

**ID WATCHDOG, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**  
**June 30, 2008**  
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recognized revenue under the aforementioned policies. The allowance for subscription refunds was \$8,193 and \$5,489 at June 30, 2008 and December 31, 2007, respectively.

**Loss per share:**

Basic net loss per ordinary share (“EPS”) is computed by dividing net loss applicable to ordinary shares by the weighted-average number of ordinary shares outstanding for the period. Diluted EPS reflects the potential dilution that would occur if securities or other contracts to issue ordinary shares were exercised or converted into ordinary shares. Currently, all potentially dilutive securities have an anti-dilutive effect on EPS and accordingly, basic and dilutive weighted average shares are the same. As of June 30, 2008, a total of 48,610,197 shares of dilutable securities have been excluded from the calculation of EPS, as the effect of including these securities would be anti-dilutive, as follows:

<b>Potentially Dilutive Securities as of June 30, 2008</b>	
	<b>(shares)</b>
Convertible debentures .....	13,036,754
Redeemable convertible preferred shares .....	11,612,723
Warrants .....	20,125,720
Stock options .....	3,835,000
Total .....	48,610,197

**Research and development:**

The Company includes in research and development expense: payroll and other expense items directly attributable to research and development. The Company does not contract its research and development work, nor does it perform research and development work for others.

**Advertising:**

Advertising costs are expensed as incurred. For the three and six months ended June 30, 2008, advertising costs were \$1,145,311 and \$1,631,241, respectively and for the three and six months ended June 30, 2007, advertising costs were \$8,213 and \$12,056, respectively.

**Share-based compensation:**

We grant stock options to employees, members of our board of directors and consultants in connection with our various business activities. These are accounted for in accordance with the provisions of SFAS No. 123 (revised 2004) “Share-Based Payment” (“SFAS No. 123R”) and Emerging Issues Task Force Abstract No. 96-18, “Accounting for Equity Instruments That are Issued to Other Than Employees for Acquiring or in Conjunction with Selling, Goods or Services” as well as other authoritative accounting pronouncements. We are required to make estimates of the fair value of the related instruments and recognize share-based compensation expense over the period benefited, usually the vesting period.

We use the Black-Scholes option pricing model to value stock options. The Black-Scholes model requires the use of a number of assumptions, including the volatility of our share price, a risk-free interest rate, and the expected term of the options. The expected term of stock options represents the period of time that the stock options granted are expected to be outstanding. The estimated volatility is based on historical volatility of a similar entity with publicly-traded securities. The risk-free interest rate represents the U.S. Treasury bill rate for

**ID WATCHDOG, INC.**  
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**June 30, 2008**  
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the expected term of the related stock options. As we do not pay dividends, the dividend rate variable in the Black-Scholes model is zero.

The following table summarizes the assumptions used to value stock options granted during the six months ended June 30, 2008 and June 30, 2007:

	<u>Six Months Ended June 30, 2008</u>	<u>Six Months Ended June 30, 2007</u>
Expected term .....	3.3 – 5.0 years	3.3 years
Estimated volatility .....	38%	45%
Risk-free interest rate .....	2.3% - 3.7%	4.5%
Dividend yield .....	0%	0%

**Income taxes:**

The Company recognizes deferred tax assets and liabilities based on the differences between the tax basis of assets and liabilities and their reported amounts in the financial statements that may result in taxable or deductible amounts in future years. The measurement of deferred tax assets may be reduced by a valuation allowance based upon management’s assessment of available evidence if it is deemed more likely than not some or all of the deferred tax assets will not be realizable. Currently, a valuation allowance of 100% is provided for the deferred tax asset resulting from the Company’s net operating loss carry forward in each of the reporting years.

The Company recognizes interest and penalties accrued on any uncertain tax positions as a component of income tax expense. The Company did not have any accrued interest or accrued penalties associated with any uncertain tax positions at June 30, 2008 and December 31, 2007; nor were any income tax expenses recognized during the three and six months ended June 30, 2008 and 2007, respectively, associated with uncertain tax positions.

**Reclassifications:**

Certain amounts in the 2007 financial statements have been reclassified to conform to the 2008 presentation.

