

Consolidated Financial Statements of

PACIFIC LOTTERY CORPORATION

Years ended December 31, 2009 and 2008

Management's Report

To the Shareholders of Pacific Lottery Corporation:

The accompanying consolidated financial statements of Pacific Lottery Corporation are the responsibility of management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada and within the framework of the Company's significant accounting policies as described in the notes to the financial statements. The consolidated financial statements reflect management's best estimates and judgments based on currently available information within reasonable limits of materiality.

Management is responsible for the integrity and fairness of the consolidated financial statements. Management designs and maintains appropriate systems of internal control to provide reasonable assurance that transactions are appropriately authorized, assets are safeguarded and financial records are properly maintained to provide reliable financial information for the preparation of the consolidated financial statements.

Meyers Norris Penny LLP, the independent auditors, are appointed by the shareholders of the Company to perform an examination of the corporate and accounting records so as to express an opinion on the consolidated financial statements. Their examination included such tests and other procedures, as they considered necessary, to provide reasonable assurance that the financial statements are presented fairly.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements in accordance with generally accepted accounting principles. The Board carries out this responsibility through its Audit Committee. The Audit Committee meets with management and the independent auditors to satisfy itself that management's responsibilities are properly discharged, to review the consolidated financial statements and recommend the consolidated financial statements be presented to the Board of Directors for approval.

The consolidated financial statements, including the notes to the consolidated financial statements, have been approved by the Board of Directors on the recommendation of the Audit Committee.

David W. Jones
Chief Executive Officer & Chief Financial Officer

Calgary, Canada
April 29, 2010

Auditors' Report

To the Shareholders of Pacific Lottery Corporation:

We have audited the consolidated balance sheets of Pacific Lottery Corporation as at December 31, 2009 and 2008 and the consolidated statements of operations and deficit and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

April 27, 2010
Calgary, Alberta

Meyer Norris Penny LLP

Chartered Accountants



PACIFIC LOTTERY CORPORATION

Consolidated Balance Sheets

As at December 31

	2009	2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 12,026	\$716,082
Interest and other receivables	152,137	92,990
	<u>164,163</u>	<u>750,017</u>
Deposits (note 5)	325,634	376,005
Capital assets (note 4)	973,489	1,245,721
	<u>\$ 1,463,286</u>	<u>\$ 2,430,798</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 421,880	\$ 260,429
Demand loan payable (note 8)	318,627	-
	<u>740,507</u>	<u>260,429</u>
Shareholders' equity:		
Share capital (note 6(b))	33,961,195	33,694,381
Shares issuable (note 6(b))	147,889	-
Warrants (note 6(b))	388,065	-
Contributed surplus (note 6(e))	3,626,424	3,626,424
Deficit	<u>(37,400,794)</u>	<u>(35,150,436)</u>
	722,779	2,170,369
	<u>\$ 1,463,286</u>	<u>\$ 2,430,798</u>

Going concern (note 1)

Commitments and contingencies (note 12)

See accompanying notes to consolidated financial statements.

Approved by the Board:

(Signed) Richard W. DeVries , Director

(Signed) Lisa Deutscher , Director



PACIFIC LOTTERY CORPORATION

Consolidated Statements of Operations and Deficit
For the years ended December 31,

	2009	2008
Revenue:		
Lottery	213,543	84,899
Expenses:		
General and administrative	\$ 2,130,385	\$ 3,239,994
Stock based compensation	-	278,188
Amortization	327,384	182,999
Bank service fees	8,988	6,166
Net loss from continuing operations	2,253,213	3,622,448
Other Income:		
Interest income	2,856	40,470
Net loss	2,250,358	3,581,978
Deficit, beginning of year	35,150,436	31,568,458
Deficit, end of year	\$ 37,400,794	\$ 35,150,436
Net loss per share – basic and diluted	\$ 0.03	\$ 0.04
Weighted average shares outstanding	89,717,555	83,871,856

See accompanying notes to consolidated financial statements.



