EXFO Electro-Optical Engineering Inc.
Interim Consolidated Balance Sheet

(in thousands of US dollars)

	As at February 28, 2007	As at August 31, 2006
	(unaudited)	
Assets		
Current assets		
Cash	$ 9,108	$ 6,853
Short-term investments	105,521	104,437
Accounts receivable		
Trade, less allowance for doubtful accounts of $272 ($451 as at August 31, 2006)	21,793	20,891
Other	3,088	2,792
Income taxes and tax credits recoverable	2,138	2,201
Inventories (note 4)	23,428	24,623
Prepaid expenses	1,191	1,404
	166,267	163,201
Income taxes and tax credits recoverable	1,309	476
Property, plant and equipment	15,695	17,392
Intangible assets	9,459	10,948
Goodwill	25,675	27,142
	$ 218,405	$ 219,159
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 5)	$ 19,302	$ 17,337
Deferred revenue	2,089	1,772
Current portion of long-term debt	104	107
	21,495	19,216
Deferred revenue	3,294	2,632
Government grants	661	723
Long-term debt	282	354
	25,732	22,925
Contingency (note 6)		
Shareholders' Equity		
Share capital	149,578	148,921
Contributed surplus	4,101	3,776
Retained earnings (note 7)	6,217	–
Cumulative translation adjustment	32,777	43,537
	192,673	196,234
	$ 218,405	$ 219,159

The accompanying notes are an integral part of these consolidated financial statements.

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Earnings

(in thousands of US dollars, except share and per share data)

	Three months ended February 28, 2007	Six months ended February 28, 2007	Three months ended February 28, 2006	Six months ended February 28, 2006
Sales	$ 35,207	$ 70,754	$ 30,066	$ 57,110
Cost of sales [1,2]	14,970	30,199	13,440	25,504
Gross margin	20,237	40,555	16,626	31,606
Operating expenses				
Selling and administrative [1]	12,184	23,726	9,303	18,361
Net research and development [1] (note 8)	4,678	9,032	3,906	7,028
Amortization of property, plant and equipment	664	1,445	873	1,769
Amortization of intangible assets	630	1,512	1,136	2,357
Total operating expenses	18,156	35,715	15,218	29,515
Earnings from operations	2,081	4,840	1,408	2,091
Interest and other income	1,105	2,277	828	1,383
Foreign exchange gain (loss)	352	735	(213)	(531)
Earnings before income taxes	3,538	7,852	2,023	2,943
Income taxes (note 9)	854	1,635	657	1,222
Net earnings for the period	$ 2,684	$ 6,217	$ 1,366	$ 1,721
Basic net earnings per share	$ 0.04	$ 0.09	$ 0.02	$ 0.03
Diluted net earnings per share	$ 0.04	$ 0.09	$ 0.02	$ 0.02
Basic weighted average number of shares outstanding (000's)	68,839	68,807	68,591	68,581
Diluted weighted average number of shares outstanding (000's) (note 10)	69,546	69,465	69,152	69,105
(1) **Stock-based compensation costs included in:**				
Cost of sales	$ 27	$ 61	$ 30	$ 72
Selling and administrative	159	356	198	379
Net research and development	55	109	53	104
	$ 241	$ 526	$ 281	$ 555

(2) The cost of sales is exclusive of amortization, shown separately.

The accompanying notes are an integral part of these consolidated financial statements.

EXFO Electro-Optical Engineering Inc.

Interim Unaudited Consolidated Statements of Retained Earnings (Deficit) and Contributed Surplus

(in thousands of US dollars)

Retained earnings (Deficit)

	Six months ended February 28,	
	2007	**2006**
Balance – Beginning of period (note 7)	$ –	$ (381,846)
Add		
Net earnings for the period	6,217	1,721
Balance – End of period	$ 6,217	$ (380,125)

Contributed surplus

	Six months ended February 28,	
	2007	**2006**
Balance – Beginning of period	$ 3,776	$ 2,949
Add (deduct)		
Stock-based compensation costs	499	555
Reclassification of stock-based compensation costs to share capital upon exercise of stock awards	(174)	–
Balance – End of period	$ 4,101	$ 3,504

The accompanying notes are an integral part of these consolidated financial statements.

