
PHONETIME INC.
CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2009
(unaudited)

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SEPTEMBER 30, 2009

NOTICE TO READER

The unaudited interim financial information of Phonetime Inc. consisting of the interim consolidated balance sheet as at September 30, 2009 and the interim consolidated statements of income (loss) and comprehensive income (loss), deficit and cash flows for the three month and nine month periods ending September 30, 2009 are the responsibility of the Company's management. They have been prepared by management and include the selection of appropriate accounting principles, judgments and estimates necessary to prepare these financial statements in accordance with Canadian generally accepted accounting principles.

These consolidated financial statements have not been reviewed by the independent external auditors of the Company, Klasner & Solomon, Chartered Accountants.

PHONETIME INC.
Consolidated Balance Sheets
At September 30

	September 30, 2009	December 31, 2008
	<i>(Unaudited)</i>	<i>(Audited)</i>
ASSETS		
Current assets		
Short-term investment	\$ 29,219	\$ 29,219
Accounts receivable	14,289,931	13,881,509
Inventories	121,248	61,707
Prepaid expenses and deposits	297,961	376,398
Future income tax assets (note 16)	67,000	67,000
	14,805,359	14,415,833
Future income tax assets (note 16)	834,669	905,423
Property and equipment (note 3)	2,321,917	1,990,611
Goodwill and other intangible assets (note 4)	15,550,112	15,525,255
	\$ 33,512,057	\$ 32,837,122
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Bank indebtedness (note 6)	\$ 5,065,153	\$ 2,713,974
Accounts payable and accrued liabilities	8,815,799	10,062,890
Customer deposits	63,402	75,791
Income taxes payable	1,579,636	1,100,983
Loan from related party (note 12)	200,000	-
Short-term loan (note 8)	250,000	-
Current portion of long-term debt (note 9)	477,670	1,530,453
Current portion of loan payable (note 10)	184,745	262,949
Current portion of capital lease obligations (note 11)	565,094	454,605
Current portion of subordinated debentures (note 12)	978,100	2,322,723
Deferred items (note 7)	368,666	515,109
	18,548,265	19,039,477
Long-term portion of deferred items (note 7)	27,716	44,345
Loan payable (note 10)	-	141,888
Capital lease obligations (note 11)	365,942	268,412
Subordinated debentures (note 12)	853,349	1,253,345
	19,795,272	20,747,467
Commitments and contingencies (notes 14 and 20)		
Shareholders' equity		
Share capital (note 15)	15,310,594	14,761,752
Warrants (note 15)	136,158	-
Contributed surplus (note 15e)	2,616,880	2,189,805
Deficit	(4,346,847)	(4,861,902)
	13,716,785	12,089,655
	\$ 33,512,057	\$ 32,837,122

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

Approved on behalf of the Board:

(signed) Wayne Silver Director (signed) Rodney Franklin Director

PHONETIME INC.
Consolidated Statements of Income and
Comprehensive Income and Deficit
Unaudited

	Three months ended		Nine months ended	
	September 30, 2009	September 30 2008	September 30 2009	September 30 2008
				<i>(Not reviewed)</i>
Sales	\$ 44,406,164	\$ 39,204,183	\$ 128,262,495	\$ 115,010,915
Cost of sales	39,211,276	33,652,608	112,170,279	99,364,079
	5,194,888	5,551,575	16,092,216	15,646,836
Operating expenses	4,510,731	3,796,237	13,458,993	10,272,855
Loss (gain) on foreign exchange	(276,621)	(128,201)	(190,611)	(197,880)
Stock based compensation	270,457	216,406	552,075	567,851
Amortization of property and equipment	248,780	216,170	627,674	638,272
Amortization of intangible assets	35,404	25,669	86,743	77,008
Interest paid financing costs	134,884	149,682	258,868	434,091
Non-cash financing costs	38,460	101,616	222,207	365,907
	4,962,095	4,377,579	15,015,949	12,158,104
Income before the undernoted and income taxes	232,793	1,173,996	1,076,267	3,488,732
Costs due to misappropriation of funds	-	-	-	228,120
Income before income taxes	232,793	1,173,996	1,076,267	3,260,612
Income tax expense (note 16)				
Current	176,781	193,623	490,458	339,546
Future income taxes	24,539	229,271	70,754	817,160
	201,320	422,894	561,212	1,156,706
Net income and comprehensive income	31,473	751,102	515,055	2,103,906
Deficit, beginning of period	(4,378,320)	(3,925,408)	(4,861,902)	(5,278,212)
Deficit, end of period	\$ (4,346,847)	\$ (3,174,306)	\$ (4,346,847)	\$ (3,174,306)
Earnings per share (note 15f)				
Basic earnings per share	\$ 0.00	\$ 0.01	\$ 0.005	\$ 0.02
Diluted earnings per share	\$ 0.00	\$ 0.01	\$ 0.005	\$ 0.02