PACIFIC LOTTERY CORPORATION

Consolidated Statements of Cash Flows
For the years ended December 31,

	2009	2008
Cash provided by (used in):		
Operations:		
Net loss	\$ (2,250,358)	\$ (3,581,978)
Items not involving cash:		
Stock based compensation	-	278,188
Amortization	327,384	182,999
Cash flow used in operations	(1,922,974)	(3,120,791)
Change in non-cash working capital balances (note 9)	471,302	1,019,899
	(1,451,672)	(2,100,892)
Financing:		
Issue of units, net of issue costs	802,768	-
	802,768	-
Investing:		
Acquisition of capital assets	(55,152)	(1,000,984)
	(55,152)	(1,000,984)
Decrease in cash and cash equivalents	(704,056)	(3,101,876)
Cash and cash equivalents, beginning of year	716,082	3,817,958
Cash and cash equivalents, end of year	\$ 12,026	\$ 716,082

Cash and cash equivalents are comprised of the following:

Short-term investments	\$ -	\$ 365,167
Cash balances with banks	12,026	350,915
	\$ 12,026	\$ 716,082

Supplemental cash flow information (note 9)

See accompanying notes to consolidated financial statements.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

1. Nature of business and going concern:

Pacific Lottery Corporation (the "Company") is incorporated under the laws of the Province of Alberta. The Company's principal business activities include research, development, manufacturing, operating and managing modern online lottery systems. During 2008, the Company ceased to be in the development stage upon the launch of the lottery in October, 2008 utilizing the proprietary technology developed by the Company.

On July 11, 2005 the Company commenced production of proprietary lottery terminals (the "Terminals"), pursuant to a lottery terminal Manufacturing Agreement between the Company and the Hanoi Electronics Corporation ("HANEL") (see Note 12 c)).

Pursuant to an agreement dated September 12, 2007 between the Company and CLC., a Government agency of the Socialist Republic of Vietnam, the Company agreed to provide system software, central equipment and lottery terminals, installation and development plans, training, marketing and maintenance programs in order to provide the government of the Socialist Republic of Vietnam with the technology and a lottery system capable of establishing a National on-line lottery program throughout Vietnam (See Note 12 b)).

On October 2, 2008, the Company announced the commercial launch in Vietnam of a new Government owned and operated lottery program exclusively using the Company's next generation on-line lottery technology. These launch activities included the sale of several newly designed on-line lottery games in association with marketing programs including nationally televised TV commercials. Lottery sale transactions occurred throughout the newly installed State authorised retailer network using the Company's proprietary National On-line Lottery Central System ("the Lottery System").



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

1. Nature of business and going concern (continued):

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles on a going concern basis which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

There is significant risk surrounding the Company's ability to continue as a going concern. The Company incurred a loss of \$2,250,358 (2008 – \$3,581,978) for the year ended December 31, 2009 and has a deficit of \$37,400,794 (2008 – \$35,150,436) as at December 31, 2009. The losses have been funded primarily by the issuance of equity. The continuation of the Company's development activities and the commercialization of its modern online lottery system is dependent upon the Company's ability to successfully finance its cash requirements through equity financings until operational cash contribution becomes sufficient for the Company to be self sustaining. However, no assurance can be given at this time as to whether the Company will achieve any of these objectives.

These consolidated financial statements do not include any adjustments to the amounts and classifications of assets and liabilities which might be necessary should the Company be unable to continue in business. These adjustments may be material.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

2. Significant accounting policies:

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles using the following significant accounting policies:

(a) Use of estimates:

The preparation of financial statements in conformity with Canadian Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. The fair value of stock options and warrants is determined using the Black-Scholes Option Pricing Model which requires the use of management estimates. Amortization is based on the estimated useful lives of capital assets. Actual results could differ from these estimates and such differences could be material.

These estimates and assumptions are reviewed periodically and, as adjustments become necessary they are reported in earnings in the periods in which they become known.

(b) Principles of consolidation:

The financial statements include the accounts of the Company and its wholly-owned subsidiaries: Applied Gaming Solutions International Inc. ("AGSI") and Emerging Market Solutions International Inc. ("EMSI"). All intercompany transactions and balances have been eliminated upon consolidation.

(c) Research and development costs:

Research costs are expensed in the year incurred. Development costs are expensed in the year incurred unless the Company believes a development project meets Canadian Generally Accepted Accounting Principles for deferral and amortization.

