



Constellation Software Inc.

# **INTERIM FINANCIAL REPORT**

Third Quarter Fiscal Year 2008

For the three and nine month periods ended  
September 30, 2008  
(UNAUDITED)

# CONSTELLATION SOFTWARE INC.

## Q308

### TO OUR SHAREHOLDERS

In a diversified company like ours, you can usually point to some businesses that are stars and some that are not. I'm currently in the happy position of being able to commend the performance of all of our Operating Groups to shareholders. In Q3, some of our businesses recorded double digit organic growth and many of them produced record profits. Others continue to be profitable despite rending and perhaps long term change in their sectors. In aggregate, Constellation generated 7% organic Net Revenue growth in Q3, managed a further 28% acquired Net Revenue growth, produced record Adjusted EBITDA (\$15.7 million) and Adjusted Net Income (\$12.3 million), and invested more in acquisitions (\$44 million) than in any previous quarter. You can't judge the quality of this quarter's acquisitions by this quarter's profit, but after 85 acquisitions over a 13 year period, we seem to have developed a knack for acquiring fundamentally sound businesses at fair prices. While it's comforting to revel in the Q3 results, I suspect that our Organic Growth will flag in 2009. Forecasters are calling for GNP contraction in North America. Constellation can't hope to be immune, but we anticipate faring far better than most software companies due to our high and growing (34% growth in Q3) Net Maintenance Revenue.

Another metric worth bringing to your attention in the table below is Tangible Net Assets / Net Revenue. Our Operating Groups did an exceptional job of managing their working capital in an economic environment where many customers are trying to hang on to their cash a little bit longer. This improvement is overshadowed by the large amount of negative Tangible Net Assets that we acquired late in the quarter as a result of the Maximus acquisition. I anticipate that we will not be able to maintain the -84% Tangible Net Assets / Net Revenue ratio in the future, but we should see continued good performance on this metric. A glossary for our quarterly Performance Metrics is appended to this letter. I encourage you to refer back to previous letters for more extensive discussions of each of the metrics.

|                                       | Q3 2006 | Q4 2006 | Q1 2007 | Q2 2007 | Q3 2007 | Q4 2007 | Q1 2008 | Q2 2008 | Q3 2008     |
|---------------------------------------|---------|---------|---------|---------|---------|---------|---------|---------|-------------|
| (\$ millions, except percentages)     |         |         |         |         |         |         |         |         |             |
| Revenue                               | 54      | 54      | 56      | 60      | 61      | 66      | 74      | 78      | 81          |
| Net Income / (Loss)                   | 2.3     | 3.8     | 2.6     | 3.5     | 3.3     | 1.6     | 4.3     | 3.4     | 3.3         |
| Net Revenue                           | 48      | 49      | 51      | 55      | 55      | 60      | 67      | 71      | 75          |
| Net Maintenance Revenue               | 28      | 30      | 31      | 33      | 35      | 38      | 42      | 44      | 46          |
| Adjusted Net Income <sup>(1)</sup>    | 7.5     | 9.0     | 6.9     | 8.4     | 8.5     | 9.4     | 11.1    | 12.0    | <b>12.3</b> |
| Average Invested Capital              | 125     | 135     | 143     | 149     | 158     | 167     | 176     | 188     | 201         |
| Net Revenue Growth (Y/Y)              | 24%     | 22%     | 10%     | 16%     | 14%     | 24%     | 31%     | 29%     | <b>35%</b>  |
| Organic Net Revenue Growth (Y/Y)      | 5%      | 3%      | -1%     | 0%      | 2%      | 3%      | 6%      | 5%      | <b>7%</b>   |
| Net Maintenance Growth (Y/Y)          | 30%     | 29%     | 20%     | 24%     | 23%     | 28%     | 34%     | 32%     | <b>34%</b>  |
| Adjusted Net Income Growth (Y/Y)      | 49%     | 115%    | 43%     | 91%     | 13%     | 5%      | 62%     | 43%     | 47%         |
| Average Invested Capital Growth (Y/Y) | 20%     | 24%     | 25%     | 25%     | 26%     | 24%     | 24%     | 26%     | <b>35%</b>  |
| Tangible Net Assets / Net Revenue     | -59%    | -73%    | -57%    | -45%    | -53%    | -74%    | -58%    | -58%    | <b>-84%</b> |
| ROIC (Annualized)                     | 24%     | 27%     | 19%     | 23%     | 22%     | 22%     | 25%     | 26%     | 25%         |
| ROIC + Organic Net Revenue Growth     | 29%     | 30%     | 18%     | 23%     | 24%     | 26%     | 32%     | 31%     | 32%         |

<sup>(1)</sup> Historical figures restated to comply with revised definition.

Because of the uncertainty in credit and equity markets, there are some great VMS investments to be had right now. We scooped up a big one this last quarter in the form of the Maximus assets. It consists of 3 good businesses, two of which came with very large uneconomic contracts. As we indicated when we announced the acquisition, the contingent liabilities associated with these contracts could exceed 50% of the purchase price. Contracts of this size and structure are unusual in our businesses (at least the way we run them). We factored these contracts into the price that we paid for these assets, and if we got it right, these 3 businesses will eventually generate good ROIC's and contribute to our organic growth.

Having bought the Maximus assets and 16 other businesses this year, combined with our purchases of publicly traded shares of VMS companies and the pending takeover offer for Gladstone plc, we have deployed and committed approximately \$94 million of capital. While we have also had record cash flows and profits, these commitments have largely tapped out our existing line of credit. I am leery about using short

term financing for acquisitions, so we are exploring financing options: Either we slow down the pace of acquisitions and live within our cash flow from operations, or we raise long term financing, whether that be equity or debt flavoured. The capital markets are volatile right now, so I wouldn't hazard a bet as to whether we will find the right investors. If we do, you can expect our acquisition pace in 2009 to continue... if not, it will slow. Irrespective of our acquisition prospects, I continue to be optimistic that our long term performance will be attractive.

Mark Leonard  
President  
Constellation Software Inc.

November 6<sup>th</sup>, 2008

### Performance Metrics Glossary

“Net Revenue” means Revenue for GAAP purposes less third party and flow-through expenses. We use Net Revenue since it captures 100% of the license, maintenance and services revenues associated with Constellation's own products, but only includes the margin on our lower value-added revenues such as commodity hardware or third party software.

“Net Maintenance Revenue” is derived from GAAP Maintenance Revenue by subtracting third party maintenance costs. We believe that Net Maintenance Revenue is one of the best indicators of the intrinsic value of a software company and that the operating profitability of a low growth software business should correlate tightly to Net Maintenance Revenues.

Effective Q1 2008, the term “Adjusted Net Income” is derived by adjusting GAAP net income for the non-cash amortization of intangibles, future income taxes, and charges related to appreciation in common shares eligible for redemption (a charge that we no longer incur now that Constellation's common shares are publicly traded). Prior to Q1 2008, Adjusted Net Income was derived by adjusting GAAP net income for the non-cash amortization of intangibles and charges related to appreciation in common shares eligible for redemption. The computation was changed to include future income taxes since the majority of future income taxes relate to the amortization of intangible assets, and thus are being added back to more closely match the non-cash future tax recovery with the amortization of intangibles. All previously reported Adjusted Net Income figures have been restated in the table above to reflect the new method of computations. We use Adjusted Net Income because it is generally a better measure of cash flow than GAAP net income and it is closely aligned with the calculation of net income we use for bonus purposes.

“Average Invested Capital” is based on the Company's estimate of the amount of money that our shareholders had invested in Constellation. Subsequent to that estimate, each period we have kept a running tally, adding Adjusted Net Income, subtracting any dividends, adding any amounts related to share issuances and making some small adjustments, including adjustments relating to our use of certain incentive programs and the amortization of impaired intangibles.

“Tangible Net Assets / Quarterly Net Revenue” provides a measure of our Tangible Net Assets as a proportion of Quarterly Net Revenue. Tangible Net Assets is calculated by taking Total Assets for GAAP purposes, and subtracting (i) intangible assets and goodwill, (ii) cash and short term investments, (iii) future income tax assets, (iv) all customer, trade and government liabilities that do not bear a coupon, excluding future income tax liabilities and acquisition holdbacks.

“ROIC (Annualized)” represents a ratio of Adjusted Net Income to Average Invested Capital.

“ROIC + Organic Net Revenue Growth” provides a historical measure of the effectiveness of our capital allocation.

### Forward Looking Statements

Certain statements herein may be “forward looking” statements that involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of Constellation or the industry to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These statements reflect current assumptions and expectations regarding future events and operating performance and speak only as of the date hereof. Forward looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to vary significantly from the results discussed in the forward looking statements. These forward looking statements are made as of the date hereof and Constellation assumes no obligation to update any forward looking statements to reflect new events or circumstances except as required by law.

### Non-GAAP Measures

Net Revenue, Net Maintenance Revenue, Adjusted Net Income, Adjusted EBITDA and Organic Net Revenue Growth are not recognized measures under GAAP and, accordingly, shareholders are cautioned that Net Revenue, Net Maintenance Revenue, Adjusted Net Income Adjusted EBITDA and Organic Net Revenue Growth should not be construed as alternatives to revenue or net income determined in accordance with GAAP as an indicator of the financial performance of the Company or as a measure of the Company’s liquidity and cash flows. The Company’s method of calculating Net Revenue, Net Maintenance Revenue, Adjusted Net Income, Adjusted EBITDA and Organic Net Revenue Growth may differ from other issuers and, accordingly, may not be comparable to similar measures presented by other issuers. Please refer to Constellation’s most recently filed Management Discussion and Analysis for a reconciliation, where applicable, between the GAAP and non-GAAP measures referred to above.

# CONSTELLATION SOFTWARE INC.

## MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A")

The following discussion and analysis should be read in conjunction with the unaudited consolidated interim financial statements for the three and nine month periods ended September 30, 2008 and the accompanying notes, and with our consolidated annual financial statements and our annual MD&A for the year ended December 31, 2007. Certain information included herein is forward-looking and based upon assumptions and anticipated results that are subject to uncertainties. Should one or more of these uncertainties materialize or should the underlying assumptions prove incorrect, actual results may vary significantly from those expected. See "Forward-Looking Statements" and "Risks and Uncertainties".

Unless otherwise indicated, all dollar amounts are expressed in U.S. dollars. All references to "\$" are to U.S. dollars and all references to "C\$" are to Canadian dollars.

Additional information about the Company, including our most recently filed Annual Information Form ('AIF'), is available on SEDAR at [www.sedar.com](http://www.sedar.com).

### Forward Looking Statements

Certain statements in this report may contain "forward looking" statements that involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company or industry to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Words such as "may", "will", "expect", "believe", "plan", "intend", "should", "anticipate" and other similar terminology are intended to identify forward looking statements. These statements reflect current assumptions and expectations regarding future events and operating performance and speak only as of the date of this MD&A, November 6, 2008. Forward looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to vary significantly from the results discussed in the forward looking statements, including, but not limited to, the factors discussed under "Risks and Uncertainties". Although the forward looking statements contained in this MD&A are based upon what management of the Company believes are reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward looking statements. The Company assumes no obligation, except as required by law, to update any forward looking statements to reflect new events or circumstances. This report should be viewed in conjunction with the Company's other publicly available filings, copies of which can be obtained electronically on SEDAR at [www.sedar.com](http://www.sedar.com).

### Non-GAAP Measures

This MD&A includes certain measures which have not been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") such as Adjusted EBITDA, Adjusted EBITDA margin, Adjusted Net Income and Adjusted Net Income margin.

The term "Adjusted EBITDA" refers to net income before deducting interest, taxes, depreciation, amortization, loss on held for trading investments related to mark to market adjustments, and foreign exchange, and before including gain (loss) on sale of short-term investments, marketable securities and other assets. The Company believes that Adjusted EBITDA is useful supplemental information as it provides an indication of the results generated by the Company's main business activities prior to taking into consideration how those activities are financed and taxed and also prior to taking into consideration asset depreciation and the other items listed above. "Adjusted EBITDA margin" refers to the percentage that Adjusted EBITDA for any period represents as a portion of total revenue for that period.

Effective Q1 2008, “Adjusted Net Income” means net income plus amortization of intangible assets and future income taxes. Prior to Q1 2008, Adjusted Net Income was reported on the basis of net income plus amortization of intangible assets. The computation was changed to include future income taxes since the majority of future income taxes relate to the amortization of intangible assets, and thus are being added back to more closely match the non-cash future tax recovery with the amortization of intangibles. All previously reported Adjusted Net Income figures have been restated here in Results of Operations to reflect the new method of computations. See “Adjusted Net Income”. The Company believes that Adjusted Net Income is useful supplemental information as it provides an indication of the results generated by the Company’s main business activities prior to taking into consideration amortization of intangibles and future income taxes as these are non-cash expenses that do not necessarily reflect the economic value of acquisitions. “Adjusted Net Income margin” refers to the percentage that Adjusted Net Income for any period represents as a portion of total revenue for that period.

Adjusted EBITDA and Adjusted Net Income are not recognized measures under GAAP and, accordingly, shareholders are cautioned that Adjusted EBITDA and Adjusted Net Income should not be construed as alternatives to net income determined in accordance with GAAP as an indicator of the financial performance of the Company. The Company’s method of calculating Adjusted EBITDA and Adjusted Net Income may differ from other issuers and, accordingly, Adjusted EBITDA and Adjusted Net Income may not be comparable to similar measures presented by other issuers. See “Results of Operations —Adjusted EBITDA” and “— Adjusted Net Income” for a reconciliation of Adjusted EBITDA and Adjusted Net Income to net income.

## **Overview**

We acquire, manage and build vertical market software (“VMS”) businesses. Generally, these businesses provide mission critical software solutions that address the specific needs of our customers in particular markets. Our focus on acquiring businesses with growth potential, managing them well and then building them, has allowed us to generate significant cash flow and revenue growth during the past several years.

