Sterne Stackhouse Inc.

Annual Report

2003

For the Year Ended October 31, 2003

Corporate Profile

Sterne Stackhouse Inc.(SSI), through its Labrador Technologies division, specializes in building connections between companies and the data they invest in. Since 1981, SSI has been developing Data-Flow Management™ and data retrieval, reporting, and analysis software for the Oil and Gas industry.

Focused on Data-Flow Management™ (DFM), Labrador Technologies has the ability to retrieve and deliver data to the right place, at the right time. Whether delivering data to a Labrador® application, an enterprise service bus, or a portal, Labrador® gets the job done efficiently. Labrador Technologies' DFM™ software and services help software vendors, data vendors, and company developers deliver data to their target audiences by 'plugging' users in, and eliminating the need for expensive and ongoing manual intervention.

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AGM

The Annual General Meeting of the Shareholders of Sterne Stackhouse Inc. will be held at 2:00 p.m. on April 15th, 2004 in the SSI Corporate Office at 350, 229 - 11th Avenue S.E., Calgary, Alberta. All shareholders are encouraged to attend and participate. Those who are unable to attend are requested to return their proxies to the registrar within the times specified in the Notice of Meeting.

Information on Sterne Stackhouse Inc.
is available through our
Internet site at

www.sternestackhouse.com

CEO'S REPORT TO SHAREHOLDERS

The Test of Time

Having incorporated in January 1981, and retained its core people through some very tough runs, the Company has stood the test of time. And, the story of the Company is really a story about its people and its technology. Accordingly, management is requesting shareholder approval at the Annual and Special Meeting, on April 15th, 2004, to change the company name to Labrador Technologies Inc. Last year's Annual Report provides a complete summary of the Company's ongoing Labrador® software offerings, as well as its rigorous approach to software development, which does not bear repeating here. However, the Company's software is well documented on its new website, which features Data-Flow Management™.

The Sale of Canadian Petro-LAB™ in Retrospect

The summary of the sale of Canadian Petro-LAB™ does bear repeating. As Peter Huggard, President of Qbyte/IBM Canada, recently summed up to me, " . . . it has never let us down." Sterne Stackhouse Inc. (SSI) received approximately $8,200,000, over a little less than a three-year period. Qbyte/IBM Canada has the source code, and has the flexibility to respond quickly to client requirements. The SSI/Qbyte relationship remains exceptionally cordial. As a result, should Qbyte/IBM Canada require additional assistance with database modeling projects or ongoing Petro-LAB™ development, SSI is not far away.

Effective Distribution is the Key to SSI Profitability

The foregoing title and the following text come directly from the 2002 Annual Report, and are particularly relevant to this reporting:

"Although the Company has a well-rounded suite of products, it did not set itself up to be a direct marketing/sales and distribution vehicle when it went public in 1997. SSI's business model has been to prove out, as much as necessary, the value of its products by working directly with clients and partners, and then create/negotiate an appropriate distribution agreement…"

"The Company has every reason to believe that its other products are equal to the quality and potential of Canadian Petro-LAB™…"

"Finding the right distribution partner is a difficult, but achievable, undertaking…"

"Management has learned to be patient, as it believes that the Company's software products offer immense upside if the Company can find the 'right' distribution partner(s)."

Finding the Right Distribution Partners

Our shareholders are aware that it seems to take a long time to find the "right" distribution partners. With that in mind, let's review the search criteria management employs to determine the right "fit" for SSI:

1. An international software/consulting company with an aggressive marketing/sales approach and long-standing customer relationships.

2. An ambitiously expansive oil and gas division, with a presence in other industries such as healthcare and/or pharmaceuticals.

3. A "work-with" culture. This must extend well beyond sales management. If software companies are going to work together effectively and profitably, they need a firm technical foundation, with considerable cooperation. Ready, practical access to key software developers is important for establishing a sound beginning. This is a heady challenge that is rarely overcome, but it is fundamental to success. Some Calgary-based Research and Development can be very helpful.

4. The financial depth and wherewithal to "make things happen", and stay the course.

Aspen Technology, Inc.

Since the summer of 2003, we have been working diligently with Aspen Technology, Inc. (AspenTech). There have been no dramatic developments to report on, until now. Trite as it is to say, the building of good, solid relationships is often done in many "baby-steps". Cultures have to be compatible, and the only way to find that out is to actually work together.

