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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

[x] QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED September 30, 2006

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT

Commission File No. 000-28423

VALIDIAN CORPORATION
(Exact name of small business issuer as specified in its charter)

NEVADA	**58-2541997**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

30 Metcalfe Street, Ottawa, Ontario, Canada K1P 5L4
(Address of principal executive offices)

Issuer's telephone number: 613-230-7211

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes [ ] No [X]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 37,940,068 Shares of the issuer's Common Stock were outstanding as of November 16, 2006.

Transitional Small Business Disclosure Format: Yes [ ] No [X]

SEC 2334 (9-05) **Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.**

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
CONSOLIDATED CONDENSED BALANCE SHEETS
(Unaudited)

	September 30, 2006	December 31, 2005
Assets		(restated)
Current assets:		
Cash and cash equivalents	$ 1,917	$ 71,193
Accounts receivable (note 13(b))	12,800	75,995
Prepaid expenses	185,487	246,917
	200,204	394,105
Property and equipment, net of accumulated depreciation of $167,663 (December 31, 2005 - $134,701)	49,161	96,868
Deferred consulting services	--	50,349
Deferred financing costs (note 3)	114,497	--
Total assets	$ 363,862	$541,322
Liabilities and Stockholders' Deficiency		
Current liabilities:		
Accounts payable and accrued liabilities (notes 12(a) and 13(b))	$ 1,291,226	$ 509,768
Promissory notes payable (note 4)	712,880	296,321
Deferred revenue	155,000	25,000
Current portion of capital lease obligation (note 5)	5,020	4,031
10% Senior secured convertible notes payable (notes 6 and 7)	--	--
Total current liabilities	2,164,126	835,120
10% Senior convertible notes payable (note 7)	70,649	--
Capital lease obligation (note 5)	2,982	6,547
Total liabilities	2,237,757	841,667
Stockholders' Deficiency:		
Common stock, ($0.001 par value. Authorized 100,000,000 shares; Issued and outstanding 36,081,691 and 32,883,691 shares at September 30, 2006 and December 31, 2005, respectively.)	36,081	32,883
Preferred stock ($0.001 par value. Authorized 7,000,000 shares; issued and outstanding Nil shares at September 30, 2006 and at December 31, 2005)	--	--
Additional paid in capital	21,731,685	20,951,097
Deficit accumulated during the development stage	(23,613,227)	(21,255,891)
Retained earnings prior to entering development stage	21,304	21,304
Treasury stock (7,000 shares at September 30, 2006 and December 31, 2005, at cost)	(49,738)	(49,738)
Total stockholders' deficiency	(1,873,895)	(300,345)
Basis of presentation (note 1)		
Guarantees and Commitments (note 13)		
Subsequent events (note15)		
Total liabilities and stockholders' deficiency	$363,862	$541,322

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Condensed Statements of Operations
For the three and nine months ended September 30, 2006 and 2005
And for the Period from August 3, 1999 to September 30, 2006
(Unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005	Period from August 3, 1999 to September 30, 2006
Operating expenses (income):		(restated)		(restated)	
Selling, general and administrative (note 13(b))	$481,349	$ 494,137	$1,476,149	$1,739,401	$10,959,600
Research and development	192,496	315,674	792,487	978,536	7,767,914
Depreciation	14,745	20,897	47,707	64,280	372,396
Gain on sale of property and equipment	--	--	--	--	(7,442)
Write-off of prepaid services	--	--	--	--	496,869
Write-off of deferred consulting services	--	--	--	--	1,048,100
Write-off of accounts receivable	--	--	--	--	16,715
Write-off of due from related party	--	--	--	--	12,575
Loss on cash pledged as collateral for operating lease	--	--	--	--	21,926
Write-down of property and equipment	--	--	--	--	14,750
	688,590	830,708	2,316,343	2,782,217	20,703,403
Loss before other income (expenses) and income taxes	(688,590)	(830,708)	(2,316,343)	(2,782,217)	(20,703,403)
Other income (expenses):					
Interest income	32	5,012	195	24,658	61,017
Gain on extinguishment of debt (note 10)	34,347	--	34,347	--	127,854
Interest and financing costs (note 9)	(127,761)	(68,205)	(191,604)	(546,257)	(3,163,507)
Other	(3,994)	(5,378)	(4,223)	(7,768)	(55,480)
	(97,376)	(68,571)	(161,285)	(529,367)	(3,030,116)
Loss before income taxes	(785,966)	(899,279)	(2,477,628)	(3,311,584)	(23,733,519)
Deferred income tax provision (note 2(g))	2,834	(11,048)	120,292	(141,084)	120,292
Net loss	$(783,132)	$(910,327)	$(2,357,336)	$(3,452,668)	$(23,613,227)
Loss per share – basic and diluted (note 11)	$(0.02)	$(0.03)	$(0.07)	$(0.11)	
Weighted average number of common shares outstanding during period	35,617,843	31,593,019	34,039,303	31,417,018	

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Statements of Changes in Stockholders' Equity (Deficiency) and Comprehensive Loss
For the period from December 31, 1998 to September 30, 2006
(Unaudited)

	Number	Common stock amount	Additional paid-in capital	Retained earnings prior to entering development stage	Deficit accumulated during development stage	Accumulated other compre-hensive income (loss)	Treasury stock	Total
			(restated)		(restated)			
Balances at December 31, 1998	61,333	$ 61	$ 23,058	$ 30,080	$ –	$ (7,426)	$ –	$ 45,773
Issued for mining claims	92,591	92	27,408	–	–	–	–	27,500
Issued for cash	3,000,000	3,000	27,000	–	–	–	–	30,000
Reverse acquisition	8,459,000	8,459	21,541	–	–	–	–	30,000
Fair value of warrants issued to unrelated parties	–	–	130,000	–	–	–	–	130,000
Shares issued upon exercise of warrants	380,000	380	759,620	–	–	–	–	760,000
Share issuance costs	–	–	(34,750)	–	–	–	–	(34,750)
Comprehensive loss:							–	
Net loss	–	–	–	(8,776)	(743,410)	–	–	(752,186)
Currency translation adjustment	–	–	–	–	–	11,837	–	11,837
Comprehensive loss								(740,349)
Balances at December 31, 1999	11,992,924	11,992	953,877	21,304	(743,410)	4,411	–	248,174
Shares issued upon exercise of warrants	620,000	620	1,239,380	–	–	–	–	1,240,000
Share issuance costs	–	–	(62,000)	–	–	–	–	(62,000)
Acquisition of common stock	–	–	–	–	–	–	(49,738)	(49,738)
Comprehensive loss:								
Net loss	–	–	–	–	(2,932,430)	–	–	(2,932,430)
Currency translation adjustment	–	–	–	–	–	(40,401)	–	(40,401)
Comprehensive loss								(2,972,831)
Balances at December 31, 2000	12,612,924	12,612	2,131,257	21,304	(3,675,840)	(35,990)	(49,738)	(1,596,395)
Shares issued in exchange for debt	2,774,362	2,774	2,216,715	–	–	–	–	2,219,489
Fair value of warrants issued to unrelated parties	–	–	451,500	–	–	–	–	451,500
Comprehensive loss:								
Net loss	–	–	–	–	(1,448,485)	–	–	(1,448,485)
Currency translation adjustment	–	–	–	–	–	62,202	–	62,202
Comprehensive loss								(1,386,283)
Balances at December 31, 2001	15,387,286	$15,386	$4,799,472	$21,304	$(5,124,325)	$26,212	$(49,738)	$(311,689)

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Statements of Changes in Stockholders' Equity (Deficiency) and Comprehensive Loss
For the period from December 31, 1998 to September 30, 2006
(Unaudited)

	Number	Common stock amount	Additional paid-in capital	Retained earnings prior to entering develop-ment stage	Deficit accumulated during development stage	Accumulated other compre-hensive income (loss)	Treasury stock	Total
			(restated)		(restated)			
Balances at December 31, 2001	15,387,286	$ 15,386	$ 4,799,472	$ 21,304	$ (5,124,325)	$ 26,212	$ (49,738)	$ (311,689)
Shares issued in consideration of consulting services	340,500	340	245,810	–	–	–	–	246,150
Comprehensive loss:								
Net loss	–	–	–	–	(906,841)	–	–	(906,841)
Currency translation adjustment on liquidation of investment in foreign subsidiary	–	–	–	–	–	(26,212)	–	(26,212)
Comprehensive loss								(933,053)
Balances at December 31, 2002	15,727,786	15,726	5,045,282	21,304	(6,031,166)	–	(49,738)	(998,592)
Shares issued in exchange for debt	4,416,862	4,417	1,453,147	–	–	–	–	1,457,564
Shares issued in consideration of consulting and financing services	422,900	423	230,448	–	–	–	–	230,871
Fair value of warrants issued to unrelated parties for services	–	–	2,896,042	–	–	–	–	2,896,042
Fair value of stock purchase options issued to unrelated parties for services	–	–	597,102	–	–	–	–	597,102
Relative fair value of warrants issued to investors in conjunction with 4% senior subordinated convertible debentures	–	–	355,186	–	–	–	–	355,186
Intrinsic value of beneficial conversion feature on 4% convertible debentures issued to unrelated parties	–	–	244,814	–	–	–	–	244,814
Deferred income taxes recognized on the temporary basis difference between accounting value and face value of the 4% senior subordinated debentures	–	–	(204,000)	–	–	–	–	(204,000)
Net loss and comprehensive loss	–	–	–	–	(2,797,900)	–	–	(2,797,900)
Balances at December 31, 2003	20,567,548	$ 20,566	$10,618,021	$ 21,304	$ (8,829,066)	$ –	$ (49,738)	$ 1,985,087

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Statements of Changes in Stockholders' Equity (Deficiency) and Comprehensive Loss
For the period from December 31, 1998 to September 30, 2006
(Unaudited)

	Number	Common stock amount	Additional paid-in capital (restated)	Retained earnings prior to entering development stage	Deficit accumulated during development stage (restated)	Accumulated other comprehensive income (loss)	Treasury stock	Total
Balances at December 31, 2003	20,567,548	$ 20,566	$10,618,021	$21,304	$(8,829,066)	$ –	$(49,738)	$1,781,087
Shares issued in exchange for debt	464,000	464	429,536	–	–	–	–	430,000
Shares issued on conversion of 4% senior subordinated convertible debentures	2,482,939	2,483	1,238,986	–	–	–	–	1,241,469
Deferred financing costs transferred to additional paid in capital on conversion of 4% senior subordinated convertible debentures into common shares	–	–	(721,097)	–	–	–	–	(721,097)
Shares issued pursuant to private placement of common shares and warrants	6,666,666	6,667	5,993,333	–	–	–	–	6,000,000
Cost of share issuance pursuant to private placement	–	–	(534,874)	–	–	–	–	(534,874)
Shares issued in consideration of consulting and financing services	70,000	70	72,730	–	–	–	–	72,800
Shares issued in consideration of penalties on late registration of shares underlying the 4% senior subordinated convertible debentures	184,000	184	110,216	–	–	–	–	110,400
Fair value of stock purchase warrants issued to unrelated parties for services	–	–	809,750	–	–	–	–	809,750
Relative fair value of warrants issued to investors in conjunction with 4% senior subordinated convertible debentures	–	$ –	$ 861,522	$ –	$ –	$ –	$ –	$ 861,522

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Statements of Changes in Stockholders' Equity (Deficiency) and Comprehensive Loss
For the period from December 31, 1998 to September 30, 2006
(Unaudited)

	Number	Common stock amount	Additional paid-in capital	Retained earnings prior to entering development stage	Deficit accumulated during development stage	Accumulated other comprehensive income (loss)	Treasury stock	Total
			(restated)		(restated)			
Intrinsic value of beneficial conversion feature on 4% convertible debentures issued to unrelated parties	–	–	538,478	–	–	–	–	538,478
Deferred income tax recovery recognized on the temporary basis difference between accounting value and face value of the 4% senior subordinated debentures	–	–	51,705	–	–	–	–	51,705
Net loss and comprehensive loss	–	–	–	–	(8,068,871)	–	–	(8,068,871)
Balances at December 31, 2004	30,435,153	30,434	19,468,306	21,304	(16,897,937)	–	(49,738)	2,572,369
Shares issued on conversion of 4% senior subordinated convertible debentures	1,157,866	1,158	577,774	–	–	–	–	578,932
Shares issued in settlement of 4% senior subordinated convertible debentures at maturity	485,672	486	242,349	–	–	–	–	242,835
Deferred financing costs transferred to additional paid in capital on conversion of 4% senior subordinated convertible debentures into common shares	–	–	(163,980)	–	–	–	–	(163,980)
Fair value of stock purchase options issued to unrelated parties for services rendered	–	–	211,496	–	–	–	–	211,496
Fair value of modifications to stock purchase warrants previously issued to unrelated parties	–	–	61,162	–	–	–	–	61,162
Shares issued on the exercise of stock purchase warrants	805,000	805	401,695	–	–	–	–	402,500
Deferred income tax recovery recognized on the temporary basis difference between accounting value and face value of the 4% senior subordinated debentures	–	–	152,295	–	–	–	–	152,295
Net loss and comprehensive loss	–	–	–	–	(4,357,954)	–	–	(4,357,954)
Balances at December 31, 2005	32,883,691	$ 32,883	$20,951,097	$ 21,304	$ (21,255,891)	$ -	$(49,738)	$ (300,345)

See accompanying notes to unaudited interim period consolidated condensed financial statements.