EXFO Electro-Optical Engineering Inc.
Interim Unaudited Consolidated Statements of Cash Flows

(in thousands of US dollars)

	Three months ended February 28, 2007	Six months ended February 28, 2007	Three months ended February 28, 2006	Six months ended February 28, 2006
Cash flows from operating activities				
Net earnings for the period	$ 2,684	$ 6,217	$ 1,366	$ 1,721
Add (deduct) items not affecting cash				
Discount on short-term investments	364	778	447	618
Stock-based compensation costs	241	526	281	555
Amortization	1,294	2,957	2,009	4,126
Deferred revenue	745	1,239	(193)	100
Government grants	–	(22)	–	–
	5,328	11,695	3,910	7,120
Change in non-cash operating items				
Accounts receivable	(210)	(3,245)	4,120	927
Income taxes and tax credits	(513)	(931)	(461)	(749)
Inventories	(510)	(129)	(1,775)	(2,908)
Prepaid expenses	133	135	88	(28)
Accounts payable and accrued liabilities	2,736	2,772	(446)	1,972
	6,964	10,297	5,436	6,334
Cash flows from investing activities				
Additions to short-term investments	(296,237)	(490,503)	(279,670)	(411,045)
Proceeds from disposal and maturity of short-term investments	291,413	482,916	288,500	420,899
Additions to property, plant and equipment and intangible assets	(835)	(1,646)	(933)	(1,568)
Net proceeds from disposal of property, plant and equipment	–	1,228	–	–
Business combination (note 3)	–	–	(17,497)	(17,497)
	(5,659)	(8,005)	(9,600)	(9,211)
Cash flows from financing activities				
Repayment of long-term debt	(24)	(51)	(42)	(74)
Exercise of stock options	362	483	137	156
	338	432	95	82
Effect of foreign exchange rate changes on cash	(276)	(469)	359	453
Change in cash	1,367	2,255	(3,710)	(2,342)
Cash – Beginning of period	7,741	6,853	8,487	7,119
Cash – End of period	$ 9,108	$ 9,108	$ 4,777	$ 4,777

The accompanying notes are an integral part of these consolidated financial statements.

EXFO Electro-Optical Engineering Inc.
Notes to Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

1. Interim financial information

The financial information as at February 28, 2007 and for the three- and six-month periods ended February 28, 2006 and 2007 is unaudited. In the opinion of management, all adjustments necessary to present fairly the results of these periods in accordance with generally accepted accounting principles (GAAP) in Canada have been included. The adjustments made were of a normal and recurring nature. Interim results may not necessarily be indicative of results anticipated for the entire year.

These interim consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada and use the same accounting policies and methods used in the preparation of the company's most recent annual consolidated financial statements. However, all disclosures required for annual financial statements have not been included in these financial statements. Consequently, these interim consolidated financial statements should be read in conjunction with the company's most recent annual consolidated financial statements.

2. New accounting standards and pronouncements

In January 2005, the Canadian Institute of Chartered Accountants (CICA) issued four new accounting standards in relation to financial instruments: Section 3855, "Financial Instruments – Recognition and Measurement"; Section 3865, "Hedges"; Section 1530, "Comprehensive Income"; and Section 3251, "Equity".

Section 3855 expands on Section 3860, "Financial Instruments – Disclosure and Presentation", by prescribing when a financial instrument is to be recognized on the balance sheet and at what amount. It also specifies how financial instrument gains and losses are to be presented in the financial statements.

Section 3865 provides an alternative to Section 3855 for entities that choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline 13, "Hedging Relationships", and on the hedging guidance in Section 1650, "Foreign Currency Translation", by specifying how hedge accounting is applied and what disclosures it requires.