Working with AspenTech became more practical and compelling since AspenTech acquired a strong, Calgary-based company, Hyprotech, Ltd., in 2002. Hyprotech, more than 25 years old, was exceedingly successful specializing in oil and gas software and services on an international basis. For more information about AspenTech's acquisition of Hyprotech, Ltd. and AspenTech's world-wide annual revenues, which in fiscal 2003 exceeded $320 Million USD, please refer to www.aspentech.com.

The consolidated Calgary offices of AspenTech/Hyprotech are only three blocks from ours, creating easy, mutual access to each other's personnel. AspenTech develops in a Microsoft.Net environment, and we are continuing to port our Labrador® tools to .Net, in addition to our existing Labrador® JAVA versions.

As AspenTech trades on the NASDAQ Exchange (AZPN:NASDAQ), and information dissemination is governed accordingly, the following information has been prepared by AspenTech for release in this 2003 Annual Report:

> ***"AspenTech Partnership with Labrador Technologies"***
>
> *"Aspen Technology has established a new partnership with Labrador Technologies, a division of Sterne Stackhouse Inc., to provide enhanced capabilities for AspenTech's production asset management solution for the oil & gas industry. Under the partnership agreement, Labrador's Well-LAB™ production and well test data-flow system will be available as an add-on module for the Aspen AssetBuilder™ modeling software.*
>
> *Well-LAB™ will enable companies using Aspen AssetBuilder™ to access a wide range of commercial and proprietary oil & gas production data sources to feed its integrated asset simulation models. It automates the process of connecting to real-time production and well test databases that exist within, or external to, an organization. The Well-LAB™ module is currently in beta test."*

An Experienced “Start-Up” Looking Forward to Fiscal 2004

Although the effective date of the sale of Canadian Petro-LAB™ was August 1st, 2003, the sale was not closed until December 18th, and the proceeds do not show up in our financials until the 1st Quarter of 2004. Since October 31st, 2003, expenses have been again reduced, as management took a further reduction in salary.

In effect, even though we have been around for over 20 years, we are treating our company as a “start-up”. Yes, we have robust, innovative software offerings, and, yes, we have a great deal of experience – but still, we are moving forward carefully and methodically. With the recent Qbyte/IBM Canada income, our cash position is sound. We have no debt. Yet, although management is extremely pleased with current developments, it continues to be focused and committed to growing and evolving distribution partnerships into immediate revenue generating initiatives.

On behalf of the Board of Directors,

H. Ronald Sterne

Chief Executive Officer
Sterne Stackhouse Inc.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the balance sheets of Sterne Stackhouse Inc. as at October 31, 2003 and 2002 and the statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at October 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

KPMG LLP

Calgary, Canada
January 23, 2004

MANAGEMENT'S DISCUSSION & ANALYSIS

October 31, 2003

The following discussion should be read in conjunction with the audited financial statements presented in accordance with accounting principles generally accepted in Canada. All amounts are stated in Canadian dollars.

Corporate Profile

Sterne Stackhouse Inc. (SSI) specializes in building connections between companies and the data they invest in. Since 1981, SSI has been developing Data-Flow Management™ and data retrieval, reporting, and analysis software for the Oil and Gas industry.

Focused on Data-Flow Management™ (DFM), Labrador Technologies, a division of SSI, has the ability to retrieve and deliver data to the right place, at the right time. Whether delivering data to a Labrador® application, a third-party application, an enterprise service bus, or a portal, Labrador® gets the job done efficiently. Labrador Technologies' DFM™ software and services help software vendors, data vendors, and company developers deliver data to their target audiences by 'plugging' users in, and eliminating the need for expensive and ongoing manual intervention. For more information, visit www.sternestackhouse.com.