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
Consolidated Statements of Changes in Stockholders' Equity (Deficiency) and Comprehensive Loss
For the period from December 31, 1998 to September 30, 2006
(Unaudited)

	Number	Common stock amount	Additional paid-in capital	Retained earnings prior to entering development stage	Deficit accumulated during development stage	Accumulated other comprehensive income (loss)	Treasury stock	Total
			(restated)		(restated)			
Balances at December 31, 2005	32,883,691	$ 32,883	$20,951,097	$ 21,304	$ (21,255,891)	$ –	$(49,738)	$ (300,345)
Shares issued in consideration of consulting services (notes 3 and 8(a))	628,000	628	104,672	–	–	–	–	105,300
Fair value of unvested employee stock options earned during period (note 8(d))	–	–	27,590	–	–	–	–	27,590
Reversal of fair value of unvested employee stock options recognized in the current and prior periods, on forfeiture of the options (note 8(d))	–	–	(2,259)	–	–	–	–	(2,259)
Shares issued on the exercise of stock purchase warrants (note 8(b))	20,000	20	9,980	–	–	–	–	10,000
Shares issued pursuant to the terms of the 10% senior secured convertible notes (note 6)	1,000,000	1,000	169,000	–	–	–	–	170,000
Shares issued pursuant to the terms of the 10% senior convertible notes (note 7)	200,000	200	23,550	–	–	–	–	23,750
Shares issued pursuant to the terms of the 10% promissory note (note 4)	1,000,000	1,000	149,000	–	–	–	–	150,000
Shares issued pursuant to the terms of an agreement to extend the payment terms of finance fees payable (note 8(a))	100,000	100	11,400	–	–	–	–	11,500
Shares issued in satisfaction of Finance fees payable, which were included in accounts payable and accrued liabilities (note 8(a))	250,000	250	28,500	–	–	–	–	28,750
Intrinsic value of beneficial conversion feature on the 10% senior secured convertible notes issued to unrelated parties (notes 6 and 7)	–	–	330,000	–	–	–	–	330,000
Intrinsic value of beneficial conversion feature on the 10% senior convertible notes issued to unrelated parties (note 7)	–	–	49,447	–	–	–	–	49,447
Deferred income taxes recognized on the temporary basis difference between accounting value and face value of the 10% senior secured convertible notes, the 10% senior convertible notes and the 10% promissory notes (note 2(g))	–	–	(120,292)	–	–	–	–	(120,292)
Net loss and comprehensive loss	–	–	–	–	(2,357,336)	–	–	(2,357,336)
Balances at September 30, 2006	36,081,691	$ 36,081	$21,731,685	$ 21,304	$ (23,613,227)	$ -	$(49,738)	$ (1,873,895)

See accompanying notes to unaudited interim period consolidated condensed financial statements

VALIDIAN CORPORATION AND SUBSIDIARIES
A DEVELOPMENT STAGE ENTERPRISE
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
For the nine months ended September 30, 2006 and 2005
And for the Period from August 3, 1999 to September 30, 2006
(Unaudited)

	Nine Months Ended September 30,		Period from August 3, 1999 to September 30,
	2006	2005	2006
Cash flows from operating activities:		(restated)	
Net loss	$ (2,357,336)	$(3,452,668)	$ (23,613,227)
Adjustments to reconcile net loss to net cash used in Operating activities:			
Depreciation of property and equipment	47,707	64,280	372,396
Non-cash compensation expense	210,366	250,983	2,449,213
Non-cash interest and financing expense	189,474	544,033	3,159,967
Non-cash penalties	11,500	--	121,900
Write-off of prepaid services	--	--	496,869
Write-off of deferred consulting services	--	--	1,048,100
Currency translation adjustment on liquidation of investment in foreign subsidiary	--	--	(26,212)
Gain on sale of property and equipment	--	--	(7,442)
Loss (gain) on extinguishment of debt	(34,347)	--	(127,854)
Write-off of accounts receivable	--	--	16,715
Write-off of due to related party	--	--	12,575
Loss on cash pledged as collateral for operating lease	--	--	21,926
Write-down of property and equipment	--	--	14,750
Deferred income tax provision (recovery)	(120,292)	141,084	(120,292)
Increase (decrease) in cash resulting from changes in:			
Accounts receivable	63,195	(9,401)	(1,037)
Prepaid expenses	(13,256)	13,263	(135,983)
Due to a related party	--	--	(5,178)
Accounts payable and accrued liabilities	686,222	101,872	2,750,112
Deferred revenue	130,000	25,000	155,000
Net cash used in operating activities	(1,186,767)	(2,321,554)	(13,417,702)
Cash flows from investing activities:			
Additions to property and equipment	--	(33,013)	(526,543)
Proceeds on sale of property and equipment	--	--	176,890
Cash pledged as collateral for operating lease	--	--	(21,926)
Net cash used in investing activities	--	(33,013)	(371,579)
Cash flows from financing activities:			
Capital lease repayments	(2,576)	(1,933)	(6,764)
Increase in due from related party	--	--	12,575
Issuance of common shares	--	--	8,030,000
Share issuance costs	--	--	(631,624)
Proceeds from exercise of stock purchase warrants	10,000	--	412,500
Redemption of common stock	--	--	(49,738)
Issuance of promissory notes	551,177	--	3,659,908
Issuance of 4% senior subordinated convertible debentures	--	--	2,000,000
Issuance of 10% senior secured convertible notes (notes 6 and 7)	500,000	--	500,000
Issuance of 10% senior convertible notes	100,000	--	100,000
Debt issuance costs	(36,500)	--	(268,279)
Repayment of promissory notes	(4,610)	--	(20,610)
Net cash provided by (used in) financing activities	1,117,491	(1,933)	13,737,968
Effects of exchange rates on cash and cash equivalents	--	--	18,431
Net increase (decrease) in cash and cash equivalents	(69,276)	(2,356,500)	(32,882)
Cash and cash equivalents:			
Beginning of period	71,193	2,747,975	34,799
End of period	$ 1,917	$ 391,475	$ 1,917

See accompanying notes to unaudited interim period consolidated condensed financial statements.

Validian Corporation (the "Company") was incorporated in the State of Nevada on April 12, 1989 as CCC Funding Corp. The Company underwent several name changes before being renamed to Validian Corporation on January 28, 2003.

Since August 3, 1999, the efforts of the Company have been devoted primarily to the development of a high speed, highly secure method of exchanging data files using the internet, and to the sale and marketing of the Company's products. Prior to August 3, 1999, the Company provided consulting services for web site implementation, multimedia CD design, computer graphic publication, as well as implementation of dedicated software solutions used in connection with the French Minitel and the internet. As the Company commenced development activities on this date, it is considered for financial accounting purposes to be a development stage enterprise and August 3, 1999 is the commencement of the development stage.

1. Basis of Presentation

The accompanying consolidated condensed financial statements include the accounts of Validian Corporation and its wholly owned subsidiaries (collectively, the "Company") after elimination of all significant intercompany balances and transactions. The financial statements have been prepared in conformity with generally accepted accounting principles in the United States of America which require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. While management has based its assumptions and estimates on the facts and circumstances currently known, final amounts may differ from such estimates.

The interim financial statements contained herein are unaudited but, in the opinion of management, include all adjustments (consisting only of normal recurring entries) necessary for a fair presentation of the financial position and results of operations of the Company for the periods presented. The results of operations for the nine months ended September 30, 2006 are not necessarily indicative of the operating results for the full fiscal year ending December 31, 2006. Moreover, these financial statements do not purport to contain complete disclosure in conformity with generally accepted accounting principles used in the United States of America and should be read in conjunction with the Company's audited financial statements at and for the year ended December 31, 2005.

The consolidated condensed financial statements have been prepared assuming that the Company will continue as a going concern. The Company has no revenues, has a stockholders deficiency of $1,873,895 as at September 30, 2006, and has incurred a loss of $2,357,336 and negative cash flow from operations of $1,186,767 for the nine months then ended. The Company also expects to continue to incur operating losses for the foreseeable future, and has no lines of credit or other financing facilities in place.

During October 2006, the Company received cash proceeds of $500,000 from the issuance of its 10% senior convertible notes. It expects to incur operating expenditures of approximately $3 million for the year ending December 31, 2006. In the event the Company cannot raise the additional funds necessary to finance its research and development and sales and marketing activities, it may have to cease operations.

All of the factors above raise substantial doubt about the Company's ability to continue as a going concern. Management's plans to address these issues include raising capital through the private placement of equity, the exercise of previously-issued equity instruments and through the issuance of additional promissory notes. The Company's ability to continue as a going concern is subject to management's ability to successfully implement these plans. Failure to do so could have a material adverse effect on the Company's position and or results of operations and could also result in the Company ceasing operations. The consolidated financial statements do not include adjustments that would be required if the assets are not realized and the liabilities settled in the normal course of operations.

1. Basis of Presentation (continued)

Even if successful in obtaining financing in the near term, the Company cannot be certain that cash generated from its future operations will be sufficient to satisfy its liquidity requirements in the longer term, and it may need to continue to raise capital by issuing additional equity or by obtaining credit facilities. The Company's future capital requirements will depend on many factors, including, but not limited to, the market acceptance of its products and the level of its promotional activities and advertising required to generate product sales. No assurance can be given that any such additional funding will be available or that, if available, it can be obtained on terms favorable to the Company.

2. Significant Accounting Policies

(a) Property and equipment:

Property and equipment is stated at cost less accumulated depreciation, and includes computer hardware and software, furniture and equipment, equipment under capital lease and leasehold improvements. These assets are being depreciated on a straight-line basis over their estimated useful lives, as follows: computer hardware, furniture and equipment: 3 years; equipment under capital lease: over the term of the lease, being 4 years; computer software: 1 year; leasehold improvements: over the term of the lease, being 2 years.

(b) Leases:

Leases are classified as either capital or operating in nature. Capital leases are those which substantially transfer the benefits and risk of ownership to the Company. Assets acquired under capital leases are depreciated on a straight-line basis over the term of the lease, being 4 years. Obligations recorded under capital leases are reduced by the principal portion of lease payments. The imputed interest portion of lease payments is charged to expense.

(c) Deferred financing costs:

Deferred financing costs relate to the costs associated with arranging the 10% senior secured convertible notes, the 10% senior convertible notes and the 10% promissory notes. The costs are being amortized over the term of the respective notes.

(d) Deferred consulting services:

Deferred consulting services represent the portion of prepaid non-cash consulting fees for services to be rendered in periods in excess of twelve months from the balance sheet date. Prepaid non-cash consulting fees related to services to be rendered within twelve months are included in prepaid expenses on the balance sheet. These are charged to expenses as the services are rendered. If for any reason circumstances arise which would indicate that the services will not be performed in the future, these prepaid non-cash consulting fees are charged to expense immediately.

(e) Revenue recognition:

For sales of product licenses, the Company recognizes revenue in accordance with Statement of Position 97-2, "Software Revenue Recognition" ("SOP 97-2"), as amended by Statement of Position 98-9, "Software Revenue Recognition with Respect to Certain Transactions", issued by the American Institute of Certified Public Accountants. Revenue from sale of product licenses is recognized when all of the following criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectibility is probable.

Revenue from product support contracts is recognized ratably over the life of the contract. Revenue from services is recognized at the time such services are rendered.

2. Significant Accounting Policies (continued)

(e) Revenue recognition (continued):

For contracts with multiple elements such as product licenses, product support and services, the Company follows the residual method. Under this method, the total fair value of the undelivered elements of the contract, as indicated by vendor specific objective evidence, is deferred and subsequently recognized in accordance with the provisions of SOP 97-2. The difference between the total contract fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. Vendor specific objective evidence for support and consulting services is obtained from contracts where these elements have been sold separately. Where the Company cannot determine the fair value of all of the obligations, the revenue is deferred until such time as it can be determined or the element is delivered.

(f) New accounting policy - stock based compensation:

Effective January 1, 2006, the Company adopted the provisions of Financial Accounting Standards Board Statement No. 123R "Share-Based Payment – a revision of FAS 123" (SFAS 123R) to account for its stock-based payments. SFAS 123R requires all share-based payments, including stock options granted by the Company to its employees, to be recognized as expenses, based on the fair value of the share-based payments at the date of grant. For purposes of estimating the grant date fair value of stock-based compensation, the Company uses the Black Scholes option-pricing model, and has elected to treat awards with graded vesting as a single award. The fair value of awards granted is recognized as compensation expense on a straight-line basis over the requisite service period, which in the Company's circumstances is the stated vesting period of the award.