**Recently adopted accounting pronouncements:**

Effective January 1, 2008 the Company adopted SFAS No. 157 “Fair Value Measurements” (“SFAS No. 157”), which defines fair value, establishes a framework for measuring fair value in accordance with U.S. GAAP and expands disclosure about fair value measurements. The standard applies whenever other standards require (or permit) assets or liabilities to be measured at fair value. The standard does not expand the use of fair value in any new circumstances. The adoption of SFAS No. 157 did not have an impact on the Company’s financial statements.

Effective January 1, 2007, the Company adopted FSAB Interpretation No. 48 “Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109” (“FIN 48”), which prescribes a comprehensive model for how the Company should recognize, measure, present and disclose in its financial statements uncertain tax positions taken or expected to be taken on a tax return. The Company has evaluated its tax positions and has determined that the adoption of FIN 48 did not have an impact on its financial statements.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**  
**June 30, 2008**  
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**Recently issued accounting pronouncements:**

In March 2008, the FASB issued SFAS No. 161 “Disclosures about Derivative Instruments and Hedging Activities – an Amendment of FASB Statement No. 133” which requires enhanced disclosures on the effect of derivatives on a Company’s financial statements. These disclosures will be required for the Company beginning with the first quarter fiscal 2009 financial statements.

In February 2008, the FASB issued FASB Staff Position No. SFAS 157-2 “Effective Date of FASB Statement No. 157”, which provides a one year deferral of the effective date of SFAS No. 157 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually. In accordance with this interpretation, the Company has only adopted the provisions of SFAS No. 157 with respect to its financial assets and liabilities that are measured at fair value within the financial statements as of June 30, 2008, and the provisions of SFAS No. 157 have not been applied to non-financial assets and non-financial liabilities as the Company does not have any non-financial assets or liabilities to which the deferral applies.

In December 2007, the FASB issued SFAS No. 141 (revised 2007) “Business Combinations” (“SFAS No. 141R”) which becomes effective for fiscal periods beginning after December 15, 2008 (fiscal 2009 for the Company). SFAS No. 141R requires all business combinations completed after the effective date to be accounted for by applying the acquisition method (previously referred to as the purchase method). Companies applying this method will have to identify the acquirer, determine the acquisition date and purchase price and recognize at their acquisition date fair values of the identifiable assets acquired, liabilities assumed, and any non-controlling interests in the acquiree. In the case of a bargain purchase the acquirer is required to reevaluate the measurements of the recognized assets and liabilities at the acquisition date and recognize a gain on that date if an excess remains. The adoption of SFAS No. 141R is not expected to have an impact on the Company’s financial statements.

In December 2007, the FASB issued SFAS No. 160 “Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB 51” (SFAS No. 160”), which becomes effective for fiscal periods beginning after December 15, 2008 (fiscal 2009 for the Company). This statement amends Accounting Research Bulletin No. 51 to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. The statement requires ownership interests in subsidiaries held by parties other than the parent be clearly identified, labeled, and presented in the consolidated statement of financial position within equity, but separate from the parent’s equity. The statement also requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest with disclosure on the face of the consolidated statement of income, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. In addition this statement establishes a single method of accounting for changes in a parent’s ownership interest in a subsidiary that do not result in deconsolidation and requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. The adoption of SFAS No. 160 is not expected to have an impact on the Company’s financial statements.

In February 2007, the FASB issued SFAS No. 159 “The Fair Value Option for Financial Assets and Financial Liabilities-Including an Amendment of FASB Statement No. 115” (“SFAS No. 159”). SFAS No. 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of SFAS No. 159 are elective; however, the amendment to SFAS No. 115, “Accounting for Certain Investments in Debt and Equity Securities” applies to all entities with available for sale or trading securities. SFAS No. 159 is elective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007

**ID WATCHDOG, INC.**  
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(fiscal 2008 for the Company). The Company has elected not to adopt this pronouncement and as a result it did not have a material impact on the Company's financial statements.