(d) Capital assets and amortization:

Capital assets are stated at cost less accumulated amortization. Amortization is provided using the declining balance basis at the following annual rates which are designed to apportion the costs of the assets over their estimated useful lives:

Assets	Rate
Lottery equipment	30%
Leasehold improvements	5 to 10 years
Computer equipment	30%
Computer software	30%
Office furniture and equipment	20%



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

2. Significant accounting policies (continued):

(e) Impairment:

The Company evaluates the carrying value of its capital assets for impairment when circumstances indicate that the carrying value may not be recoverable. The carrying value of an asset is considered impaired when the anticipated undiscounted cash flow from its use and disposal is less than its carrying value. In that event, a write-down is recognized based on the amount by which the carrying value exceeds the fair market value. Fair market value is determined using the anticipated cash flows discounted at a rate commensurate with the risk involved. Any impairment is included in earnings for the year.

(f) Cash and cash equivalents

Cash and cash equivalents include highly liquid investments with original maturities of 90 days or less when purchased.

(g) Income taxes:

The asset and liability method is used for determining income taxes. Under this method of tax allocation, future income tax assets and liabilities are determined based on differences between the financial statement carrying values and their respective income tax basis. Future income tax assets and liabilities are measured using the substantially enacted tax rates expected to be in effect when the temporary differences are likely to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included in operations in the period in which the change is enacted or substantially enacted. The amount of future income tax assets recognized is limited to the amount that is more likely than not to be realized.

No recognition of future income assets has been reflected in these financial statements as the Company has yet to achieve profitable operations.

(h) Stock-based compensation:

The Company recognizes the value of equity instruments awarded to employees and non-employees in the financial statements as if the fair value method had been used at the date of grant. The Company calculates the value of stock options issued using the Black-Scholes option pricing model with consideration of factors specific to the Company. For options granted to employees and directors, the value is recognized at the date of grant and is deferred and expensed over the period the options vest, with a corresponding increase to contributed surplus. For options granted to consultants, an expense is recognized as services are provided.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

2. Significant accounting policies (continued):

(i) Earnings and loss per share:

Basic earnings or loss per share is calculated by dividing net income or loss by the weighted average number of shares outstanding during the year. Diluted earnings or loss per share is calculated by dividing net earnings or loss by the weighted average number of common shares outstanding during the year after giving effect to dilutive potential common shares. The dilutive effects of stock options and warrants are determined using the treasury stock method. The dilutive effects of convertible securities are determined using the if-converted method.

(j) Deferred financing:

Transaction costs attributable to financial instruments classified as other than held-for-trading are included in the recognized amount of the related financial instrument and recognized over the life of the resulting financial instrument.

(k) Foreign currency:

Monetary items denominated in foreign currency are converted to Canadian dollars at exchange rates in effect at the balance sheet date and non-monetary items are converted at rates of exchange in effect at the time of the transactions. Foreign exchange gains and losses are included in income.

The accounts of its foreign subsidiaries are maintained in US dollars. The Company has determined that its subsidiaries, Applied Gaming Solutions International Inc. and Emerging Market Solutions International Inc are integrated foreign operations and as a result, the Company has used the temporal method to translate the financial statements into Canadian dollars. Accordingly, monetary assets and liabilities are translated using the exchange rates in effect at the consolidated balance sheet date and non monetary assets and liabilities at the historical exchange rate prevailing during the year. Foreign currency gains and losses are reported on the income statement.

(l) Revenue recognition:

Revenue consists of the Company's share of wagers placed and is recognized upon receipt of cash proceeds.

(m) Comprehensive income:

Comprehensive income consists of net earnings on the consolidated statements of earnings and other comprehensive income (loss) ("OCI"). OCI represents changes in shareholders' equity in a period arising from the portion of the change in the fair values of the Company's derivatives designated as cash flow hedges that are determined to be effective, gains and losses on derivatives designated as cash flow hedges that are transferred to net earnings in the current period, and the unrealized effect of foreign currency translation of foreign operations. The Company does not have any items giving rise to OCI, nor is there any accumulated balance of OCI.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

2. Significant accounting policies (continued):

(n) Financial instruments:

Financial instruments are initially recognized at fair value. The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arm's-length transaction between knowledgeable, willing parties who are under no compulsion to act. Fair values of financial instruments are based on independent prices quoted in active markets. In the absence of an active market, fair values are determined based on valuation models such as discounted cash flows, which require the use of assumptions concerning the amount and timing of estimated future cash flows and discount rates. Subsequent measurement depends on management's classification of the financial assets as held-for-trading, available-for-sale, held-to-maturity or loans and receivables, and financial liabilities as held-for-trading or other liabilities. The classification of financial instruments depends on the nature of and the purpose of the financial instruments, management's choice and in some circumstances, management's intentions.