In adopting SFAS 123R, the Company has applied the modified-prospective transition method. Under this method, the Company will recognize compensation costs for all share-based payments granted, modified, or settled after January 1, 2006, as well as for any awards that were granted prior to January 1, 2006 for which the requisite service had not been provided as of that date (unvested awards). Under the modified prospective method, prior periods are not adjusted, and the Company continues to provide pro forma disclosure for these periods, as presented below.

For reporting periods ending on or before December 31, 2005, the Company applied the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations including FASB Interpretation No. 44, "Accounting for Certain Transactions involving Stock Compensation an interpretation of APB Opinion No. 25" issued in March 2000, to account for its stock options granted to employees. Under this method, compensation expense was recorded on the date of grant only if the then current market price of the underlying stock exceeded the exercise price. Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. These provisions were required to be applied to stock compensation granted to non-employees. As permitted by SFAS No. 123, the Company elected to apply the intrinsic value-based method of accounting described above for awards granted to employees, and adopted the disclosure requirements of SFAS No. 123, for reporting periods ending on or before December 31, 2005.

2. Significant accounting policies (continued)

(f) New accounting policy - stock based compensation (continued):

Had compensation costs in respect of options granted to employees been determined using the fair value based method at the grant date, the Company's pro forma net loss and basic and diluted loss per share for the three and nine months ended September 30, 2005 would have been as follows:

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net loss, as reported (restated)	$(910,327)	$(3,452,668)
Add stock-based employee compensation expense included in net loss	--	--
Deduct total stock-based employee compensation expense determined under the fair value-based method for all awards	(3,363)	(961,451)
Pro forma net loss	$(913,690)	$(4,414,119)
Loss per share:		
Basic and diluted - as reported	$(0.03)	$(0.11)
Basic and diluted – pro forma	$(0.03)	$(0.14)

(g) New accounting policy – income tax consequences of issuing convertible debt with a beneficial conversion feature:

In September 2005, the FASB ratified the consensus reached by the Emerging Issues Task Force ("EITF") on Issue 05-8, "Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature" ("EITF 05-8"). The Task Force reached the following consensus:

- The issuance of convertible debt with a beneficial conversion feature results in a basis difference in applying FASB Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes." Recognition of such a feature effectively creates a debt instrument and a separate equity instrument for reporting purposes, whereas the convertible debt is treated entirely as a debt instrument for income tax purposes;
- The resulting basis difference should be deemed a temporary difference because it will result in a taxable amount when the recorded amount of the liability is recovered or settled;
- Recognition of deferred income tax for the temporary difference should be reported as an adjustment to additional paid-in capital.

The foregoing consensus is effective for reporting periods commencing after December 15, 2005, and is required to be applied retrospectively to all debt instruments containing beneficial conversion features that are subject to EITF 00-27, "Application of Issue No. 98-5 to Certain Convertible Debt Instruments," and thus is applicable to debt instruments converted or extinguished in prior periods but which are still presented in the financial statements.

2. Significant accounting policies (continued)

(g) New accounting policy – income tax consequences of issuing convertible debt with a beneficial conversion feature (continued):

The Company has accounted for the effect of applying the consensus retrospectively with respect to its 4% senior subordinated convertible debentures, which matured on December 31, 2005. The effects of this change on the comparative information presented in the current financial statements are an increase in deferred income tax expense and net loss for the three and nine months ended September 30, 2005 of $11,048 and $141,084, respectively. Additional paid-in capital, net loss and comprehensive loss and deficit accumulated during the development stage presented in the consolidated statement of changes in stockholders' equity (deficiency) and comprehensive loss for the period from December 31, 1998 to September 30, 2006 have been adjusted as follows: additional paid-in capital for the years ended December 31, 2003, 2004 and 2005 has increased (decreased) by ($204,000), $51,705 and $152,295, respectively; net loss and comprehensive loss, and deficit accumulated during the development stage for the years ended December 31, 2003, 2004 and 2005 have been increased (decreased) by $(204,000), $51,705 and $152,295, respectively.

During the nine months ended September 30, 2006, the Company issued $500,000 of its 10% senior secured convertible notes (note 6). At the date of issuance, the conversion feature of the notes was "in-the-money," and was valued at $330,000. The value of the beneficial conversion feature was allocated to additional paid in capital, to be accreted to notes payable through periodic charges to interest expense over the term of the notes. The temporary basis difference between accounting value and income tax value of the notes which occurred as a result of this allocation, has been accounted for in accordance with the consensus. Accordingly, a deferred tax liability of $104,652 was recorded through an adjustment to additional paid-in capital; and a deferred tax asset of $104,652 was recognized, with a corresponding credit to deferred income tax expense on the income statement. On July 11, 2006, the 10% senior secured convertible notes were modified. As a result of this modification, the deferred tax liability of $104,652 and the deferred tax asset of $104,652 were written off, with corresponding adjustments to additional paid-in capital and deferred income tax recovery on the statement of operations, respectively.

During the nine months ended September 30, 2006, the Company also issued $100,000 of its 10% senior convertible notes (note 7). At the date of issuance, the conversion feature of the notes was "in-the-money," and was valued at $49,447. Additionally, as noted above, the Company modified the terms of the $500,000 senior secured convertible notes, effectively removing the security feature and extending the maturity date by one year. At the date of the modification, the conversion feature of the 10% senior convertible notes was "in-the money," and was valued at $330,000. The value of the beneficial conversion features was allocated to additional paid in capital, and will be accreted to notes payable through periodic charges to interest expense over the term of the notes. The temporary basis difference between accounting value and income tax value of the notes which occurred as a result of this allocation, has been accounted for in accordance with the consensus. A deferred tax liability of $120,292 has been recorded through an adjustment to additional paid-in capital; and a deferred tax asset of $120,292 has been recognized, with a corresponding credit to deferred income tax expense on the income statement. The deferred tax liability and the deferred tax asset have been offset on the unaudited condensed balance sheet.

2. Significant accounting policies (continued)

(g) New accounting policy – income tax consequences of issuing convertible debt with a beneficial conversion feature (continued):

The temporary basis difference relating to the above notes will result in periodic adjustments to reflect changes in the respective balances of accounting value and tax value of the notes, until the notes are repaid in full.

3. Deferred financing costs

The following table sets forth the cost and accumulated amortization of the deferred financing costs:

	September 30, 2006	December 31, 2005
Balance deferred financing costs, beginning of period	$ --	$ 281,224
Additions		
Fees paid or payable in cash	90,250	--
Fair value of fees paid through the issuance of 328,000 common shares of the Company	45,300	--
	135,550	--
Amortization		
Amortization of fees payable in cash	(15,181)	(117,244)
Amortization of fees payable in common stock of the Company	(5,872)	--
	(21,053)	(117,244)
Financing costs transferred to additional paid in capital on conversion of $555,000 in principal value of the 4% senior subordinated convertible debentures into common shares of the Company	--	(163,980)
Balance deferred financing costs, end of period	$ 114,497	$ --

During the nine months ended September 30, 2006, the Company issued a total of $500,000 in principal amount of 10% senior secured convertible notes (note 6), $100,000 in principal amount of 10% senior convertible notes (note 7), and $250,000 in principal of 10% promissory notes (note 4). In connection with the placement of these notes, the Company incurred costs totaling $135,550, of which $90,250 was paid or payable in cash and $45,300 was paid through the issuance of 328,000 common shares of the Company. These costs are being amortized over the term of the respective notes.

During December 2003 and January 2004, the Company issued a total of $2,000,000 in principal amount of 4% senior subordinated convertible debentures. In connection with the placement of the debentures, the Company incurred costs of $1,486,279, of which $1,254,500 was financed through the issuance of the Company's Series H warrants and common shares. These costs were amortized over the term of the debentures, which matured on December 31, 2005.

4. Promissory Notes Payable

	September 30, 2006	December 31, 2005
Promissory notes payable, bearing interest at 12%, due on demand; unsecured	$ 592,888	$ 296,321
Promissory notes payable, bearing interest at 10%, due July 13, 2007; unsecured	119,992	--
	$ 712,880	$ 296,321

During the nine months ended September 30, 2006, the Company issued $301,177 in principal amount of its12% promissory notes.

On July 13, 2006, in conjunction with the modification of the 10% senior secured promissory notes (note 6), the Company issued $250,000 in principal amount of its 10% promissory notes. The notes mature on July 13, 2007, and are unsecured. Under the terms of the notes, the Company may pre-pay all or any portion of the balance outstanding on the notes at any time, without penalty or bonus; interest is payable at maturity. The note and accrued interest thereon must be repaid immediately upon receipt by the Company of $500,000 in financing from a pre-identified source.

Holders of the notes were granted 1,000,000 common shares of the Company upon issuance of the notes. In accordance with APB 14, "Accounting for Convertible Debt and Debt issued with Stock Purchase Warrants," $150,000, representing the relative fair value of the shares at the issuance date, was allocated to the shares.

The 10% promissory notes are being accreted to their face value on an effective yield basis, through periodic charges to interest expense over the term of the notes.

During the three months ended September 30, 2006, the Company accreted the notes payable through charges to interest expense totaling $19,992**.**

The following table sets forth the financial statement presentation of the note proceeds on issuance:

Note proceeds	$ 250,000
Allocated to common stock and additional paid-in capital for market value of stock issued to holders of the notes:	
Allocated to common stock	(1,000)
Allocated to additional paid-in capital	(149,000)
	(150,000)
Proceeds allocated to 10% promissory notes upon issuance	$ 100,000

The following table sets forth the changes in the financial statement presentation of the balance allocated to 10% promissory notes at September 30, 2006:

Proceeds allocated to 10% promissory notes upon issuance	$ 100,000
Accretion of the 10% promissory notes as a charge to interest and financing costs during the period	19,992
Balance allocated to 10% promissory notes, end of period	$ 119,992

5. Capital Lease Obligation

During April 2004, the Company entered into a capital lease arrangement in respect of office equipment. Future minimum payments remaining under this agreement are approximately as follows:

Year ended December 31:	
2006	$ 1,626
2007	6,504
2008	1,626
Total minimum lease payments	9,756
Less amount representing interest, at 23.9%	1,754
Present value of net minimum lease payments	8,002
Current portion of capital lease obligation	5,020
	$ 2,982

6. 10% Senior secured convertible notes payable

On June 1, 2006, the Company issued a total of $500,000 of its 10% senior secured convertible notes. The notes were secured by a first position lien on all of the assets of the Company, and had a maturity date of June 1, 2007. Under the terms of the notes, the holders were permitted, at any time, to convert all or a portion of the outstanding principal plus accrued interest into common stock of the Company at a ratio of one common share for each $0.10 of debt converted; the Company had the option of pre-paying all or any portion of the balance outstanding on the notes at any time, without penalty or bonus; and interest was payable quarterly, in arrears. Additionally, the holders could demand repayment of 50% of the principal value of the note, at such time as the Company completed an equity financing of $500,000 or more.

Holders of the notes were also granted 1,000,000 common shares of the Company upon issuance of the notes. In accordance with APB 14, "Accounting for Convertible Debt and Debt issued with Stock Purchase Warrants,"$170,000, representing the relative fair value of the shares at the issuance date, was allocated to the shares.

At the date of issuance, the conversion feature of the notes was "in-the-money". The intrinsic value of this beneficial conversion feature was $330,000. In accordance with EITF 98-5, "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios" and EITF 00-27, "Application of Issue No. 98-5 to Certain Convertible Instruments," this amount was recorded as additional paid-in capital.

The 10% senior secured convertible notes were being accreted to their face value on an effective yield basis, through periodic charges to interest expense over the term of the notes.

During the nine months ended September 30, 2006, the Company accreted the notes payable through charges to interest expense totaling $38,097**.**

6. 10% Senior secured convertible notes payable (continued)

The following table sets forth the financial statement presentation of the note proceeds on issuance:

Note proceeds	$ 500,000
Allocated to common stock and additional paid-in capital for market value of stock issued to holders of the notes:	
Allocated to common stock	(1,000)
Allocated to additional paid-in capital	(169,000)
	(170,000)
Allocated to additional paid-in capital for the intrinsic value of the beneficial conversion feature	(330,000)
Proceeds allocated to 10% senior secured convertible notes upon issuance	$ --

On July 11, 2006, in conjunction with the issuance of $250,000 in promissory notes (note 4), the 10% senior secured convertible notes were amended and restated as follows: the first position lien on all of the assets of the Company was removed; the date of maturity was extended by one year to June 1, 2008; the Company was given the option of paying the quarterly interest either in cash or in common shares of the Company; the provision allowing the holder to demand immediate repayment of 50% of the face value of the note in the event of an equity financing by the Company of at least $500,000, was removed. These amendments collectively resulted in the new notes being “substantially different” from the original notes, as that term is defined in EITF 96-19: “Debtor’s Accounting for a Modification or Exchange of Debt Instruments”. Accordingly, the Company has accounted for the modification as an extinguishment of the original debt, which resulted in a gain on the extinguishment of $38,097.