**3. Furniture and Equipment:**

Furniture and equipment consists of the following at June 30, 2008 and December 31, 2007:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Office equipment .....	\$ 116,396	\$ 236,419
Furniture and fixtures .....	61,898	42,079
Computer software .....	331,507	6,200
Total furniture and equipment.....	<u>509,801</u>	<u>284,698</u>
Less: accumulated depreciation and amortization	<u>(131,089)</u>	<u>(72,269)</u>
Furniture and equipment, net .....	<u>\$ 378,712</u>	<u>\$ 212,429</u>

Office equipment at June 30, 2008 and December 31, 2007 includes \$18,670 of assets under a capital lease.

Depreciation and amortization expense for the three and six months ended June 30, 2008 was \$34,591 and \$59,620, respectively and for the three and six months ended June 30, 2007 was \$10,286 and \$20,572, respectively, and is included in general and administrative expense.

**4. Related Party Transactions:**

**Consulting services expense – related parties:**

The Company recorded consulting services expense - related parties as follows:

	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
	<u>June 30, 2008</u>	<u>June 30, 2007</u>	<u>June 30, 2008</u>	<u>June 30, 2007</u>
Chief executive officer .....	\$ 31,358	\$ 21,250	\$ 56,775	\$ 52,500
President, cash compensation .....	—	18,000	—	36,000
Director, cash compensation .....	15,000	—	30,000	—
Director, share-based compensation .....	33,000	—	33,000	—
Advisory board member – former president, share –based compensation .....	—	—	—	74,500
Advisory board members – all other, cash compensation ..	—	15,940	—	45,440
Share-based compensation – employees (previously classified as related party expenses) .....	—	23,808	—	24,390
Total consulting services expense – related parties .....	<u>\$ 79,358</u>	<u>\$ 78,998</u>	<u>\$ 119,775</u>	<u>\$ 232,830</u>

Consulting services expense – related parties is included in general and administrative expense in the consolidated statements of operations.

**Marketing expense – related parties:**

In January 2008, the Company entered into a month-to-month agreement with Veracity Credit Consultants, LLC, (“VCC”) an entity controlled by the majority shareholder of the Company, to provide call center facilities and call center services at prevailing market rates. The Company incurred \$75,000 and \$145,000 of call center

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marking expense during the three and six months ending June 30, 2008, respectively. Marketing expense – related parties is included in marketing expense in the consolidated statements of operations.

**Interest expense – related party:**

During 2006 and 2007 the Company received cash advances from VCC and incurred \$10,848 and \$17,640 of interest expense to VCC during the three and six months ended June 30, 2007, respectively. The Company did not incur related party interest expense in 2008. Interest expense – related party is included in interest expense in the consolidated statements of operations.

**Accounts payable – related parties:**

At June 30, 2008 and December 31, 2007, accounts payable to related parties was \$0 and \$21,152, respectively.

**5. Borrowings:**

At June 30, 2008 and December 31, 2007, our borrowings net of discounts, consisted of the following:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Current borrowings:		
Current portion of capital lease obligation .....	\$ 2,290	\$ 2,290
Total current borrowings .....	<u>\$ 2,290</u>	<u>\$ 2,290</u>
Long-term borrowings:		
Convertible debentures.....	\$ 3,650,291	\$ 3,725,291
Unamortized discount.....	<u>(175,775)</u>	<u>(269,155)</u>
Convertible debentures, net .....	3,474,516	3,456,136
Long-term capital lease obligation, net .....	<u>9,100</u>	<u>10,289</u>
Total long-term borrowings .....	<u>\$ 3,483,616</u>	<u>\$ 3,466,425</u>

During the three and six months ended June 30, 2008, the Company recognized \$48,439 and \$93,380, respectively of debt discount amortization applicable to the convertible debentures. During the three and six months ended June 30, 2008, the Company recognized \$81,685 and \$163,369 of debt offering costs amortization applicable to the convertible debentures, respectively.

During the three and six months ended June 30, 2007, the Company recognized \$3,735 of debt discount amortization applicable to the convertible debentures. During the three and six months ended June 30, 2007, the Company recognized \$6,384 of debt offering costs amortization applicable to the convertible debentures.