Held-for-Trading

Financial instruments classified as held-for-trading are measured at fair value with the realized and unrealized changes in fair value recognized each reporting period through interest and financing costs, net on the consolidated statement of operations. The Company has designated cash and cash equivalents as held-for-trading.

Available-for-Sale

Financial assets classified as available-for-sale are measured at fair value with the unrealized changes in fair value recorded each reporting period in OCI. Investments in equity instruments classified as available-for-sale that do not have a quoted price in an active market are recorded at cost. Each reporting period, available-for-sale assets are written down to fair value through interest and financing costs, net on the consolidated statement of operations to reflect impairments that are considered to be other than temporary. The Corporation does not have any financial instruments classified as available for sale.

Held-to-Maturity, Loans and Receivables and Other Liabilities

Financial instruments classified as held-to-maturity, loans and receivables and other liabilities are measured at amortized cost using the effective interest method. The Company has designated interest and other receivables as "loans and receivables" and accounts payable and accrued liabilities and demand loan payable as "other liabilities".



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
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3. Changes in Accounting Policies (continued):

On January 1, 2009, the Company adopted prospectively the following new accounting standards of the Canadian Institute of Chartered Accountants (“CICA”):

(a) Goodwill and Intangible Assets:

In February 2008, the CICA issued Section 3064, “Goodwill and Intangible Assets”, which replaces Section 3062, “Goodwill and Other Intangible Assets”, and Section 3450, “Research Development Costs”. This section provides more specific guidance on the recognition of internally developed intangible assets and requires that research and development expenditures be evaluated against the same criteria as expenditures for intangible assets. The section increases harmonization of Canadian standards with international financial reporting standards and applies to annual interim financial statements relating to fiscal years beginning on or after October 1, 2008. The adoption of this section did not have any impact on the Company’s consolidated financial statements.

Recent Accounting Pronouncements

(a) International Financial Reporting Standards (“IFRS”)

In February 2008, the Accounting Standards Board (“AcSB”) confirmed that the use of IFRS will be required in 2011 for publicly accountable enterprises in Canada. In April 2008, the AcSB issued an IFRS Omnibus Exposure Draft proposing that publicly accountable enterprises be required to apply IFRS, in full and without modification, on January 1, 2011. In June 2008, the Canadian Securities Administrators (“CSA”) issued Staff Notice 52-321, Early Adoption of IFRS which indicated that the CSA would be prepared to grant an exemption to allow Canadian financial statement issuers to adopt IFRS early on a case-by-case basis, provided that they could demonstrate that they met certain conditions. The adoption of IFRS will require the restatement of amounts reported by the Company for its previous year ended, and of the opening balance sheet as at the date of adoption. The Company intends to adopt IFRS for the accounting period commencing January 1, 2011 and is continuing to assess the financial reporting impacts of the adoption of IFRS. The Company expects financial reporting impacts to deferred tax, intangible assets and share based payments. However, the impact on future financial position and results of operations is not reasonably determinable or estimable at this time. The Company does anticipate a significant increase in disclosure resulting from the adoption of IFRS and is continuing to assess the level of disclosure required. The IFRS conversion project consists of three phases: Scoping and Diagnostics, Analysis and Development, and Implementation and Review.

Phase One: Scoping and Diagnostics, which involved project planning, and staffing and identification of differences between current Canadian GAAP and IFRS, has been completed.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

Recent Accounting Pronouncements (continued):

Phase Two: Analysis and Development, involves detailed diagnostics and evaluation of the financial impacts of various options and alternative methodologies provided for under IFRS; identification and design of operational and financial business processes; initial staff and audit committee training; analysis of IFRS 1 optional exemptions and mandatory exceptions to the general requirement for full retrospective application upon transition to IFRS; summarization of 2011 IFRS disclosure requirements; and development of required solutions to address identified issues. Phase Two will commence in fiscal 2010.