Section 1530, "Comprehensive Income", introduces a new requirement to temporarily present certain gains and losses outside net income.

Consequently, Section 3250, "Surplus", has been revised as Section 3251, "Equity".

Sections 1530, 3251, 3855 and 3865 apply to fiscal years beginning on or after October 1, 2006. The company will adopt these new standards on September 1, 2007. Although the final adjustments will be based on the financial instruments that the company will be a party to on the adoption date, the company is currently assessing the effects of these new standards and impacts consistent with the adjustments described under note 20 item b) of the company's most recent annual consolidated financial statements are expected.

3. Business Combination

On January 26, 2006, the company acquired substantially all the assets of Consultronics Limited. Based in Toronto, Canada, and with operations in the United Kingdom and Hungary, Consultronics was a privately held company specializing in x-Digital Subscriber Line (xDSL), Internet Protocol TV and Voice-over-Internet Protocol (VoIP) test solutions for broadband access networks.

This acquisition was settled for a total cash consideration valued at $19,093,000, or $18,838,000 net of $255,000 of cash acquired. The total consideration included severance expenses of $660,000 for the termination of employees of the acquired business as well as other acquisition-related costs of $822,000.

This acquisition was accounted for using the purchase method and, consequently, the results of operations of the acquired business have been included in the consolidated statements of earnings of the company since January 26, 2006, being the date of acquisition.

The purchase price, including acquisition-related costs, was allocated based on the estimated fair value of acquired net assets at the date of acquisition as follows:

Assets acquired	
Current assets	$ 5,135
Property, plant and equipment	3,115
Core technology	8,709
Current liabilities assumed	(2,826)
Loans assumed	(402)
Net identifiable assets acquired	13,731
Goodwill	5,107
Purchase price, net of cash acquired	$ 18,838

Acquired core technology is amortized on a straight-line basis over its estimated useful life of five years.

This business, including acquired goodwill, reports to the Telecom Division. Acquired goodwill is deductible for tax purposes.

4. Inventories

	As at February 28, 2007	As at August 31, 2006
	(unaudited)	
Raw materials	$ 12,828	$ 14,353
Work in progress	1,226	1,043
Finished goods	9,374	9,227
	$ 23,428	$ 24,623

5. Accounts payable and accrued liabilities

	As at February 28, 2007	As at August 31, 2006
	(unaudited)	
Trade	$ 9,848	$ 7,487
Salaries and social benefits	6,174	5,991
Warranty	789	1,006
Commissions	1,014	835
Restructuring charges	174	691
Other	1,303	1,327
	$ 19,302	$ 17,337

Changes in the warranty provision are as follows:

	Six months ended February 28,	
	2007	**2006**
	(unaudited)	
Balance - Beginning of period	$ 1,006	$ 725
Provision	408	543
Settlements	(625)	(440)
Addition from business combination	–	31
Balance - End of period	$ 789	$ 859

Changes in the restructuring charges payable are as follows:

	Balance as at August 31, 2006	Payments	Balance as at February 28, 2007
		(unaudited)	**(unaudited)**
Fiscal 2006 plan			
Severance expenses	$ 631	$ (472)	$ 159
Fiscal 2003 plan			
Exited leased facilities	60	(45)	15
Total for all plans	$ 691	$ (517)	$ 174

6. Contingency

On November 27, 2001, a class action suit was filed in the United States District Court for the Southern District of New York against the company, four of the underwriters of its Initial Public Offering and some of its executive officers pursuant to the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder and Sections 11, 12 and 16 of the Securities Act of 1933. This class action alleges that the company's registration statement and prospectus filed with the Securities and Exchange Commission on June 29, 2000, contained material misrepresentations and/or omissions resulting from (i) the underwriters allegedly soliciting and receiving additional, excessive and undisclosed commissions from certain investors in exchange for which they allocated material portions of the shares issued in connection with the company's Initial Public Offering; and (ii) the underwriters allegedly entering into agreements with customers whereby shares issued in connection with the company's Initial Public Offering would be allocated to those customers in exchange for which customers agreed to purchase additional amounts of shares in the after-market at pre-determined prices.