Our revenue consists primarily of software license fees, maintenance fees, and professional service fees. Software license revenue is comprised of license fees charged for the use of our software products generally licensed under single-year, multiple-year or perpetual arrangements in which the fair value of the license fee is separately determinable from maintenance and/or professional service fees. Maintenance revenue consists of fees charged for customer support on our software products post-delivery. Maintenance fee arrangements generally include ongoing customer support and rights to certain product updates “if and when available” and products sold on a subscription basis. Professional service revenue consists of fees charged for product training, consulting and implementation services. Our customers typically purchase a combination of software, maintenance and professional services, although the types, mix and quantity of each solution varies by customer and by product.

Cost of revenue consists primarily of the costs directly related to revenues including third party costs and internal costs related to the delivery of professional services and maintenance. Cost of revenue is generally expected to increase in the future as a result of increases in revenue.

Research and development expenses include personnel and related costs associated with our research and development efforts.

Sales and marketing expenses consist primarily of personnel and related costs associated with our sales and marketing functions, including advertising, commissions, trade shows and other promotional materials.

General and administration expenses include personnel and related costs associated with the administration of our business, rental of office space, legal and professional fees and insurance.

## Results of Operations

(In thousands of dollars, except percentages and per share amounts)

|  | Three months ended<br>Sep. 30, |               | Period-Over-Period<br>Change |              | Nine months ended<br>Sep. 30, |                | Period-Over-Period<br>Change |              |
|--|--------------------------------|---------------|------------------------------|--------------|-------------------------------|----------------|------------------------------|--------------|
|  | 2008                           | 2007          | \$                           | %            | 2008                          | 2007           | \$                           | %            |
| <b>Revenue</b>   | <b>80,790</b>                  | <b>60,574</b> | <b>20,216</b>                | <b>33.4%</b> | <b>232,135</b>                | <b>176,955</b> | <b>55,180</b>                | <b>31.2%</b> |
| Cost of Revenue  | 29,722                         | 22,368        | 7,354                        | 32.9%        | 86,974                        | 66,904         | 20,070                       | 30.0%        |
| Gross Profit   | 51,068                         | 38,206        | 12,862                       | 33.7%        | 145,161                       | 110,051        | 35,110                       | 31.9%        |
| Expenses   |                                |               |                              |              |                               |                |                              |              |
| Research and development   | 11,856                         | 9,127         | 2,729                        | 29.9%        | 34,813                        | 26,899         | 7,914                        | 29.4%        |
| Sales and marketing  | 8,930                          | 6,727         | 2,203                        | 32.7%        | 26,812                        | 21,093         | 5,719                        | 27.1%        |
| General and administration   | 14,539                         | 10,994        | 3,545                        | 32.2%        | 41,389                        | 31,440         | 9,949                        | 31.6%        |
| Total Expenses (pre amortization)  | 35,325                         | 26,848        | 8,477                        | 31.6%        | 103,014                       | 79,432         | 23,582                       | 29.7%        |
| <b>Adjusted EBITDA</b>   | <b>15,743</b>                  | <b>11,358</b> | <b>4,385</b>                 | <b>38.6%</b> | <b>42,147</b>                 | <b>30,619</b>  | <b>11,528</b>                | <b>37.6%</b> |
| Depreciation   | 883                            | 863           | 20                           | 2.3%         | 2,509                         | 2,411          | 98                           | 4.1%         |
| Total Expenses   | 36,208                         | 27,711        | 8,497                        | 30.7%        | 105,523                       | 81,843         | 23,680                       | 28.9%        |
| <b>Income before the undernoted</b>  | <b>14,860</b>                  | <b>10,495</b> | <b>4,365</b>                 | <b>41.6%</b> | <b>39,638</b>                 | <b>28,208</b>  | <b>11,430</b>                | <b>40.5%</b> |
| Amortization of intangible assets  | 9,709                          | 5,302         | 4,407                        | 83.1%        | 27,006                        | 14,945         | 12,061                       | 80.7%        |
| Other expenses   | 0                              | 70            | (70)                         | NA           | 0                             | 70             | (70)                         | NA           |
| (Gain) loss on sale of short-term investments,<br>marketable securities and other assets | 15                             | 0             | 15                           | NA           | (9)                           | (1,354)        | 1,345                        | -99.3%       |
| Loss on held for trading investments related to<br>mark to market adjustments            | 134                            | 0             | 134                          | NA           | 134                           | 0              | 134                          | NA           |
| Interest expense (income)  | 120                            | (249)         | 369                          | NA           | 517                           | (398)          | 915                          | NA           |
| Foreign exchange (gain) loss   | 176                            | 690           | (514)                        | -74.5%       | (487)                         | 2,042          | (2,529)                      | NA           |
| Income before income taxes   | 4,706                          | 4,682         | 24                           | 0.5%         | 12,477                        | 12,903         | (426)                        | -3.3%        |
| <b>Income taxes (recovery)</b>   |                                |               |                              |              |                               |                |                              |              |
| Current  | 2,083                          | 1,471         | 612                          | 41.6%        | 4,035                         | 4,050          | (15)                         | -0.4%        |
| Future   | (670)                          | (115)         | (555)                        | 482.6%       | (2,582)                       | (617)          | (1,965)                      | 318.5%       |
|  | 1,413                          | 1,356         | 57                           | 4.2%         | 1,453                         | 3,433          | (1,980)                      | -57.7%       |
| <b>Net income</b>  | <b>3,293</b>                   | <b>3,326</b>  | <b>(33)</b>                  | <b>-1.0%</b> | <b>11,024</b>                 | <b>9,470</b>   | <b>1,554</b>                 | <b>16.4%</b> |
| <b>Adjusted net income <sup>(1)</sup></b>  | <b>12,332</b>                  | <b>8,513</b>  | <b>3,819</b>                 | <b>44.9%</b> | <b>35,448</b>                 | <b>23,798</b>  | <b>11,650</b>                | <b>49.0%</b> |
| Weighted avg # of shares outstanding (000's)   |                                |               |                              |              |                               |                |                              |              |
| Basic  | 21,153                         | 21,119        |                              |              | 21,130                        | 21,107         |                              |              |
| Diluted  | 21,192                         | 21,192        |                              |              | 21,192                        | 21,192         |                              |              |
| <b>Net income per share</b>  |                                |               |                              |              |                               |                |                              |              |
| Basic  | \$ 0.16                        | \$ 0.16       | \$ -                         | 0.0%         | \$ 0.52                       | \$ 0.45        | \$ 0.07                      | 15.6%        |
| Diluted  | \$ 0.16                        | \$ 0.16       | \$ -                         | 0.0%         | \$ 0.52                       | \$ 0.45        | \$ 0.07                      | 15.6%        |
| <b>Adjusted EBITDA per share</b>   |                                |               |                              |              |                               |                |                              |              |
| Basic  | \$ 0.74                        | \$ 0.54       | \$ 0.20                      | 37.0%        | \$ 1.99                       | \$ 1.45        | \$ 0.54                      | 37.2%        |
| Diluted  | \$ 0.74                        | \$ 0.54       | \$ 0.20                      | 37.0%        | \$ 1.99                       | \$ 1.44        | \$ 0.55                      | 38.2%        |
| <b>Adjusted net income per share <sup>(1)</sup></b>                                      |                                |               |                              |              |                               |                |                              |              |
| Basic  | \$ 0.58                        | \$ 0.40       | \$ 0.18                      | 45.0%        | \$ 1.68                       | \$ 1.13        | \$ 0.55                      | 48.7%        |
| Diluted  | \$ 0.58                        | \$ 0.40       | \$ 0.18                      | 45.0%        | \$ 1.67                       | \$ 1.12        | \$ 0.55                      | 49.1%        |

<sup>(1)</sup> Adjusted net income figures for 2007 have been restated to reflect future income taxes. See "Non-GAAP Measures".

## Comparison of the third quarter and nine months ended September 30, 2008 and 2007

### Revenue:

Total revenue for the third quarter ended September 30, 2008 was \$80.8 million, an increase of 33%, or \$20.2 million, compared to \$60.6 million for the comparable period in 2007. For the first nine months of 2008 total revenues were \$232.1 million, an increase of 31%, or \$55.2 million, compared to \$177.0 million for the comparable period in 2007. The increase for both the third quarter and nine month periods compared to the same periods in the prior year, was mainly attributable to growth from acquisitions, as organic growth from our existing businesses was estimated at approximately 6% for the third quarter and 6% for the first nine

months. The remaining 27% growth for the third quarter and 25% for the first nine months is due to acquisitions completed since the beginning of 2007.

Software license revenue for the quarter ended September 30, 2008 increased by 28%, or \$2.0 million to \$9.1 million, from \$7.1 million for the same period in 2007. During the nine months ended September 30, 2008, license revenue increased by 32% or \$6.6 million to \$27.0 million, from \$20.4 million for the same period in 2007. Professional services and other services revenue for the quarter ended September 30, 2008 increased by 37%, or \$5.4 million to \$19.8 million, from \$14.4 million for the same period in 2007. During the nine months ended September 30, 2008, professional services and other services revenue increased by 28% or \$11.9 million to \$54.1 million, from \$42.2 million for the same period in 2007. Hardware and other revenue for the quarter ended September 30, 2008 increased by 35%, or \$1.0 million to \$4.0 million from \$3.0 million for the same period in 2007. During the nine months ended September 30, 2008, hardware and other revenue increased by 24% or \$2.7 million to \$13.8 million, from \$11.1 million for the same period in 2007. Maintenance revenues for the quarter ended September 30, 2008 increased by 33%, or \$11.8 million to \$47.9 million, from \$36.1 million for the same period in 2007. During the nine months ended September 30, 2008, maintenance revenue increased by 33% or \$34.0 million to \$137.3 million, from \$103.2 million for the same period in 2007. The following table displays the breakdown of our revenue according to revenue type:

|                                  | Three months ended Sep. 30, |             |                      |             | Nine months ended Sep. 30, |             |                      |             |
|----------------------------------|-----------------------------|-------------|----------------------|-------------|----------------------------|-------------|----------------------|-------------|
|                                  | <u>2008</u>                 | <u>2007</u> | <u>2008</u>          | <u>2007</u> | <u>2008</u>                | <u>2007</u> | <u>2008</u>          | <u>2007</u> |
|                                  | (\$000)                     |             | (% of total revenue) |             | (\$000)                    |             | (% of total revenue) |             |
| Licenses                         | 9,064                       | 7,079       | 11.2%                | 11.7%       | 26,993                     | 20,417      | 11.6%                | 11.5%       |
| Professional services and other: |                             |             |                      |             |                            |             |                      |             |
| Services                         | 19,750                      | 14,395      | 24.4%                | 23.8%       | 54,117                     | 42,211      | 23.3%                | 23.9%       |
| Hardware and other               | 4,045                       | 3,006       | 5.0%                 | 5.0%        | 13,764                     | 11,089      | 5.9%                 | 6.3%        |
| Maintenance                      | 47,931                      | 36,094      | 59.3%                | 59.6%       | 137,261                    | 103,238     | 59.1%                | 58.3%       |
|                                  | 80,790                      | 60,574      | 100.0%               | 100.0%      | 232,135                    | 176,955     | 100.0%               | 100.0%      |

We aggregate our business into two distinct segments for financial reporting purposes: (i) the public sector segment, which includes businesses focused primarily on government and government-related customers, and (ii) the private sector segment, which includes businesses focused primarily on commercial customers.

The following table displays our revenue by reporting segment and the percentage change for the three and nine months ended September 30, 2008 compared to the same periods in 2007:

|                                  | Three months ended Sep. 30, |             | Period-Over-Period Change |       | Nine months ended Sep. 30,  |             | Period-Over-Period Change |       |
|----------------------------------|-----------------------------|-------------|---------------------------|-------|-----------------------------|-------------|---------------------------|-------|
|                                  | <u>2008</u>                 | <u>2007</u> | \$                        | %     | <u>2008</u>                 | <u>2007</u> | \$                        | %     |
|                                  | (\$000, except percentages) |             |                           |       | (\$000, except percentages) |             |                           |       |
| <b>Public Sector</b>             |                             |             |                           |       |                             |             |                           |       |
| Licenses                         | 6,204                       | 4,643       | 1,561                     | 33.6% | 17,595                      | 12,583      | 5,012                     | 39.8% |
| Professional services and other: |                             |             |                           |       |                             |             |                           |       |
| Services                         | 15,648                      | 10,924      | 4,724                     | 43.2% | 42,189                      | 31,482      | 10,707                    | 34.0% |
| Hardware and other               | 3,108                       | 2,063       | 1,045                     | 50.7% | 10,695                      | 7,950       | 2,745                     | 34.5% |
| Maintenance                      | 30,399                      | 21,831      | 8,568                     | 39.2% | 85,963                      | 61,552      | 24,411                    | 39.7% |
|                                  | 55,359                      | 39,461      | 15,898                    | 40.3% | 156,442                     | 113,567     | 42,875                    | 37.8% |
| <b>Private Sector</b>            |                             |             |                           |       |                             |             |                           |       |
| Licenses                         | 2,860                       | 2,436       | 424                       | 17.4% | 9,399                       | 7,833       | 1,566                     | 20.0% |
| Professional services and other: |                             |             |                           |       |                             |             |                           |       |
| Services                         | 4,102                       | 3,471       | 631                       | 18.2% | 11,928                      | 10,729      | 1,199                     | 11.2% |
| Hardware and other               | 937                         | 944         | (7)                       | -0.7% | 3,069                       | 3,140       | (71)                      | -2.3% |
| Maintenance                      | 17,532                      | 14,262      | 3,270                     | 22.9% | 51,297                      | 41,686      | 9,611                     | 23.1% |
|                                  | 25,431                      | 21,113      | 4,318                     | 20.5% | 75,693                      | 63,388      | 12,305                    | 19.4% |



## Public Sector

For the quarter ended September 30, 2008, total revenue in the public sector segment increased 40%, or \$15.9 million, to \$55.4 million, compared to \$39.5 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008 total revenue increased by 38% or \$42.9 million, to \$156.4 million, compared to \$113.6 million for the comparable period in 2007. The increases for both the three and nine month periods were significant across all revenue types. Revenue growth from acquired businesses was significant for both the three and nine month periods as we completed 20 acquisitions since the beginning of 2007 in our public sector segment. It is estimated that these acquisitions contributed approximately \$10.7 million to our Q3 2008 revenues and \$28.4 million to our revenues in the nine months ended September 30, 2008. The remaining \$5.2 million of revenue growth for Q3 and \$14.5 million of revenue growth for the first nine months of 2008 in this sector was generated from organic sources. The organic growth was primarily driven by the following:

- **Trapeze Operating Group** (increase of approximately \$2.2 million for Q3 and \$8.5 million for the first nine months). Trapeze experienced a significant increase in all revenue types in the quarter and year to date due to strong bookings in their UK, Continental Europe and North American businesses.
- **Harris Operating Group** (increase of approximately \$2.6 million for Q3 and \$6.1 million for the first nine months). Harris experienced a significant increase in all revenue types in the quarter and year to date primarily from strong bookings to new and existing customers in its utility and municipal government segments.