See accompanying notes

PHONETIME INC.**Consolidated Statements of Cash Flows****Unaudited**

	Three months ended September 30		Nine months ended September 30	
	2009	2008	2009	2008
	<i>(Not reviewed)</i>			
Operating activities				
Net income	\$ 31,473	\$ 751,102	\$ 515,055	\$ 2,103,906
Non-cash items				
Amortization	284,184	241,839	714,417	715,280
Stock based compensation	270,457	216,402	552,075	567,846
Future income taxes	24,539	229,271	70,754	817,159
Unrealized foreign exchange losses (gains)	3,387	21,182	(168,843)	150,045
	614,040	1,459,796	1,683,458	4,354,236
Net change in non-cash working capital items				
Short term investment	-	-	-	29,219
Accounts receivable	(3,181,149)	(660,064)	(408,422)	(1,333,101)
Inventories	(43,248)	(1,850)	(59,541)	(4,454)
Prepaid expenses and other receivables	178,271	2,554	78,437	129,345
Dealer deposits	(6,520)	10,592	(12,389)	10,465
Accounts payable and accrued liabilities	1,979,769	739,145	(1,245,340)	(229,134)
Income taxes payable	105,000	197,932	478,653	332,642
Deferred revenue	(67,340)	53,839	(146,443)	(97,818)
	(1,035,217)	342,148	(1,315,045)	(1,162,836)
Cash flows from operating activities	(421,177)	1,801,944	368,413	3,191,400
Investing activities				
Acquisition of (proceeds) property and equipment	(76,677)	13,142	(343,229)	(223,528)
Additions to intangible assets	(111,599)	-	(111,599)	-
Cash flows from investing activities	(188,276)	13,142	(454,828)	(223,528)
Financing activities				
Issuance of share capital	423,842	-	423,842	165,000
Issuance of warrants	136,158	-	136,158	-
Long-term debt	(534,883)	(257,133)	(1,048,143)	(771,001)
Loan from related party	200,000	-	200,000	-
Short-term loan	250,000	-	250,000	-
Loan payable	(79,475)	(49,144)	(220,091)	(1,931,129)
Capital lease obligations, net	(76,890)	(121,610)	(391,185)	(396,338)
Subordinated debentures	(592,840)	(456,689)	(1,615,345)	(1,417,515)
Other debts	-	(5,899)	-	(23,706)
Cash flows from financing activities	(274,088)	(890,475)	(2,264,764)	(4,374,689)
Net increase (decrease) in cash and cash equivalents during the period	(883,541)	924,611	(2,351,179)	(1,406,817)
Bank indebtedness, beginning of period	(4,181,612)	(4,255,496)	(2,713,974)	(1,924,068)
Bank indebtedness, end of period	\$(5,065,153)	\$(3,330,885)	\$(5,065,153)	\$(3,330,885)

Supplementary disclosure of cash flow information (note 17)

See accompanying notes

PHONETIME INC.
Condensed Notes to Interim Consolidated Financial Statements
September 30, 2009
Unaudited

1) NATURE OF OPERATIONS AND GOING CONCERN

Phonetime Inc. (the "Company" or "Phonetime") provides wholesale long distance telephone services to North American and other international long distance carriers and also sells and markets long distance telephone services and calling cards to ethnic residential and small and medium business enterprise markets across Canada.

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles on a going concern basis which presumes the realization of assets and discharges of liabilities in the normal course of business for the foreseeable future.

The Company has experienced significant profitable growth in the past two years. In addition, the Company achieved Net Income of \$515,055 for the nine months ended September 30, 2009 and Net Income of \$2,103,906 for the nine months ended September 30, 2008.

The Company has implemented its growth primarily through the issuance of debt from both senior and subordinated lenders. Since the quarter ended September 30, 2008, the Company has been in violation of its senior lender's covenants and remains in violation of those covenants as at September 30, 2009. In prior quarters, the senior lender has issued tolerance letters to the Company regarding the covenant violations, subsequent to filing by the Company of its financial results and the Company believes that the bank will do so again. The Company is in discussions with several senior and subordinated lenders and while no assurance is possible management believes that they will be able to restructure its debt in the coming months. If Management are unable to restructure the Company's debt then management, the Company will have to consider additional strategic alternatives which may include, among other strategies, exploring the monetization of certain intangible assets, modification of planned operating expenditures or the sale of the Company or divisions of the Company.

The Company has a working capital deficit of \$3.74 million as at September 30, 2009 compared to \$4.6 million as at December 31, 2008 and \$5.4 million at June 30, 2009.

The Company's future operations are dependent upon its ability to secure additional funds that will mend the breach of the financial covenants under which the Company negotiated a credit facility from its bank or to enable the bank to continue to tolerate the breach of the financial covenants under which the loans were given. These factors raise substantial doubt as to the Company's ability to continue as a going concern. These consolidated financial statements do not include adjustments to the amounts and classifications of assets and liabilities that might be necessary should the Company be unable to continue as a going concern.