Financial Results

Cash Flow Analysis

	Years ended October 31 2003	Years ended October 31 2002
Sources of cash		
Decrease in accounts receivable – Qbyte/IBM	**$ 565,322**	$ 756,138
Decrease in accounts receivable – other	**—**	26,491
Increase in accounts payable and accrued liabilities	**26,702**	—
Proceeds received on the sale of capital assets	**22,719**	—
	$ 614,743	$ 782,629
Uses of cash		
Operations	**911,800**	566,502
Decrease in accounts payable and accrued liabilities	**—**	35,321
Capital asset additions	**21,024**	46,956
	$ 932,824	$ 648,779
Sources of cash minus uses of cash	**(318,081)**	$ 133,850
Cash balance at the beginning of the year	**$ 407,506**	$ 273,656
Cash balance at the end of the year	**$ 89,425**	$ 407,506

In the foregoing table, cash used in operations is equal to the net loss shown on the Statement of Operations and Deficit adjusted for: depreciation and amortization, deferred revenue, stock-based compensation and prepaid expenses. These adjustments are shown in the following table.

Cash Used in Operations

	Years ended October 31 2003	Years ended October 31 2002
Operations:		
Revenue	**$ 883,605**	$ 1,817,395
Expenses	**(1,850,067)**	(2,562,484)
Net loss	**$ (966,462)**	$ (745,089)
Non-cash adjustments		
Non-cash reorganization and related costs	**$ —**	$ 96,000
Stock-based compensation	**5,800**	—
Depreciation and amortization	**58,161**	95,039
Deferred revenue	**—**	(32,000)
Prepaid expenses	**(9,299)**	19,548
Cash used in operations	**$ (911,800)**	$ (566,502)

Results of Operations

Financial Summary

As explained in previous reports, according to the terms of the Qbyte/IBM Agreement, revenue is only recognized as the licenses are renewed. During the year, there was renewal revenue from Qbyte/IBM of $853,987.

Financial Summary

	Years ended October 31 2003	Years ended October 31 2002
Revenue	**$ 883,605**	$ 1,817,395
Expenses	**1,850,067**	2,562,484
Loss	**(966,462)**	(745,089)
Loss per share	**(0.12)**	(0.09)
Outstanding shares	**8,249,685**	8,549,685

	October 31 2003	October 31 2002
Cash balance	**$ 89,425**	$ 407,506
Shareholders' equity	**152,383**	1,113,045
Total assets	**305,615**	1,239,575

Revenue

SSI's total revenue for the year ended October 31, 2003 was $883,605 compared to $1,817,395 for the previous year ended October 31, 2002, a decrease of $933,790. The decrease in revenue is mainly attributed to the fact that in the prior year there was additional license renewal revenue due to the conversion of two Petro-LAB™ clients from annual licenses to perpetual licenses. The absence of any conversions in the current year resulted in the reduction in revenue. The revenue for the year is comprised of $853,987 recognized on the renewal of Petro-LAB™ licenses, $25,388 for new business royalties arising from the Qbyte/IBM Agreement (see below), $810 for consulting services to Qbyte/IBM related to Petro-LAB™, and $3,420 for annual maintenance for Labrador® licenses.

On December 18, 2003, the Company completed a transaction with Qbyte/IBM to accelerate the purchase of the Petro-LAB™ software by Qbyte/IBM (see Petro-LAB™ - Qbyte/IBM Agreement). The transaction also included a termination of the royalty agreement with Qbyte/IBM. As a result of this transaction, the Company will no longer receive any payments from Qbyte/IBM and, as a result, the Company has no ongoing revenues. A more detailed explanation of the transaction is contained in the Financial Liquidity section.

Petro-LAB™ - Qbyte/IBM Agreement

On March 16th, 2001, the Company negotiated a cash and royalty-bearing agreement with Qbyte/IBM, a leading provider of software to the Canadian oil and gas industry. Under the terms of the agreement, Qbyte/IBM was to acquire the Canadian rights to SSI's Petro-LAB™ application over 5 years. The effective date of the agreement was February 28th, 2001. For a discussion of the terms of the agreement, the reader can refer to the previous year's annual report.

From the effective date of the agreement (February 28, 2001) to October 31, 2003, SSI has received cash payments from Qbyte/IBM, related to the sale of Petro-LAB™ of $6,390,116 ($1,500,000 from the royalty prepayment, $1,900,000 from the first year of monthly payments, $2,380,000 from the second year of monthly payments, and $610,116 being eight months payments from the third year of monthly payments). In addition, from the effective date of the Agreement to October 31, 2003, actual Petro-LAB™ license renewal revenue from existing clients was $6,016,198.