## Private Sector

For the quarter ended September 30, 2008, total revenue in the private sector segment increased 21%, or \$4.3 million, to \$25.4 million, compared to \$21.1 million for the quarter ended September 30, 2007. For the nine months ended September 30, 2008 total revenue increased by 19% or \$12.3 million, to \$75.7 million, compared to \$63.4 million for the comparable period in 2007. The increases for both the three and nine month periods were primarily due to license, professional services and maintenance revenues. Revenue growth from acquired businesses was significant for both the three and nine month periods as we completed 11 acquisitions since the beginning of 2007 in our private sector segment. It is estimated that these acquisitions contributed approximately \$5.8 million to our Q3 2008 revenues and \$16.0 million to our revenues in the nine months ended September 30, 2008. Revenue decreased organically by \$1.5 million in Q3 2008 and by \$3.7 million in the nine months ended September 30, 2008. The organic revenue decline was primarily driven by the following:

- **Jonas Operating Group** (increase of approximately \$1.5 million for Q3 and \$3.9 million for the first nine months). The Jonas organic growth in the quarter and year to date was driven by sales to new and existing customers in the construction vertical, increasing customer share in the private club vertical through selling add on products, and by strong license and professional services revenue in the food services vertical.
- **Homebuilder and Friedman Operating Groups** (decrease of approximately \$3.0 million for Q3 and \$7.6 million for the first nine months). These Operating Groups continued to feel the effects of the housing slowdown in the U.S. The decline was particularly apparent in licenses and services revenue as many of our clients and prospective clients have delayed purchasing decisions.

### Gross Profit by Source:

The following table displays the breakdown of our gross profit by revenue source and as a percentage of total revenue:

|                                     | Three months ended Sep. 30, |       |        |        | Nine months ended Sep. 30, |       |         |         |
|-------------------------------------|-----------------------------|-------|--------|--------|----------------------------|-------|---------|---------|
|                                     | 2008                        | 2007  | 2008   | 2007   | 2008                       | 2007  | 2008    | 2007    |
|                                     | (\$000)                     |       |        |        |                            |       |         |         |
| Gross profit licenses               | 90.9%                       | 89.7% | 8,243  | 6,351  | 90.7%                      | 90.9% | 24,493  | 18,567  |
| Gross profit services & maintenance | 62.2%                       | 62.1% | 42,083 | 31,377 | 61.5%                      | 61.5% | 117,745 | 89,397  |
| Gross profit hardware & other       | 18.3%                       | 15.9% | 742    | 478    | 21.2%                      | 18.8% | 2,924   | 2,087   |
| Gross profit on total revenue       | 63.2%                       | 63.1% | 51,068 | 38,206 | 62.5%                      | 62.2% | 145,162 | 110,051 |

|                            | Three months ended Sep. 30, |        | Period-Over-Period Change |       | Nine months ended Sep. 30, |        | Period-Over-Period Change |       |
|----------------------------|-----------------------------|--------|---------------------------|-------|----------------------------|--------|---------------------------|-------|
|                            | 2008                        | 2007   | \$                        | %     | 2008                       | 2007   | \$                        | %     |
|                            | (\$000, except percentages) |        |                           |       |                            |        |                           |       |
| Research and development   | 11,856                      | 9,127  | 2,729                     | 29.9% | 34,813                     | 26,899 | 7,914                     | 29.4% |
| Sales and marketing        | 8,930                       | 6,727  | 2,203                     | 32.7% | 26,812                     | 21,093 | 5,719                     | 27.1% |
| General and administration | 14,539                      | 10,994 | 3,545                     | 32.2% | 41,389                     | 31,440 | 9,949                     | 31.6% |
| Depreciation               | 883                         | 863    | 20                        | 2.3%  | 2,509                      | 2,411  | 98                        | 4.1%  |
|                            | 36,208                      | 27,711 | 8,497                     | 30.7% | 105,523                    | 81,843 | 23,680                    | 28.9% |

Gross profit increased for the quarter ended September 30, 2008 to \$51.1 million, or 63.2% of total revenue, from \$38.2 million, or 63.1% of total revenue for the quarter ended September 30, 2007. The increase in gross margin dollars is attributable to the overall increase in total revenue. For the first nine months of 2008, our gross profit increased to \$145.2 million or 62.5% of total revenue, from \$110.1 million or 62.2% of total revenue for the comparable period in 2007. The increase in gross margin dollars is attributable to the overall increase in total revenue. Our licenses, services and maintenance revenue margins experienced minimal change vs. 2007 in both the three and nine month periods. Our hardware and other revenue margins continued to strengthen in the three and nine month periods as compared to the same periods in 2007 as we realized stronger margins in our hardware and forms businesses. Management believes there could be significant fluctuations in gross profit margins for future periods if we experience a significant shift in our revenue mix.

### Operating Expenses:

The following table displays the breakdown of our operating expenses by category:

|                            | Three months ended Sep. 30, |        | Period-Over-Period Change |       | Nine months ended Sep. 30, |        | Period-Over-Period Change |       |
|----------------------------|-----------------------------|--------|---------------------------|-------|----------------------------|--------|---------------------------|-------|
|                            | 2008                        | 2007   | \$                        | %     | 2008                       | 2007   | \$                        | %     |
|                            | (\$000, except percentages) |        |                           |       |                            |        |                           |       |
| Research and development   | 11,856                      | 9,127  | 2,729                     | 29.9% | 34,813                     | 26,899 | 7,914                     | 29.4% |
| Sales and marketing        | 8,930                       | 6,727  | 2,203                     | 32.7% | 26,812                     | 21,093 | 5,719                     | 27.1% |
| General and administration | 14,539                      | 10,994 | 3,545                     | 32.2% | 41,389                     | 31,440 | 9,949                     | 31.6% |
| Depreciation               | 883                         | 863    | 20                        | 2.3%  | 2,509                      | 2,411  | 98                        | 4.1%  |
|                            | 36,208                      | 27,711 | 8,497                     | 30.7% | 105,523                    | 81,843 | 23,680                    | 28.9% |

Overall operating expenses for the quarter ended September 30, 2008 increased 31%, or \$8.5 million, to \$36.2 million, compared to \$27.7 million over the same period in 2007. As a percentage of total revenue, operating expenses decreased slightly from 46% in the quarter ended September 30, 2007 to 45% in the quarter ended September 30, 2008. During the nine months ended September 30, 2008, operating expenses increased 29%, or \$23.7 million, to \$105.5 million, compared to \$81.8 million over the same period in 2007. As a percentage of total revenue, operating expenses decreased slightly from 46% in the nine months ended September 30, 2007 to 45% in the nine months ended September 30, 2008. The growth in expenses for the three and nine month periods is primarily due to the growth in the number of employees and an increase in our employee bonus accrual. Our average employee count associated with operating expenses grew 25% from 749 in the quarter ended September 30, 2007 to 939 in the quarter ended September 30, 2008 primarily due to acquisitions. During the nine months ended September 30, 2008, headcount associated with operating

expenses was up 25% to an average headcount of 910 compared to an average of 727 during the same period in 2007.

**Research and development** – Research and development expenses increased 30%, or \$2.7 million, to \$11.9 million for the quarter ended September 30, 2008 compared to \$9.1 million for the same period in 2007. As a percentage of total revenue, research and development expense decreased slightly to 14.7% in Q3 2008 from 15.1% in Q3 2007. During the nine months ended September 30, 2008, research and development expense increased 29%, or \$7.9 million, to \$34.8 million, compared to \$26.9 million over the same period in 2007. As a percentage of total revenue, research and development decreased slightly to 15.0% in the nine months ended September 30, 2008 from 15.2% in the nine months ended September 30, 2007. The increase in expenses as a dollar amount for the three and nine month periods is largely attributable to our growth in headcount from both acquisitions and internal hiring. For Q3 2008, we averaged 517 staff compared to 419 in the same period in 2007, representing a 23% increase in headcount. For the nine months ending September 30, 2008, we averaged 506 staff compared to 404 in the same period in 2007.

We currently do not have any capitalized software development costs. All of our software development costs are expensed as incurred unless they meet Canadian generally accepted accounting criteria for deferral and amortization. Software development costs incurred prior to the establishment of technological feasibility do not meet these criteria, and are expensed as incurred. Capitalized costs would be amortized over the estimated benefit period of the software developed. No costs were deferred in the third quarter of 2008 as most projects did not meet the criteria for deferral and, for those projects that met these criteria, the period between achieving technological feasibility and the completion of software development was minimal, and the associated costs immaterial.

**Sales and marketing** – Sales and marketing expenses increased 33%, or \$2.2 million to \$8.9 million, in the quarter ended September 30, 2008 compared to \$6.7 million for the same period in 2007. As a percentage of total revenue, sales and marketing expenses remained consistent at 11.1% in the quarter ended September 30, 2008 over the same period in 2007. During the nine months ended September 30, 2008, sales and marketing expense increased 27%, or \$5.7 million, to \$26.8 million, compared to \$21.1 million over the same period in 2007. As a percentage of total revenue, sales and marketing decreased to 11.6% from 11.9% in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. The increase in expenses as a dollar amount during the quarter is largely attributable to our growth in headcount from both acquisitions and internal hiring. For Q3 2008, we averaged 212 staff compared to 172 in the same period in 2007, representing a 23% increase in headcount. For the nine months ending September 30, 2008, we averaged 209 staff compared to 166 in the same period in 2007.

**General and administration** – General and administration (“G&A”) expenses increased 32%, or \$3.5 million, to \$14.5 million in the quarter ended September 30, 2008 from \$11.0 million for the same period in 2007. As a percentage of total revenue, G&A expenses decreased slightly to 18.0% in Q3 2008 from 18.1% in Q3 2007. During the nine months ended September 30, 2008, G&A expense increased 32%, or \$9.9 million, to \$41.4 million, compared to \$31.4 million over the same period in 2007. As a percentage of total revenue, G&A remained unchanged at 17.8% in the nine months ended September 30, 2008 compared to the nine months ended September 30, 2007. The increase in expenses as a dollar amount during the quarter is largely attributable to our growth in headcount from both acquisitions and internal hiring. For Q3 2008, we averaged 210 staff compared to 158 in the same period in 2007, representing a 33% increase in headcount. For the nine months ending September 30, 2008, we averaged 195 staff compared to 156 in the same period in 2007. In addition to the increased headcount in Q3, there was a higher employee bonus accrual driven by higher period over period revenue growth rates in 2008 versus 2007.

**Depreciation of property and equipment** – Depreciation of property and equipment for the quarter and nine months ended September 30, 2008 did not change materially from the comparable periods in 2007. As a percentage of total revenue, depreciation was 1.1% in Q3 2008 compared to 1.4% in Q3 2007, and 1.1% for the nine months ended September 30, 2008 compared to 1.4% in the same period in 2007.

Non-Operating Expenses:

The following table displays the breakdown of our non-operating expenses by category.

|   | Three months ended          |       | Period-Over-Period |        | Nine months ended |         | Period-Over-Period |        |
|---|-----------------------------|-------|--------------------|--------|-------------------|---------|--------------------|--------|
|   | Sep. 30,                    |       | Change             |        | Sep. 30,          |         | Change             |        |
|   | 2008                        | 2007  | \$                 | %      | 2008              | 2007    | \$                 | %      |
|   | (\$000, except percentages) |       |                    |        |                   |         |                    |        |
| Amortization of intangible assets   | 9,709                       | 5,302 | 4,407              | 83.1%  | 27,006            | 14,945  | 12,061             | 80.7%  |
| Other expenses  | 0                           | 70    | (70)               | NA     | 0                 | 70      | (70)               | NA     |
| (Gain) loss on sale of short term investments, marketable securities and other assets | 15                          | 0     | 15                 | NA     | (9)               | (1,354) | 1,345              | -99.3% |
| Loss on held for trading investments related to mark to market adjustments            | 134                         | 0     | 134                | NA     | 134               | 0       | 134                | NA     |
| Interest expense (income)   | 120                         | (249) | 369                | NA     | 517               | (398)   | 915                | NA     |
| Foreign exchange (gain) loss  | 176                         | 690   | (514)              | -74.5% | (487)             | 2,042   | (2,529)            | NA     |
| Income tax expense  | 1,413                       | 1,356 | 57                 | 4.2%   | 1,453             | 3,433   | (1,980)            | -57.7% |
|   | 11,567                      | 7,169 | 4,398              | 61.3%  | 28,614            | 18,738  | 9,876              | 52.7%  |

**Amortization of intangible assets** – Amortization of intangible assets was \$9.7 million for the quarter ended September 30, 2008 compared to \$5.3 million for the same period in 2007, representing an increase of 83%. For the nine months ended September 30, 2008, amortization of intangibles increased 81%, to \$27.0 million, compared to \$14.9 million over the same period in 2007. Both the three and nine month increases are attributable to the increases in our intangible asset balance (on a cost basis) over the nine month period ended September 30, 2008 as a result of the acquisitions that we completed during this period.