The notes presented in these interim consolidated financial statements do not contain all disclosures normally provided in Phonetime Inc.'s annual audited financial statements and therefore should be read in conjunction with the audited annual consolidated financial statements and notes for the year ended December 31, 2008. Management has prepared these unaudited interim consolidated financial statements following the same accounting policies and methods of their application as set out in the Phonetime Inc. consolidated financial statements for the year ended December 31, 2008, other than as set out in note 2.

2) ACCOUNTING POLICY DEVELOPMENTS

a) Goodwill and intangible assets

In February 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets," replacing Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". Various changes have been made to other sections of the CICA Handbook for consistency purposes. The new Section will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company has adopted the new standards for its fiscal year beginning January 1, 2009. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The adoption of this new Section has not had a material impact on its consolidated financial statements.

b) Convergence with International Financial Reporting Standards

The CICA Accounting Standards Board has confirmed the convergence of Canadian GAAP with International Financial Reporting Standards ("IFRS") for publicly accountable enterprises will be effective January 1, 2011. The Company's changeover date for both interim and annual financial statements is January 1, 2011. The Company is in the process of assessing the impacts on itself of the Canadian convergence initiative. There are several stages in this process that Phonetime will have to complete in order to implement IFRS standards. The first phase is to perform an initial assessment of the impact of IFRS on the Company by identifying the significant differences between existing Canadian GAAP and IFRS that is relevant and material to the Company. The second stage is the identification, evaluation and selection of the appropriate IFRS accounting policies necessary for the Company to make the changeover. This stage includes other operational considerations such as information technology requirements, internal controls over financial reporting and training. The final stage will involve integrating the new policies into the Company's financial systems and processes.

Because the Company will be required to report prior period's comparative financial information using IFRS upon the adoption of IFRS on January 1, 2011, Phonetime will effectively need to maintain two parallel books of account for its 2010 fiscal year.

The Company has undertaken a preliminary review of the various differences between Canadian GAAP and IFRS that may have a material impact on its financial reporting and will continue to do so. In respect of stage two, the Company has identified that its financial reporting technology infrastructure is not sufficient to support the accounting requirements and have begun to assess various enterprise reporting technologies that are available to it.

c) Business combinations and non-controlling interests

In January 2009, the CICA replaced existing recommendations for business combinations and non-controlling interests with Sections 1582, "Business Combinations", 1601, "Consolidated Financial Statements", and 1602, "Non-Controlling Interests". These new sections are consistent with Canadian GAAP convergence with IFRS. These sections will be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Whether the Company will be materially affected by the new recommendations will depend upon the specific facts of business combinations, if any, occurring subsequent to January 1, 2011.

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d) Credit risk and the fair value of financial assets and financial liabilities

On January 20, 2009, the Emerging Issues Committee issued EIC-173, "Credit risk and the fair value of financial assets and financial liabilities". This new EIC states that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities. This abstract is to apply to all financial asset and liabilities measured at fair value in interim and annual financial statements for periods ending on or after January 20, 2009. The Company has incorporated this information into its consideration of the fair value of its financial instruments.

3) PROPERTY AND EQUIPMENT

September 30, 2009

	Cost	Accumulated Amortization	Net book value
Furniture and fixtures	\$ 157,093	\$ 147,619	\$ 9,474
Computer and telecommunication equipment	3,263,397	2,234,997	1,028,400
Computer and telecommunication equipment under capital leases	3,256,298	2,117,498	1,138,800
Computer software	758,235	676,196	82,039
Leasehold improvements	247,409	184,205	63,204
	\$ 7,682,432	\$ 5,360,515	\$ 2,321,917

December 31, 2008

	Cost	Accumulated Amortization	Net book value
Furniture and fixtures	\$ 153,024	\$ 139,200	\$ 13,824
Computer and telecommunication equipment	2,961,485	1,935,951	1,025,534
Computer and telecommunication equipment under capital leases	2,622,161	1,844,133	778,028
Computer software	742,481	635,260	107,221
Leasehold improvements	227,546	161,542	66,004
	\$ 6,706,697	\$ 4,716,086	\$ 1,990,611

In the year to date ended September 30, 2009, \$634,136 (2008 - \$175,723) of equipment was acquired through capital lease obligations.

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Condensed Notes to Interim Consolidated Financial Statements
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4) GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill

	September 30, 2009	December 31, 2008
Goodwill – Acquisition of 100% of Symphony Holdings	\$ 14,361,424	\$ 14,361,424
Goodwill – 20% Call Select Inc.	905,468	905,468
	\$ 15,266,892	\$ 15,266,892

Other intangible assets

	September 30, 2009		December 31, 2008	
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Customer lists	\$ 624,992	\$ 341,772	\$ 283,220	\$ 258,363

5) FINANCING COSTS

Financing costs for the nine months ending September 30, 2009 are as follows:

	2009	2008
Interest on credit facility (note 6)	\$ 160,647	\$ 206,879
Interest on long-term debt (note 9)	52,958	165,669
Interest on loans payable (note 10)	23,596	55,944
Interest on capital lease obligations (note 11)	45,263	61,543
Interest on subordinated debentures (note 12)	198,611	309,963
	\$ 481,075	\$ 799,998

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6) BANK INDEBTEDNESS

On June 22, 2009, the Company's credit facility agreement was amended and is comprised of the following:

- a) A revolving demand facility of \$5,000,000 on which it had drawn \$5,000,000 at September 30, 2009 (December 31, 2008 – \$3,471,800). The amount of the draw on the line of credit is limited to 75% of accounts receivable aged less than 90 days plus 90% of receivables that have been insured by the Export Development Corporation ("EDC"). Interest under the operating line facility is based on the bank's prime lending rate plus 3.65%, which at September 30 is a rate of 5.90%.