The following table sets forth the changes in the financial statement presentation of the balance allocated to 10% senior secured convertible notes at September 30, 2006:

Proceeds allocated to 10% senior secured convertible notes upon issuance	$ --
Accretion of the 10% senior secured convertible notes as a charge to interest and financing costs during the period	38,097
Reduction of the 10% senior secured convertible notes through gain on extinguishment of debt at date of modification	(38,097)
Balance allocated to 10% senior secured convertible notes, end of period	$ --

As a result of the modifications to the 10% senior secured convertible notes, the notes have been reclassified as 10% senior convertible notes (note 7) as of the date of the modifications.

7. 10% Senior convertible notes payable

During the nine months ended September 30, 2006, the Company issued $100,000 of its 10% senior convertible notes. The notes mature on July 1, 2008 and are unsecured. Under the terms of the notes, the holders are permitted, at any time, to convert all or a portion of the outstanding principal plus accrued interest into common stock of the Company at a ratio of one common share for each $0.10 of debt converted; the Company may pre-pay all or any portion of the balance outstanding on the notes at any time, without penalty or bonus; interest is payable quarterly, and may, at the Company's option, be paid either in cash or in common shares of the Company. If interest is paid in common shares, the number of shares required for settlement will be calculated using a 10% discount to the average closing price of the common stock, as listed on the exchange where the Company's common stock is traded, for the ten days prior to the date the interest is due to the holder.

Holders of the notes were also granted 200,000 common shares of the Company upon issuance of the notes. In accordance with APB 14, "Accounting for Convertible Debt and Debt issued with Stock Purchase Warrants," $23,750, representing the relative fair value of the shares at the issuance date, was allocated to the shares.

At the date of issuance, the conversion feature of the notes was "in-the-money". The intrinsic value of this beneficial conversion feature was $49,447. In accordance with EITF 98-5, "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios" and EITF 00-27, "Application of Issue No. 98-5 to Certain Convertible Instruments," this amount was recorded as additional paid-in capital.

In addition, $500,000 in principal amount of the Company's 10% senior secured convertible notes (note 6) were amended and restated effective July 11, 2006, to the same terms as the 10% senior convertible notes described above. As discussed in note 6, the modification was accounted for as an extinguishment of debt; accordingly, the carrying value of the 10% senior secured convertible notes was reduced to $nil at the date of modification. The principal amount assigned to the modified notes was calculated on a relative fair value basis, as follows: $170,000, representing the relative fair value of the 1,000,000 common shares granted to the holders of the 10% senior secured convertible notes at the date of their issuance, was allocated to the shares; $330,000, representing the intrinsic value of the beneficial conversion feature at the modification date, was allocated to additional paid-in capital.

The 10% senior convertible notes are being accreted to their face value on an effective yield basis, through periodic charges to interest expense over the term of the notes.

During the nine months ended September 30, 2006, the Company accreted the 10% senior convertible notes payable through charges to interest expense totaling $43,846.

7. 10% Senior convertible notes payable (continued)

The following table sets forth the financial statement presentation of the note proceeds on issuance:

Note proceeds	
10% senior convertible notes issued during the period	$ 100,000
10% senior convertible notes issued in exchange for the 10% senior secured convertible notes issued and extinguished during the period	500,000
	600,000
Allocated to common stock and additional paid-in capital for market value of stock issued to holders of the notes:	
Allocated to common stock	(1,200)
Allocated to additional paid-in capital	(192,550)
	(193,750)
Allocated to additional paid-in capital for the intrinsic value of the beneficial conversion feature	(379,447)
Proceeds allocated to 10% senior convertible notes upon issuance	$ 26,803

The following table sets forth the changes in the financial statement presentation of the balance allocated to 10% senior convertible notes at September 30, 2006:

Proceeds allocated to 10% senior convertible notes upon issuance	$ 26,803
Accretion of the 10% senior convertible notes as a charge to interest and financing costs during the period	43,846
Balance allocated to 10% senior convertible notes, end of period	$ 70,649

8. Stockholders' Equity

(a) Common stock transactions

During the nine months ended September 30, 2006, the Company issued 300,000 shares of its common stock, valued at $60,000, to an unrelated party in consideration for consulting services rendered prior to September 30, 2006.

During the nine months ended September 30, 2006, the Company issued 20,000 shares of its common stock in connection with the exercise of 20,000 Series H stock purchase warrants for cash proceeds of $10,000 (note 8(b)).

In connection with the issuance of the Company's 10% senior secured convertible notes on June 1 and June 30, 2006 (note 6), the Company issued a total of 1,000,000 of the Company's common shares, valued at $170,000, to the holders of the notes. The 10% senior secured convertible notes were modified on July 11, and replaced with 10% senior secured convertible notes.

In connection with the issuance of the Company's 10% senior convertible notes on June 30, September 1 and September 14, 2006 (note 7), the Company issued a total of 200,000 of the Company's common shares, valued at $23,750, to the holders of the notes.

In connection with the issuance of the Company's 10% promissory notes on July 13, 2006 (note 4), the Company issued a total of 1,000,000 of the Company's common shares, valued at $150,000, to the holders of the notes.

8. Stockholders' Equity (continued)

(a) Common stock transactions (continued)

During the nine months ended September 30, 2006, the Company issued 328,000 shares of its common stock, valued at $45,300, to an unrelated party in consideration for finance fees relating to the issuance of the Company's 10% senior secured convertible notes, 10% senior convertible notes and 10% promissory notes.

During the nine months ended September 30, 2006, the Company issued 100,000 shares of its common stock in exchange for the deferral of payment of fees owing, which are included in accounts payable and accrued liabilities. $11,500, representing the market value of the shares at date of issuance, has been accounted for as a penalty and is included in sales, general and administrative expenses.

During the nine months ended September 30, 2006, the Company issued 250,000 shares of its common stock, valued at $28,750, in settlement of accounts payable in the amount of $25,000.

(b) Transactions involving stock purchase warrants

On April 20, 2006, holders of the Series H warrants exercised 20,000 warrants, and purchased 20,000 shares of the Company's common stock for cash proceeds of $10,000.

Following is a description of stock purchase warrants outstanding at September 30, 2006 and December 31, 2005:

	Exercise Price	Expiry	Outstanding September 30, 2006	Outstanding December 31, 2005
Series E	$0.33	December, 2007	2,155,000	2,155,000
Series F	0.50	May, 2007	3,146,000	3,146,000
Series G	0.75	December, 2006	400,000	400,000
Series H	0.50	December, 2006	2,652,500	2,672,500
Series I	0.90	March, 2009	3,513,333	3,513,333
			11,866,833	11,886,833

(c) Transactions involving stock options

The Company has two incentive equity plans, under which a maximum of 7,000,000 options to purchase 7,000,000 common shares may be granted to officers, employees and consultants of the Company. The granting of options, and the terms associated with them, occurs at the discretion of the board of directors, who administers the plan. As of September 30, 2006, there were a total of 4,902,302 options granted under these plans, with exercise prices ranging from $0.33 to $0.90, and expiry dates ranging from May 7, 2008 to January 1, 2011. 4,577,302 of these options vested immediately upon issuance; 325,000 vest on dates ranging from November 14, 2006 to January 1, 2009. 2,097,698 options remained available for grant under these plans as of September 30, 2006.

During the nine months ended September 30, 2006, the Company granted 100,000 stock options to an employee as an incentive to enter into full-time employment with the Company. The options vest on various dates between January 1, 2007 and January 1, 2009; have an exercise price of $0.67; and an expiry date for unexercised options of January 12, 2011, with provision for early forfeiture in the event the holder ceases to be employed by the Company prior to the stated expiry date. The fair value of these options at date of grant was $19,556, determined using the following weighted average assumptions: expected dividend yield 0%; risk-free interest rate of 4.39%; expected volatility of 158%; an expected life of 5 years; and an expected forfeiture rate of 1.5%.

8. Stockholders' Equity (continued)

(a) Transactions involving stock options (continued)

In accordance with the Company's policy in respect of stock options granted to employees (note 2(f)), the Company has included $4,752, representing the fair value of these options earned during the nine month period ended September 30, 2006, in selling general and administrative expenses for the nine month period then ended. $14,804, representing the fair value of the options attributable to the period remaining until the options are fully vested, will be recognized as expense on a straight-line basis over the period from October 1, 2006 to January 1, 2009.

During the nine months ended September 30, 2006, the Company also included in expenses the following amounts related to options granted to employees during 2005, which were unvested as at December 31, 2005: $12,899 was included in selling, general and administrative expense; and $9,939 was included in research and development expense. $60,258, representing the fair value of the options attributable to the period remaining until the options are fully vested, will be recognized as expense on a straight-line basis over the remaining service periods, which range from October 1, 2006 to January 1, 2011. During the nine months ended September 30, 2006, 100,000 of the options granted to employees during 2005, which were unvested as at December 31, 2005, were forfeited as a result of the termination of the related employment agreement. In order to reflect this forfeiture, the following amounts were reversed from selling, general and administrative expenses: $184 in respect of expense recognized during the three months ended June 30, 2006; and $2,075 in respect of expense recognized during the three months ended March 31, 2006.

During the nine months ended September 30, 2006, 350,000 stock options granted to employees during 2005, which were fully vested as at December 31, 2005, expired as a result of the termination of the related employment agreements.

Following is a summary of stock options outstanding at September 30, 2006 and December 31, 2005:

	Nine months ended September 30, 2006		Year ended December 31, 2005	
	# of Options	Weighted Average Exercise Price	# of Options	Weighted Average Exercise Price
Options outstanding, beginning of period	5,252,302	$ 0.53	3,912,302	$ 0.33
Granted	100,000	0.67	2,750,000	0.73
Expired	(350,000)	0.67	(1,410,000)	0.37
Forfeited	(100,000)	0.74	--	--
Options outstanding, end of period	4,902,302	$ 0.51	5,252,302	$ 0.53

8. Stockholders' Equity (continued)

(c) Transactions involving stock options (continued)

The following table summarizes information regarding stock options outstanding at September 30, 2006:

	Options Outstanding			Options Exercisable	
Exercise price	Number outstanding At 09/30/06	Weighted average remaining contractual life	Weighted average exercise price	Number outstanding At 09/30/06	Weighted average exercise price
$ 0.33	2,602,302	2.7 years	$ 0.33	2,602,302	$ 0.33
0.50	375,000	4.2 years	0.50	225,000	0.50
0.67	400,000	4.2 years	0.67	225,000	0.67
0.76	1,475,000	3.8 years	0.76	1,475,000	0.76
0.90	50,000	2.7 years	0.90	50,000	0.90
	4,902,302		$ 0.51	4,577,302	$ 0.50

(d) Stock-based compensation

The following table presents the total of stock-based compensation included in the expenses of the Company for the three and nine months ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Selling, general and administrative:				
Relating to the amortization of prepaid consulting fees recorded in 2003 and 2005 on the issuance of warrants and on the extension of the expiry date of previously-issued warrants, respectively, in exchange for services to be rendered	$ 41,678	$ 34,033	$125,035	$ 94,452
Relating to the issuance of common stock as compensation for services rendered	--	--	60,000	156,531
Fair value of unvested employee stock options earned during period	3,199	--	17,651	--
Reversal of fair value of unvested employee stock options recognized during the current and prior periods, in respect of unvested options forfeited during the period	--	--	(2,259)	--
Total stock-based compensation included in selling, general and administrative expenses	44,877	34,033	200,427	250,983
Research and development:				
Fair value of unvested employee stock options earned during period	3,313	--	9,939	--
Total stock-based compensation included in research and development expenses	3,313	--	9,939	--
Total stock-based compensation included in expenses	$ 48,190	$34,033	$210,366	$250,983

During the nine months ended September 30, 2006, the Company was granted an extension of the payment period for finance fees payable. In exchange for this extension, the Company issued 100,000 shares of its common stock, valued at $11,500. This amount is included in general and administrative expenses for the three and nine months ended September 30, 2006.

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(Unaudited)

9. Interest and Financing Costs

The following table sets forth the charges to interest and financing costs during the three and nine months ended September 30, 2006 and 2005:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Interest and financing costs relating to 10% senior secured convertible notes:				
Accrued interest	$ 1,478	$ --	$ 5,645	$ --
Accretion of the notes payable (note 6)	10,479	--	38,097	--
Amortization of deferred financing costs (note 3)	1,571	--	5,843	--
	13,528	--	49,585	--
Interest and financing costs relating to 10% senior convertible notes:				
Accrued interest	12,598	--	12,598	--
Accretion of the notes payable (note 7)	43,846	--	43,846	--
Amortization of deferred financing costs (note 3)	7,325	--	7,325	--
	63,769	--	63,769	--
Interest and financing costs relating to 10% promissory notes:				
Accrued interest	5,400	--	5,400	--
Accretion of the notes payable (note 4)	19,992	--	19,992	--
Amortization of deferred financing costs (note 3)	7,885	--	7,885	--
	33,277	--	33,277	--
Interest and financing costs relating to 4% senior convertible debentures:				
Accrued interest	--	2,250	--	9,397
Accretion of the debentures payable	--	32,494	--	414,951
Amortization of deferred financing costs	--	23,811	--	93,096
	--	58,555	--	517,444
Accrued interest on 12% promissory notes	16,655	8,965	43,232	26,590
Interest portion of capital lease payments	532	685	1,741	2,223
Total interest and financing costs	$ 127,761	$ 68,205	$ 191,604	$ 546,257

10. Gain on extinguishment of debt

Gain on extinguishment of 10% senior secured convertible promissory notes (note 6)	$ 38,097
Loss on issuance of 250,000 common shares, valued at $28,750, in satisfaction of accounts payable totaling $25,000 (note 8(a))	(3,750)
	$ 34,347

11. Loss Per Share

For the purposes of the loss per share computation, the weighted average number of common shares outstanding has been used. Had the treasury stock method been applied to the unexercised stock options and warrants, the effect on the loss per share would be anti-dilutive.