Royalty revenue from Petro-LAB™ license renewals from existing clients is recognized when the license renewals occur. Since $0.50 of each $1.00 of license renewal revenue has already been recognized in the one-time gain of $4,480,619, the remaining $0.50 of each $1.00 of license renewal revenue is recognized when the renewal invoice is sent to the client. As a result, as of October 31, 2003, Qbyte/IBM had invoiced $6,016,198 of Petro-LAB™ license renewal fees. SSI recognized $3,008,099, or half of these renewal fees, as revenue ($853,987 during the current year ended October 31, 2003). Royalty revenue from new Petro-LAB™ business is recognized when Qbyte/IBM pays the royalties to SSI. As of October 31, 2003, SSI had received $71,300 of royalty revenue from new Petro-LAB™ business ($25,388 from the current year ended October 31, 2003).

On the effective date of the agreement, February 28th, 2001, the Company recorded a cash receipt of $1,500,000 from the Qbyte/IBM agreement and an account receivable of $1,999,375. The account receivable is reduced by the monthly payments received from Qbyte/IBM, and was increased by an amount equal to the royalty revenue recognized when a license renewal occurs. As a result, the account receivable from Qbyte/IBM at October 31, 2003 was equal to $117,358 (i.e. $1,999,375 less monthly payments totaling $4,890,116, plus royalty revenue recognized from Petro-LAB™ license renewals from existing clients of $3,008,099).

On December 18, 2003, the Company completed a transaction with Qbyte/IBM to accelerate the purchase of the Petro-LAB™ software by Qbyte/IBM. The transaction also included a termination of the royalty agreement with Qbyte/IBM. As a result of this transaction, the Company received a cash payment of $1,591,000 and will no longer receive any payments from Qbyte/IBM. A more detailed explanation of the transaction is contained in the Financial Liquidity section.

Expenses

General and Administrative

This category of expenses is comprised primarily of office rent, office equipment rentals, administrative salaries, corporate expenses related to shareholder reporting, and professional fees. General and administrative expenses for the year ended October 31, 2003 were $1,027,724 compared to $1,108,473 for the year ended October 31, 2002, a decrease of $80,749. The decrease arose from a reduction in rental equipment expenses of $87,135, a reduction in administrative salaries of $52,671 and an increase in office rent of $33,596. The remainder of the difference is due to minor changes in various miscellaneous accounts.

Effective September 1, 2003, the Company sub-leased its McFarlane Tower office space and relocated to smaller space. The sublease terminates at the end of January, 2005 when the primary lease expires. Based on the terms of the sublease, the Company is able to recapture all but $61,738 of its lease costs. This amount was charged as an expense in the current year and was the reason for the increase in office rent expense over the prior year. Going forward, the Company expects to save approximately $16,000 per month in office rent expenses as a result of the sublease and relocation.

Sales, Marketing and Support

Sales and marketing expenses include expenses for sales and support salaries/consulting fees, sales commissions, and promotion/advertising. For the year ended October 31, 2003, sales and marketing expenses were $248,493 compared to $404,965 for the year ended October 31, 2002, a decrease of $156,472. The decrease is due to a reduction in sales and support salaries/consulting fees of $172,709 and minor changes to other miscellaneous accounts.

Computer and Related Costs

Computer and related costs include hardware maintenance, programmer's salaries, and software costs. This category of expenses totaled $509,889 for the year ended October 31, 2003, compared to $831,090 for the year ended October 31, 2002, a decrease of $321,201. The decrease is due to a decrease in programmer's salaries of $202,783 and a reduction in third party software costs of $57,069. The remainder of the difference is due to small changes in various miscellaneous accounts.

Reorganization and related costs

During the prior year, the Company underwent an internal reorganization. As a result, reorganization and related costs for the prior year included a write-off of capital assets totaling $96,000 relating to the fact that certain assets were no longer being fully utilized and severance costs of $26,364. There were no equivalent costs during the current year.

Depreciation

Depreciation expense for the year ended October 31, 2003 was $58,161 compared to $95,039 for the previous fiscal year. The reduction of $36,878 is due primarily to the write-off of capital assets from the reorganization and related costs (see above) of the prior year.