**Loss (Gain) on sale of short-term investments, marketable securities and other assets** – The loss for the quarter ended September 30, 2008 was \$15,000 compared to nil for Q3 2007. The gain for the nine months ended September 30, 2008 was \$9,000 compared to \$1.4 million during the same period in 2007. The gain in 2007 was the result of liquidating a portion of our investment in certain marketable securities. We expect to realize gains or losses on an infrequent basis as our strategic goal is to buy VMS businesses and hold them indefinitely. Occasionally we will acquire an ownership interest that is less than 100% of a publicly traded VMS business and subsequently sell these shares if we cannot acquire the entire business, or cannot achieve a position of influence, generating either gains or losses. As of September 30, 2008, we had three investments that would have the potential to create such gains or losses. For the nine months ended September 30, 2008, we had an unrealized loss of \$1.4 million relating to the difference between the market value of these investments and the historical cost which is reflected in the Statement of Comprehensive Income. In the future, we may liquidate these holdings if we feel we have a better use for the capital, or if our outlook for the businesses changes.

**Loss on held for trading investments related to mark to market adjustments** – Loss on held for trading for investments related to mark to market adjustments was \$134,000 for the three and nine months ended September 30, 2008. The loss relates to fair value adjustments to warrants held by the company that are not publicly traded.

**Interest expense (income)** – Net interest expense was \$120,000 for the quarter ended September 30, 2008 compared to interest income of \$249,000 for the same period in the previous year. For the nine months ended September 30, 2008, interest expense was \$517,000 compared to interest income of \$398,000 for the comparable period in 2007. At the end of the second quarter of 2007, we completed an investment in VCG Inc. which generates approximately \$0.1 million per quarter in interest income. Our excess cash balances (to the extent that we have excess cash) also generate interest income. These sources of interest income are offset by periodic borrowings on our line of credit to fund acquisitions. As a result, we expect interest income / expense to fluctuate significantly in the future depending upon the timing of acquisitions and the amount we borrow against our line of credit to complete them.

**Foreign exchange loss (gain)** – Most of our businesses are organized geographically so that many of our expenses are incurred in the same currency as our revenues, which mitigates some of our exposure to currency fluctuations. For the quarter ended September 30, 2008, our foreign exchange loss was \$0.2 million compared to a loss of \$0.7 million for Q3 2007. For the nine months ended September 30, 2008, the gain was \$0.5 million versus a loss of \$2.0 million during the same period in 2007. The foreign exchange gain for the

nine months ended September 30, 2008 is mainly attributable to a 6% decrease in the closing rate for the Canadian dollar vs. the US dollar at September 30, 2008 vs. December 31, 2007. As we generally run our business with negative working capital and we had a portion of our net liabilities denominated in Canadian dollars, when we re-valued Canadian dollar net liabilities to U.S. dollars (our functional currency) at quarter end, we recorded a foreign exchange gain.

**Income taxes** – We operate globally and we calculate our tax provision in each of the jurisdictions in which we conduct business. Our tax rate is, therefore, affected by the realization and anticipated relative profitability of our operations in those various jurisdictions, as well as different tax rates that apply and our ability to utilize tax losses. For the quarter ended September 30, 2008, there was an income tax expense of \$1.4 million, compared to an expense of \$1.4 million for the same period in 2007. For the nine months ended September 30, 2008, the provision for income taxes was \$1.5 million compared to \$3.4 million in 2007. The decrease in the tax provision for the nine months ended September 30, 2008 compared to the same period in 2007 is mainly due to future income tax recovery primarily arising from the amortization of acquired intangible assets which have a zero basis for tax purposes.

#### Net Income

Net income for the quarter ended September 30, 2008 was \$3.3 million compared to net income of \$3.3 million for the same period in 2007. On a per share basis this translated into a net income per diluted share of \$0.16 in Q3 2008 vs. a net income per diluted share of \$0.16 in Q3 2007. For the first nine months of 2008, net income was \$11.0 million or \$0.52 per diluted share compared to \$9.5 million or \$0.45 per share in the first nine months of 2007. Net income for the first nine months of 2008 was positively impacted by the growth in our Adjusted EBITDA offset by an increase in amortization of intangibles.

#### Adjusted EBITDA:

For Q3 2008, Adjusted EBITDA increased by \$4.4 million to \$15.7 million compared to \$11.4 million in Q3 2007, representing an increase of 39%. Adjusted EBITDA margin was 19.5% in the third quarter of 2008 and was 18.8% in the comparable period in 2007. For the first nine months of 2008, Adjusted EBITDA increased by \$11.5 million to \$42.1 million compared to \$30.6 million during the same period in 2007, representing an increase of 38%. Adjusted EBITDA margin was 18.2% in the first nine months of 2008, compared to 17.3% of total revenue for the same period in 2007. See “Non-GAAP Measures” for a description of Adjusted EBITDA and Adjusted EBITDA margin.

The following table reconciles Adjusted EBITDA to net income:

|   | Three months ended           |                  | Nine months ended            |                   |
|---|------------------------------|------------------|------------------------------|-------------------|
|   | Sep. 30,                     |                  | Sep. 30,                     |                   |
|   | 2008                         | 2007             | 2008                         | 2007              |
|   | (\$'000, except percentages) |                  | (\$'000, except percentages) |                   |
| <b>Total revenue</b>  | <b>\$ 80,790</b>             | <b>\$ 60,574</b> | <b>\$ 232,135</b>            | <b>\$ 176,955</b> |
| <b>Net income</b>   | 3,293                        | 3,326            | 11,024                       | 9,470             |
| <b>Add back:</b>  |                              |                  |                              |                   |
| Income tax expense  | 1,413                        | 1,356            | 1,453                        | 3,433             |
| Foreign exchange (gain) loss  | 176                          | 690              | (487)                        | 2,042             |
| Interest expense (income)   | 120                          | (249)            | 517                          | (398)             |
| Loss on held for trading investments related to mark to market adjustments            | 134                          | 0                | 134                          | 0                 |
| (Gain) loss on sale of short-term investments, marketable securities and other assets | 15                           | 0                | (9)                          | (1,354)           |
| Other expenses  | 0                            | 70               | 0                            | 70                |
| Amortization of intangible assets   | 9,709                        | 5,302            | 27,006                       | 14,945            |
| Depreciation  | 883                          | 863              | 2,509                        | 2,411             |
| Adjusted EBITDA   | 15,743                       | 11,358           | 42,147                       | 30,619            |
| Adjusted EBITDA margin  | 19.5%                        | 18.8%            | 18.2%                        | 17.3%             |

Adjusted Net Income:

For Q3 2008, Adjusted Net Income increased by \$3.8 million to \$12.3 million compared to \$8.5 million in Q3 2007, representing an increase of 45%. Adjusted Net Income margin was 15.3% in the third quarter of 2008, compared to 14.1% of total revenue for the same period in 2007. For the first nine months of 2008, Adjusted net income increased by \$11.7 million to \$35.4 million compared to \$23.8 million during the same period in 2007, representing an increase of 49%. Adjusted net income margin was 15.3% in the first nine months of 2008, compared to 13.4% of total revenue for the same period in 2007. See “Non-GAAP Measures” for a description of Adjusted Net Income and Adjusted Net Income margin.

In Q1 2008, the method of calculating Adjusted Net Income was modified. The change was a result of the large increase in “future tax expense (recovery)” in the first quarter. Future tax recovery primarily relates to the amortization of intangible assets. Adjusted Net Income is now defined to exclude the impact of this non-cash amount. Management believes that excluding the impact of future tax provides a more accurate picture of the company’s results as it more closely matches the non cash future tax items with the associated amortization of intangibles. The following table reconciles Adjusted Net Income to net income:

|                                   | Three months ended           |                  | Nine months ended            |                   |
|-----------------------------------|------------------------------|------------------|------------------------------|-------------------|
|                                   | Sep. 30,                     |                  | Sep. 30,                     |                   |
|                                   | 2008                         | 2007             | 2008                         | 2007              |
|                                   | (\$'000, except percentages) |                  | (\$'000, except percentages) |                   |
| <b>Total revenue</b>              | <b>\$ 80,790</b>             | <b>\$ 60,574</b> | <b>\$ 232,135</b>            | <b>\$ 176,955</b> |
| <b>Net income</b>                 | 3,293                        | 3,326            | 11,024                       | 9,470             |
| <b>Add back:</b>                  |                              |                  |                              |                   |
| Amortization of intangible assets | 9,709                        | 5,302            | 27,006                       | 14,945            |
| Future income taxes (recovery)    | (670)                        | (115)            | (2,582)                      | (617)             |
| Adjusted net income               | 12,332                       | 8,513            | 35,448                       | 23,798            |
| Adjusted net income margin        | 15.3%                        | 14.1%            | 15.3%                        | 13.4%             |

The following table provides a restatement of our previously reported Adjusted net income figures to include the new adjustment for future income taxes:

|                               | Quarter Ended                     |                 |                 |                 |                 |                 |                 |                 |
|-------------------------------|-----------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
|                               | Dec 31,<br>2006                   | Mar 31,<br>2007 | Jun 30,<br>2007 | Sep 30,<br>2007 | Dec 31,<br>2007 | Mar 31,<br>2008 | Jun 30,<br>2008 | Sep 30,<br>2008 |
|                               | (\$000, except per share amounts) |                 |                 |                 |                 |                 |                 |                 |
| ANI per previous method       | 8,975                             | 7,036           | 8,751           | 8,628           | 9,059           | 12,425          | 12,603          | 13,002          |
| Future tax expense (recovery) | (15)                              | (154)           | (348)           | (115)           | 302             | (1,309)         | (603)           | (670)           |
| ANI per current method        | 8,960                             | 6,882           | 8,403           | 8,513           | 9,361           | 11,116          | 12,000          | 12,332          |
| Fully diluted shares          | 21,192                            | 21,192          | 21,192          | 21,192          | 21,192          | 21,192          | 21,192          | 21,192          |
| ANI/share per previous method | 0.42                              | 0.33            | 0.41            | 0.41            | 0.43            | 0.59            | 0.59            | 0.61            |
| ANI/share per current method  | 0.42                              | 0.32            | 0.40            | 0.40            | 0.44            | 0.52            | 0.57            | 0.58            |

## Quarterly Results

|                             | Quarter Ended                     |                  |                  |                  |                  |                  |                  |                  |
|-----------------------------|-----------------------------------|------------------|------------------|------------------|------------------|------------------|------------------|------------------|
|                             | Dec. 31,<br>2006                  | Mar. 31,<br>2007 | Jun. 30,<br>2007 | Sep. 30,<br>2007 | Dec. 31,<br>2007 | Mar. 31,<br>2008 | Jun. 30,<br>2008 | Sep. 30,<br>2008 |
|                             | (\$000, except per share amounts) |                  |                  |                  |                  |                  |                  |                  |
| Revenue                     | 53,519                            | 55,893           | 60,487           | 60,574           | 66,068           | 73,603           | 77,742           | 80,790           |
| Net Income (loss)           | 3,831                             | 2,602            | 3,542            | 3,326            | 1,640            | 4,329            | 3,402            | 3,293            |
| Net Income (loss) per share |                                   |                  |                  |                  |                  |                  |                  |                  |
| Basic                       | 0.18                              | 0.12             | 0.17             | 0.16             | 0.08             | 0.21             | 0.16             | 0.16             |
| Diluted                     | 0.18                              | 0.12             | 0.17             | 0.16             | 0.08             | 0.20             | 0.16             | 0.16             |

We do not generally experience significant seasonality in our operating results from quarter to quarter. However, our quarterly results may fluctuate as a result of the various acquisitions which may be completed by the Company in any given quarter. We may experience variations in our net income on a quarterly basis depending upon the timing of certain one-time expenditures or gains such as: loss (gain) on the sale of short-term investments, marketable securities and other assets.

## Liquidity

Our cash position (net of borrowings on our line of credit) at September 30, 2008 decreased to negative \$41 million, from \$1.2 million at December 31, 2007. The decrease in cash over the nine month period was largely attributable to cash deployed on acquisitions and holdbacks of \$62 million and cash invested in marketable securities of \$12 million offset by cash generated from operating activities.

Total assets increased \$94 million, from \$267 million at December 31, 2007 to \$361 million at September 30, 2008. The majority of the increase can be explained by increases in: a) intangible assets and goodwill of \$65 million due to the completion of several acquisitions b) short term investments and marketable securities of \$10.1 million due to the investment made in UK based Gladstone PLC and U.S. based Mediware and c) accounts receivable and work in progress of \$19.7 million which is driven by growth in the business and by acquisitions. These amounts were partially offset by decrease in cash of \$7.9 million (as explained below).

Current liabilities increased \$85 million, from \$156 million as of December 31, 2007, to \$241 million at September 30, 2008. From an individual category perspective the increases were driven by a) bank indebtedness up \$35.4 million due to acquisitions made in the first nine months of 2008 b) a deferred revenue increase of \$35.6 million, due to the growth in our business and due to acquisitions c) an increase of \$7.8 million in accounts payable and accrued liabilities due to the accrual of 2008 employee bonuses and due to growth in the business and d) an increase of \$6.6 million in acquisition holdback payments relating to acquisitions made in 2008.

**Net Changes in Cash Flow****Nine months ended  
September 30, 2008**  
(in millions of \$)

|  |              |
|--|--------------|
| Net cash provided by operating activities                    | \$39.2       |
| Net cash provided by financing activities                    | 32.5         |
| Net cash used in investing activities                        | (79.1)       |
| Effect of exchange rate changes on cash and cash equivalents | (0.4)        |
| <b>Net decrease in cash and cash equivalents</b>             | <b>(7.9)</b> |

The net cash flow from operating activities was \$39.2 million for the nine months ended September 30, 2008. In the first nine months of 2008, we generated cash flows from operating activities of \$37.0 million excluding a net decrease in operating working capital of \$2.1 million.