11. Loss Per Share (continued)

The following securities could potentially dilute basic earnings per share in the future but have not been included in diluted earnings per share because their effect was antidilutive:

	September 30, 2006	September 30, 2005
Stock options	4,902,302	4,852,302
Series E stock purchase warrants	2,155,000	2,155,000
Series F stock purchase warrants	3,146,000	3,896,000
Series G stock purchase warrants	400,000	400,000
Series H stock purchase warrants	2,652,500	2,727,500
Series I stock purchase warrants	3,513,333	3,513,333
	16,769,135	17,544,135

12. Related Party Transactions

As discussed further in note 13(b), the Company subleases excess office space to a related party.

Included in accounts payable and accrued liabilities is $80,811 (December 31, 2005: $nil) in accrued salaries payable to the directors of the Company.

13. Guarantees and Commitments

(a) Guarantees

The Company has entered into agreements which contain features which meet the definition of a guarantee under FASB Interpretation No. 45 (“FIN 45”). FIN 45 defines a guarantee to be a contract that contingently requires the Company to make payments (either in cash, financial instruments, other assets, common stock of the Company or through the provision of services) to a third party based on changes in an underlying economic characteristic (such as interest rates or market value) that is related to an asset, liability or an equity security of the other party.

The Company has the following guarantees which are subject to the disclosure requirements of FIN 45:

(i) In the normal course of business, the Company entered into a lease agreement for facilities. As the lessee, the Company agreed to indemnify the lessor for liabilities that may arise from the use of the leased facility. The maximum amount potentially payable under the foregoing indemnity cannot be reasonably estimated. The Company has liability insurance that relates to the indemnification described above.

(ii) The Company includes standard intellectual property indemnification clauses in its software license and service agreements. Pursuant to these clauses, the Company holds harmless and agrees to defend the indemnified party, generally the Company’s business partners and customers, in connection with certain patent, copyright or trade secret infringement claims by third parties with respect to the Company’s products. The term of the indemnification clauses is generally perpetual any time after execution of the software license and service agreement. In the event an infringement claim against the Company or an indemnified party is successful, the Company, at its sole option, agrees to do one of the following: (i) procure for the indemnified party the right to continue use of the software; (ii) provide a modification to the software so that its use becomes non-infringing; (iii) replace the software with software which is substantially similar in functionality and performance; or (iv) refund the residual value of the software license fees paid by the indemnified party for the infringing software. The Company believes the estimated fair value of these intellectual property indemnification clauses is minimal.

13. Guarantees and Commitments (continued)

(a) Guarantees (continued)

Historically, the Company has not made any significant payments related to the above-noted indemnities and accordingly, no liability related to the contingent features of these guarantees has been accrued in the financial statements.

(b) Commitment

During April 2004, the Company entered into a lease agreement for office space. In July 2005, the option to extend the initial lease period for an additional year was exercised. Minimum annual rent payable under this contract is approximately as follows:

2006	$ 18,775
2007	25,033
Total	$ 43,808

Effective July 1, 2004, the Company also entered into an agreement to sublease excess office space to a related company. The companies are related by virtue of an officer and director of Validian Corporation being also an officer and director of the other company. Included in accounts receivable is $nil (December 31, 2005 - $5,508) in rent receivable pursuant to this sublease agreement; included in accounts payable and accrued liabilities is $2,868 (December 31, 2005 - $nil) in rent received in advance of the due date pursuant to this sublease agreement. Rental expense for the period, which is included in selling, general and administrative expenses, has been reduced by sublease income of $23,823 (2005 - $22,033). The anticipated remaining sublease income is approximately as follows: 2006 - $8,081; and 2007 - $10,774. The transaction has been recorded at the exchange amount.

Rent expense incurred under the operating lease for the nine months ended September 30, 2006, net of sublease income was $88,152 (2005 - $85,054).

14. Supplementary Cash Flow Information

The Company paid no income taxes during the nine months ended September 30, 2006, nor during the nine months ended September 30, 2005. Interest paid in cash during the nine months ended September 30, 2006 and September 30, 2005 was $2,130 and $2,223, respectively.

Non-cash financing activities are excluded from the consolidated condensed statement of cash flows. The following is a summary of such activities for the nine months ended September 30, 2006 and September 30, 2005:

	2006	2005
Conversion of 4% senior subordinated convertible debentures and accrued interest, net of deferred financing cost of $163,980	$ -	$ 414,952
Debt issuance costs	99,050	
Issuance of 250,000 shares of the Company's common stock, valued at $28,750, in satisfaction of accounts payable in the amount of $25,000	28,750	
Total	$ 127,800	$ 414,952

15. Subsequent Events

On October 1, 2006, the Company issued 118,378 shares of its common stock to the holders of the 10% senior convertible notes, in satisfaction of $13,637 of accrued interest on the notes.

On October 3, 2006, the Company issued 500,000 shares of its common stock pursuant to the terms of a contract with an unrelated party to provide investor relations services to the Company for a period of six months, commencing October 1, 2006.

On October 5, 2006, the Company received $500,000 in cash proceeds from the issuance of its 10% senior convertible notes. The notes mature on October 1, 2008 and are unsecured. Under the terms of the notes, the holders are permitted, at any time, to convert all or a portion of the outstanding principal plus accrued interest into common stock of the Company at a ratio of one common share for each $0.10 of debt converted; the Company may pre-pay all or any portion of the balance outstanding on the notes at any time, without penalty or bonus; interest is payable quarterly, and may, at the Company's option, be paid either in cash or in common shares of the Company. If interest is paid in common shares, the number of shares required for settlement will be calculated using a 10% discount to the average closing price of the common stock, as listed on the exchange where the Company's common stock is traded, for the ten days prior to the date the interest is due to the holder. The Company issued 1,000,000 shares of its common stock to the holder pursuant to the terms of the note.

On October 5, 2006, the Company issued 240,000 shares of its common stock in satisfaction of finance fees relating to the $500,000 in senior convertible notes issued on the same date.

In accordance with the terms of the 10% promissory notes, the Company issued 500,000 shares of its common stock to the holders of the notes on October 11, 2006, as a result of the note plus accrued interest thereon not being fully repaid as of that date.

Item 2. Management's Discussion and Analysis or Plan of Operations

FORWARD-LOOKING INFORMATION

We caution readers that certain important factors may affect our actual results and could cause such results to differ materially from any forward-looking statements that we make in this report. For this purpose, any statements that are not statements of historical fact may be deemed to be forward-looking statements. This report contains statements that constitute "forward-looking statements." These forward-looking statements can be identified by the use of predictive, future-tense or forward-looking terminology, such as "believes," "anticipates," "expects," "estimates," "plans," "may," or similar terms. These statements appear in a number of places in this report and include statements regarding our intent, belief or current expectations with respect to many things, some of which are:

- trends affecting our financial condition or results of operations for our limited history;
- our business and growth strategies;
- our technology;
- the Internet; and
- our financing plans.

We caution readers that any such forward-looking statements are not guarantees of future performance and involve significant risks and uncertainties. In fact, actual results most likely will differ materially from those projected in the forward-looking statements as a result of various factors. Some factors that could adversely affect actual results and performance include:

- our limited operating history;
- our lack of sales to date;
- our requirements for additional capital funding;
- the failure of our technology and products to perform as specified;
- the discontinuance of growth in the use of the Internet;
- the enactment of new adverse government regulations; and
- the development of better technology and products by others.

You should carefully consider and evaluate all of these factors. In addition, we do not undertake to update forward-looking statements after we file this report with the SEC, even if new information, future events or other circumstances have made them incorrect or misleading.

CRITICAL ACCOUNTING POLICIES

We prepare our financial statements in accordance with generally accepted accounting principles in the United States of America. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant accounting policies and methods used in preparation of the financial statements are described in note 2 to our 2005 Consolidated Financial Statements included in our Annual Report on Form 10-KSB for the year ended December 31, 2005, and updated in note 2 to our September 30, 2006 Interim Consolidated Condensed Financial Statements included in this Quarterly Report on Form 10-QSB. We evaluate our estimates and assumptions on a regular basis, based on historical experience and other relevant factors. Actual results could differ materially from these estimates and assumptions. The following critical accounting policies are impacted by judgments, assumptions and estimates used in preparation of our September 30, 2006 Interim Consolidated Condensed Financial Statements.

Revenue recognition:

For sales of product licenses, we recognize revenue in accordance with Statement of Position 97-2, "Software Revenue Recognition" ("SOP 97-2"), as amended by Statement of Position 98-9, "Software Revenue Recognition with Respect to Certain Transactions", issued by the American Institute of Certified Public Accountants. Revenue from sale of product licenses is recognized when all of the following criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectibility is probable.

Revenue from product support contracts is recognized ratably over the life of the contract. Revenue from services is recognized at the time such services are rendered.

For contracts with multiple elements such as product licenses, product support and services, we follow the residual method. Under this method, the total fair value of the undelivered elements of the contract, as indicated by vendor specific objective evidence, is deferred and subsequently recognized in accordance with the provisions of SOP 97-2. The difference between the total contract fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. Vendor specific objective evidence for support and consulting services is obtained from contracts where these elements have been sold separately. Where we cannot determine the fair value of all of the obligations, the revenue is deferred until such time as it can be determined or the element is delivered.

Long-lived assets:

We perform impairment tests on our long-lived assets if events or changes in circumstances indicate that an impairment loss may have occurred. We estimate the useful lives of capital assets and deferred charges based on the nature of the asset, historical experience and the terms of any supplier contracts. The valuation of long-lived assets is based on the amount of future net cash flows these assets are estimated to generate. Revenue and expense projections are based on management's estimates, including estimates of current and future industry conditions. A significant change to these assumptions could impact the estimated useful lives or valuation of long-lived assets resulting in a change to depreciation or amortization expense and impairment charges.

Research and development expenses:

We expense all of our research and development expenses in the period in which they are incurred. At such time as our product is determined to be commercially available, we will capitalize those development expenditures that are related to the maintenance of the commercial products, and amortize these capitalized expenditures over the estimated life of the commercial product. The estimated life of the commercial product will be based on management's estimates, including estimates of current and future industry conditions. A significant change to these assumptions could impact the estimated useful life of our commercial product resulting in a change to amortization expense and impairment charges.

Stock based compensation:

Effective January 1, 2006, the Company adopted the provisions of Financial Accounting Standards Board Statement No. 123R "Share-Based Payment – a revision of FAS 123" (SFAS 123R) to account for its stock-based payments. SFAS 123R requires all share-based payments, including stock options granted by the Company to its employees, to be recognized as expenses, based on the fair value of the share-based payments at the date of grant. For purposes of estimating the grant date fair value of stock-based compensation, the Company uses the Black Scholes option-pricing model, and has elected to treat awards with graded vesting as a single award. The fair value of awards granted is recognized as compensation expense on a straight-line basis over the requisite service period, which in the Company's circumstances is the stated vesting period of the award.

In adopting SFAS 123R, the Company has applied the modified-prospective transition method. Under this method, the Company will recognize compensation costs for all share-based payments granted, modified, or settled after January 1, 2006, as well as for any awards that were granted prior to January 1, 2006 for which the requisite service had not been provided as of that date (unvested awards). Under the modified prospective method, prior periods are not adjusted, and the Company continues to provide pro forma disclosure for these periods, as presented below.

For reporting periods ending on or before December 31, 2005, the Company applied the intrinsic value-based method of accounting prescribed by Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations including FASB Interpretation No. 44, "Accounting for Certain Transactions involving Stock Compensation an interpretation of APB Opinion No. 25" issued in March 2000, to account for its stock options granted to employees. Under this method, compensation expense was recorded on the date of grant only if the then current market price of the underlying stock exceeded the exercise price. Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. These provisions were required to be applied to stock compensation granted to non-employees. As permitted by SFAS No. 123, the Company elected to apply the intrinsic value-based method of accounting described above for awards granted to employees, and adopted the disclosure requirements of SFAS No. 123, for reporting periods ending on or before December 31, 2005.