Debt discount amortization and debt offering cost amortization is included in interest expense in the Company's consolidated statements of operations.

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**6. Commitments and Contingencies**

**Commitments:**

On August 26, 2008, the Company filed a final prospectus dated August 14, 2008, with the British Columbia, Alberta and Ontario Securities Commissions in connection with its initial public offering of 17,000,000 units (“Units”) at the price of CDN\$0.60 per Unit for gross proceeds of CDN\$10,200,000 (the “Offering”). Each Unit will consist of one ordinary share of the Company and one-half of one ordinary share purchase warrant, with each whole warrant entitling the holder thereof to purchase one additional ordinary share of the Company at the price of CDN\$0.90 for a period of 24 months from the date that the ordinary shares are posted and listed for trading on the TSX Venture Exchange.

Bolder Investment Partners, Ltd. (“Bolder”) and Green Drake, Inc. (together, the “Agents”) are assisting the Company in selling the Units under the Offering pursuant to an Agency Agreement dated June 30, 2008. On completion of the Offering, the Company will pay the Agents a cash commission equal to 8% of the gross proceeds of the Offering and issue to the Agents placement agents’ warrants equal to 8% of the total number of Units sold under the Offering, each such placement agents’ warrant entitling the holder to purchase one ordinary share of the Company at the price of CDN\$0.60 for a period of 24 months from the date that the ordinary shares are posted and listed for trading on the TSX Venture Exchange (the “Listing Date”). The Company will also issue to Bolder 50,000 Units and pay to Bolder a corporate finance fee of CDN\$150,000 on the closing of the Offering.

In the event that the Company terminates the Agency Agreement prior to closing and the Company completes a debt or equity financing in excess of \$1,000,000 or a merger or reverse merger transaction within 12 months from the date of termination, then the Company will be obligated to pay Bolder a \$250,000 fee.

**Contingencies:**

On June 4, 2008, the Company received notice from the New York City Department of Consumer Affairs (the “DCA”) alleging violations of the New York City Consumer Protection Law and Rules. The notice alleges the Company used its advertisements in print media, television, the internet and other media to deceive or mislead consumers.

Upon receiving the notice from the DCA, the Company has taken action to remove its advertisement, suspend sales in New York and continue to service its existing New York customers, without charge, while this matter is pending or until the Company believes it has resolved the claims. After communications with the DCA and revisions to the Company’s advertisements and other sales materials, in August 2008, the Company resumed its advertising and sales efforts in New York. The company continues to be in correspondence with the DCA to resolve any remaining issues.

**7. Redeemable Convertible Preferred Shares and Warrants**

On January 28, 2008, the Company amended its Articles of Incorporation (“Amended Articles of Incorporation”) authorizing 1,750,000 shares of Series A Convertible Preferred Shares (“Series A Preferred”) with a stated value of \$2.00 per share (“Stated Value”).

On June 9, 2008, the Company further amended its Articles of Incorporation authorizing 500,000 shares of Series B Convertible Preferred Shares (“Series B Preferred”) with a Stated Value of \$2.00 per share to be pari

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passu with the Series A Preferred shares in all respects except that the Series B Preferred shares shall not have voting rights and shall not be deemed “Junior Securities” as defined in the Amended Articles of Incorporation.

The Series A and Series B Preferred shares include the following preferences, limitations and rights.

**Dividends:**

Dividends on Series A and Series B Preferred shares accrue at 12% per annum on the Stated Value, are cumulative, and are payable in cash on the first day of each quarter when the Company becomes profitable. Series A and Series B Preferred dividends have priority over dividends on ordinary shares and any other share capital of the Company. Series A and Series B Preferred shares are participating in any ordinary share dividends and will be paid on the same terms and in the same fashion as if all of the Series A and series B Preferred shares were converted into ordinary shares.

**Liquidation preferences:**

Series A and Series B Preferred shares have a liquidation preference in an amount equal to the greater of: a.) the Stated Value per share plus any accrued and unpaid dividends, or, b.) the amount per share that would have been payable had each share been converted into ordinary shares immediately prior to liquidation.