The net cash provided by financing activities was \$32.5 million. Borrowings on our line of credit generated cash of \$35.4 million and the repayment of shareholder loans a further \$0.9 million. This was offset by the payment of our annual dividend of \$0.18 per share for cash usage of \$3.8 million.

The net cash used in investing activities was due primarily to acquisitions completed in the period ended September 30, 2008 for an aggregate of \$62.3 million (including payments for holdbacks relating to prior acquisitions) and the investment of marketable securities of \$12.2 million. We also invested approximately \$2.4 million in property and equipment.

We believe we have more than sufficient cash to continue to operate for the foreseeable future. Generally our VMS businesses operate with negative working capital as a result of the collection of maintenance payments and other revenues in advance of the performance of the related services. As such, management anticipates that it can continue to grow the business organically without any additional funding. If we continue to acquire VMS businesses we may need additional external funding depending upon the size and timing of the acquisitions.

**Capital Resources and Commitments**

We have a \$105 million credit facility that is collateralized by substantially all of our assets including the assets of the majority of our material Canadian and U.S. subsidiaries. Certain other subsidiaries also guarantee this facility. The facility is available for acquisitions, working capital needs, and other general corporate purposes and for the needs of our subsidiaries. As of September 30, 2008, we had drawn \$54.7 million on this facility and issued letters of credit for \$12.0 million which limits our borrowing capacity dollar for dollar.

Commitments include operating leases for office equipment and facilities, letters of credit, bank guarantees, and performance bonds that are routinely issued on our behalf by financial institutions in connection with facility leases and contracts with public sector customers. Also, occasionally we structure some of our acquisitions with “earn out” payments based on the future performance of the acquired VMS business. Aside from the aforementioned, we do not have any other business arrangements, derivative financial instruments, or any equity interests in unconsolidated companies (aside from our shareholdings in publicly traded companies included in our short term investments and our investment in VCG Inc.) that would have a significant effect on our assets and liabilities as at September 30, 2008.

**Foreign Currency Exposure**

We operate internationally and have foreign currency risks related to our revenue, operating expenses, assets and liabilities denominated in currencies other than the U.S. dollar. Consequently, we believe movements in the foreign currencies in which we transact could significantly affect future net earnings. Currently, we do not use hedging techniques to mitigate such currency risks. We cannot predict the effect of



foreign exchange losses in the future; however, if significant foreign exchange losses are experienced, they could have a material adverse effect on our business, results of operations, and financial condition.

### **Off-Balance Sheet Arrangements**

As a general practice, we have not entered into off-balance sheet financing arrangements. Except for operating leases, bank guarantees, letters of credit and other low probability and/or contingent liabilities for which we cannot reasonably estimate the outcome (not accrued in accordance with Canadian GAAP), all of our commitments are reflected on our balance sheet.

### **Transactions with Related Parties**

Aside from our Key Employee Loan Program (“KELP”), we had no material related party transactions during Q3 2008. The outstanding balance of loans granted under the KELP as of September 30, 2008 was \$1.1 million as compared to \$1.9 million as of December 31, 2007.

### **Proposed Transactions**

We seek potential acquisition targets on an ongoing basis and may complete several acquisitions in any given fiscal year.

### **Critical Accounting Estimates**

Details of the critical accounting estimates are available in the management’s discussion and analysis for the year ended December 31, 2007.

### **Changes in Accounting Policies**

Effective January 1, 2008, the Company adopted the recommendations included in the Canadian Institute of Chartered Accountants (“CICA”) Handbook, Section 1535, *Capital Disclosures*. The new standard requires disclosure of qualitative and quantitative information that enables users of financial statements to evaluate the Company’s objectives, policies and processes for managing capital. The adoption of this standard did not have a material impact on the Company’s financial statements.

On January 1, 2008, the Company adopted CICA Handbook Section 3862, *Financial Instruments – Disclosures* and Section 3863, *Financial Instruments – Presentation*. Section 3862 requires disclosure about the significance of financial instruments for an entity’s financial position, the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. Section 3862 and 3863 replace Section 3861, *Financial Instruments – Disclosure and Presentation*. The adoption of these standards did not have a material impact on the Company’s financial statements.

On January 1, 2007, the Company adopted the recommendations of CICA Handbook Section 1530, *Comprehensive Income*; Section 3855, *Financial Instruments - Recognition and Measurement*; Section 3861, *Financial Instruments - Disclosure and Presentation*; Section 3865, *Hedges*; and Section 3251, *Equity*. These sections apply to fiscal years beginning on or after October 1, 2006 and provide standards for recognition, measurement, disclosure and presentation of financial assets, financial liabilities and non-financial derivatives, and describe when and how hedge accounting may be applied. Section 1530 provides standards for the reporting and presentation of comprehensive income, which represents the change in equity from transactions and other events and circumstances from non-owner sources. Other comprehensive income is defined by revenue, expenses, gains and losses that are recognized in comprehensive income, but excluded from net income, in conformity with generally accepted accounting principles.

Under the new standards, all financial assets are classified as held for trading, held-to-maturity investments, loans and receivables or available-for-sale categories. Also, all financial liabilities must be classified as held for trading or other financial liabilities. All financial instruments are recorded on the

consolidated balance sheet at fair value. After initial recognition, the financial instruments should be measured at their fair values, except for held-to-maturity investments, loans and receivables and other financial liabilities, which should be measured at amortized cost. The effective interest related to the financial liabilities and the gain or loss arising from a change in the fair value of a financial asset or financial liability classified as held for trading is included in net income for the period in which it arises. If a financial asset is classified as available for sale, the gain or loss should be recognized in other comprehensive income until the financial asset is derecognized and any cumulative gain or loss is then recognized in net income.

As a result of the implementation of this standard, the Company has classified cash and cash equivalents as held for trading. Short-term investments and marketable securities have been classified as available for sale. Accounts receivable has been classified as loans and receivables. Bank indebtedness, accounts payable and certain accrued liabilities have been classified as other financial liabilities. The Company has not classified any financial asset as held to maturity. The remeasurement on adoption to fair value resulted in an increase of short-term investments and marketable securities of \$1,154 as of January 1, 2007 and a corresponding increase in other comprehensive income.

### **Recent Accounting pronouncements**

The CICA plans to converge Canadian GAAP with International Financial Reporting Standards ("IFRS") over a transition period expected to end in 2011. The impact on the transition to IFRS on the Company's financial statements is not yet determinable.

In 2008, the CICA issued Handbook Section 3064, "*Goodwill and Intangible Assets*". Section 3064 replaces Section 3062 "*Goodwill and Intangible Assets*", and Section 3450, "*Research and Development Costs*". It establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. This new standard is effective for the Company's interim and annual consolidated financial statements commencing January 1, 2009. The Company has assessed that the new standard will have no impact on its financial statements.

### **Share Capital**

As at November 6, 2008, there were 21,191,530 total shares outstanding comprised of 16,903,530 common shares and 4,288,000 class A non-voting shares.

### **Outlook**

Although we anticipate that our annual revenue and Adjusted EBITDA will vary from year to year, management's objective is to grow each of our annual revenue per share and Adjusted EBITDA per share at an average rate, in the five year period commencing January 1, 2006 and ending December 31, 2010, in excess of 20% per annum. While the mix of organic growth and growth from acquisitions will change from year to year, we anticipate that approximately one half to three quarters of our growth will be attributable to acquisitions over this five year period. The foregoing objectives are based on various assumptions of management, including, without limitation, that (i) there will be a sufficient number of reasonably-priced acquisitions available, and (ii) we will continue to declare modest dividends. See "Forward-Looking Statements" and "Risks and Uncertainties".

### **Risks and Uncertainties**

The risks and uncertainties affecting the Company are described in the Company's most recently filed AIF. Additional risks and uncertainties not presently known to us or that we currently consider immaterial also may impair our business and operations and cause the price of the common shares to decline. If any of the noted risks actually occur, our business may be harmed and the financial condition and results of operation may suffer significantly. In that event, the trading price of the common shares could decline, and shareholders may lose all or part of their investment.

## **Controls and Procedures**

### ***Evaluation of disclosure controls and procedures:***

Management is responsible for establishing and maintaining disclosure controls and procedures as defined under Multilateral Instrument 52-109. At September 30, 2008, the President and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective and that material information relating to the Company, including its subsidiaries, was made known to them and was recorded, processed, summarized and reported within the time periods specified under applicable securities legislation.

### ***Internal controls over financial reporting:***

Management is responsible for the design of its internal controls over financial reporting as defined under Multilateral Instrument 52-109. At December 31, 2007, the President and Chief Financial Officer concluded that the design of these internal controls and procedures was effective in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements for external purposes in accordance with Canadian GAAP. The President and CFO have evaluated whether there were changes to internal controls over financial reporting during the interim period ended September 30, 2008 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting. No such changes were identified.

Interim Consolidated Financial Statements  
(In U.S. dollars)

# **CONSTELLATION SOFTWARE INC.**

For the three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

# CONSTELLATION SOFTWARE INC.

Interim Consolidated Balance Sheets  
(In thousands of U.S. dollars)

|  | September 30,<br>2008 | December 31,<br>2007 |
|--|-----------------------|----------------------|
|  | (Unaudited)           |                      |
| <b>Assets</b>  |                       |                      |
| Current assets:  |                       |                      |
| Cash   | \$ 11,914             | \$ 19,796            |
| Restricted cash  | 1,658                 | 750                  |
| Short-term investments and marketable securities available for sale (note 4) | 11,327                | 1,217                |
| Accounts receivable  | 59,588                | 47,177               |
| Work in progress   | 18,083                | 10,839               |
| Inventory  | 2,491                 | 2,069                |
| Prepaid expenses and other current assets                                    | 9,702                 | 7,608                |
| Investment tax credit recoverable  | 975                   | 661                  |
| Future income taxes (note 9)   | 1,233                 | 1,096                |
|  | 116,971               | 91,213               |
| Property and equipment   | 9,895                 | 8,025                |
| Future income taxes (note 9)   | 3,377                 | 3,890                |
| Notes receivable   | 3,611                 | 3,490                |
| Share purchase warrants  | 487                   | 571                  |
| Investment tax credit recoverable  | 2,108                 | 1,779                |
| Other long-term assets   | 2,083                 | 643                  |
| Intangible assets (note 6)   | 181,429               | 128,942              |
| Goodwill   | 40,908                | 28,594               |
|  | \$ 360,869            | \$ 267,147           |
| <b>Liabilities and Shareholders' Equity</b>                                  |                       |                      |
| Current liabilities:   |                       |                      |
| Bank indebtedness (note 7)   | \$ 54,700             | \$ 19,342            |
| Accounts payable and accrued liabilities                                     | 51,675                | 43,892               |
| Acquisition holdback payments  | 17,029                | 10,442               |
| Deferred revenue   | 114,478               | 78,870               |
| Income taxes payable   | 2,778                 | 3,426                |
| Future income taxes (note 9)   | 327                   | 347                  |
|  | 240,987               | 156,319              |
| Future income taxes (note 9)   | 22,802                | 21,238               |
| Acquisition holdback payments  | 928                   | 1,000                |
| Other long-term liabilities  | 3,295                 | 1,708                |
| Shareholders equity:   |                       |                      |
| Capital stock  | 99,283                | 99,283               |
| Shareholder loans (note 8)   | (1,055)               | (1,915)              |
| Accumulated other comprehensive loss   | (5,332)               | (3,237)              |
| Deficit  | (39)                  | (7,249)              |
|  | 92,857                | 86,882               |
| Subsequent events (note 15)  |                       |                      |
|  | \$ 360,869            | \$ 267,147           |

See accompanying notes to interim consolidated financial statements.

# CONSTELLATION SOFTWARE INC.

Interim Consolidated Statements of Operations

(In thousands of U.S. dollars, except per share amounts)

|  | Three months ended<br>September 30, |           | Nine months ended<br>September 30, |            |
|--|-------------------------------------|-----------|------------------------------------|------------|
|  | 2008                                | 2007      | 2008                               | 2007       |
|  | (Unaudited)                         |           | (Unaudited)                        |            |
| Revenue  | \$ 80,790                           | \$ 60,574 | \$ 232,135                         | \$ 176,955 |
| Cost of revenue  | 29,722                              | 22,368    | 86,974                             | 66,904     |
|  | 51,068                              | 38,206    | 145,161                            | 110,051    |
| Research and development   | 11,856                              | 9,127     | 34,813                             | 26,899     |
| Sales and marketing  | 8,930                               | 6,727     | 26,812                             | 21,093     |
| General and administration   | 14,539                              | 10,994    | 41,389                             | 31,440     |
| Depreciation   | 883                                 | 863       | 2,509                              | 2,411      |
|  | 36,208                              | 27,711    | 105,523                            | 81,843     |
| Income before the undernoted   | 14,860                              | 10,495    | 39,638                             | 28,208     |
| Amortization of intangible assets  | 9,709                               | 5,302     | 27,006                             | 14,945     |
| Other expenses   | -                                   | 70        | -                                  | 70         |
| (Gain) loss on sale of short-term investments,<br>marketable securities and other assets | 15                                  | -         | (9)                                | (1,354)    |
| Loss on held for trading investments related to<br>mark to market adjustments            | 134                                 | -         | 134                                | -          |
| Interest expense (income), net   | 120                                 | (249)     | 517                                | (398)      |
| Foreign exchange (gain) loss   | 176                                 | 690       | (487)                              | 2,042      |
| Income before income taxes   | 4,706                               | 4,682     | 12,477                             | 12,903     |
| Income taxes (recovery) (note 9):  |                                     |           |                                    |            |
| Current  | 2,083                               | 1,471     | 4,035                              | 4,050      |
| Future   | (670)                               | (115)     | (2,582)                            | (617)      |
|  | 1,413                               | 1,356     | 1,453                              | 3,433      |
| Net Income   | \$ 3,293                            | \$ 3,326  | \$ 11,024                          | \$ 9,470   |
| Income per share (note 10):  |                                     |           |                                    |            |
| Basic  | \$ 0.16                             | \$ 0.16   | \$ 0.52                            | \$ 0.45    |
| Diluted  | 0.16                                | 0.16      | 0.52                               | 0.45       |
| Weighted average number of shares<br>outstanding (note 10):                              |                                     |           |                                    |            |
| Basic  | 21,153                              | 21,119    | 21,130                             | 21,107     |
| Diluted  | 21,192                              | 21,192    | 21,192                             | 21,192     |
| Outstanding at the end of the period   | 21,192                              | 21,192    | 21,192                             | 21,192     |

See accompanying notes to interim consolidated financial statements.