Had compensation costs in respect of options granted to employees been determined using the fair value based method at the grant date, the Company's pro forma net loss and basic and diluted loss per share for the three and nine months ended September 30, 2005 would have been as follows:

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net loss, as reported (restated)	$(910,327)	$(3,452,668)
Add stock-based employee compensation expense included in net loss	--	--
Deduct total stock-based employee compensation expense determined under the fair value-based method for all awards	(3,363)	(961,451)
Pro forma net loss	$(913,690)	$(4,414,119)
Loss per share:		
Basic and diluted - as reported	$(0.03)	$(0.11)
Basic and diluted – pro forma	$(0.03)	$(0.14)

RESULTS OF OPERATIONS

The Three Months Ended September 30, 2006 Compared to the Three Months Ended September 30, 2005

Revenue: We completed our first commercial sale during the third quarter of 2005, however we were unable to recognize revenue in connection with this sale, as all of the criteria required for us to do so as set out in our accounting policies were not met. During April 2006, we determined that collection of the amount invoiced in connection with this sale was in jeopardy, and have recorded an allowance against the entire amount, as an offset against deferred revenue.

On January 1, 2006, we entered into an agreement with a Value Added Reseller ("VAR"), pursuant to which we granted the VAR a license to sell our software to the VAR's customers for a period of three years. Our fee for this license, excluding applicable sales taxes, was $155,000, of which $151,650 had been received as of the financial statement date. We will recognize revenue in connection with this sale once all of the criteria required for us to do so as set out in our accounting policies, have been met.

Since August 1999 we have directed all of our attention towards the completion, and sales and marketing of, our software applications. We believe that if we are successful in our development and sales and marketing efforts, we will generate a source of revenues in the future from sales and/or licensing of our software applications

Selling, general and administrative expenses: Selling, general and administrative expenses consist primarily of personnel costs, professional fees, insurance, communication expenses, occupancy costs and other miscellaneous costs associated with supporting our research and development and sales and marketing activities. During the three months ended September 30, 2006, we incurred a total of $481,349, including $436,472 in cash-based expenses and $44,877 in stock-based expenses, as compared to $494,137, of which $460,104 was cash-based and $34,033 was stock-based expense, during the three months ended September 30, 2005. There was an overall decrease in selling, general and administrative expenses of $12,788 (3%), comprised of a $23,632 (5%) decrease in the cash-based component, which was partially offset by a $10,844 (32%) increase in the stock-based component of this expense. The decrease in the cash-based component of selling, general and administrative expenses occurred primarily as a result of a reduction in the level of activity of our sales and marketing departments, as compared to the level of activity of these departments during the three months ended September 30, 2005, during which we were in the process of scaling back our sales and marketing efforts in response to a delay in the expected release date of one of our products. During 2006 to date, we have made efforts to further reduce costs in these departments, through measures such as reducing the number of trade shows in which we participate, and delaying production of new promotional material. We will continue to carefully monitor these costs as we work within current budgetary limits leading up to the full commercial release of our products.

Cash-based administrative expenses also decreased significantly during the three months ended September 30, 2006 as compared with the three months ended September 30, 2005, primarily as a result of a reduction in professional fees, which occurred due to lower ongoing reporting costs relating to our private debt and equity placements which took place during the fourth quarter of 2003 and the first quarter of 2004. This reduction in professional fees was partially offset by an

$11,500 penalty incurred to defer the payment of consulting fees, for which there was no comparable cost during the three months ended September 30, 2005.

The stock-based component of selling, general and administrative expense for the three month period ended September 30, 2006 consisted of the amortization of prepaid consulting fees recognized on the issuance of warrants during 2003, and on the extension, during the three months ended September 30, 2005, of the expiry date of these warrants from August 31, 2005 to December 31, 2006; and the fair value of unvested employee stock options earned during the period. The stock-based component of this expense for the three-month period ended September 30, 2005 consisted of the amortization of prepaid consulting fees recognized on the issuance of warrants during 2003 only.

Research and development expenses: Research and development expenses consist primarily of personnel costs and consulting expenses directly associated with the development of our software applications. During the three months ended September 30, 2006, we incurred $192,496 developing our software applications, which represents a decrease of $123,178 (39%) from the $315,674 we incurred during the three months ended September 30, 2005. The overall decrease is due primarily to a decrease in the size of the Europe-based contract development group from an average of 26 personnel during the three months ended September 30, 2005, to an average of 20 personnel during the three months ended September 30, 2006.

Interest and financing costs: Interest and financing costs during the three months ended September 30, 2006 consisted of interest and financing costs associated with our 10% senior secured convertible notes, our 10% senior convertible notes, our 10% and 12% promissory notes and interest on the capital lease. For the three months ended September 30, 2005, these costs included interest and financing costs associated with our 4% senior convertible debentures, interest on our 12% promissory notes and interest on the capital lease. During the three months ended September 30, 2006, we incurred $127,761 in interest and financing costs, an increase of $59,556 (87%) from the $68,205 in interest and financing costs incurred during the three months ended September 30, 2005.

Of the $127,761 in interest and financing costs we incurred during the three months ended September 30, 2006, $13,528 relates to our 10% senior secured convertible notes, $63,769 relates to our 10% senior convertible notes, $33,277 relates to our 10% promissory notes, $16,655 relates to our 12% promissory notes and $532 relates to the capital lease. The $13,528 in interest and financing costs relating to our 10% secured convertible notes is comprised of: $1,478 of accrued interest charges; $10,479 of accretion of the principal through charges to interest expenses; and $1,571 of amortization of deferred financing costs, prior to the notes being cancelled on July 11, 2006, and exchanged for our 10% senior convertible notes. The 10% senior secured convertible notes were issued during the three months ended June 30, 2006, therefore there is no comparable cost for the three months ended September 30, 2005.

The $63,769 in interest and financing costs relating to our 10% convertible notes is comprised of: $12,598 of accrued interest charges; $43,846 of accretion of the principal through charges to interest expenses; and $7,325 of amortization of deferred financing costs. The 10% senior convertible notes were issued during the second and third quarters of 2006, therefore there is no comparable cost for the three months ended September 30, 2005.

The $33,277 in interest and financing costs relating to our 10% promissory notes is comprised of: $5,400 of accrued interest charges; $19,992 of accretion of the principal through charges to interest expenses; and $7,885 of amortization of deferred financing costs. The 10% promissory notes were issued during the third quarter of 2006, therefore there is no comparable cost for the three months ended September 30, 2005.

Of the $68,205 in interest and financing costs we incurred during the three months ended September 30, 2005, $58,555 related to our 4% senior subordinated convertible debentures, which matured on December 31, 2005, resulting in there being no comparable cost during the three months ended September 30, 2006. The remaining $9,650 in interest and financing costs for the three months ended September 30, 2005 consisted of $8,965 in interest on our 12% promissory notes and $685 in interest on the capital lease.

Interest on our 12% promissory notes increased by $7,690 (86%), from $8,965 during the three months ended September 30, 2005, to $16,655 during the three months ended September 30, 2006. This increase occurred as a result of an increase of $301,177 in the principal outstanding on the notes during the period from February to September, 2006, which increased the balance on which interest was charged during the three months ended September 30, 2006 as compared with the three months ended September 30, 2005. There was a decrease of $153 in the amount of interest incurred on our capital lease, as a result of a reduction in the principal outstanding.

Gain on extinguishment of debt: During the three months ended September 30, 2006, the terms of our 10% senior secured promissory notes were modified. A gain of $38,097 was recorded on this transaction. This gain was partially offset by a loss of $3,750 on the issuance of 250,000 common shares of the Company, valued at $28,750, in satisfaction of accounts payable totaling $25,000. There were no comparable transactions during the three months ended September 30, 2005.

Net Loss: We incurred a loss of $783,132 ($0.02 per share) for the three months ended September 30, 2006, compared to a loss of $910,327 ($0.03 per share) for the three months ended September 30, 2005. Our revenues and future profitability are substantially dependent on our ability to:

- license the software applications to a sufficient number of clients;
- be cash-flow positive on an ongoing basis;
- modify the successful software applications, over time, to provide enhanced benefits to then-existing users; and
- successfully develop related software applications.

The Nine Months Ended September 30, 2006 Compared to the Nine Months Ended September 30, 2005

Revenue: We completed our first commercial sale during the third quarter of 2005, however we were unable to recognize revenue in connection with this sale, as all of the criteria required for us to do so as set out in our accounting policies were not met. During April 2006 we determined that collection of the amount invoiced in connection with this sale was in jeopardy, and have recorded an allowance against the entire amount, as an offset against deferred revenue.

On January 1, 2006, we entered into an agreement with a Value Added Reseller ("VAR"), pursuant to which we granted the VAR a license to sell our software to the VAR's customers for a period of three years. Our fee for this license, excluding applicable sales taxes, was $155,000, of which $151,650 had been received as of the financial statement date. We will recognize revenue in connection with this sale once all of the criteria required for us to do so as set out in our accounting policies, have been met.

Since August 1999 we have directed all of our attention towards the completion, and sales and marketing of, our software applications. We believe that if we are successful in our development and sales and marketing efforts, we will generate a source of revenues in the future from sales and/or licensing of our software applications

Selling, general and administrative expenses: Selling, general and administrative expenses consist primarily of personnel costs, professional fees, insurance, communication expenses, occupancy costs and other miscellaneous costs associated with supporting our research and development and sales and marketing activities. During the nine months ended September 30, 2006, we incurred a total of $1,476,149, including $1,275,722 in cash-based expenses and $200,427 in stock-based expenses, as compared to $1,739,401, of which $1,488,418 was cash-based and $250,983 was stock-based expense, during the nine months ended September 30, 2005. There was an overall decrease in selling, general and administrative expenses of $263,252 (15%), comprised of a $212,696 (14%) decrease in the cash-based component, and a $50,556 (20%) decrease in the stock-based component of this expense. The decrease in the cash-based component of selling, general and administrative expenses occurred primarily as a result of a reduction in the level of activity of our sales and marketing departments, as compared to the level of activity of these departments during the nine months ended September 30, 2005, during which we were in the process of scaling back our sales and marketing efforts in response to a delay in the expected release date of one of our products. During 2006 to date, we have made efforts to further reduce costs in these departments, through measures such as reducing the number of sales personnel, discontinuing the services of our public relations firm, reducing the number of trade shows in which we participate, and delaying production of new promotional material. We will continue to carefully monitor these costs as we work within current budgetary limits leading up to the full commercial release of our products.

In addition to the reduction in cash-based costs incurred by our sales and marketing departments, cash-based administrative expenses also decreased during the nine months ended September 30, 2006 as compared with the nine months ended September 30, 2005, primarily as a result of a reduction in professional fees, which occurred due to lower ongoing reporting costs relating to our private debt and equity placements which took place during the fourth quarter of 2003 and the first quarter of 2004. We also incurred $26,000 during the nine months ended September 30, 2005 in relation to our annual general meeting, for which there was no comparable expense during the nine months ended September 30, 2006. These reductions were partially offset by increases in cash-based investor relation consultants' fees and travel costs, due to our efforts to raise additional capital.

Much of our selling, general and administrative expenses are incurred in Canadian dollars. As such, the decreased costs in these departments were partially offset by the higher average exchange rate between the Canadian dollar and the United States dollar experienced during the nine months ended September 30, 2006, as compared with the nine months ended September 30, 2005.

The stock-based component of selling, general and administrative expense for the nine month period ended September 30, 2006 consisted of the amortization of prepaid consulting fees recognized on the issuance of warrants during 2003, and on the extension, during the three months ended September 30, 2005, of the expiry date of these warrants from August 31, 2005 to December 31, 2006; the fair value of common stock issued as compensation for investor relations services rendered; and the fair value of unvested employee stock options earned during the period, reduced by a reversal of the fair value of unvested employee stock options forfeited during the period. The stock-based component of this expense for the nine months ended September 30, 2005 consisted of the amortization of prepaid consulting fees recognized on the issuance of warrants during 2003; and the fair value of common stock issued to consultants in our sales department as compensation for services provided.

Research and development expenses: Research and development expenses consist primarily of personnel costs and consulting expenses directly associated with the development of our software applications. During the nine months ended September 30, 2006, we incurred $792,487 developing our software applications, which represents a decrease of $186,049 (19%) from the $978,536 we incurred during the nine months ended September 30, 2005. This decrease is due primarily to a reduction in the size of the Europe-based contract development group from an average of 26 personnel during the nine months ended September 30, 2005, to an average of 20 personnel during the nine months ended September 30, 2006. Additionally, we engaged external consultants to perform technical writing and testing of our products during the nine months ended September 30, 2005, for which there were no comparable costs during the nine months ended September 30, 2006. In an effort to reduce overall expenses, we also incurred lower travel costs relating to meetings with our Europe-based contract development group during the nine months ended September 30, 2006, as compared with the nine months ended September 30, 2005.

Interest and financing costs: Interest and financing costs during the nine months ended September 30, 2006 consisted of interest and financing costs associated with our 10% senior secured convertible notes, our 10% senior convertible notes, our 10% and 12% promissory notes and interest on the capital lease. For the nine months ended September 30, 2005, these costs included interest and financing costs associated with our 4% senior convertible debentures, interest on our 12% promissory notes and interest on the capital lease. During the nine months ended September 30, 2006, we incurred $191,604 in interest and financing costs, a decrease of $354,653 (65%) from the $546,257 in interest and financing costs incurred during the nine months ended September 30, 2005.