Phase Three: Implementation and Review will involve the execution of changes to information systems and business processes; completion of formal authorization processes to approve recommended accounting policy changes; and further training programs across the Company's finance and other affected areas, as necessary. It will culminate in the collection of financial information necessary to compile IFRS-compliant financial statements and reconciliations; embedding of IFRS in business processes; and audit committee approval of IFRS-compliant financial statements.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

4. Capital assets:

December 31, 2009	Cost	Accumulated Depreciation	Net Book Value
Lottery equipment	\$ 1,203,761	\$ 459,634	\$ 744,127
Computer equipment	84,141	52,431	31,710
Computer software	496,058	402,524	93,534
Intangible assets	1,275	312	963
Office furniture and equipment	97,237	55,317	41,920
Leasehold Improvements	79,088	17,853	61,235
	\$ 1,961,560	\$ 988,071	\$ 973,489

December 31, 2008	Cost	Accumulated Depreciation	Net Book Value
Lottery equipment ¹	\$ 1,151,152	\$ 201,064	\$ 950,088
Computer equipment	76,127	42,105	34,022
Computer software	495,558	369,357	126,201
Intangible assets	-	-	-
Office furniture and equipment	97,817	46,332	51,485
Leasehold Improvements	88,178	4,253	83,925
	\$ 1,908,832	\$ 663,111	\$ 1,245,721

¹ Lottery equipment cost and accumulated depreciation were equally reduced by \$2,576,687 in 2008, which resulted in no change to net book value. The adjustment represented equipment purchased for the previous Hanoi lottery program which had been fully amortized by 2003 and is no longer in operation.

5. Deposits:

	2009	2008
Rent (multi-year lease)	\$ 5,129	\$ 59,878
HANEL (terminal manufacturing) (see note 12)	317,858	316,127
Legal deposit	2,647	-
	\$ 325,634	\$ 376,005



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

6. Share capital:

(a) Authorized:

Unlimited number of common shares

Unlimited number of preferred shares issuable in series with terms and conditions to be determined by the Board of Directors

(b) Issued:

	Number of Shares	Amount
Common shares:		
Balance, December 31, 2007	83,871,856	\$33,694,381
Nil activity	-	-
Balance, December 31, 2008	83,871,856	\$33,694,381
Issued per April 7, 2009 private placement (i)	7,910,910	870,200
Warrants value included in private placement (i)		(357,337)
Shares issuable, paid and contracted in 2009, not yet issued		(78,617)
Issue costs		(167,432)
Issued December 23, 2009 private placement (ii)	1,250,000	100,000
Warrants value included in private placement (ii)		(30,728)
Shares issuable, paid and contracted in 2009, not yet issued		(69,272)
Balance, December 31, 2009	93,032,766	\$33,961,195

- i) On April 7, 2009 the Corporation announce it had arranged a non brokered financing of \$1.98 million. Existing shareholder and Board member Mr. Richard W. DeVries agreed to subscribe to a Private Placement (through his company Oceanic Greystone Securities Inc.) that included a placement of 8.6 million units at \$0.11 each, consisting of one (1) common share and one (1) common purchase warrant exercisable at \$0.12 until April 3, 2014 for total expected gross proceeds of \$ 1.98 million. Of this Private Placement, 7,910,910 units have been issued to date for gross proceeds of \$870,200.
- ii) On December 23, 2009 the Corporation issued 1,250,000 units at \$0.08 each, consisting of one (1) common share and one (1) common purchase warrant exercisable at \$0.10 until December 23, 2014 through a non brokered financing for gross proceeds of \$100,000. This Private Placement was unannounced and utilized the prevailing share price for that day.



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

6. Share capital (continued):

(c) Stock options:

Under the Company's stock option plan, the Company may grant options to employees, consultants, officers and directors totaling up to 10% of the issued and outstanding common shares. In addition, the aggregate number of shares so reserved for issuance, in any twelve month period, to any one person shall not exceed 5% of the issued and outstanding common shares, unless that person is a consultant or provider of investor relations and as such issuance shall not exceed 2%.