# CONSTELLATION SOFTWARE INC.

Interim Consolidated Statements of Deficit  
(In thousands of U.S. dollars)

|                              | Three months ended<br>September 30, |             | Nine months ended<br>September 30, |             |
|------------------------------|-------------------------------------|-------------|------------------------------------|-------------|
|                              | 2008                                | 2007        | 2008                               | 2007        |
|                              | (Unaudited)                         |             | (Unaudited)                        |             |
| Deficit, beginning of period | \$ (3,332)                          | \$ (12,215) | \$ (7,249)                         | \$ (15,180) |
| Net income                   | 3,293                               | 3,326       | 11,024                             | 9,470       |
| Dividends                    | -                                   | -           | (3,814)                            | (3,179)     |
| Deficit, end of period       | \$ (39)                             | \$ (8,889)  | \$ (39)                            | \$ (8,889)  |

Interim Consolidated Statements of Comprehensive Income  
(In thousands of U.S. dollars)

|   | Three months ended<br>September 30, |          | Nine months ended<br>September 30, |          |
|---|-------------------------------------|----------|------------------------------------|----------|
|   | 2008                                | 2007     | 2008                               | 2007     |
|   | (Unaudited)                         |          | (Unaudited)                        |          |
| Net Income  | \$ 3,293                            | \$ 3,326 | \$ 11,024                          | \$ 9,470 |
| Other comprehensive income (loss), net of tax:  |                                     |          |                                    |          |
| Net unrealized mark-to-market adjustment<br>gain (loss) on available-for-sale financial<br>assets during the period   | 438                                 | (121)    | (1,401)                            | (42)     |
| Net unrealized foreign exchange adjustment<br>gain (loss) on available-for-sale financial<br>assets during the period | (646)                               | 5        | (740)                              | 12       |
| Transfer of unrealized gain from prior periods<br>upon derecognition of available-for-sale<br>investments             | -                                   | -        | (39)                               | -        |
| Comprehensive income  | \$ 3,085                            | \$ 3,210 | \$ 8,844                           | \$ 9,440 |

See accompanying notes to interim consolidated financial statements.

# CONSTELLATION SOFTWARE INC.

Interim Consolidated Statements of Cash Flows  
(In thousands of U.S. dollars)

|  | Three months ended<br>September 30, |           | Nine months ended<br>September 30, |           |
|--|-------------------------------------|-----------|------------------------------------|-----------|
|  | 2008                                | 2007      | 2008                               | 2007      |
|  | (Unaudited)                         |           | (Unaudited)                        |           |
| Cash flows from operating activities:  |                                     |           |                                    |           |
| Net income   | \$ 3,293                            | \$ 3,326  | \$ 11,024                          | \$ 9,470  |
| Adjustments to reconcile net income to<br>net cash flows from operations:                  |                                     |           |                                    |           |
| Decrease (increase) in investment tax<br>credit recoverable                                | 158                                 | (35)      | (870)                              | (193)     |
| Depreciation   | 883                                 | 863       | 2,509                              | 2,411     |
| Amortization of intangible assets  | 9,709                               | 5,302     | 27,006                             | 14,945    |
| Accretion interest   | (29)                                | -         | (86)                               | -         |
| Interest on shareholder loans  | (14)                                | (25)      | (51)                               | (74)      |
| Future income taxes  | (670)                               | (115)     | (2,582)                            | (617)     |
| (Gain) loss on sale of short-term investments,<br>marketable securities, and other assets  | 15                                  | -         | (9)                                | (1,354)   |
| Loss on held for trading investments related to<br>mark to market adjustments              | 134                                 | -         | 134                                | -         |
| Unrealized foreign exchange loss   | 307                                 | 713       | (66)                               | 1,996     |
| Change in non-cash operating working<br>capital (note 14)                                  | 10,070                              | 5,474     | 2,149                              | (6,567)   |
| Cash flows from operating activities   | 23,856                              | 15,503    | 39,158                             | 20,017    |
| Cash flows from financing activities:  |                                     |           |                                    |           |
| Increase in long-term liabilities  | 172                                 | 310       | 395                                | 101       |
| Increase (decrease) in bank indebtedness   | 26,500                              | (1,881)   | 35,358                             | 1,712     |
| Credit facility financing fees   | -                                   | -         | (354)                              | -         |
| Dividends  | -                                   | -         | (3,814)                            | (3,179)   |
| Issuance of shareholder loans  | -                                   | -         | -                                  | (447)     |
| Repayment of shareholder loans, net  | -                                   | -         | 885                                | 869       |
| Cash flows from (used in) financing activities   | 26,672                              | (1,571)   | 32,470                             | (944)     |
| Cash flows from investing activities:  |                                     |           |                                    |           |
| Acquisition of businesses, net of cash<br>acquired (note 5)                                | (43,590)                            | (2,783)   | (59,679)                           | (18,190)  |
| Acquisition holdback payments  | (1,831)                             | (320)     | (2,571)                            | (3,728)   |
| Investment in VCG Inc.   | (85)                                | -         | (85)                               | (4,000)   |
| Reduction (additions) to short-term investments,<br>marketable securities and other assets | -                                   | (869)     | (12,158)                           | 3,082     |
| Decrease (increase) in restricted cash   | 89                                  | -         | (908)                              | 858       |
| Increase in other assets   | (1,096)                             | (25)      | (1,291)                            | (249)     |
| Property and equipment purchased   | (874)                               | (544)     | (2,385)                            | (1,829)   |
| Cash flows used in investing activities  | (47,387)                            | (4,541)   | (79,077)                           | (24,056)  |
| Effect of currency translation adjustment on<br>cash and cash equivalents                  | (543)                               | (1,038)   | (433)                              | (1,847)   |
| Increase (decrease) in cash and cash equivalents   | 2,598                               | 8,353     | (7,882)                            | (6,830)   |
| Cash, beginning of period  | 9,316                               | 10,624    | 19,796                             | 25,807    |
| Cash, end of period  | \$ 11,914                           | \$ 18,977 | \$ 11,914                          | \$ 18,977 |

See accompanying notes to interim consolidated financial statements.



# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

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## 1. Basis of presentation:

The accompanying unaudited condensed interim consolidated financial statements (the "Interim Consolidated Financial Statements") include the accounts of the Company and its subsidiaries, all of which are wholly owned. All significant inter-company transactions and balances have been eliminated. During the nine months ended September 30, 2008, the Company completed certain acquisitions as described in note 5 to the Interim Consolidated Financial Statements. The results of operations of these acquired companies have been included in these Interim Consolidated Financial Statements from the dates of acquisition.

These Interim Consolidated Financial Statements are expressed in U.S. dollars and are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and reflect all adjustments consisting only of normal adjustments which, in the opinion of management, are necessary for a fair presentation of the results of the interim periods presented. These Interim Consolidated Financial Statements are based upon accounting policies and methods of their application that are consistent with those used and described in the Company's annual consolidated financial statements, except as described in note 2. The Interim Consolidated Financial Statements do not include all of the financial statement disclosures included in the annual financial statements prepared in accordance with Canadian GAAP and, therefore, should be read in conjunction with the 2007 consolidated financial statements and notes.

## 2. Changes in accounting policies:

### (a) Capital disclosures:

Effective January 1, 2008, the Company adopted the recommendations included in the Canadian Institute of Chartered Accountants ("CICA") Handbook, Section 1535, Capital Disclosures. The new standard requires disclosure of qualitative and quantitative information that enables users of financial statements to evaluate the Company's objectives, policies and processes for managing capital.

# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

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## 2. Changes in accounting policies (continued):

### (b) Financial instruments - disclosures:

On January 1, 2008, the Company adopted CICA Handbook Section 3862, Financial Instruments - Disclosures and Section 3863, Financial Instruments - Presentation.

Section 3862 requires disclosure about the significance of financial instruments for an entity's financial position, the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks.

Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives.

Section 3862 and 3863 replace Section 3861, Financial Instruments - Disclosure and Presentation.

The additional disclosures, required as a result of adoption of these standards, have been included in Note 11, Capital risk management and Note 12, Financial risk management and financial instruments.

# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

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### 3. Changes in accounting policies not yet adopted:

The following accounting pronouncements have been released but have not yet been adopted by the Company.

(a) International Financial Reporting Standards:

The CICA plans to converge Canadian GAAP with International Financial Reporting Standards ("IFRS") over a transition period expected to end in 2011. The impact on the transition to IFRS on the Company's financial statements is not yet determinable.

(b) Goodwill and Intangible Assets:

In 2008, the CICA issued Handbook Section 3064 "Goodwill and Intangible Assets". Section 3064 replaces Section 3062 "Goodwill and Intangible Assets", and Section 3450, "Research and Development Costs". It establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. This new standard is effective for the Company's interim and annual consolidated financial statements commencing January 1, 2009. The Company has assessed that the new standard will have no impact on its financial statements.

### 4. Short-term investments and marketable securities:

At September 30, 2008, the Company held investments in three public companies listed in the U.K. and U.S., all of which develop and sell software solutions.

|               | September 30,<br>2008 |                 | December 31,<br>2007 |                 |
|---------------|-----------------------|-----------------|----------------------|-----------------|
|               | Cost                  | Market<br>Value | Cost                 | Market<br>Value |
| Common shares | \$ 13,507             | \$ 11,327       | \$ 1,303             | \$ 1,217        |

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# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

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## 5. Business acquisitions:

### 2008

- (a) On September 30, 2008, the Company acquired substantially all of the assets of MAXIMUS Inc.'s Justice, Education, and Asset Solutions businesses for aggregate net cash consideration of \$35,000 plus cash holdbacks of \$5,000 resulting in total consideration of \$40,000. The holdbacks are payable over a one-year period and are adjusted for any claims under the representations and warranties of the agreement. Transaction costs associated with this acquisition incurred to date are estimated to be \$200. The acquisition has been accounted for using the purchase method with the results of operations included in these consolidated financial statements from the date of acquisition. The following table summarizes the aggregate preliminary estimated fair value of the assets acquired and liabilities assumed at the date of acquisition:

---

|  |                       |
|--|-----------------------|
| Assets acquired:                         |                       |
| Current assets                           | \$ 19,626             |
| Property and equipment                   | 1,172                 |
| Intangibles                              | 50,121                |
|  | <hr/> 70,919          |
| Liabilities assumed:                     |                       |
| Current liabilities                      | 7,332                 |
| Deferred revenue                         | 23,387                |
|  | <hr/> 30,719          |
| <hr/> Total purchase price consideration | <hr/> \$ 40,200 <hr/> |

The Company is in the process of determining the fair value of the intangible assets, long-term contracts and acquired deferred revenue.

This acquisition has been allocated to the Public Sector.

# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

- (b) During the nine months ended September 30, 2008, the Company made fifteen acquisitions for aggregate net cash consideration of \$24,479 plus cash holdbacks of \$4,909 and earnout arrangements of \$960 resulting in total consideration of \$30,348. The holdbacks are payable over a two-year period and are adjusted for any claims under the representations and warranties of the agreements. The acquisitions have been accounted for using the purchase method with the results of operations included in these consolidated financial statements from the date of each acquisition. The following table summarizes the aggregate preliminary estimated fair value of the assets acquired and liabilities assumed at the date of each acquisition:

---

|                                    |                 |
|------------------------------------|-----------------|
| Assets acquired:                   |                 |
| Current assets                     | \$ 9,182        |
| Property and equipment             | 887             |
| Future income taxes                | 176             |
| Technology assets                  | 25,984          |
| Customer assets                    | 8,928           |
| Non-compete agreements             | 1,000           |
| Backlog                            | 735             |
| Goodwill                           | 3,540           |
|                                    | <hr/> 50,432    |
| Liabilities assumed:               |                 |
| Current liabilities                | 2,879           |
| Deferred revenue                   | 11,769          |
| Future income taxes                | 5,204           |
| Long-term liabilities              | 232             |
|                                    | <hr/> 20,084    |
| Total purchase price consideration | <hr/> \$ 30,348 |

# CONSTELLATION SOFTWARE INC.

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## 5. Business acquisitions (continued):

### 2007

#### (b) PG Govern QC Inc. ("PG"):

On March 1, 2007, the Company acquired the assets and shares of PG for net cash consideration of \$13,112 on closing plus a holdback of \$2,228 resulting in total consideration of \$15,340. The holdback is expected to be paid out as assets are converted into cash, subject to no claims under the representations and warranties of the agreement. The acquisition has been accounted for by the purchase method with the results of operations included in these consolidated financial statements from the date of acquisition. The following table summarizes the fair value of the assets acquired and liabilities assumed at the date of acquisition:

---

|                                    |                 |
|------------------------------------|-----------------|
| Assets acquired:                   |                 |
| Current assets                     | \$ 8,115        |
| Property and equipment             | 1,030           |
| Other long-term assets             | 2,212           |
| Technology assets                  | 16,694          |
| Customer assets                    | 4,346           |
| Backlog                            | 767             |
|                                    | <hr/> 33,164    |
| Liabilities assumed:               |                 |
| Current liabilities                | 8,441           |
| Deferred revenue                   | 7,068           |
| Future income tax liability        | 1,533           |
| Other long-term liabilities        | 782             |
|                                    | <hr/> 17,824    |
| Total purchase price consideration | <hr/> \$ 15,340 |