**Voting rights:**

Series A Preferred shares have voting rights and powers equal to the voting rights of ordinary shares on an “as if” converted to ordinary shares basis. As long as one-third of the series A Preferred shares are outstanding, the Company must obtain a waiver from the holders of the majority of the outstanding Series A Preferred shares before: a.) declaring or paying cash dividends on ordinary shares or other share capital of the Company, b.) authorizing or issuing additional shares of Series A Preferred, c.) amending the rights, preferences or privileges of the Series A Preferred, d.) authorizing any equity security senior to or on parity with the Series A Preferred, e.) merging or consolidating with any other company, or selling all or substantially all of the Company’s assets, or, f.) effecting any transaction in which the holders of the Company’s voting interest prior to such transaction hold less than 50% of the voting interest in the Corporation following such transaction.

**Conversion rates:**

During the period January 28, 2008, through December 31, 2008, the Series A and Series B Preferred shares and accrued and unpaid dividends thereon will automatically convert into shares issued in the “Next Round of Financing” (defined to be the issuance of ordinary or preferred shares of the Company resulting in gross proceeds of at least \$5.0 million) at a rate equal to 0.8 times the price paid per share by investors purchasing such shares in the Next Round of Financing.

Subsequent to December 31, 2008, Series A and Series B Preferred shares, at Stated Value (plus any dividends accrued and unpaid dividends per share) will be convertible into ordinary shares at a price that is the lesser of: a.) \$0.28 per ordinary share, or, b.) the market price (as defined in the Amended Articles of Incorporation) of the ordinary shares at the date of conversion, but in no event less than \$0.15 per ordinary share (the “Conversion Price”).

Conversion rates are subject to certain anti-dilution adjustments as defined in the Amended Articles of Incorporation.

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**Redemption:**

On or before December 31, 2008, the Company may call, with 70 days prior written notice, all Series A and Series B Preferred shares at an amount equal to 120% of the Stated Value per share (plus accrued and unpaid dividends per share) as of the redemption date. Upon or prior to giving notice, the Company must set aside a redemption fund in an amount equal to the total sum payable to the shareholders on the redemption date.

Any Series A and series B Preferred shares outstanding on January 28, 2011, will be, at the option of the holder, either: a.) mandatorily converted into ordinary shares at the Conversion Price in effect on January 28, 2011, or, b.) mandatorily redeemed in cash equal to the Stated Value plus all accrued and unpaid dividends.

**Series B redeemable convertible preferred shares and warrants:**

During May and June 2008, the Company sold 497,500 shares of Series B Preferred shares and five-year warrants to purchase 425,860 shares of the Company's ordinary shares for gross proceeds of \$995,000. The warrants have an exercise price of \$0.60 per share. \$83,532 of Series B issuance costs were charged to ordinary shares on the consolidated balance sheets at June 30, 2008.

Initially, the Series B Preferred shares will automatically convert into equity securities valued \$1,243.750 if the Company issues and sells at least \$5,000,000 of equity securities (i.e. ordinary shares, preferred shares or securities convertible into, or exchangeable for ordinary or preferred shares) on or before December 31, 2008.

The Series B Preferred shares are considered to be contingently redeemable shares and is classified as temporary equity on the Company's balance sheet as the Next Round of Financing may occur prior to December 31, 2008, and the Series B Preferred shares do not become mandatorily convertible unless the Next Round of Financing fails to occur on or before December 31, 2008.

In accordance with EITF 00-27, the Company allocated the \$995,000 gross proceeds between the warrants and the Series B Preferred on a basis of the relative fair values of each on the date of issuance. Using a ordinary share market price of \$0.50 per share, estimated annual volatility of 38% and a discount rate of 3.41%, the warrants were valued using the Black-Scholes model. The amount of gross proceeds allocated to the warrants was \$64,156 on the dates of issuance and recorded as an increase in share capital and as a discount to the Series B Preferred shares. This discount is being accreted over the period from the issuance dates to the contractual date of conversion of the Series B Preferred shares (December 31, 2008) on a straight-line basis which approximates the effective interest method. The accretion is recorded as an increase to net loss applicable to ordinary shares in the consolidated statement of operations. Accretion of Series B preferred shares discount was \$9,558 during the three and six months ended June 30, 2008. There was no accretion of Series B preferred shares discount during the three and six months ended June 30, 2007.