The Company also has the ability to issue up to \$500,000 of either standby letters of credit or letters of guarantee under the operating line facility. At September 30, 2009, the Company had no standby letters of credit or guarantee outstanding.

- b) The Company arranged a \$2,500,000 non-revolving term facility to finance the purchase of its wholly-owned subsidiary, Symphony Holdings. The facility bears interest at the Bank's prime lending rate plus 8%. Principal repayments of \$154,762 per month plus interest are required until it is fully repaid by December 18, 2009 (see note 9 for future principal repayments).

Under this credit facility agreement, the Company has pledged as collateral a General Security Agreement constituting a first ranking security interest in all personal property of the Company and its subsidiaries. In addition, the Company is required to meet three financial tests on a quarterly basis related to the Company's ability to service all of its loan repayment requirements from operating cash flows as well as its ability to meet its obligations if called upon from net working capital. These financial tests were also amended (see also, Capital structure financial policies, note 19).

The Company continues to be in breach of bank financial covenants as at September 30, 2009. The Company did not meet the three ratios being the Funded debt to EBITDA, the Fixed Charge coverage and the Current ratio requirements all detailed in note 19. As a result of the delay in closing a planned subordinated debt financing (note 8), the closing of which was expected to remedy the breaches, the covenants remained in breach. The Company continues to work with the bank to remedy the situation (see also Note 1).

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7) DEFERRED ITEMS

Deferred items consist of deferred revenue from the Company's phone card division and the deferred gain on a sale-leaseback arrangement of some telecommunications equipment in 2007.

	September 30 2009	December 31 2008
Deferred revenue	\$ 346,494	\$ 492,936
Deferred gain on a sale-leaseback arrangement	49,888	66,518
	396,382	559,454
Less: current portion	(368,666)	(515,109)
	\$ 27,716	\$ 44,345

The deferred gain is amortized on a straight-line basis over four years. Included in amortization of property equipment is an amount of \$16,629 for 2009 (September 30, 2008 – \$16,629).

8) SHORT-TERM LOAN

On September 28, 2009, \$250,000 and subsequent to the quarter end a further \$200,000, was advanced to Phonetime by the lending group that the Company has been in discussions with regarding a subordinated debenture financing of up to \$5,000,000. The Loans is due and demand and bears interest of 14.5% per annum.

Phonetime continues to work with the lending group to satisfy all the pre-conditions of the subordinated debenture financing.

9) LONG-TERM DEBT

	September 30 2009	December 31 2008
Bank loan bearing interest at the bank's prime rate plus 8% per annum with monthly repayments of \$154,762 plus interest to maturity on December 18, 2009. Refer to note 6 for details of security.	\$ 464,286	\$ 1,500,000
Export Development Corporation unsecured term loan bearing interest at 8.03% per annum with quarterly repayments of US\$6,250 plus interest to maturity in December 2009	13,384	30,453
	477,670	1,530,453
Less: current portion	(477,670)	(1,030,453)
	-	500,000
Less: long-term debt reclassified to current due to breach of bank covenants, see note 6	-	(500,000)
	\$ -	\$ -

After the amendment to the credit facility agreement in June, all principal repayments on the term loan are due in the current fiscal year.

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10) LOAN PAYABLE

Loans payable relate to the acquisition of Symphony Holdings and are as follows.

	September 30 2009	December 31 2008
\$600,000 USD payable to vendors with monthly repayments of \$20,000 to maturity in June 2010 at 0% interest	\$ 184,745	\$ 404,837
	184,745	404,837
Less: current portion	(184,745)	(262,949)
	\$ -	\$ 141,888

Principal repayments due in subsequent years are as follows:

2009	60,018
2010	124,727
	\$ 184,745

11) CAPITAL LEASE OBLIGATIONS

The Company has entered into leases for certain equipment that have been capitalized. The minimum future lease payments under capital leases are as follows:

2009	\$ 183,546
2010	515,052
2011	259,330
2012	23,208
	981,136
Less: interest portion at an average rate of 5.67%	(50,100)
	931,036
Less: current portion	(565,094)
	\$ 365,942

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12) SUBORDINATED DEBENTURES

In August 2009, the holders of the convertible debentures agreed to a revision of the terms and conditions of the debentures. Under the original terms of the debentures, monthly payments of US\$176,667 were required and have been amended to US\$95,000. In addition, the term of the loans were extended by twelve months and now mature at June 30, 2011. In turn, the holders of the debentures have agreed to eliminate the conversion feature of the debenture in return for a higher rate of interest to be paid on the balance outstanding as at July 31, 2009.