The options issued in 2008 were valued at \$278,188 using the Black-Scholes pricing model assuming a life of 5 years, 50% volatility and an average risk free rate of 3.9%. As these options became fully exercisable in the year, the full value of \$278,188 was expensed as stock based compensation. No options were issued in 2009.

The following table summarizes the status of the stock option plan as of December 31, 2009 and December 31, 2008 and the changes during the years then ended:

	2009		2008	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of year	8,390,000	\$ 0.34	5,580,000	\$ 0.30
Granted	-	-	1,350,000	0.40
Granted	-	-	2,810,000	0.40
Cancelled	-	-	(1,350,000)	(0.32)
Outstanding, end of year	8,390,000	\$ 0.34	8,390,000	\$ 0.34
Exercisable	2,810,000	\$ 0.40	2,810,000	\$ 0.40

Of the options outstanding, 2,810,000 are currently exercisable at \$0.40, with the balance of 5,580,000 exercisable upon the Company earning its first revenues from the Ho Chi Minh City region, an event which did not occur during the year ended December 31, 2009.

The weighted average remaining term of the options at December 31, 2009 is 2.17 years (2008 – 3.17).



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements,
Years ended December 31, 2009 and 2008

6. Share capital (continued):

(d) Warrants:

The following table summarizes warrants issued by the Company as of December 31, 2009 and December 31, 2008 and the changes during the years then ended:

	2009		2008	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of year	-	\$ -	3,760,000	\$ 1.50
Granted	7,910,909	0.12	-	-
Granted	1,250,000	0.10	-	-
Exercised	-	-	-	-
Cancelled	-	-	-	-
Expired	-	-	(3,760,000)	(1.50)
Outstanding and exercisable, end of year	9,160,909	\$ 0.12	-	\$ -

The weighted average remaining term of the warrants at December 31, 2009 is 4.41 years (2008 – Nil).

(e) Contributed surplus:

The following table summarizes changes in contributed surplus.

	2009	2008
Beginning of year	\$ 3,626,424	\$ 2,638,899
Warrants expired	-	709,337
Stock based compensation (<i>note 6(c)</i>)	-	278,188
End of year	\$ 3,626,424	\$ 3,626,424



PACIFIC LOTTERY CORPORATION

Notes to Consolidated Financial Statements
Years ended December 31, 2009 and 2008

7. Income taxes:

The provision for income taxes in the statement of operations differs from that which would be expected by applying the applicable statutory tax rates. Differences for the years ended December 31, are as follows:

	2009	2008
Loss before income taxes	(2,250,358)	(3,581,978)
Statutory income tax rate	29.50%	32.62%
Expected income tax recovery	(652,604)	(1,168,441)
Effect on income taxes of:		
Tax rate difference between Canadian and foreign jurisdictions	179,807	92,267
Stock based compensation	-	83,790
Change in enacted rates	338,039	471,773
Non-deductible items	7,066	5,916
Non-capital losses expired	1,086,814	1,313,197
Change in valuation allowance	(917,895)	(631,497)
Share issue costs	(41,228)	-
Opening pool balances	-	(167,005)
Income tax provision	-	-

The components of the Company's future income tax asset are as follows:

	2009	2008
Future income tax assets		
Property and equipment	348,636	286,674
Cumulative eligible capital	100,821	108,080
Non-capital losses (Canadian)	2,254,518	3,203,618
Non-capital losses (Foreign)	59,552	42,590
Capital losses	272,500	292,120
Scientific research and experimental development	118,306	126,823
Share issue costs	81,783	94,105
Net future tax assets	3,236,115	4,154,010
Valuation allowance	(3,236,115)	(4,154,010)
Net future income tax asset	-	-

The Company has Canadian non-capital losses that may be deducted against taxable income in future years that will expire as follows:

<u>Amount</u>	<u>Expiration</u>
1,943,070	2010
1,346,127	2014
1,507,582	2015
1,747,683	2026
2,159,258	2027
3,250,078	2028
2,090,047	2029



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Notes to Consolidated Financial Statements,
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7. Income taxes (continued):

The Company also has foreign non-capital losses that may be deducted against taxable income in future years of approximately \$1,700,000.