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## 5. Business acquisitions (continued):

(c) Other acquisitions:

During the nine months ended September 30, 2007, the Company made seven other acquisitions for aggregate net initial cash consideration of \$4,928 plus holdbacks of \$1,216 resulting in total consideration of \$6,144. Holdbacks of \$816 have subsequently been paid (\$497 during the nine months ended September 30, 2008). The acquisitions have been accounted for using the purchase method with the results of operations included in these consolidated financial statements from the date of each acquisition. The following table summarizes the fair value of the assets acquired and liabilities assumed at the date of each acquisition:

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|  |                      |
|--|----------------------|
| Assets acquired:                         |                      |
| Current assets                           | \$ 2,390             |
| Property and equipment                   | 219                  |
| Technology assets                        | 6,401                |
| Customer assets                          | 2,236                |
| Goodwill                                 | 33                   |
|  | <hr/> 11,279         |
| Liabilities assumed:                     |                      |
| Current liabilities                      | 1,518                |
| Deferred revenue                         | 2,193                |
| Future income taxes                      | 1,424                |
|  | <hr/> 5,135          |
| <hr/> Total purchase price consideration | <hr/> \$ 6,144 <hr/> |

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## 6. Intangible assets:

|                         |            |                             | September 30,<br>2008 | December 31,<br>2007 |
|-------------------------|------------|-----------------------------|-----------------------|----------------------|
|                         | Cost       | Accumulated<br>amortization | Net book<br>value     | Net book<br>value    |
| Technology assets       | \$ 173,545 | \$ 71,959                   | \$ 101,586            | \$ 71,866            |
| Non-compete agreements  | 2,680      | 1,747                       | 933                   | 91                   |
| Customer assets         | 39,463     | 12,625                      | 26,838                | 15,175               |
| Trademarks              | 133        | 100                         | 33                    | 40                   |
| Backlog                 | 2,643      | 1,448                       | 1,195                 | 128                  |
| Contract related assets | 903        | 180                         | 723                   | 549                  |
| Other                   | 50,121     | -                           | 50,121                | 41,093               |
|                         | \$ 269,488 | \$ 88,059                   | \$ 181,429            | \$ 128,942           |

Note: At December 31, 2007, the purchase price allocation of certain intangible amounts was not determinable and recorded as "Other". During the six months ended June 30, 2008, the preliminary purchase price allocation was determined and the amounts were allocated as follows: \$24,210 to technology assets, \$8,275 to customer assets, \$732 to backlog, and \$7,876 to goodwill. At September 30, 2008 "Other" includes intangibles assets relating to the preliminary purchase price allocation for the acquisition of Maximus Inc.'s Justice, Education, and Asset Solutions businesses. The allocations will be finalized over the next four quarters.

## 7. Credit facilities:

The Company has an operating line-of-credit with a Canadian chartered bank in the amount of \$105,000 (December 31, 2007 - \$50,000). The line-of-credit bears a variable interest rate and is due in full on April 28, 2011. It is secured by a general security agreement covering the majority of the assets of the Company and its subsidiaries, and is subject to various standard debt covenants. As at September 30, 2008, \$54,700 (December 31, 2007 - \$19,342) had been drawn from this credit facility, and letters of credit totalling \$12,000 (December 31, 2007 - \$7,186) were issued, which limits the borrowing capacity on a dollar-for-dollar basis. Interest expense paid on the line-of-credit for the nine months ended September 30, 2008 totalled \$1,190.



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## 8. Shareholder loans:

Share purchase loans receivable of \$1,055 (December 31, 2007 - \$1,915) under the Company's share purchase plan are included as a reduction of shareholders' equity. Interest rates on these loans range from 5.0% to 6.5% depending on the year the loan was advanced. The balances outstanding are secured by the shares for which they were used to purchase.

The following table summarizes the shareholder loan activity for the period:

---

|                                 |    |       |
|---------------------------------|----|-------|
| Balance at December 31, 2007    | \$ | 1,915 |
| Repayment of shareholder loans  |    | (885) |
| Interest                        |    | 51    |
| Currency translation adjustment |    | (26)  |
| <hr/>                           |    |       |
| Balance, September 30, 2008     | \$ | 1,055 |

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## 9. Income taxes:

The Company operates in various tax jurisdictions, and accordingly, the Company's income is subject to varying rates of tax. Losses incurred in one jurisdiction cannot be used to offset income taxes payable in another. The Company's ability to use income tax losses and future income tax deductions is dependent upon the profitable operations of the Company in the tax jurisdictions in which such losses or deductions arise. As of September 30, 2008, the Company had total net future tax assets of \$4,610 (December 31, 2007 - \$4,986) and total future tax liabilities of \$23,129 (December 31, 2007 - \$21,585).

In assessing the valuation of future income tax assets, management considers whether it is more likely than not that some portion or all of the future income tax assets will be realized. The ultimate realization of future income tax assets is dependent upon the generation of future taxable income during the years in which the temporary differences are deductible. Management considers the scheduled reversals of future income tax liabilities, the character of the income tax assets, and tax planning strategies in making this assessment. To the extent that management believes that the realization of the future income tax assets does not meet the more likely than not realization criterion, a valuation allowance is recorded against the future tax assets.

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## 10. Income per share:

|  | Three months ended<br>September, 30 |          | Nine months ended<br>September, 30 |          |
|--|-------------------------------------|----------|------------------------------------|----------|
|  | 2008                                | 2007     | 2008                               | 2007     |
|  | (Unaudited)                         |          | (Unaudited)                        |          |
| Numerator:                             |                                     |          |                                    |          |
| Net income                             | \$ 3,293                            | \$ 3,326 | \$ 11,024                          | \$ 9,470 |
| Denominator:                           |                                     |          |                                    |          |
| Weighted average number<br>of shares:  |                                     |          |                                    |          |
| Basic                                  | 21,153                              | 21,119   | 21,130                             | 21,107   |
| Effect of dilutive securities:         |                                     |          |                                    |          |
| Shares secured by<br>shareholder loans | 39                                  | 73       | 62                                 | 85       |
| Diluted                                | 21,192                              | 21,192   | 21,192                             | 21,192   |
| Net income per share:                  |                                     |          |                                    |          |
| Basic                                  | \$ 0.16                             | \$ 0.16  | \$ 0.52                            | \$ 0.45  |
| Diluted                                | 0.16                                | 0.16     | 0.52                               | 0.45     |

## 11. Capital risk management:

The Company's objectives in managing capital are to ensure sufficient liquidity to pursue its strategy of organic growth combined with strategic acquisitions and to provide returns to its shareholders. The Company manages its capital with the objective of ensuring that there are adequate capital resources while maximizing the return to shareholders through the optimization of the debt and equity balance. The capital structure of the Company consists of cash, credit facilities and components of shareholders' equity including deficit and capital stock.

The Company is subject to certain covenants on its credit facilities. The covenants include a leverage ratio and an interest coverage ratio, as well as a minimum net worth requirement. The Company monitors the ratios on a monthly basis. As at September 30, 2008, the Company is in compliance with the covenants on its credit facilities. Other than the covenants required for the credit facilities, the Company is not subject to any externally imposed capital requirements.

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## 11. Capital risk management (continued):

The Company's policy is to pay annual dividends, subject to Board approval, based on the Company's financial results. The Board of Directors will determine if and when dividends should be declared and paid based on all relevant circumstances, including the desirability of financing further growth of the Company and its financial position at the relevant time. There is no guarantee that dividends will continue to be paid in the future. In addition, the Company is restricted, pursuant to financial covenants under its operating line of credit, from paying dividends of more than 20% of its consolidated adjusted net income as defined in the agreement.

The Company makes adjustments to its capital structure in light of general economic conditions, the risk characteristics of the underlying assets and the Company's working capital requirements. In order to maintain or adjust its capital structure, the Company, upon approval from its Board of Directors, may pay dividends, increase or decrease the line of credit or undertake other activities as deemed appropriate under the specific circumstances. The Board of Directors reviews and approves any material transactions not in the ordinary course of business, including significant acquisitions or other major investments.

## 12. Financial risk management and financial instruments:

### (a) Overview:

The Company is exposed to risks of varying degrees of significance which could affect its ability to achieve its strategic objectives for growth. The main objectives of the Company's risk management process are to ensure that risks are properly identified and that the capital base is adequate in relation to those risks. The principal financial risks to which the Company is exposed are described below.

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## 12. Financial risk management and financial instruments (continued):

### (b) Market risk:

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

The Company manages risk related to fluctuations in the market prices of its publicly traded investments by regularly conducting financial reviews of publicly available information to ensure that any risks are within established levels of risk tolerance. The Company does not routinely engage in risk management practices such as hedging, derivatives or short selling with respect to its publicly traded investments.

The following table details the Company's sensitivity to a 1% strengthening in the market price of the marketable securities it currently holds. For a 1% weakening in the market price, there would be an equal and opposite impact on net income and comprehensive income.

|                      |    |     |
|----------------------|----|-----|
| Net income           | \$ | -   |
| Comprehensive income |    | 113 |

The Company is exposed to interest rate risk on the utilized portion of its credit facilities and does not currently hold any financial instruments that mitigate this risk. Management does not believe that the impact of interest rate fluctuations on the current level of borrowings will be significant and, therefore, has not provided a sensitivity analysis of the impact of fluctuations on net income and comprehensive income. A breakdown of the components of interest expense (income) amount recorded on the financial statements is as follows:

|   | Three months ended |       | Nine months ended |        |
|---|--------------------|-------|-------------------|--------|
|   | September 30,      |       | September 30,     |        |
|   | 2008               | 2007  | 2008              | 2007   |
| Interest expense on credit facilities (Other financial liability) | \$ 324             | \$ 22 | \$ 1,190          | \$ 113 |
| Interest income on notes receivable (Loans and receivables)       | (149)              | (168) | (446)             | (168)  |
| Bank interest (Held for trading)                                  | (41)               | (78)  | (176)             | (269)  |
| Interest income on shareholder loans                              | (14)               | (25)  | (51)              | (74)   |
|   | 120                | (249) | 517               | (398)  |

The Company operates internationally, giving rise to exposure to market risks from changes in foreign exchange rates. The Company currently does not use derivative instruments to hedge its exposure to those risks. Most of the Company's businesses are organized geographically so that many of its expenses are incurred in the same currency as its revenues thus mitigating some of its exposure to currency fluctuations.

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## 12. Financial risk management and financial instruments (continued):

### *Foreign currency sensitivity analysis:*

The Company is mainly exposed to fluctuations in the Canadian dollar and British pound. The major currency exposures, as of September 30, 2008, are summarized in USD equivalents in the following table. The local currency amounts have been converted to USD equivalents using the period end exchange rates.

|   | Canadian Dollar   | British Pound   |
|---|-------------------|-----------------|
| Cash  | \$ 895            | \$ 3,040        |
| Restricted cash   | -                 | -               |
| Short-term investments and marketable securities available for sale | -                 | 5,368           |
| Accounts receivable   | 6,876             | 5,973           |
| Other financial assets  | 4,844             | 4,415           |
| Accounts payable and accrued liabilities                            | (15,585)          | (4,183)         |
| Other financial liabilities   | (5,801)           | (5,053)         |
| Shareholder loans   | 219               | 35              |
| <b>Net financial assets</b>   | <b>\$ (8,551)</b> | <b>\$ 9,595</b> |

The following table details the Company's sensitivity to a 1% strengthening of the Canadian dollar and British pound on net income and comprehensive income against the U.S. dollar. The sensitivity analysis includes foreign currency denominated monetary assets and liabilities and adjusts their translation at period end for a 1% change in foreign currency rates. For a 1% weakening against the U.S. dollar, there would be an equal and opposite impact on net income and comprehensive income.

|                      | Canadian Dollar Impact | British Pound Impact |
|----------------------|------------------------|----------------------|
| Net income           | \$ (86)                | \$ 42                |
| Comprehensive income | (86)                   | 96                   |

### (c) Liquidity risk:

Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due or can do so only at excessive cost. The Company manages liquidity risk through the management of its capital structure and financial leverage, as outlined in note 11 to the unaudited interim consolidated financial statements. The Company's growth is financed through a combination of the cash flows from operations and borrowing under the existing credit facilities. One of management's primary goals is to maintain an optimal level of liquidity through the active management of the assets and liabilities as well as the cash flows. The Company's credit facilities are disclosed in note 7 to the unaudited interim consolidated financial statements. As at September 30, 2008, the undrawn portion of the Company's bank credit facility was \$38,300. Utilizations include advances borrowed under the bank credit facility and issuances of letters of credits.

The majority of the Company's financial liabilities recorded in accounts payable and accrued liabilities are due within 60 days. Holdbacks payable are due within two years.

Given the Company's available liquid resources as compared to the timing of the payments of liabilities, management assesses the Company's liquidity risk to be low.

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## 12. Financial risk management and financial instruments (continued):

### (d) Credit risk:

Credit risk represents the financial loss that the Company would experience if a counterparty to a financial instrument, in which the Company has an amount owing from the counterparty failed to meet its obligations in accordance with the terms and conditions of its contracts with the Company. The carrying amount of the Company's financial assets represents the Company's maximum credit exposure.

The Company manages credit risk related to accounts receivable by maintaining reserves for potential credit losses and returns, but historically has not experienced any significant losses related to individual customers or groups of customers in any particular industry or geographic area. Also, the majority of the accounts receivable balance relates to maintenance invoices to customers that have a history of payment. As at September 30, 2008, 33% of the Company's accounts receivable balance is over 90 days past due which is in line with the balance at December 31, 2007. Accounts receivable are net of allowance for doubtful accounts of \$4,084 at September 30, 2008 (December 31, 2007 - \$2,227).

There is no significant credit risk associated with the Company's short term investments. The Company manages its credit risk related to short-term investments by conducting financial and other assessments of these investments on a regular basis.