The fair value of the equity securities into which the Series B Preferred was convertible on the date of issuance, \$1,776,786, exceeded the proceeds allocated to the Series B Preferred by \$846,302, resulting in a beneficial conversion feature in the same amount that was recorded as an increase in share capital and as a further discount to the Series B Preferred shares. This discount is being amortized over the period from the issuance date to the contractual date of conversion on a straight-line basis which approximates the effective interest method. The amortization is recorded as a deemed dividends on redeemable convertible preferred shares and results in an increase to net loss applicable to ordinary shares in the consolidated statement of operations. Deemed dividends on Series B redeemable convertible preferred shares were \$125,378 during the three and six months ended June 30, 2008, respectively. There were no deemed dividends on Series B redeemable convertible preferred shares during the three and six months ended June 30, 2007.

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The Series B Preferred shares earn cumulative dividends at 12% per annum. No dividends were paid during the six months ended June 30, 2008, because of losses sustained by the Company. Dividends on the Series B Preferred shares were \$9,169 during the three and six months ended June 30, 2008. There were no dividends on the Series B Preferred shares during the six months ended June 30, 2007.

Accrued dividends payable were \$6,169, or \$0.00 per share, and \$0 as of June 30, 2008 and December 31, 2007, respectively, and are included in Series B redeemable convertible preferred shares on the Company's balance sheets.

**Series A redeemable convertible preferred shares and warrants:**

On January 28, 2008, the Company issued 1,750,000 shares of its Series A Preferred shares and five-year warrants to purchase 3,000,000 shares of its ordinary shares at an exercise price of \$0.35 per share for gross proceeds of \$3,500,000.

Initially, the Series A Preferred shares will automatically convert into equity securities valued \$4,375,000 if the Company issues and sells at least \$5,000,000 of equity securities (i.e. ordinary shares, preferred shares or securities convertible into, or exchangeable for ordinary or preferred shares) on or before December 31, 2008.

The Series A Preferred shares are considered to be contingently redeemable shares and is classified as temporary equity on the Company's balance sheet as the Next Round of Financing may occur prior to December 31, 2008, and the Series A Preferred shares do not become mandatorily convertible unless the Next Round of Financing fails to occur on or before December 31, 2008.

In accordance with EITF No. 00-27, the Company allocated the \$3,500,000 gross proceeds between the warrants and the Series A Preferred on a basis of the relative fair values of each on the date of issuance. Using a market price of \$0.35, estimated annual volatility of 38% and a discount rate of 2.8%, the warrants were valued using the Black-Scholes model. The amount of gross proceeds allocated to the warrants was \$355,749 on the date of issuance and recorded as an increase in share capital and as a discount to the Series A Preferred shares. This discount is being accreted over the period from the issuance date to the contractual date of conversion of the Series A Preferred shares (December 31, 2008) on a straight-line basis which approximates the effective interest method. The accretion is recorded as an increase to net loss applicable to ordinary shares in the statement of operations. Accretion of preferred shares discount was \$69,117 and \$215,997 during the three and six months ended June 30, 2008, respectively. There was no accretion of preferred shares discount during the three and six months ended June 30, 2007.

The fair value of the equity securities into which the Series A Preferred was convertible on the date of issuance, \$4,375,000, exceeded the proceeds allocated to the Series A Preferred by \$1,230,749, resulting in a beneficial conversion feature in the same amount that was recorded as an increase in share capital and as a further discount to the Series A Preferred shares. This discount is being amortized over the period from the issuance date to the contractual date of conversion (December 31, 2008) on a straight-line basis which approximates the effective interest method. The amortization is recorded as a deemed dividends on redeemable convertible preferred shares and results in an increase to net loss applicable to ordinary shares in the consolidated statement of operations. Deemed dividends on Series A redeemable convertible preferred shares were \$239,103 and \$747,279 during the three and six months ended June 30, 2008, respectively. There were no deemed dividends on Series A redeemable convertible preferred shares during the three and six months ended June 30, 2007.