Financing and Investing

During the year ended October 31, 2003, the Company's cash position decreased by $318,081. During the year, the Company did not undertake any financing activities.

Financial Condition, Liquidity and Requirements Outlook

At October 31, 2003, SSI had cash of $89,425, no debt, and working capital of $91,473. Prior to the December 18th 2003 transaction, detailed below, the Company also had guaranteed monthly cash inflow from Qbyte/IBM of $76,248 through February 2004 (see Petro-LAB™ - Qbyte/IBM Agreement above).

On December 18, 2003, the Company completed a transaction with Qbyte/IBM Canada to accelerate the purchase of the Petro-LAB™ software by Qbyte/IBM. The transaction also included a termination of the royalty agreement with Qbyte. As a result of this transaction, the Company received a cash payment of approximately $1,591,000, including adjustments and the settlement of accounts receivables (see Petro-LAB™ – Qbyte/IBM Agreement above). As a result of the transaction, the Company has no ongoing revenue and is relying on future sales to generate additional revenue. The cash received from the transaction gives the Company enough cash to continue operations for the foreseeable future. Based on the current level of expenditures, the Company has an average cash usage rate of approximately $105,000 per month.

Forward Looking Statements

Certain statements in Management's Financial Discussion and Analysis, other than statements of historical fact, are forward-looking information that involve various risks and uncertainties. These risks and uncertainties include, but are not restricted to, the Company's continuing ability to promote and license its products, the Company's ability to attract and retain key employees, and the Company's ability to raise capital on acceptable terms when needed. These uncertainties may cause actual results to differ from information contained herein. There can be no assurance that such statements will prove to be accurate. Actual results and future events could differ materially from those anticipated in such statements. These forward-looking statements are based on the estimates and opinions of management on the dates they are made and are expressly qualified in their entirety by this notice. The Company assumes no obligation to update forward-looking statements should circumstances, management's estimates, or opinions change.

STERNE STACKHOUSE INC.

Balance Sheets

October 31, 2003 and 2002

	2003	2002
ASSETS		
Current assets:		
Cash	**$ 89,425**	$ 407,506
Accounts receivable (notes 6 and 9)	**119,684**	685,006
Prepaid expenses	**35,596**	26,297
	244,705	1,118,809
Capital assets (note 3)	**60,910**	120,766
	$ 305,615	$ 1,239,575
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	**$ 153,232**	126,530
Shareholders' equity:		
Share capital (note 4)	**4,902,884**	5,081,178
Contributed surplus (note 4)	**184,094**	–
Deficit	**(4,934,595)**	(3,968,133)
	152,383	1,113,045
Future operations (note 1)		
Commitments (note 8)		
Subsequent events (note 4 and 6)		
	$ 305,615	$ 1,239,575

See accompanying notes to financial statements.

STERNE STACKHOUSE INC.

Statements of Operations and Deficit

Years ended October 31, 2003 and 2002

	2003	2002
REVENUES:		
Royalty income	**$ 879,375**	$ 1,491,264
Consulting fees	**810**	271,331
License fees	**3,420**	54,800
	883,605	1,817,395
EXPENSES:		
General and administration	**1,027,724**	1,108,473
Computer and related costs	**509,889**	831,090
Sales and marketing	**248,493**	404,965
Depreciation	**58,161**	95,039
Stock-based compensation (note 4)	**5,800**	–
Reorganization and related costs	**–**	122,364
Interest	**–**	553
	1,850,067	2,562,484
Net loss	**(966,462)**	(745,089)
Deficit, beginning of year	**(3,968,133)**	(3,223,044)
Deficit, end of year	**$(4,934,595)**	$(3,968,133)
Net loss per share (note 4):		
Basic and diluted	**$ (0.12)**	$ (0.09)

See accompanying notes to financial statements.

STERNE STACKHOUSE INC.