On April 19, 2002, the plaintiffs filed an amended complaint containing master allegations against all of the underwriters in all of the 310 cases included in this class action and also filed an amended complaint containing allegations specific to four of the company's underwriters, the company and two of its executive officers. In addition to the allegations mentioned above, the amended complaint alleges that the underwriters (i) used their analysts to manipulate the stock market; and (ii) implemented schemes that allowed issuer insiders to sell their shares rapidly after an initial public offering and benefit from high market prices. As concerns the company and its two executive officers in particular, the amended complaint alleges that (i) the company's registration statement was materially false and misleading because it failed to disclose the additional commissions and compensation to be received by underwriters; (ii) the two named executive officers learned of or recklessly disregarded the alleged misconduct of the underwriters; (iii) the two named executive officers had motive and opportunity to engage in alleged wrongful conduct due to personal holdings of the company's stock and the fact that an alleged artificially inflated stock price could be used as currency for acquisitions; and (iv) the two named executive officers, by virtue of their positions with the company, controlled the company and the contents of the registration statement and had the ability to prevent its issuance or cause it to be corrected. The plaintiffs in this suit seek an unspecified amount for damages suffered.

In July 2002, the issuers filed a motion to dismiss the plaintiffs' amended complaint and a decision was rendered on February 19, 2003. Only one of the claims against the company was dismissed. On October 8, 2002, the claims against its officers were dismissed pursuant to the terms of Reservation of Rights and Tolling Agreements entered into with the plaintiffs.

In June 2003, a committee of the company's Board of Directors conditionally approved a proposed settlement between the issuer defendants, the individual defendants, and the plaintiffs. If approved, the settlement would provide, among other things, a release of the company and of the individual defendants for the conduct alleged in the action to be wrongful in the amended complaint. The company would agree to undertake other responsibilities under the settlement, including agreeing to assign away, not assert, or release certain potential claims the company may have against its underwriters.

On June 25, 2004, the Plaintiffs moved for preliminary approval of the settlement. The court granted the preliminary approval motion on February 15, 2005, subject to certain modifications. On August 31, 2005, the court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The court also appointed the Notice Administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members beginning on November 15, 2005. A settlement fairness hearing was held on April 24, 2006; however, no ruling has been issued yet by the court.

The plaintiffs have continued to litigate against the underwriter defendants. The district court has directed that the litigation proceed within a number of "focus cases" rather than in all of the 310 cases that have been consolidated. The company's case is not one of these focus cases. On October 13, 2004, the district court certified the focus cases as class actions. The underwriter defendants appealed that ruling, and on December 5, 2006, the Court of Appeals for the Second Circuit reversed the district court's class certification decision. Because the company's settlement with the plaintiffs involves the certification of the case as a class action as part of the approval process, the impact of the Court of Appeals' ruling on the company's settlement is unclear. On January 5, 2007, the plaintiffs filed a petition for rehearing en banc by the Second Circuit. That request is still pending.

If the court determines that the settlement is fair to the class members, and that the settlement classes can be certified, the settlement will be approved. The settlement provides that, if the plaintiffs do not obtain any recovery from the underwriter defendants, the members of the class action would receive an amount not expected to exceed $2,507,678. Any direct financial impact plus any legal fees are expected to be borne by the company's insurance carriers. However, there can be no assurance that this proposed settlement would be approved and implemented in its current form, or at all. Therefore, it is not possible to predict the final outcome of the case, nor to determine the amount of any possible losses. If the settlement process fails, the company will continue to defend its position in this litigation that the claims against it, and its officers, are without merit. Accordingly, no provision for this case has been made in the interim consolidated financial statements as at February 28, 2007.