The repayments converted to Canadian dollars are as follows:

2009	\$	305,154
2010		1,220,617
2011		610,309
		2,136,080
Less: interest portion at 17.4%		(304,631)
		1,831,449
Less: current portion		(978,100)
	\$	853,349

The convertible debentures had been originally classified into their debt and equity components based on fair values. On issuance, this resulted in \$4,657,979 being classified as a liability and \$370,717 being classified as equity (contributed surplus). Since the amendments have been considered to be a renegotiation of the debt instrument, the existing portion classified as equity has not been maintained.

13) RELATED PARTY TRANSACTIONS

The following table summarizes the Company's related party transactions for the period:

	September 30, 2009	June 30, 2008
Operating expenses		
Rent paid on premises owned by certain directors	\$ 108,900	\$ 74,798
Consulting fees paid to shareholders and directors	\$ 401,297	\$ 120,000
Loan from related party		
Advances from a director	\$ 200,000	\$ -

During the quarter, a director of the Company who is also an officer of the Company advanced \$200,000 to the Company that is non-interest bearing, payable on demand and unsecured. Subsequent to the quarter end, \$100,000 of this loan was repaid.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

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14) COMMITMENTS

The Company is committed to future minimum annual lease payments under various operating leases as follows:

2009	\$	161,000
2010		716,000
2011		343,000
2012		17,000
2013 and subsequent years		18,000
	\$	1,255,000

15) SHARE CAPITAL

a) Authorized:

The authorized share capital of the Company consists of 500,000 redeemable, voting, Series A special shares, and an unlimited number of common shares and special shares.

b) Issued and outstanding common shares:

September 30, 2009

	Number of Shares	Dollar Amount
Balance as at December 31, 2008	107,988,092	\$ 14,761,752
Issues of common shares for cash consideration	3,733,332	423,842
Issues of common shares for services	1,250,000	125,000
Balance as at September 30, 2009	112,971,424	\$ 15,310,594

December 31, 2008

	Number of Shares	Dollar Amount
Balance as at December 31, 2007	94,838,092	\$ 11,937,636
Shares issued on acquisition of Symphony Holdings, Inc.	12,000,000	2,520,000
Stock options exercised	1,150,000	304,116
Balance as at December 31, 2008	107,988,092	\$ 14,761,752

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15) SHARE CAPITAL (continued)

- (i) On July 17, 2009 the Company generated gross proceeds of \$560,000 through the issue of 3,733,332 units comprised of one common share and one common share purchase warrant. The warrants are exercisable at \$0.30 per common share at any time prior to their expiry date in July, 2011.
- (ii) Also in connection with the private placement, 180,000 compensation options were issued to purchase broker shares. These options may be exercised to purchase common shares of the Company at \$0.15 per share for a period of 24 months and expire on July 17, 2011.
- (iii) Also on July 17, 2009, 1,250,000 common shares were issued at a price of \$0.10 per share to settle liabilities arising from the acquisition of consulting services. The expense of \$125,000 has been included in stock based compensation expenses in the statement of income.
- (iv) On January 2, 2008, as part of the consideration to acquire 100% of the shares of Symphony Holdings Inc., 12,000,000 common shares valued at \$0.21 per share were issued to the former shareholders of Symphony.

d) Issued and outstanding warrants

September 30, 2009

	Number of Warrants	Attributed Value
Balance as at December 31, 2008	-	\$ -
Issues of common shares for cash consideration	3,733,332	136,158
Balance as at September 30, 2009	3,733,332	\$ 136,158

	Warrant Exercise Price Range	Weighted Average Remaining Life	Number
Balance as at December 31, 2008	\$ -	-	-
Warrants issued in connection with private placement	\$ 0.30	1.79 years	3,733,332
Balance as at September 30, 2009	\$ 0.30	1.79 years	3,733,332

d) Stock option plan:

The Company has a stock option plan under which, the maximum aggregate number of shares which may be granted shall not exceed 18,600,000 subject to adjustment or increase of such numbers pursuant to changes in the capital stock of the Company.

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15) SHARE CAPITAL (continued)

d) Stock option plan (continued):

At September 30, 2009, common shares of the Company were reserved as follows for stock options:

Price	Expiry Date	Number
\$0.10	December 2010	1,388,000
\$0.10	August 2014	500,000
\$0.15	October 2011	1,145,330
\$0.432	January 2012	2,000,000
\$0.45	February 2012	1,000,000
\$0.18	December 2012	1,950,500
\$0.28	August 2013	500,000

Options granted vest over a period not exceeding three years and the purchase price is payable in full at the time the options are exercised.