Statements of Cash Flows

Years ended October 31, 2003 and 2002

	2003	2002
Cash provided by (used in):		
Operating activities:		
Net loss	$ (966,462)	$ (745,089)
Items not involving cash:		
Depreciation	58,161	95,039
Stock-based compensation	5,800	–
Non-cash reorganization and related costs	–	96,000
	(902,501)	(554,050)
Changes in non-cash working capital (note 7)	582,725	2,148
	(319,776)	(551,902)
Investing activities:		
Proceeds received on the sale of capital assets	22,719	–
Capital assets additions	(21,024)	(46,956)
Change in non-cash working capital relating to investing activities (note 7)	–	732,708
	1,695	685,752
Increase (decrease) in cash	(318,081)	133,850
Cash, beginning of year	407,506	273,656
Cash, end of year	$ 89,425	$ 407,506

See accompanying notes to financial statements.

Sterne Stackhouse Inc. (the "Corporation") is engaged in the research and development and marketing of data retrieval technology for customers.

1. Future operations:

These financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assume that the Corporation will continue in operation for the foreseeable future and will be able to realize its assets and discharge its obligations in the normal course of operations.

At October 31, 2003 the Corporation had a working capital balance totaling $91,473. Subsequent to October 31, 2003 the Corporation terminated its royalty agreement with the purchaser of the Petro-LAB™ software for proceeds totaling approximately $1,591,000 (see note 6) and as a result, the Corporation will no longer receive royalty payments from the purchaser and to date, has generated no alternative source of revenue.

While management believes that the Corporation has sufficient cash to discharge its obligations in the normal course of operations through fiscal 2004, future operations will regardless be dependent upon the successful ongoing development and marketing of the Corporation's data retrieval technology and the corresponding generation of future cash flows. Management believes the going concern assumption is appropriate for these financial statements. If the going concern assumption were not appropriate for these financial statements, then adjustments might be necessary to the carrying value of assets and liabilities, reported revenues and expenses and the balance sheet classifications used.

2. Significant accounting policies:

The financial statements of the Corporation have been prepared by management in accordance with Canadian generally accepted accounting principles. In the preparation of these financial statements, management has made estimates and assumptions that affect the recorded amounts of certain of the Corporation's assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. While it is the opinion of management that these financial statements have been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below, actual results could differ from the estimates made.

(a) Revenue recognition:

Substantially all revenue is derived from one customer as a result of the sale of the Petro-LAB™ software (see notes 6 and 9). Royalty income is recognized as a percentage of the fees generated and collected by the customer.

Revenue from the sale of licenses as well as revenue attributable to undelivered elements, including maintenance and other post-customer support services, is recognized ratably over the contract period. Revenue from consulting services is recognized when the services are performed and/or when earned.

2. Significant accounting policies (continued):

(b) Capital assets:

Capital assets are recorded at cost upon acquisition. Depreciation is provided annually over the estimated useful lives of the assets as follows:

Asset	Basis	Rate
Computer equipment	Declining balance	30%
Furniture and equipment	Declining balance	20%
Purchased computer software	Declining balance	50%
Leasehold improvements	Straight line	2 years

(c) Stock based compensation plan:

Effective November 1, 2002, the Corporation prospectively adopted the new Canadian accounting standard relating to stock-based compensation. Under this standard the Corporation continues to follow the settlement method of accounting for stock options granted to employees whereby the proceeds received on the exercise of options are included in capital stock and no compensation expense is recognized. For stock-based compensation to non-employees, the Corporation will calculate a fair value using an option pricing model, and record the expense to earnings over the term of the option.

(d) Per share amounts:

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted per share amounts reflect the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options, warrants and other dilutive instruments.

(e) Income taxes:

The Corporation uses the liability method of accounting for income taxes (see note 5). Under this method, future income tax liabilities and future income tax assets are recorded based on temporary differences – the difference between the carrying amount of an asset and liability in the balance sheet and its tax basis using income tax rates enacted at the balance sheet date. The effect of changes in rates on future income tax liabilities and assets is recognized in the period that the change occurs.

3. Capital assets:

2003	Cost	Accumulated depreciation	Net book value
Computer equipment	$ 453,447	$ 428,706	$ 24,741
Furniture and equipment	182,092	164,344	17,748
Purchased computer software	291,469	278,054	13,415
Leasehold improvements	81,506	76,500	5,006
	$ 1,008,514	$ 947,604	$ 60,910
2002			
Computer equipment	$ 461,217	$ 413,273	$ 47,944
Furniture and equipment	184,456	158,618	25,838
Purchased computer software	288,492	266,128	22,364
Leasehold improvements	76,045	51,425	24,620
	$ 1,010,210	$ 889,444	$ 120,766

4. Share capital:

(a) Authorized:

Unlimited preferred shares, Series A and Series B; and

Unlimited common shares.