7. Elimination of deficit

On August 31, 2006, upon the approval of the Board of Directors on that date, the company eliminated its deficit of $373,711,000 against its share capital.

8. Net research and development expenses

	Three months ended February 28, 2007	Six months ended February 28, 2007	Three months ended February 28, 2006	Six months ended February 28, 2006
	(unaudited)		(unaudited)	
Gross research and development expenses	$ 5,939	$ 11,448	$ 4,940	$ 8,946
Research and development tax credits and grants	(1,261)	(2,416)	(1,034)	(1,918)
	$ 4,678	$ 9,032	$ 3,906	$ 7,028

9. Income taxes

During the three- and six-month periods ended February 28, 2006 and 2007, the company recorded income taxes of $657,000, $1,222,000, $854,000 and $1,635,000, respectively. Most of these income taxes represent income taxes payable at the Canadian federal level, which are reduced by research and development tax credits that are recorded against gross research and development expenses in the statements of earnings.

The company records a full valuation allowance against its future income tax assets because it is more likely than not that these assets will not be recovered. This causes its income tax rate to be distorted in relation to its pre-tax accounting income.

10. Earnings per share

The following table summarizes the reconciliation of the basic weighted average number of shares outstanding and the diluted weighted average number of shares outstanding:

	Three months ended February 28, 2007	Six months ended February 28, 2007	Three months ended February 28, 2006	Six months ended February 28, 2006
	(unaudited)		(unaudited)	
Basic weighted average number of shares outstanding (000's)	68,839	68,807	68,591	68,581
Plus dilutive effect of:				
Stock options (000's)	468	451	466	446
Restricted share units (000's)	190	161	65	51
Deferred share units (000's)	49	46	30	27
Diluted weighted average number of shares outstanding (000's)	69,546	69,465	69,152	69,105
Stock awards excluded from the calculation of diluted weighted average number of shares outstanding because their exercise price was greater than the average market price of the common shares (000's)	1,213	1,299	1,829	1,816

11. Segment information

The company is organized under two reportable segments: the Telecom Division and the Life Sciences and Industrial Division. The Telecom Division offers integrated test solutions to network service providers, cable TV operators, system vendors and component manufacturers throughout the global telecommunications industry. The Life Sciences and Industrial Division mainly leverages developed and acquired core telecom technologies for high-precision assembly and research sectors.

EXFO Electro-Optical Engineering Inc.
Notes to Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The following tables set out information by segment:

	Three months ended February 28, 2007			Six months ended February 28, 2007		
	Telecom Division	Life Sciences and Industrial Division	Total	Telecom Division	Life Sciences and Industrial Division	Total
		(unaudited)			(unaudited)	
Sales	$ 29,297	$ 5,910	$ 35,207	$ 58,819	$ 11,935	$ 70,754
Earnings from operations	$ 1,078	$ 1,003	$ 2,081	$ 2,881	$ 1,959	$ 4,840
Unallocated items:						
Interest and other income			1,105			2,277
Foreign exchange gain			352			735
Earnings before income taxes			3,538			7,852
Income taxes			854			1,635
Net earnings for the period			$ 2,684			$ 6,217

	Three months ended February 28, 2006			Six months ended February 28, 2006		
	Telecom Division	Life Sciences and Industrial Division	Total	Telecom Division	Life Sciences and Industrial Division	Total
		(unaudited)			(unaudited)	
Sales	$ 25,254	$ 4,812	$ 30,066	$ 47,330	$ 9,780	$ 57,110
Earnings from operations	$ 1,220	$ 188	$ 1,408	$ 1,708	$ 383	$ 2,091
Unallocated items:						
Interest and other income			828			1,383
Foreign exchange loss			(213)			(531)
Earnings before income taxes			2,023			2,943
Income taxes			657			1,222
Net earnings for the period			$ 1,366			$ 1,721

Total assets by reportable segment are detailed as follows:

	As at February 28, 2007 (unaudited)	As at August 31, 2006
Total assets		
Telecom Division	$ 91,124	$ 93,853
Life Sciences and Industrial Division	9,205	11,339
Unallocated assets	118,076	113,967
	$ 218,405	$ 219,159

Unallocated assets are comprised of cash, short-term investments and income taxes and tax credits recoverable.