8. Related party transactions:

In anticipation of future financings to repay short term loans, Aftergood Incorporated, a company controlled by a consultant of the Corporation, agreed to loan the Corporation \$318,627 to sustain operations and advance its business plan in the short term. This loan is repayable on demand, carries an annual interest rate of 8% and is unsecured.

During the year ended December 31, 2009, the Corporation incurred recoverable administrative expenses in the amount of \$123,736 (2008 – nil) on behalf of a company that has the same CFO and Vice-President as the Corporation. The administrative costs incurred were in the normal course of operations and were based on the exchange value of the goods and services provided. Of the costs incurred, \$123,736 remained in interest and other receivables at year end.

9. Supplemental disclosure of cash flow information:

(a) Change in non-cash working capital balances:

	2009	2008
Interest and other receivables	\$ (59,147)	\$ 126,601
Deposits	50,371	844,731
Accounts payable and accrued liabilities	161,451	48,567
Demand loan payable	318,627	-
	\$ 471,302	\$ 1,019,899

(b) Other cash transactions:

	2009	2008
Interest paid	\$ 8,988	\$ 6,166



PACIFIC LOTTERY CORPORATION

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10. Capital Disclosures:

The Company's capital structure comprises:

- Cash and cash equivalents;
- Shareholders' equity

The Company's objectives are to maintain a flexible capital structure that optimizes the cost of capital at acceptable risk levels and to manage capital in a manner that balances the interests of equity holders. The Company manages its capital structure in light of changes in economic conditions and the risk characteristics of the Company's operations. The Company's major capital allocation decisions include a comparison of whether the expected financial returns from those investments exceed its estimated weighted average cost of capital. The Company currently plans to use its cash and cash equivalents and cash flows from operations to finance expansion of its gaming operations in Vietnam.

11. Financial instruments:

(a) Fair values:

The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and current portion of long-term debt, the fair values of which approximate their carrying values due to the short term to maturity. The fair value of these financial instruments are based on Level one inputs.

The fair value of the Company's long-term debt approximates its carrying value because interest charges under the terms of the debt are based upon current bank prime rates. The fair value of this financial instrument is based on the Level two inputs.

The fair value hierarchy established by CICA Handbook Section 3862 – Financial Instruments – Disclosures established three levels to classify the inputs to valuation techniques used to measure fair value. Level one inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level two inputs are quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability (for example, interest rate and yield curves observable at commonly quoted intervals, forward pricing curves used to value currency and commodity contracts and volatility measurements used to value option contracts), or inputs that are derived principally from or corroborated by observable market data or other means. Level three inputs are unobservable (supported by little or no market activity). The fair value hierarchy gives the highest priority to Level one inputs and lowest priority to Level three inputs.



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11. Financial instruments (continued):

(b) Credit risk:

Credit risk is the risk of loss associated with a counterparty's inability to fulfill its payment obligation. The Company's credit risk is primarily attributable to accounts receivable. Management believes that the credit risk with respect to accounts receivable is acceptably low as a small portion pertains to revenue accrued, which is paid weekly, amounts advanced for marketing under close control and the majority advanced to a strategic partner for which the largest portion has been recovered subsequent to December 31, 2009.

(c) Liquidity risk:

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. As at December 31, 2009 the Company had a cash and cash equivalents balance of \$12,026. To the extent that the Company does not believe it has sufficient liquidity to meet current obligations, consideration will be given to obtaining additional funds through equity financing, assuming these could be obtained.

The Company does not have sufficient operating cash flows to fund its projects in Vietnam. There is no assurance that additional funding will be available to allow the Company to fulfill its obligations on existing or future exploration projects.

(d) Market Risk:

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates, and equity prices will affect the Company's net income or loss or the value of its financial instruments.

(e) Interest rate risk

The Company's cash balances are invested in short-term deposit certificates or bankers' acceptances issued by Canadian Chartered banks. The Company has no interest bearing debt. The Company believes its interest rate risk is not significant.

(f) Foreign exchange risk:

The Company enters into transactions denominated in U.S. dollars and Euros for which the related revenues, expenses, accounts receivable and accounts payable balances are subject to exchange rate fluctuations. A change of 1% in the exchange rate would have resulted in a change of approximately \$11,675 in the net loss of the Company.