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The Series A Preferred shares earn cumulative dividends at 12% per annum. No dividends were paid during the six months ended June 30, 2008, because of losses sustained by the Company. Dividends on the Series A Preferred shares were \$104,426 and \$176,919 during the three and six months ended June 30, 2008, respectively. There were no dividends on the Series A Preferred shares during the six months ended June 30, 2007. Accrued dividends payable were \$176,919, or \$0.01 per share, and \$0 as of June 30, 2008 and December 31, 2007, respectively, and are included in Series A redeemable convertible preferred shares on the Company's consolidated balance sheets.

Assuming that the Series A and B Preferred shares are not automatically converted and are held until mandatory redemption date, the Company expects to record dividends on redeemable convertible preferred shares in the amount of \$458,212 \$539,400, \$539,400 and \$39,901 for the years ending December 31, 2008, 2009, 2010 and 2011, respectively.

The Series A and Series B Preferred shares and accrued dividends were potentially convertible into 11,612,723 ordinary shares on June 30, 2008, if the Next Round of Financing were priced at \$0.50 per share.

At June 30, 2008, the Company has reserved 37,158,333 ordinary shares to effect the conversion of Series A and series B Preferred shares and any accrued but unpaid dividends thereon.

**8. Shareholders' Deficit:**

**Share capital:**

On June 24, 2008, the Company completed a private placement of 1,041,667 ordinary shares and detachable warrants to purchase 734,374 ordinary shares at exercise prices ranging from \$0.60 to \$0.90. Each unit, priced at \$0.48 per unit, consists of one ordinary share, 0.5 five year warrant to purchase ordinary shares at \$0.60 per share and 0.205 two year warrant to purchase ordinary shares at \$0.90 per share. The term of the two year \$0.90 warrant expires on the earlier of December 31, 2010 or twenty four months from the date that the ordinary shares are listed on the TSX Venture Exchange. Total proceeds from the private placement were \$500,000 and the proceeds were allocated to the warrants and ordinary shares based on the relative fair market value of each on the date the offering closed; the allocated amounts were \$46,669 and \$453,331, respectively. The fair values of the warrants were calculated using the Black Scholes valuation model with the following assumptions on June 24, 2008:

Expected term .....	2.1 – 5.0 years
Estimated volatility .....	38%
Risk-free interest rate .....	2.87% - 3.52%
Dividend yield .....	0%

**Stock options:**

In December 2005, the Company adopted the Identity Rehab Corporation Stock Option Plan (the "Plan") authorizing a pool of up to five million stock options available for grant. The exercise prices of the options granted are determined by the Plan Committee, which members are appointed by the Board of Directors, and are generally established at or above the estimated market price of the Company's ordinary shares at the date of grant. Options granted expire five years from the grant date and vest in accordance with the terms of the specific option agreement, generally over a period of 18 to 36 months.

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During the six months ended June 30, 2008, the Company granted 2,235,000 options to employees and consultants at exercise prices ranging from \$0.35 to \$0.60 per share. Employee options vest over 36 months as long as the grantee remains in the Company's employ. Share-based compensation expense is recognized over the period that the stock options vest. Consultant options generally vest over 18 months and share-based compensation expense is recognized during periods that the services are rendered.

A summary of stock option activity for the six months ended June 30, 2008 follows:

	<b>Shares Under Option</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term (in years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding as of January 1, 2007 .....	1,655,556	\$ 0.20	3.86	\$ 124,223
Granted .....	2,235,000	0.58		
Exercised .....	(55,556)	0.15		11,111
Forfeited .....	—	—		
Cancelled .....	—	—		
Outstanding as of June 30, 2008 .....	<u>3,835,000</u>	<u>\$ 0.43</u>	<u>4.30</u>	<u>\$ 483,251</u>
Exercisable at June 30, 2008 .....	<u>1,400,000</u>	<u>\$ 0.24</u>	<u>3.45</u>	<u>\$ 379,000</u>

During the three and six months ending June 30, 2007, the Company's chief executive officer transferred ordinary shares owned by him to the Company's Chief Financial Officer and to a former employee of the Company. The Company recognized \$22,350 and \$74,500 of share-based compensation expense, respectively, applicable to these transfers.