12. Stock-based compensation

On September 1, 2003, the company adopted the amendment made to the CICA Handbook Section 3870, "Stock-Based Compensation and Other Stock-Based Payments". Accordingly, employee stock awards granted on or after September 1, 2003, were accounted for using the fair value-based method. However, if the fair value-based method had been applied to employee stock awards granted prior to September 1, 2003, and outstanding as at February 28, 2006 and 2007, the pro forma net earnings per share would have been the same as the net earnings per share for all reporting periods.

13. Differences between Canadian and U.S. GAAP

These interim consolidated financial statements are prepared in accordance with Canadian GAAP and significant differences in measurement and disclosure from U.S. GAAP are set out in note 20 to the company's most recent annual consolidated financial statements. This note describes significant changes occurring since the most recent annual consolidated financial statements and provides a quantitative analysis of all significant differences. All disclosures required in annual financial statements under U.S. GAAP and Regulation S-X of the Securities and Exchange Commission in the United States have not been provided in these interim consolidated financial statements.

Comprehensive income (loss) under U.S. GAAP

Comprehensive income (loss) under U.S. GAAP is as follows:

	Three months ended February 28, 2007	Six months ended February 28, 2007	Three months ended February 28, 2006	Six months ended February 28, 2006
	(unaudited)		(unaudited)	
Net earnings for the period in accordance with Canadian GAAP and U.S. GAAP	$ 2,684	$ 6,217	$ 1,366	$ 1,721
Other comprehensive income (loss)				
Foreign currency translation adjustment	(4,472)	(10,304)	4,263	7,311
Unrealized gains (losses) on forward exchange contracts	(3,718)	(5,793)	1,699	2,796
Reclassification of realized gains on forward exchange contracts in net earnings	(108)	(844)	(582)	(1,017)
Comprehensive income (loss) under U.S. GAAP	$ (5,614)	$ (10,724)	$ 6,746	$ 10,811

Reconciliation of shareholders' equity to conform to U.S. GAAP

The following summary sets out the significant differences between the company's reported shareholders' equity under Canadian GAAP as compared to U.S. GAAP:

	As at February 28, 2007	As at August 31, 2006
	(unaudited)	
Shareholders' equity in accordance with Canadian GAAP	$ 192,673	$ 196,234
Forward exchange contracts	(1,186)	5,451
Goodwill	(11,465)	(11,908)
Shareholders' equity in accordance with U.S. GAAP	$ 180,022	$ 189,777

EXFO Electro-Optical Engineering Inc.
Notes to Unaudited Interim Consolidated Financial Statements

(tabular amounts in thousands of US dollars, except share and per share data and as otherwise noted)

The following table summarizes the shareholders' equity activity under U.S. GAAP since August 31, 2006:

	Share capital	Contributed surplus	Deficit	Deferred stock-based compensation costs	Other capital	Accumulated other comprehensive income	Shareholders' equity
	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Balance as at August 31, 2006	$ 598,421	$ 1,537	$ (458,944)	$ (1,371)	$ 5,504	$ 44,630	$ 189,777
Net earnings for the period	–	–	3,533	–	–	–	3,533
Stock-based compensation costs	–	–	–	(347)	593	–	246
Foreign currency translation adjustment	–	–	–	–	–	(5,832)	(5,832)
Unrealized losses on forward exchange contracts	–	–	–	–	–	(2,811)	(2,811)
Exercise of stock options	121	–	–	–	–	–	121
Reclassification of stock-based compensation costs upon exercise of stock awards	47	–	–	–	(47)	–	–
Balance as at November 30, 2006	$ 598,589	$ 1,537	$ (455,411)	$ (1,718)	$ 6,050	$ 35,987	$ 185,034
Net earnings for the period	–	–	2,684	–	–	–	2,684
Stock-based compensation costs	–	–	–	(510)	750	–	240
Foreign currency translation adjustment	–	–	–	–	–	(4,472)	(4,472)
Unrealized losses on forward exchange contracts	–	–	–	–	–	(3,826)	(3,826)
Exercise of stock options	362	–	–	–	–	–	362
Reclassification of stock-based compensation costs upon exercise of stock awards	127	–	–	–	(127)	–	–
Balance as at February 28, 2007	$ 599,078	$ 1,537	$ (452,727)	$ (2,228)	$ 6,673	$ 27,689	$ 180,022