A summary of the status of the stock option plan as of September 30, 2009 and December 31, 2008, and changes during the periods ended on those dates is presented below:

Options	September 30 2009		December 31 2008	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding at beginning of period	7,983,830	\$ 0.24	13,531,330	\$ 0.22
Granted	500,000	0.10	750,000	\$ 0.32
Exercised	-	-	(1,150,000)	\$ 0.14
Forfeited	-	-	(5,147,500)	\$ 0.18
Outstanding at end of period	8,483,830	\$ 0.22	7,983,830	\$ 0.24
Options exercisable period end	4,614,497	\$ 0.23	4,468,386	\$ 0.23

Included in options are 3,225,000 options issued to the officers and directors of the Company at an average exercise price of \$0.32.

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15) SHARE CAPITAL (continued)

d) Stock option plan (continued):

The following table summarized information about stock options outstanding at September 30, 2009:

Options Outstanding			
Range of Exercise Prices	Number Outstanding September 30, 2009	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
\$ 0.10 - \$0.17	3,033,330	2.12 years	\$0.119
\$ 0.18 - \$0.27	2,950,500	2.88 years	\$0.211
\$ 0.28 - \$0.432	2,500,000	2.50 years	\$0.402

Options Exercisable			
Range of Exercise Prices	Number Outstanding September 30, 2009	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
\$ 0.10 - \$0.17	2,099,997	1.51 years	\$0.117
\$ 0.18 - \$0.27	1,014,500	2.93 years	\$0.269
\$ 0.28 - \$0.432	1,500,000	2.38 years	\$0.415

For the year to date, the Company has recognized a compensation expense of \$427,075 for previously granted stock option awards.

The fair value of options granted is estimated at the attribution date using the Black-Scholes options pricing model using the average exercise price and vesting period along with assumptions for the average risk free interest rate and the average expected annual volatility of the Company's market price.

	August 31 2009
Total options granted	500,000
Average exercise price	\$ 0.10
Risk free interest rate	3.20%
Vesting period	3 years
Expected annual volatility	158%

For purposes of calculating compensation cost, the fair value of stock options is recognized over the graded vesting period of the stock options.

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15) SHARE CAPITAL (continued)

e) Contributed surplus:

The following is a continuity of the changes in contributed surplus arising from the issue and exercise of options and the equity portion of debt instruments issued.

	September 30 2009	December 31 2008
Opening balance	\$ 2,189,805	\$ 1,612,817
Stock-based compensation expense during the period	427,075	716,104
Allocated to share capital on exercise of options during the period	-	(139,116)
Ending balance	\$ 2,616,880	\$ 2,189,805

f) Earnings per share:

Earnings per share is calculated using the weighted average number of common shares outstanding throughout the period.

	Basic	Fully Diluted
Balance, September 30, 2009	108,298,409	108,568,124
Balance, September 30, 2008	107,548,676	131,484,429

The following table sets forth the computation of basic and diluted earnings per share:

	September 30 2009	September 30 2008
Numerator for basic earnings per share	\$ 515,055	\$ 2,103,906
Denominator:		
Weighted average number of common shares	108,298,409	107,548,676
Dilutive effect of stock options and warrants	269,714	23,935,753
Denominator for diluted earnings per share	108,568,124	131,484,429
Earnings per share		
Basic	\$ 0.00	\$ 0.02
Diluted	\$ 0.00	\$ 0.02

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f) Earnings per share (continued):

The following lists the equity securities excluded from the computation of diluted earnings per share because the exercise prices exceeded the average market value of the common shares of \$0.12 (2008 - \$0.34) for the current year and because they were anti-dilutive in the previous year.

	September 30 2009	September 30 2008
Stock options	6,595,830	-
Warrants	3,913,332	-
Convertible debentures	-	3,785,000

16) INCOME TAXES

For the nine months ended, September 30, 2009 Income tax expense differs from the amounts which would be obtained by applying the combined Canadian basic Federal and Provincial tax rate at approximately 33.5% (2008 - 35.00%) and US Federal and State income tax rate at approximately 36.5% (2008 - 38.00%) to earnings before income taxes.

	September 30 2009	September 30 2008
Income taxes based on combined income tax rate	\$ 367,412	\$1,190,123
Non deductible expenses	264,259	352,647
Change in valuation allowance	(70459)	(386,064)
Income tax expense	\$ 561,212	\$1,156,706

The Company currently has non-capital losses of approximately \$2,045,000 which expires as follows:

Years	\$
2010	198,000
2014	281,000
2015	288,000
2026	508,000
2027	770,000
	\$ 2,045,000

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16) INCOME TAXES (continued)

Significant components of the Company's future income tax assets are as follows:

	September 30 2009	December 31 2008
Potential tax benefit related to:		
Non-capital losses carried forward	\$ 720,581	\$ 774,837
Tax value of property and equipment and intangible assets in excess of accounting value	181,088	197,586
Total future income tax assets	901,669	972,423
Less: Current portion	(67,000)	(67,000)
Future income tax assets	\$ 834,669	\$ 905,423