A summary of share-based compensation expense follows:

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30, 2008</b>	<b>June 30, 2007</b>	<b>June 30, 2008</b>	<b>June 30, 2007</b>
Share-based compensation expense – employees and directors .....	\$ 12,346	\$ 23,808	\$ 20,284	\$ 24,390
Share-based compensation expense – consultants - related parties ...	33,000	—	33,000	74,500
Share-based compensation expense – consultants – other .....	100,650	—	100,650	—
Total share-based compensation expense .....	<u>\$ 145,996</u>	<u>\$ 23,808</u>	<u>\$ 153,934</u>	<u>\$ 98,890</u>
Share-based compensation expense deferred in connection with the Company's pending IPO .....	<u>\$ 6,938</u>	<u>\$ —</u>	<u>\$ 6,938</u>	<u>\$ —</u>

As of June 30, 2008, there were 1,400,000 unvested stock options outstanding and the total unrecognized share-based compensation expense relating to these options was \$198,556. The weighted average term of unrecognized share-based compensation expense was 2.77 years at June 30, 2008.

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**Warrants:**

A summary of warrant activity for the six months ended June 30, 2008 follows:

	<u>Shares</u>	<u>Weighted Average Exercise Price</u>
Outstanding as of January 1, 2007 .....	15,965,486	\$ 0.375
Issued .....	4,160,234	0.457
Exercised .....	—	—
Cancelled .....	—	—
Outstanding as of June 30, 2008 .....	<u>20,125,720</u>	<u>\$ 0.392</u>

The following table presents the composition of warrants outstanding as of June 30, 2008:

<u>Range of Exercise Prices</u>	<u>Shares</u>	<u>Weighted Average Remaining Contractual Life (years)</u>
\$0.35 .....	10,982,743	4.16
\$0.40 .....	7,982,743	4.01
\$0.60 .....	639,401	4.95
\$0.90 .....	520,833	2.18
Total warrants outstanding as of June 30, 2008 .....	<u>20,125,720</u>	<u>4.07</u>

**Ordinary shares reserved for future issuance:**

The following ordinary shares are reserved for future issuance at June 30, 2008:

	<u>Shares</u>
Stock option plan .....	3,835,000
Warrants .....	20,125,720
Convertible debentures .....	13,036,754
Redeemable convertible preferred shares .....	37,158,333
Total .....	<u>74,155,807</u>

**9. Subsequent Events:**

As previously mentioned, on August 26, 2008, the Company filed a final prospectus dated August 14, 2008 with the British Columbia, Alberta and Ontario Securities Commissions in connection with its initial public offering of 17,000,000 Units at the price of CDN\$0.60 per Unit for gross proceeds of CDN\$10,200,000. Each Unit will consist of one ordinary share of the Company and one-half of one ordinary share purchase warrant, with each whole warrant entitling the holder thereof to purchase one additional ordinary share of the Company at the price of CDN\$0.90 for a period of 24 months from the date that the ordinary shares are posted and listed for trading on the TSX Venture Exchange (the "Listing Date"). On August 25, 2008 the Company received conditional approval for the listing of its ordinary shares on the TSX Venture Exchange.

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Concurrent with the completion of the Offering, 1,750,000 outstanding Series A Convertible Preferred shares and 497,500 outstanding Series B Convertible Preferred shares of the Company will be automatically converted into Units of the Company. The total number of Units issuable upon such automatic conversion shall be determined by dividing (i) the aggregate issue price of the Series A Convertible Preferred shares and the Series B Convertible Preferred shares based on U.S. \$2.00 per share (plus accrued but unpaid 12% cumulative dividends thereon) by (ii) the conversion price of CDN\$0.48 per ordinary share (being 0.8 times the price per Unit under the Offering).

**10. Generally Accepted Accounting Principles in Canada:**

The Company prepares its financial statements in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). There are no differences between U.S. GAAP and Canadian generally accepted accounting principles that would have a material effect on the Company's financial statements.