Accumulated other comprehensive income is comprised of the following:

	As at February 28, 2007	As at August 31, 2006
	(unaudited)	
Foreign currency translation adjustment		
Current period	$ (10,304)	$ 12,322
Cumulative effect of prior periods	39,179	26,857
	28,875	39,179
Unrealized gains (losses) on forward exchange contracts		
Current period	(6,637)	2,514
Cumulative effect of prior periods	5,451	2,937
	(1,186)	5,451
	$ 27,689	$ 44,630

Research and development tax credits

Under Canadian GAAP, all research and development tax credits are recorded as a reduction of gross research and development expenses. Under U.S. GAAP, tax credits that are refundable against taxable income are recorded in the income taxes. These tax credits amounted to $659,000, $1,195,000, $776,000, and $1,547,000 for the three- and six- month periods ended February 28, 2006 and 2007, respectively. This difference has no impact on the net earnings and the net earnings per share for the reporting periods.

Statements of cash flows

For the three- and six-month periods ended February 28, 2006 and 2007, there were no significant differences between the statements of cash flows under Canadian GAAP as compared to U.S. GAAP, except for the subtotal before change in non-cash operating items, whose presentation is not permitted under U.S. GAAP.

New accounting standards and pronouncements

In May 2005, the Financial Accounting Standard Board (FASB) issued Statement of Financial Accounting Standard (SFAS) 154, “Accounting Changes and Error Corrections – a replacement of APB Opinion No. 20 and FASB Statement No. 3”. This statement replaces APB Opinion No. 20, “Accounting Changes”, and FASB Statement No. 3, “Reporting Accounting Changes in Interim Financial Statements”, and changes the requirements for the accounting and reporting of a change in accounting principle. This statement applies to all voluntary changes in accounting principle. It also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. In general, this statement requires a company to account for the adoption of a new accounting policy by applying the new principle to prior accounting periods as if that principle had always been adopted. The company adopted this new statement on September 1, 2006, and its adoption had no effect on its financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), “Accounting for Uncertainty in Income Taxes”, which clarifies the accounting for uncertainties in income taxes recognized in accordance with SFAS 109, “Accounting for Income Taxes”. The interpretation is effective for fiscal years beginning after December 15, 2006. The company will adopt this interpretation on September 1, 2007, and is currently assessing the impact its adoption will have on its financial statements.

On September 15, 2006, the FASB issued SFAS 157, "Fair Value Measurements", which establishes a framework for measuring fair value in GAAP, and is applicable to other accounting pronouncements, in which fair value is considered to be the relevant measurement attribute. SFAS 157 also expands disclosures about fair value measurement. This statement is effective for fiscal years beginning after November 15, 2007. The company will adopt this statement on September 1, 2008, and has not yet assessed the impact its adoption will have on its financial statements.

On February 15, 2007, the FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of FASB Statement No. 115", which permits entities to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of this statement apply only to entities that elect the fair value option. However, the amendment to SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", applies to all entities with available-for-sale and trading securities. This statement is effective for fiscal years beginning after November 15, 2007, but the company has not yet determined if it will adopt this statement, nor the impact it might have on its financial statements. Should the company decide to adopt SFAS 159, it will be adopted on September 1, 2008.