17) SUPPLEMENTARY DISCLOSURE OF CASH FLOW INFORMATION

	September 30 2009	September 30 2008
Acquisition of property and equipment through lease obligations	\$ 634,136	\$ 175,723
Common shares issued for consulting services	\$ 125,000	-
Common shares issued on Symphony purchase	\$ -	\$ 2,520,000
Interest paid	\$ 258,868	\$ 434,091

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18) SEGMENTED INFORMATION

The Company's reportable segments are consumer sales and services ("Consumer") and global wholesale telecommunications ("Wholesale"). The consumer sales and services division includes its original calling card business as well as a 1+ Equal Access long distance service for consumers and small and medium size enterprises. The calling card business represents less than 5% of the Company's total sales and therefore has been included as part of the Consumer segment. The Wholesale division provides long distance call origination and delivery services for switchless long distance resellers and VoIP service providers on a wholesale basis.

The Company accounts for intersegment revenues and expenses at either prices that approximate current market prices or costs, depending upon the type of service. Substantially all of the intersegment revenue that is eliminated represents international long distance costs to terminate traffic on behalf of the Consumer division which in turn records it as a cost of sale.

The following table provides further segmented information.

Three month periods ended
September 30
['000s]

	Wholesale		Consumer		Corporate		Eliminations		Consolidated	
	2009	2008	2009	2008	2009	2008	2009	2008	2009	2008
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Operating revenues										
External revenue	36,388	32,665	8,018	6,539	-	-	-	-	44,406	39,204
Intersegment revenue	6,312	5,648	-	-	-	-	(6,312)	(5,648)	-	-
	42,700	38,313	8,018	6,539	-	-	(6,312)	(5,648)	44,406	39,204
Cost of sales										
External cost of sales	38,421	32,431	790	1,222	-	-	-	-	39,211	33,653
Intersegment cost of sales	1,395	2,534	4,917	3,114	-	-	(6,312)	(5,648)	-	-
	39,816	34,965	5,707	4,336	-	-	(6,312)	(5,648)	39,211	33,653
Gross margin	2,884	3,348	2,311	2,203	-	-	-	-	5,195	5,551
Operating expenses									4,505	3,884
EBITDA (1)									690	1,667
Capital expenditures	72	(27)	5	14	-	-	-	-	77	(13)
Total Assets	31,640	27,622	6,399	5,522	5,083	6,494	(9,593)	(9,313)	33,529	30,325
Goodwill and other Intangible assets	14,361	14,361	1,189	1,190	-	-	-	-	15,550	15,551

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18) SEGMENTED INFORMATION (continued)

Geographically, the Company purchases and sells products and services in Canada and the United States and Internationally. Geographic disclosures are as follows:

	September 30 2009	September 30 2008
Revenue:		
Canada	\$ 22,607,735	\$ 9,916,099
U.S. and international	105,654,760	105,094,816
	\$ 128,262,495	\$115,010,915

Revenues are attributed to countries based on the location of the customer.

	September 30 2009	September 30 2008
Property and equipment and intangibles		
Canada	\$ 3,476,042	\$ 3,059,554
U.S.	14,395,987	14,429,965
	\$ 17,872,029	\$ 17,489,519

19) CAPITAL STRUCTURE FINANCIAL POLICIES

The Company's objectives when managing capital are (i) to maintain an acceptable level of liquidity risk so that the Company can continue to cover its financial obligations and investment requirements under its current business model and (ii) to enhance shareholder value by maintaining an efficient cost of capital.

The Company manages capital through the monitoring of a number of measures, being the working capital ratio, funded debt to Earnings Before Interest, Taxes, Depreciation and Amortization excluding stock compensation costs and misappropriation costs (EBITDA) and fixed charges to EBITDA on a trailing four quarter basis.

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19) CAPITAL STRUCTURE FINANCIAL POLICIES (continued)

The ratios the Company monitors are as follows (see also notes 6 and 9).

September 30, 2009

Components of debt and coverage ratios

Total funded debt	8,490,053
Short term portion of funded debt	7,270,762
EBITDA (rolling four quarters, as adjusted)(note)	2,560,440
Free cash flow (note)	1,715,282
Financing costs, (rolling four quarters, as adjusted)	703,199

Debt ratio

Funded debt to EBITDA, as adjusted ratio 3.32 (required - <1.75)

Coverage ratios

Fixed charge coverage 0.54 (required - >0.85)
 Current ratio 0.80 (required - >0.90)

Note: The calculations of EBITDA and Free cash flow do not have any standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers.

The reconciliation of EBITDA is as follows:

['000s]	Quarter ended				Total
	December 31 2008	March 31 2009	June 30 2009	September 30 2009	
EBITDA for the quarter	\$(75)	\$ 1,038	\$ 913	\$ 684	\$ 2,560
Add/deduct					
Foreign exchange gain (loss)	957	(177)	263	(277)	766
Stock based compensation	148	179	104	271	702
Amortization	255	255	176	284	970
Financing costs	222	161	147	174	704
Income tax expense	23	384	(24)	201	584
Net income	\$(1,680)	\$ 236	\$ 247	\$ 31	\$ (1,166)

Free cash flow as calculated for bank purposes ('000s):

EBITDA, total for the rolling four quarters, per above	\$ 2,560
Deduct:	
Income tax payments made in the four quarter period	215
Capital expenditures in the four quarter period	630
	<u>\$ 1,715</u>

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Funded debt is calculated as follows.