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11. Financial instruments (continued):

As at December 31, 2009, the following items are denominated in U.S. dollars converted into their Canadian dollar equivalent:

	2009	2008
Cash	\$ (507)	\$ 341,129
Interest and other receivable	\$ 26,097	\$ 423,491
Accounts payable and accrued liabilities	\$ 22,550	\$ -

As at December 31, 2009, the following items are denominated in Euros converted into their Canadian dollar equivalent:

	2009	2008
Accounts payable and accrued liabilities	\$ 47,164	\$ 27,823

Foreign exchange risk is the risk that variations in exchange rates between the Canadian dollar and foreign currencies will affect the Company's operating and financial results. The Company earns a significant portion of its operating revenue in U.S. dollars and does not use derivative instruments to reduce its exposure to this foreign exchange risk.



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12. Commitments and contingencies:

- (a) Pursuant to an agreement (“Hanoi Agreement”) dated May 27, 1998 and subsequent amendments between the Company and the Ha Noi Capital Construction Lottery Company Ltd. (“CLC”), a Government agency of the Socialist Republic of Vietnam, the Company agreed to provide system software, central equipment and lottery terminals, installation and development plans, training, marketing and maintenance programs in order to provide the government of the Socialist Republic of Vietnam with technology and a lottery system capable of establishing an on-line lottery program in Hanoi.

The term of the agreement is seven years, commencing August 9, 1999, the date the first on-line sales began. The Company is paid, weekly, 4% of the gross sales of the on-line lottery system during each of the first five years of the agreement and one percent of the gross sales in the sixth and seventh year. All amounts payable to the Company are paid in U.S. dollars to a financial institution outside of the Socialist Republic of Vietnam. During 2006 and 2007, the Company agreed to extend the Hanoi Agreement an additional year. Expiration of this agreement will occur on the date of the first on-line sale in accordance with the agreement outlined in (b).

- (b) Pursuant to an agreement dated September 12, 2007 between the Company and CLC., the Company agreed to provide system software, central equipment and lottery terminals, installation and development plans, training, marketing and maintenance programs in order to provide the government of the Socialist Republic of Vietnam with the technology and a lottery system capable of establishing a National on-line lottery program throughout Vietnam.

The term of the agreement is ten years, commencing on the date that on-line sales begin. The Company is to be paid, weekly, 8% of the gross sales of the on-line lottery system of which 3% of gross sales is to be used by the Company for marketing expenditures. All amounts payable directly to the Company are paid in U.S. dollars to a financial institution outside of the Socialist Republic of Vietnam.

In conjunction with the Agreement, the Company contracted consultants to facilitate implementation of the Company’s responsibilities, for which they are paid 0.5% of gross sales.

- (c) The Company executed an agreement on April 19, 2005 with HANEL (“Manufacturing Agreement”) for the manufacture of the Terminals in the amount of \$1,867,380 USD. The Manufacturing Agreement allows for pricing at various volume levels, with manufacturing commencing with the payment of the required deposit in accordance with terms of the agreement. A bank guarantee reimburses the Company for the entire deposit amount (amounting to 50% of the total contract price or \$978,600 USD), in the event there is any default by HANEL in the manufacture of the Terminals. The agreement requires the Company to make a further 40% payment of the cost of the Terminals at time of delivery and the remaining 10% to be paid one month after delivery and installation of the Terminals. The Company continues to work with the Vietnamese government on the timing of introducing the new lottery system and the specifications of the Terminals.



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13. Segmented information:

In the opinion of management, the Company, at this time, has only one business segment. This segment is the business of operating and managing modern online lottery systems and has the following geographical segments:

Revenue

	2009	2008
Canada	\$ -	\$ 35,532
Vietnam	213,543	49,367
	\$ 213,543	\$ 84,899

Deposits and capital assets

	2009	2008
Canada	\$ 164,448	\$ 223,276
Vietnam	1,134,675	1,398,450
	\$ 1,299,123	\$ 1,621,726

14. Comparative figures:

Certain comparative figures have been reclassified in order to conform to the current period's financial statement presentation.