The Company manages credit risk related to notes receivable by monitoring the results of the business to which the note relates, and maintaining security over the assets of the business.

The Company manages credit risk related to cash by maintaining bank accounts with Schedule 1 banks.

In the ordinary course of business the Company and its subsidiaries have provided performance bonds and other guarantees for the completion of certain customer contracts. The Company has not experienced a loss to date and future losses are not anticipated; therefore, no liability has been recorded in the unaudited interim consolidated balance sheets related to these types of indemnifications or guarantees at September 30, 2008.

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## 12. Financial risk management and financial instruments (continued):

### (e) Financial instruments:

#### (i) Classification of financial instruments

|  | Classification              | Measurement    |
|--|-----------------------------|----------------|
| Cash   | Held for trading            | Fair value     |
| Restricted cash                                  | Held for trading            | Fair value     |
| Short term investments and marketable securities | Available for sale          | Fair value     |
| Accounts receivable                              | Loans and receivables       | Amortized cost |
| Notes receivable                                 | Loans and receivable        | Amortized cost |
| Share purchase warrants                          | Held for trading            | Fair value     |
| Other long-term assets                           | Loans and receivables       | Amortized cost |
| Bank indebtedness                                | Other financial liabilities | Amortized cost |
| Accounts payable and accrued liabilities         | Other financial liabilities | Amortized cost |
| Holdbacks on acquisitions                        | Other financial liabilities | Amortized cost |

#### (ii) Fair values of financial instruments

The carrying values of cash, restricted cash, accounts receivable, bank indebtedness, accounts payable, accrued liabilities, acquisition holdbacks, and accrued liabilities approximate their fair values due to the short-term nature of these instruments.

The fair values of short-term investments, which are publicly traded, are determined by the quoted market values for each investment (note 4).

Notes receivable are recorded at amortized cost, which approximates the fair value.

Warrants which are not publicly traded are fair valued using valuation techniques and adjusted by the Company after considering the fair value of the underlying security and the strike price of the warrants. As at September 30, 2008, there was a decrease of \$134 in the fair value of the warrants as compared to December 31, 2007.

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## 13. Segmented information:

The Company has a number of operating subsidiaries, which have been aggregated into two reportable segments in accordance with CICA Handbook Section 1701. The Company's Public Sector segment develops and distributes software solutions primarily to government and government-related customers. The Company's Private Sector segment develops and distributes software solutions primarily to commercial customers.

The accounting policies of the segments are the same as those described in the significant accounting policies in note 1 of the 2007 annual financial statements. The Company evaluates performance of the Public Sector businesses and the Private Sector businesses based on several factors, of which the primary financial measures are revenue and earnings (loss) from operations. The Company defines earnings (loss) from operations as earnings (loss) prior to: amortization of intangible assets, (gain) loss on sale of short-term investments and marketable securities and other assets, interest expense (income), foreign exchange gains and losses, inter-company expenses and income taxes.



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## 13. Segmented information (continued):

(a) Reportable segments:

| Three months ended September 30, 2008   | Public Sector | Private Sector | Other    | Total     |
|---|---------------|----------------|----------|-----------|
| Revenue   | \$ 55,359     | \$ 25,431      | \$ -     | \$ 80,790 |
| Cost of revenue   | 21,751        | 7,971          | -        | 29,722    |
|   | 33,608        | 17,460         | -        | 51,068    |
| Research and development  | 8,071         | 3,785          | -        | 11,856    |
| Sales and marketing   | 5,703         | 3,227          | -        | 8,930     |
| General and administration  | 9,541         | 4,998          | -        | 14,539    |
| Depreciation  | 619           | 264            | -        | 883       |
|   | 23,934        | 12,274         | -        | 36,208    |
| Income before the undernoted  | 9,674         | 5,186          | -        | 14,860    |
| Amortization of intangible assets   | 6,374         | 3,265          | 70       | 9,709     |
| Gain on sale of short-term investments,<br>marketable securities and other assets | 6             | 9              | -        | 15        |
| Loss on held for trading investments related to<br>mark to market adjustments     | -             | -              | 134      | 134       |
| Interest expense (income), net  | (40)          | 1              | 159      | 120       |
| Foreign exchange (gain) loss  | 318           | (132)          | (10)     | 176       |
| Inter-company expenses (income)   | 270           | 911            | (1,181)  | -         |
| Income before income taxes  | 2,746         | 1,132          | 828      | 4,706     |
| Income taxes (recovery):  |               |                |          |           |
| Current   | 1,512         | 758            | (187)    | 2,083     |
| Future  | (356)         | (314)          | -        | (670)     |
|   | 1,156         | 444            | (187)    | 1,413     |
| Net Income  | \$ 1,590      | \$ 688         | \$ 1,015 | \$ 3,293  |
| Other selected information:   |               |                |          |           |
| Property and equipment purchased  | \$ 684        | \$ 190         | \$ -     | \$ 874    |

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## 13. Segmented information (continued):

| Nine months ended September 30, 2008  | Public Sector | Private Sector | Other    | Total      |
|---|---------------|----------------|----------|------------|
| Revenue   | \$ 156,442    | \$ 75,693      | \$ -     | \$ 232,135 |
| Cost of revenue   | 63,136        | 23,838         | -        | 86,974     |
|   | 93,306        | 51,855         | -        | 145,161    |
| Research and development  | 22,938        | 11,875         | -        | 34,813     |
| Sales and marketing   | 16,536        | 10,276         | -        | 26,812     |
| General and administration  | 26,687        | 14,702         | -        | 41,389     |
| Depreciation  | 1,738         | 771            | -        | 2,509      |
|   | 67,899        | 37,624         | -        | 105,523    |
| Income before the undernoted  | 25,407        | 14,231         | -        | 39,638     |
| Amortization of intangible assets   | 17,407        | 9,419          | 180      | 27,006     |
| Gain (loss) on sale of short-term investments, marketable securities and other assets | 29            | 8              | (46)     | (9)        |
| Loss on held for trading investments related to mark to market adjustments            | -             | -              | 134      | 134        |
| Interest expense (income), net  | (143)         | (22)           | 682      | 517        |
| Foreign exchange gain   | 94            | (295)          | (286)    | (487)      |
| Inter-company expenses (income)   | 1,033         | 2,637          | (3,670)  | -          |
| Income before income taxes  | 6,987         | 2,484          | 3,006    | 12,477     |
| Income taxes (recovery):  |               |                |          |            |
| Current   | 3,061         | 1,472          | (498)    | 4,035      |
| Future  | (1,118)       | (1,464)        | -        | (2,582)    |
|   | 1,943         | 8              | (498)    | 1,453      |
| Net Income  | \$ 5,044      | \$ 2,476       | \$ 3,504 | \$ 11,024  |
| Other selected information:   |               |                |          |            |
| Property and equipment purchased  | \$ 1,737      | \$ 609         | \$ 39    | \$ 2,385   |

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## 13. Segmented information (continued):

| Three months ended September 30, 2007   | Public Sector | Private Sector | Other   | Total     |
|---|---------------|----------------|---------|-----------|
| Revenue   | \$ 39,461     | \$ 21,113      | \$ -    | \$ 60,574 |
| Cost of revenue   | 15,564        | 6,804          | -       | 22,368    |
|   | 23,897        | 14,309         | -       | 38,206    |
| Research and development  | 5,685         | 3,442          | -       | 9,127     |
| Sales and marketing   | 4,345         | 2,382          | -       | 6,727     |
| General and administration  | 6,780         | 4,214          | -       | 10,994    |
| Depreciation  | 630           | 233            | -       | 863       |
|   | 17,440        | 10,271         | -       | 27,711    |
| Income before the undernoted  | 6,457         | 4,038          | -       | 10,495    |
| Amortization of intangible assets   | 3,684         | 1,618          | -       | 5,302     |
| Other expenses  | -             | (230)          | 300     | 70        |
| Gain on sale of short-term investments,<br>marketable securities and other assets | -             | -              | -       | -         |
| Interest expense (income), net  | (76)          | (16)           | (157)   | (249)     |
| Foreign exchange loss   | 172           | 593            | (75)    | 690       |
| Inter-company expenses (income)   | 298           | 805            | (1,103) | -         |
| Income before income taxes  | 2,379         | 1,268          | 1,035   | 4,682     |
| Income taxes (recovery):  |               |                |         |           |
| Current   | 614           | 738            | 119     | 1,471     |
| Future  | (107)         | (8)            | -       | (115)     |
|   | 507           | 730            | 119     | 1,356     |
| Net Income  | \$ 1,872      | \$ 538         | \$ 916  | \$ 3,326  |
| Other selected information:   |               |                |         |           |
| Property and equipment purchased  | \$ 337        | \$ 187         | \$ 20   | \$ 544    |

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## 13. Segmented information (continued):

| Nine months ended September 30, 2007  | Public<br>Sector | Private<br>Sector | Other    | Total      |
|---|------------------|-------------------|----------|------------|
| Revenue   | \$ 113,567       | \$ 63,388         | \$ -     | \$ 176,955 |
| Cost of revenue   | 46,005           | 20,899            | -        | 66,904     |
|   | 67,562           | 42,489            | -        | 110,051    |
| Research and development  | 16,983           | 9,916             | -        | 26,899     |
| Sales and marketing   | 13,822           | 7,271             | -        | 21,093     |
| General and administration  | 19,443           | 11,997            | -        | 31,440     |
| Depreciation  | 1,713            | 698               | -        | 2,411      |
|   | 51,961           | 29,882            | -        | 81,843     |
| Income before the undernoted  | 15,601           | 12,607            | -        | 28,208     |
| Amortization of intangible assets   | 10,014           | 4,931             | -        | 14,945     |
| Other expenses  | -                | (230)             | 300      | 70         |
| Gain on sale of short-term investments,<br>marketable securities and other assets | -                | -                 | (1,354)  | (1,354)    |
| Interest expense (income), net  | (175)            | (56)              | (167)    | (398)      |
| Foreign exchange loss   | 353              | 1,032             | 657      | 2,042      |
| Inter-company expenses (income)   | 1,204            | 1,934             | (3,138)  | -          |
| Income before income taxes  | 4,205            | 4,996             | 3,702    | 12,903     |
| Income taxes (recovery):  |                  |                   |          |            |
| Current   | 1,827            | 2,111             | 112      | 4,050      |
| Future  | (311)            | (306)             | -        | (617)      |
|   | 1,516            | 1,805             | 112      | 3,433      |
| Net Income  | \$ 2,689         | \$ 3,191          | \$ 3,590 | \$ 9,470   |
| Other selected information:   |                  |                   |          |            |
| Property and equipment purchased  | \$ 1,160         | \$ 581            | \$ 88    | \$ 1,829   |

# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

## 13. Segmented information (continued):

### (b) Geographic information:

The Company's external revenue by geographic region is based on the region in which the revenue is transacted.

|               | Three months ended September 30,<br>2008 |             | 2007             |             | Nine months ended September 30,<br>2008 |             | 2007              |             |
|---------------|--|-------------|------------------|-------------|---|-------------|-------------------|-------------|
| Canada        | \$ 12,820                                | 16%         | \$ 11,617        | 19%         | \$ 36,594                               | 16%         | \$ 28,182         | 16%         |
| United States | 56,267                                   | 70%         | 41,198           | 68%         | 161,860                                 | 70%         | 123,891           | 70%         |
| Other         | 11,703                                   | 14%         | 7,759            | 13%         | 33,681                                  | 14%         | 24,882            | 14%         |
| <b>Total</b>  | <b>\$ 80,790</b>                         | <b>100%</b> | <b>\$ 60,574</b> | <b>100%</b> | <b>\$ 232,135</b>                       | <b>100%</b> | <b>\$ 176,955</b> | <b>100%</b> |

As at September 30, 2008 and December 31, 2007 and for the nine months ended September 30, 2008 and 2007, no single customer accounted for more than 10% of the Company's total accounts receivable and total revenues, respectively.

## 14. Change in non-cash operating working capital:

|   | Three months ended<br>September 30,<br>2008 |                 | 2007            |                   | Nine months ended<br>September 30,<br>2008 |  | 2007 |  |
|---|---|-----------------|-----------------|-------------------|--|--|------|--|
| Decrease in accounts receivable   | \$ 6,866                                    | \$ 2,416        | \$ 8,515        | \$ 173            |  |  |      |  |
| Increase in work in progress  | (375)                                       | (975)           | (3,449)         | (230)             |  |  |      |  |
| Decrease (increase) in inventory  | 139   | (334)           | (202)           | (622)             |  |  |      |  |
| Decrease (increase) in prepaid expenses<br>and other current assets   | (304)                                       | 1,166           | 522             | 598               |  |  |      |  |
| Increase (decrease) in accounts payable and<br>accrued liabilities excluding holdbacks from<br>acquisitions | 7,426                                       | 804             | (2,799)         | (11,698)          |  |  |      |  |
| Increase (decrease) in deferred revenue   | (4,017)                                     | (148)           | 428             | 1,167             |  |  |      |  |
| Increase (decrease) in income taxes payable   | 335   | 2,545           | (866)           | 4,045             |  |  |      |  |
|   | <b>\$ 10,070</b>                            | <b>\$ 5,474</b> | <b>\$ 2,149</b> | <b>\$ (6,567)</b> |  |  |      |  |

# CONSTELLATION SOFTWARE INC.

Notes to Interim Consolidated Financial Statements  
(In thousands of U.S. dollars, except per share amounts)

Three and nine month periods ended September 30, 2008 and 2007  
(Unaudited)

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**15. Subsequent events:**

On October 31, 2008, the Company made an offer to Gladstone PLC ("Gladstone") shareholders to purchase all outstanding shares of Gladstone for 25 pence (\$0.45) per share for a total purchase price of approximately £8,980 GBP (\$16,315).

**16. Comparative figures:**

Certain comparative figures have been reclassified to conform to the current year's presentation.