Of the $191,604 in interest and financing costs we incurred during the nine months ended September 30, 2006, $49,585 relates to our 10% senior secured convertible notes, $63,769 relates to our 10% senior convertible notes, $33,277 relates to our 10% promissory notes, $43,232 relates to our 12% promissory notes and $1,741 relates to the capital lease.. The $49,585 in interest and financing costs relating to our 10% secured convertible notes is comprised of: $5,645 of accrued interest charges; $38,097 of accretion of the principal through charges to interest expenses; and $5,843 of amortization of deferred financing costs, prior to the notes being cancelled on July 11, 2006, and exchanged for our 10% senior convertible notes. The 10% senior secured convertible notes were issued during the nine months ended September 30, 2006, therefore there is no comparable cost for the nine months ended September 30, 2005.

The $63,769 in interest and financing costs relating to our 10% convertible notes is comprised of: $12,598 of accrued interest charges; $43,846 of accretion of the principal through charges to interest expenses; and $7,325 of amortization of deferred financing costs. The 10% senior convertible notes were issued during the second and third quarters of 2006, therefore there is no comparable cost for the nine months ended September 30, 2005.

The $33,277 in interest and financing costs relating to our 10% promissory notes is comprised of: $5,400 of accrued interest charges; $19,992 of accretion of the principal through charges to interest expenses; and $7,885 of amortization of deferred financing costs. The 10% promissory notes were issued during the third quarter of 2006, therefore there is no comparable cost for the nine months ended September 30, 2005.

Of the $546,257 in interest and financing costs we incurred during the nine months ended September 30, 2005, $517,444 related to our 4% senior subordinated convertible debentures, which matured on December 31, 2005, resulting in there being no comparable cost during the nine months ended September 30, 2006. The remaining $28,813 in interest and financing costs for the nine months ended September 30, 2005 consisted of $26,590 in interest on our 12% promissory notes and $2,223 in interest on the capital lease.

Interest on our 12% promissory notes increased by $16,642 (63%), from $26,590 during the nine months ended September 30, 2005, to $43,232 during the nine months ended September 30, 2006. This increase occurred as a result of an increase of $301,177 in the principal outstanding on the notes during the period from February to September, 2006, which increased the balance on which interest was charged during the nine months ended September 30, 2006 as compared with the nine months ended September 30, 2005. There was a decrease of $482 in the amount of interest incurred on our capital lease, as a result of a reduction in the principal outstanding.

Gain on extinguishment of debt: During the nine months ended September 30, 2006, the terms of our 10% senior secured promissory notes were modified. A gain of $38,097 was recorded on this transaction. This gain was partially offset by a loss of $3,750 on the issuance of 250,000 common shares of the Company, valued at $28,750, in satisfaction of accounts payable totaling $25,000. There were no comparable transactions during the nine months ended September 30, 2005.

Net Loss: We incurred a loss of $2,357,336 ($0.07 per share) for the nine months ended September 30, 2006, compared to a loss of $3,452,668 ($0.11 per share) for the nine months ended September 30, 2005. Our revenues and future profitability are substantially dependent on our ability to:

- license the software applications to a sufficient number of clients;
- be cash-flow positive on an ongoing basis;
- modify the successful software applications, over time, to provide enhanced benefits to then-existing users; and
- successfully develop related software applications.

LIQUIDITY AND CAPITAL RESOURCES

General: Since inception, we have funded our operations from private placements of debt and equity securities. In addition, until September 1999 we derived revenues from consulting contracts with affiliated parties, the proceeds of which were used to fund operations. Until such time as we are able to generate adequate revenues from the licensing of our software applications, we cannot assure that we will be successful in raising additional capital, or that cash from the issuance of debt securities, the exercise of existing warrants and options, and the placements of additional equity securities, if any, will be sufficient to fund our long-term research and development and selling, general and administrative expenses.

At September 30, 2006, we had $1,917 in cash and cash equivalents, and at December 31, 2005, we had $71,193 in cash and cash equivalents. Our cash and cash equivalents decreased during the nine months ended September 30, 2006 primarily as a result of our net loss of $2,357,336, and resulting cash used in operations of $1,186,767, which was partially offset by an increase in cash resulting from the issuance of $296,567, net of repayments of $4,610, of 12% promissory notes; $250,000 from the issuance of 10% promissory notes; $500,000 from the issuance of 10% senior secured convertible notes (which were cancelled on July 11, 2006 and replaced with our 10% senior convertible notes); $100,000 from the issuance of 10% senior convertible notes; and $10,000 from the exercise of stock purchase warrants. Our cash and cash equivalents also decreased during the nine months ended September 30, 2005 primarily as a result of our net loss of $3,452,668, and resulting cash used in operations of $2,321,554. In October 2006, we raised an additional $500,000 through the issuance of 10% senior convertible notes.

Our independent registered public accountants included an explanatory paragraph to their audit opinion issued in connection with our consolidated financial statements for the year ended December 31, 2005. It states that the following conditions exist, which raise substantial doubt regarding our ability to continue as a going concern: our lack of revenues to date; our negative working capital of $441,014 and our accumulated deficit of $21,255,891 as at December 31, 2005; our loss of $4,205,659 and negative cash flow from operations of $3,035,255 for the year then ended; our expectation of continued operating losses for the foreseeable future; and the fact that we have no lines of credit or other financing facilities in place. At September 30, 2006, we had negative working capital of $1,963,922 and an accumulated deficit during the development stage of $23,613,227; for the nine months then ended we had a net loss of $2,337,941 and negative cash flow from operations of $1,186,767; and note 1 to our unaudited interim condensed financial statements for the period ended September 30, 2006 also discusses the continuing substantial doubt regarding our ability to continue as a going concern.

We achieved our first commercial sale during the third quarter of 2005, however we were unable to recognize revenue in connection with this sale, as all of the criteria required for us to do so as set out in our accounting policies were not met. During April 2006 we determined that collection of the amount invoiced in connection with this sale was unlikely, and have recorded an allowance against the entire amount, as an offset against deferred revenue. On January 1, 2006 we entered into an agreement with a Value Added Reseller ("VAR"), pursuant to which we granted the VAR a license to sell our software to the VAR's customers for a period of three years. Our fee for this license, excluding applicable sales taxes, was $155,000, of which $151,650 had been received as of August 11, 2006. We will recognize revenue in connection with this sale once all of the criteria required for us to do so as set out in our accounting policies, have been met.

We anticipate additional commercial sales during the fourth quarter of 2006, however we cannot be assured that this will be the case. During the nine months ended September 30, 2006, we hired one additional person in our sales department, and had one full-time employee and one part-time consultant leave the Company. While we expect to replace the two individuals who left during the period, we do not expect to add any additional personnel during the next 6 months. We have not made, nor do we expect to make, any material commitments for capital equipment expenditures during the next 12 months.

We have an immediate requirement for additional working capital in order to proceed with our business plan. We review our cash needs and sources on a month-to-month basis and we are currently pursuing appropriate opportunities to raise additional capital to fund operations. Additional sources of capital could involve issuing equity or debt. Since February 2006, we have engaged financial advisers to provide advice to us with respect to capital raising. However, additional funding may not be available to us on reasonable terms, if at all. The perceived risk associated with the possible sale of a large number of shares could cause some of our stockholders to sell their stock, thus causing the price of our stock to decline. In addition, actual or anticipated downward pressure on our stock price due to actual or anticipated issuance of stock could cause some institutions or individuals to engage in short sales of our common stock, which may itself cause the price of our stock to decline. We may be unable to raise additional capital if our stock price is too low. A sustained inability to raise capital could force us to limit or curtail our operations.

We expect the level of our future operating expenses to be driven by the needs of our research and development and marketing programs offset by the availability of funds. In addition, we have since inception made an effort to keep our expenses relatively low and conserve available cash until we begin generating sufficient operating cash flow.

Sources of Capital: Our principal sources of capital for funding our business activities have been the private placements of debt and equity securities. During the nine months ended September 30, 2006, we issued $296,567, net of repayments of $4,610, of 12% promissory notes; $250,000 of 10% promissory notes; $500,000 of 10% senior secured convertible notes; $100,000 of 10% senior convertible notes; and we received $10,000 on the exercise of 20,000 Series H warrants, all of which generated cash for funding operations. In addition, we issued 300,000 common shares in consideration for consulting services rendered, 328,000 common shares in consideration for finance fees, 100,000 common shares in exchange for the deferral of payment of fees owing, and 250,000 common shares in settlement of accounts payable, all of which reduced our requirement for cash. During October 2006, we received $500,000 on the issuance of 10% senior convertible notes.

The Company has not entered into any off-balance sheet arrangements which would have provided the Company with a source of capital.

Uses of Capital: Over the past several years, we have scaled our development activities to the level of available cash resources. Research and development expenses for the nine months ended September 30, 2006 decreased by approximately 20% as compared to the nine months ended September 30, 2005, as a result of cash conservation efforts. Selling, general and administrative expenses for the nine months ended September 30, 2006 decreased by approximately 15% as compared to the nine months ended September 30, 2005, due to several factors, including a reduction in selling and marketing initiatives, and as explained more fully under "Results of Operation."

During 2004, we added a total of five people to our sales and marketing team, in order to accelerate our efforts to generate future commercial sales of our products. We also added two administrative employees, increased the area of our leased premises, and acquired new property and equipment. Additionally, we increased the size of our contract software application development group, and hired two employees in the product development department, in order to implement revisions and enhancements to those of our products currently in use as they are identified, while continuing to develop additional products. During the fourth quarter of 2004, and continuing through the latter part of the third quarter of 2005, we scaled back our sales and marketing program, in order to maintain a sustainable level for sales and marketing expenditures leading up to the first commercial release of our products. We began hiring additional personnel in our sales and marketing departments during the latter part of the third quarter of 2005, in anticipation of imminent commercial sales, the first of which took place during September 2005. We have not replaced the one full-time employee and one part-time consultant who left our Company during the first quarter of 2006, as we await completion of our current financing efforts. We have not entered into any off-balance sheet arrangements which would have resulted in our use of capital.

The cost to implement appropriate controls and procedures to ensure compliance with Section 404 of the Act is included in our budget for 2006.

ITEM 3. CONTROLS AND PROCEDURES

The term "disclosure controls and procedures" is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, or the Exchange Act. This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission.

In connection with the audit of our consolidated financial statements for the year ended December 31, 2005, our independent registered public accounting firm advised the Board of Directors and management of certain significant internal control deficiencies that they considered to be, in the aggregate, a material weakness. In particular, our independent registered public accounting firm identified the following weaknesses in our internal control system: (1) a lack of segregation of duties; and (2) the lack of timely preparation of certain back up schedules. The independent registered public accounting firm indicated that they considered these deficiencies to be reportable conditions as that term is defined under standards established by the American Institute of Certified Public Accountants. A material weakness is a significant deficiency in one or more of the internal control components that alone or in the aggregate precludes our internal controls from reducing to an appropriately low level of risk that material misstatements in our financial statements will not be prevented or detected on a timely basis. We considered these matters in connection with the period-end closing of accounts and preparation of the related consolidated financial statements and determined that no prior period financial statements were materially affected by such matters. Notwithstanding the material weakness identified by our independent registered public accountants, we believe that the financial statements, and other financial information included in this report, fairly present in all material respects, the financial condition, results of operation and cash flows of the Company as of, and for, the periods represented in this report.

In connection with the audit of our consolidated financial statements for the year ended December 31, 2004, our independent registered public accounting firm advised the Board of Directors and management of certain significant internal control deficiencies that they considered to be, in the aggregate, a material weakness. Of the five weaknesses identified by our independent registered public accountants in connection with the audit of our consolidated financial statements for the year ended December 31, 2004, and as previously disclosed, we believe that three of the significant internal control deficiencies identified at that time have been remediated. The two significant internal control deficiencies that were identified in regards to the audit of our consolidated financial statements for the year ended December 31, 2004 that have not been remediated are those which were identified by our independent registered public accountants during the audit of our consolidated financial statements for the year ended December 31, 2005.

Our size has prevented us from being able to employ sufficient resources at this time to enable us to have an adequate level of supervision and segregation of duties within our internal control system. We will continue to monitor and assess the costs and benefits of additional staffing within the Company.

We were unable to implement improvements in all areas of concern with respect to the period covered by this report. However, we began to implement some of the steps identified below to remediate the material weakness to the extent that our size and resources allowed us, commencing during the second quarter of 2004. Set forth below is a discussion of the significant internal control deficiencies which have not been remediated.

Lack of segregation of duties. Since commencing the development phase of our operations in August 1999, our size has prevented us from being able to employ sufficient resources to enable us to have an adequate level of supervision and segregation of duties within our internal control system. We have only three people involved with the processing of accounting entries: the Office Administrator, the Controller and the Chief Financial Officer. Therefore, it is difficult to effectively segregate accounting duties. During the fourth quarter of 2005, we retained the services of a part-time independent consultant to assist in performing routine, month end accounting procedures, however we later determined that this individual did not meet our requirements and his services were discontinued in March 2006. We are currently seeking, but cannot be assured that we will be able to find, a qualified part time person to replace this individual. While we strive to segregate duties as much as practicable, there is insufficient volume of transactions to justify additional full time staff. As a result, this significant internal control deficiency had not been remediated as of the end of the period covered by this report, nor do we know if we will be able to remediate this weakness in the foreseeable future. However, we will continue to monitor and assess the costs and benefits of additional staffing.