September 30, 2009

Bank indebtedness	\$ 5,065,153
Long-term debt including short term portion	477,670
Loan payable and other debts including short-term portion	184,745
Subordinated debentures	1,831,449
Capital lease obligations	931,036
<hr/>	
Total funded debt	\$ 8,490,053
<hr/>	
Portion of funded debt that is current	
Bank indebtedness	\$ 5,065,153
Long-term debt	477,670
Long payable and other debts	184,745
Convertible debentures	978,100
Capital lease obligations	565,094
<hr/>	
Current portion of funded debt	\$ 7,270,762

20) COMPETITON BUREAU CLAIM

Subsequent to the quarter end, the Company signed an agreement with the Competition Bureau and paid a \$300,000 penalty which had been previously accrued. The settlement requires that the Company place corrective notices in a number of national newspapers, the details of which are in the process of being confirmed. As a result, the Company has accrued a further \$50,000 to cover such advertising expenditures that will be incurred in the fourth quarter.

21) FINANCIAL INSTRUMENT RISK MANAGEMENT

a) Fair value

The Company's financial instruments include short-term investments, accounts receivable, bank indebtedness, accounts payable and accrued liabilities, current income taxes, customer deposits, capital lease obligations, long-term debt, loans payable, convertible debentures and other debts. Due to the short-term nature of short-term investments, accounts receivable, bank indebtedness, accounts payable and accrued liabilities and income tax payable, the carrying values of these financial instruments are reasonable estimates of their fair value. Capital lease obligations, long-term debt, loans payable, convertible debentures and other debts are carried at amortized cost using the effective interest rate method. The fair values of these financial instruments reflect the Company's best estimate based upon estimated interest rates at which the Company believes it could enter into with similar instruments at the consolidated balance sheet date and approximate carrying values.

19) FINANCIAL INSTRUMENT RISK MANAGEMENT (continued)

b) Credit risk

The Company's exposure to credit risk arises from the possibility that its customers may fail to meet their obligations. The Company has credit evaluation, approval and monitoring processes, and insurance of certain accounts receivable from the Export Development Corporation of Canada which mitigates these potential credit risks. The Company continually evaluates the collectability of accounts receivable and records an allowance for doubtful accounts, which reduces the receivables to the amount management, reasonably believes will be collected. A specific allowance is recorded against customer receivables that are considered to be impaired based upon the Company's knowledge of the financial condition of its customers. The failure of a large customer would have a significant effect on the Company.

Short-term investment consists of investments with maturities between 90 days and one year at the date of purchase. Short-term investment held by the Company has consisted of guaranteed investment certificates, treasury bills and money market funds held with a Canadian financial institution. All short-term investments have been classified as held for trading and are carried at fair value with gains or losses recorded in the Statement of Operations. Transaction costs are expensed as incurred.

The carrying amount of accounts receivable and short-term investments represents the maximum credit exposure.

c) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, long distance rates and interest rates will affect the Company's net earnings or the value of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

d) Currency risk

Approximately 76% and 71% of the Company's purchases and sales, respectively, are denominated in U.S. dollars and consequently, those related liabilities and receivable balances are exposed to foreign exchange fluctuations. As at September 30, accounts payable to U.S. suppliers was \$5,240,000 (December 31, 2008 - \$7,412,000) and accounts receivable from U.S. customers was \$11,784,000 (December 31, 2008 - \$10,903,000). While purchases and sales amounts in U.S. are approximately equal and may reflect a natural hedge, or mitigation of currency risk; the difference between the amounts of accounts receivable and payable better indicate the risk that arises due to the timing of settlement of customer and vendor accounts. In periods where the Canadian dollar is strengthening versus the US dollar, the Company is susceptible to realizing foreign exchange losses between the time when a sale is recorded, a carrier paid and the receivable ultimately collected. In turn, outstanding debt commitments denominated in U.S. dollars (notes 10 and 12) will be settled with fewer Canadian dollars and therefore result in foreign exchange gains.

21) FINANCIAL INSTRUMENT RISK MANAGEMENT (continued)

e) Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate risk related to its credit facility agreement where both the revolving demand facility and the non-revolving term facility have interest rates tied to the lending Bank's prime lending rate. In the current year the term rate declines and as the Company continues to repay the debt the exposure to rising prime lending rates declines. Other current and long-term obligations bear no interest or are at fixed interest rates.

f) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The Company's exposure to liquidity risk is dependent on the collection of accounts receivable, the sale of inventory and the settlement of obligations and arranging to obtain funds to meet commitments and sustain operations. The Company controls liquidity risk by management of working capital and cash flows as well as ensuring the availability of borrowing facilities and regular consideration of additional equity placements.