(b) Issued and outstanding:

	2003		2002	
Common shares	Number of shares	Amount	Number of shares	Amount
Balance, beginning of year	8,549,685	$ 5,081,178	8,549,685	$ 5,081,178
Cancelled	(300,000)	(178,294)	–	–
Balance, end of year	8,249,685	$ 4,902,884	8,549,685	$ 5,081,178

During the year ended October 31, 2003 the Corporation cancelled 300,000 common shares for $nil proceeds. As a result, the weighted average book value of the common shares cancelled totaling $178,294 was recorded as contributed surplus.

(c) Stock option plan:

The Corporation has a stock option plan for its directors, officers and employees. Details of the stock options outstanding under this plan were as follows:

	Number	Exercise price	Weighted average exercise price
Outstanding at October 31, 2001	855,000	$ 0.25 – 1.55	$ 0.60
Granted	570,000	0.60 – 1.55	0.66
Expired	(465,000)	0.35	0.35
Cancelled	(200,000)	0.25 – 1.05	0.61
Outstanding at October 31, 2002	760,000	0.25 – 1.50	0.38
Expired	(110,000)	0.25 – 1.50	0.59
Granted	294,969	0.12 – 0.20	0.17
Cancelled	(200,000)	0.25 – 0.80	0.34
Outstanding at October 31, 2003	744,969	$ 0.12 – 0.35	$ 0.28

4. Share capital (continued):

(c) Stock option plan (continued):

	Options outstanding and exercisable	
Exercise price outstanding	Number outstanding at October 31, 2003	Weighted average remaining contractual life (months)
$0.12	40,000	55
0.16	140,000	15
0.20	114,969	55
0.35	370,000	38
0.35	80,000	41
	744,969	38

Subsequent to October 31, 2003, 60,000 options exercisable at a price of $0.20 per share were granted to an employee and 60,000 options exercisable at a price of $0.16 per share were cancelled.

(d) Stock-based compensation:

The Corporation does not record compensation expense when stock options are issued to employees, officers and directors.

Had compensation expense been determined based on the fair value at the grant dates, the net loss and loss per share would have been as shown in the pro forma amounts indicated below:

Stock-based compensation expense	$ 16,744
Net loss:	
As reported	$ (966,462)
Pro-forma	$ (983,206)
Net loss per share (basic and diluted):	
As reported	$ (0.12)
Pro-forma	$ (0.12)

The Corporation recognized compensation expense of $5,800 for stock options granted to consultants and non-employees for the year ended October 31, 2003.

The fair value of stock options granted during the year ended October 31, 2003 was estimated using the Black-Scholes option-pricing model with the following assumptions:

Dividend yield	0%
Expected volatility	60%
Risk free rate of return	5%
Expected option life	2 – 5 years

4. Share capital (continued):

(e) Warrants:

Information with respect to the outstanding warrants is as follows:

Outstanding at October 31, 2001	781,750
Expired	(631,750)
Outstanding at October 31, 2002	150,000
Expired	(150,000)
Outstanding at October 31, 2003	–

(f) Per share amounts:

The weighted average number of common shares outstanding during the year ended October 31, 2003 was 8,547,219 (2002 – 8,549,685).

The dilutive effect of options and warrants for the year ended October 31, 2003 was nil (2002 – nil) and nil (2002 – nil), respectively.

5. Income taxes:

Total income taxes are different from the amount computed by applying the combined expected Canadian Federal and Provincial tax rate of 37.2% (2002 – 39.7%) to income before income taxes and other items. The reasons for the difference are as follows:

	2003	2002
Computed expected tax recovery	$ (360,000)	$ (296,000)
Add (deduct) the following:		
Non-deductible expenses	20,000	21,000
Net increase in valuation allowance	340,000	275,000
	$ –	$ –

5. Income taxes (continued):

The components of the future income tax assets and liabilities at October 31, 2003 is as follows:

	2003	2002
Future income tax assets:		
Share issue costs	$ 19,000	$ 37,000
Non-capital losses	1,677,000	1,342,000
Capital assets	85,000	61,000
Bad debt reserve	–	105,000
Future income tax liabilities:		
Accounts receivable reserve	–	(218,000)
Capital assets	–	–
	1,781,000	1,327,000
Less valuation allowance	(1,781,000)	(1,327,000)
Net future income tax asset (liability)	$ –	$ –

As at October 31, 2003, the Corporation has investment tax credits carryforward of approximately $363,000 (2002 - $363,000), which may be used to offset federal taxes payable in future years. These investment tax credits expire in the years 2007 to 2010. As at October 31, 2003, the Corporation has federal non-capital losses totalling approximately $4,212,000, and Alberta non-capital losses totaling approximately $3,998,000, which expire in the years 2007 to 2010. The potential income tax benefit arising from these amounts has not been reflected in these financial statements.

6. Gain on sale of Petro-LAB™:

During the year ended October 31, 2001 the Corporation closed a transaction with a provider of software to the Canadian oil and gas industry which resulted in the sale of the Petro-LAB™ software. The rights to use Petro-LAB™ outside of Canada have not been sold and have been retained by the Corporation. Under the terms of the agreement, the Corporation received an immediate $1,500,000 royalty pre-payment and received additional royalty payments which were contingent upon sales made by the purchaser to customers of the Corporation that existed prior to the sale of the Petro-LAB™ software.

As a result of the transaction, the Corporation recognized a gain on the sale of the Petro-LAB™ assets totaling $4,480,619 based upon the minimum level of cash to be received. Amounts received subsequent to the sale of the Petro-LAB™ software were recorded as royalty income.

On December 18, 2003 the Corporation entered into an agreement to terminate its royalty agreement with the purchaser of the Petro-LAB™ software resulting in the Corporation receiving a final cash payment, including adjustments, of approximately $1,591,000 and the settlement of accounts payable and accrued liabilities totaling approximately $63,000. As a result, a total gain on termination of the agreement and royalty payments of approximately $1,654,000 will be recorded in fiscal 2004. As such, the Corporation will receive no further royalty payments from the purchaser of the Petro-LAB™ software.

7. Supplemental cash flow disclosure:

(a) Changes in non-cash working capital are as follows:

	2003	2002
Accounts receivable	$ 565,322	$ 782,629
Prepaid expenses	(9,299)	19,548
Accounts payable and accrued liabilities	26,702	(35,321)
Deferred revenue	–	(32,000)
	582,725	734,856
Add (deduct) changes in non-cash working capital relating to investing activities	–	(732,708)
	$ 582,725	$ 2,148

(b) The following cash payments were made:

	2003	2002
Interest	$ –	$ 553

8. Commitments:

The Corporation has leases on its premises and certain computer and office equipment, which expire through 2005. Minimum annual payments under the leases are approximately as follows:

2004	$ 153,000
2005	83,000

9. Segmented information and customer concentration:

(a) Segment information:

The Corporation had two operating segments for the development and marketing of its data retrieval technology: 1) the oil and gas industry; and 2) other commercial applications. As the activities of the segment relating to the development and marketing of data retrieval technology to the oil and gas industry were minimal during the years ended October 31, 2003 and 2002, no segment disclosure has been presented.

(b) Customer concentration:

As a result of the Corporation's sale of Petro-LAB™ (see note 6), substantially all the Corporation's current revenues were derived from one customer. As such, accounts receivable from this customer totaled $119,684 (2002 - $685,006) as at October 31, 2003.

10. Fair values:

As at October 31, 2003 and 2002, the fair values of the Corporation's monetary assets and liabilities approximated their carrying values.

Notes

Notes

CORPORATE INFORMATION

Board of Directors
H. Ronald Sterne, Calgary, Alberta
Darryl K. Stackhouse, Calgary, Alberta
George A. Wilson*, Q.C., Toronto, Ontario
K. Garry Cook*, Calgary, Alberta
John D. Riddell*, Calgary, Alberta
Jeff Howe, Toronto, Ontario

* - members of the Audit Committee

Executives and Officers
H. Ronald Sterne, Chief Executive Officer and Chief Operating Officer
Darryl K. Stackhouse, President and Chief Financial Officer

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Chartered Accountants
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Stock Exchange
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Trading Symbol: SSX

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