Lack of timely preparation of back up schedules. During the third and fourth quarters of 2004, we expanded our accounting system in order to facilitate the more timely preparation of financial reports, and we involved the Office Administrator in some of the data entry functions of the accounting department. Notwithstanding these measures and the more formal month end procedures implemented by us commencing in the second quarter of 2004, we continued to experience challenges in preparing our periodic external reports on a timely basis, primarily as a result of an increase in our internal and external reporting requirements due to the expansion of our operations.

When our independent registered public accountants' audit staff arrived to start their field work with respect to our 2004 financial statements, not all of the back up schedules had been prepared. Some of the back up schedules that we prepare to support the information in the financial statements and Form 10-KSB were not completed by us until the later stages of the field work. As we completed the back up schedules, we identified some adjusting entries that were required to provide complete, accurate disclosure. Our failure to timely prepare all of the relevant back up schedules resulted in a delay in the process, which contributed to our not being able to file our Form 10-KSB for the year ended December 31, 2004 until April 15, 2005. In fact, our inability to be prepared on time for our independent registered public accountants' periodic scheduled field work caused us difficulty in meeting our filing deadlines throughout 2004.

While we did not file our Form 10-QSB for the quarter ended March 31, 2005 until May 20, 2005, we did file our Forms 10-QSB for the periods ended June 30, 2005 and September 30, 2005 on August 15, 2005 and November 14, 2005, respectively. For the year ended December 31, 2005 we did not file our Form 10-KSB until the first week of April, 2006; for the quarter ended March 31, 2006 we did not file our Form 10-QSB until May 22, 2006; and for the quarter ended June 30, 2006 we did not file our Form 10-QSB until August 21. For these reporting periods, we were able to complete most of our back up prior to the arrival of our independent registered public accountants' staff. As such, we believe this material weakness had not been remediated as of the end of the period covered by this report, although progress in remediation had been made. One of our objectives in seeking a qualified part time person to perform routine, month end accounting procedures, is to improve the timeliness of preparation of back up schedules and thus permit us to complete our financial reporting on a more timely basis.

If we are unable to remediate the identified material weakness, there is a more than remote likelihood that a material misstatement to our SEC reports will not be prevented or detected, in which case investors could lose confidence in the accuracy and completeness of our financial reports, which could have an adverse effect on our ability to raise additional capital and could also have an adverse effect on our stock price.

As required by the SEC rules, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report. This evaluation was performed under the supervision and with the participation of our management, including the President and Chief Executive Officer and Chief Financial Officer and Treasurer. Based upon that evaluation, our President and Chief Executive Officer and Chief Financial Officer and Treasurer have concluded that our controls and procedures were not effective as of the end of the period covered by this Report due to the existence of the significant internal control deficiencies described above.

No change in our internal control over financial reporting occurred during the quarter ended September 30, 2006 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On September 1, and September 14, 2006 the Company issued a total of $50,000 of its 10% senior convertible promissory notes to accredited investors. The 10% senior secured promissory notes and accrued interest thereon are convertible, at the sole discretion of the holder, into shares of the Company's common stock, at any time, at a conversion rate of 1 common share for every $0.10 in principal converted. In addition, the Company issued 100,000 shares of its common stock pursuant to the terms of the note.

On July 13, 2006, the Company issued $250,000 of its 10% promissory notes to an accredited investor. Pursuant to the terms of the note, the Company issued 1,000,000 shares of its common stock to the holder at the date of issuance. In accordance with the terms of the note, the Company issued a further 500,000 shares of its common stock to the accredited investor on October 11, 2006, as a result of the note plus accrued interest thereon not being fully repaid as of that date.

On September 1, 2006, the Company issued a total of 328,000 shares of its common stock to accredited investors, in consideration for finance fees owing in relation to the issuance of the Company's 10% senior secured convertible, 10% senior convertible notes and 10% promissory notes; 100,000 shares of its common stock to an accredited investor in exchange for the deferral of payment of fees owing; and 250,000 shares of its common stock to an accredited investor in settlement of accounts payable.

On October 1, 2006, the Company issued 118,378 shares of its common stock to the holders of the 10% senior convertible notes, in satisfaction of accrued interest on the notes.

On October 3, 2006, the Company issued 500,000 shares of its common stock to an accredited investor in consideration for consulting services to be rendered.

On October 5, 2006, the Company issued $500,000 of its 10% senior convertible promissory notes to accredited investors. The 10% senior secured promissory notes and accrued interest thereon are convertible, at the sole discretion of the holder, into shares of the Company's common stock, at any time, at a conversion rate of 1 common share for every $0.10 in principal converted. In addition, the Company issued 1,000,000 shares of its common stock pursuant to the terms of the note.

On October 5, 2006, the Company issued 240,000 shares of its common stock to an accredited investor, in consideration for finance fees owing in relation to the issuance of the Company's 10% senior convertible promissory notes on the same date.

The foregoing securities were issued in reliance upon the exemption provided by Section 4(2) of the Securities Act of 1933, as amended, and the rules promulgated thereunder.

Item 6. Exhibits

(a) Exhibits.

4.1	Form of 10% Senior Convertible Notes and Stock Grant Agreement
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the small business issuer has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

VALIDIAN CORPORATION

By: /s/ Bruce Benn
Bruce Benn

President and Chief Executive Officer
(principal executive officer)

Dated: November 24, 2006

By: /s/ Ronald Benn

Ronald Benn

Chief Financial Officer and Treasurer
(principal financial and accounting officer)

Dated: November 24, 2006

Exhibit 4.1

THE SALE AND ISSUANCE OF THE SECURITIES REPRESENTED BY THIS 10% CONVERTIBLE NOTE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), OR UNDER THE SECURITIES LAW OF ANY STATE OR OTHER JURISDICTION. THESE SECURITIES HAVE BEEN ACQUIRED FOR INVESTMENT AND NOT WITH A VIEW TO, OR IN CONNECTION WITH, THE DISTRIBUTION THEREOF. THESE SECURITIES MAY NOT BE OFFERED, SOLD, PLEDGED, OR TRANSFERRED UNLESS (I) A REGISTRATION STATEMENT UNDER THE ACT IS IN EFFECT AS TO THESE SECURITIES AND SUCH OFFER, SALE, PLEDGE, OR TRANSFER IS IN COMPLIANCE WITH APPLICABLE SECURITIES LAW OF ANY STATE OR OTHER JURISDICTION OR (II) AN EXEMPTION FROM THE ACT IS AVAILABLE AND SUCH OFFER, SALE, PLEDGE, OR TRANSFER IS IN COMPLIANCE WITH APPLICABLE SECURITIES LAW OF ANY STATE OR OTHER JURISDICTION.

10% CONVERTIBLE NOTE

$___________ (date)

For value received, Validian Corporation, a Nevada corporation (together with its successors and assigns, the "Company"), with an address at 30 Metcalfe Street, Ottawa, Ontario, Canada K1P 5L4, promises to pay to ___________(the "Holder") with an address at _________________, the principal amount of ____________ ($________) and to pay interest thereon, all as hereinafter specified.

1. Identification of Note. This Note is issued as part of the Holder's investment into the Company.

2. Maturity.

2.1 Maturity Date. Unless earlier converted as provided in Section 3 hereof, this Note will automatically mature and be due and payable on the earlier of (a) ___________ (the "Maturity Date") or (b) the occurrence of an Event of Default (as defined in Section 8 hereof).

2.2 Interest. Interest shall accrue from the date of this Note on the unpaid principal amount at a rate equal to ten percent (10%) per annum, computed on the basis of the actual number of days elapsed and a year of 365 days from the date of this Note until the principal amount and all interest accrued thereon are paid (or converted, as provided in Section 3 hereof). Interest shall be due and paid to the Holder quarterly. The first quarterly payment shall be paid to the Holder on __________. At the Company's option, interest can be paid in either (a) cash or (b) shares of common stock, calculated at a ten percent (10%) discount to the average closing price of the common stock, as listed on the exchange where the Company's Common Stock is traded, for the ten (10) trading days prior to the date the interest is due to the Holder. The stock referenced in this Section 2.2 shall be included in the registration rights provisions in Section 5 and be subject to the calculation for purposes of Section 4.

2.3 Prepayment. The Company shall not have the right to prepay this Note without first obtaining prior written consent from the Holder. Such consent shall not be unreasonably withheld.

3. Conversion.

3.1 Voluntary Conversion. The holder may voluntarily convert the Note, in whole or in part, into Common Stock of the Company at any time.

3.2 Mechanics and Effect of Conversion.

(a) The principal and any unpaid and accrued interest of this Note shall convert into shares of Common Stock at a conversion price of ten cents ($0.10) per share ("Conversion Price").

(b) No fractional shares will be issued upon conversion of this Note. In lieu of any fractional shares to which the Holder would otherwise be entitled, the Company will pay to the Holder in cash the unconverted amount that would otherwise be converted into such fractional shares.

(c) In the event that the Outstanding Amount under this Note is converted into Common Stock pursuant to Section 3.1 hereof, the Holder shall surrender this Note, duly endorsed, to the Company and the Note shall thereupon be canceled, provided that if Holder partially converts pursuant to Section 3.2(a) hereof, the Company shall issue a Note to Holder for the remaining amount of principal that was not converted. At its expense, the Company will issue and deliver to such Holder, a certificate or certificates representing the number of duly authorized, validly issued, fully paid and non-assessable shares of Common Stock to which such Holder is entitled upon such conversion, together with a check payable to the Holder for any cash amounts payable pursuant to Section 3.2(b) hereof.

(d) Unless a registration statement under the Securities Act of 1933, as amended, with respect to the shares of Common Stock issued upon conversion of this Note has been filed with the Securities and Exchange Commission, each share issued upon conversion of this Note shall be stamped or otherwise imprinted with a legend substantially in the following form:

> "THIS SECURITY HAS NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 ACT"), OR APPLICABLE STATE SECURITIES LAWS AND MAY NOT BE TRANSFERRED OR OTHERWISE DISPOSED OF UNLESS IT HAS BEEN REGISTERED UNDER THE 1933 ACT AND SUCH LAWS OR AN EXCEPTION FROM REGISTRATION IS AVAILABLE."

(e) Upon conversion of this Note in accordance with Section 3 hereof, all rights with respect to this Note shall terminate, whether or not the Note has been surrendered for cancellation, and the Company will be forever released from all of its obligations and liabilities under this Note except its obligations pursuant to Section 3.2(c) hereof, except if Holder partially converts the Note pursuant to Section 3 hereof, whereby all rights with respect to the portion of the Note that has been converted will terminate pursuant to this Section 3.2(e), but the remainder Note will possess all of the rights granted in this Note.

4. Limitations on Conversion. In no event shall the Holder be entitled to convert any portion of this Note in excess of that portion of this Note upon conversion of which the sum of (1) the number of shares of Common Stock beneficially owned by the Holder and its affiliates (other than shares of Common Stock which may be deemed beneficially owned through the ownership of the unconverted portion of the Notes or the unexercised or unconverted portion of any other security of the Borrower (including, without limitation, the warrants issued by the Borrower pursuant to the Purchase Agreement) subject to a limitation on conversion or exercise analogous to the limitations contained herein) and (2) the number of shares of Common Stock issuable upon the conversion of the portion of this Note with respect to which the determination of this proviso is being made, would result in beneficial ownership by the Holder and its affiliates of more than 9.9% of the outstanding shares of Common Stock. For purposes of the proviso to the immediately preceding sentence, beneficial ownership shall be determined in accordance with Section 13(d) of the Securities Exchange Act of 1934, as amended, and Regulations 13D-G thereunder, except as otherwise provided in clause (1) of such proviso. Holder may waive the limitations set forth herein by sixty-one (61) days prior written notice to the Company.

5. Registration Rights. The Company shall file a registration statement, and any amendments thereto, with the Securities and Exchange Commission (the "SEC") by ________________ and cooperate with the SEC to have such registration statement, and any amendments thereto, declared effective, which includes the shares underlying this Note and those shares issued pursuant to Section 2.2 hereof, as soon as reasonably practicable, provided that Holder shall have piggy-back rights with respect to any registration statement filed by the Company. If a registration statement covering the shares underlying this Note is not filed prior to _____________, then in addition to any rights the Holder may have hereunder or under applicable law, the Company shall pay to the Holder, as partial liquidated damages and not as a penalty, an amount in cash of 2% of the value of the shares underlying this Note for the first month the registration statement is not filed after _______________ and an amount in cash of 1% of the value of the shares underlying this Note for any month after the first month where a registration statement has not been filed. For purposes of calculating the liquidated damages in this Section 5, the calculation provided in Section 4 is not applicable. The Company shall bear the full cost of filing the registration statement pursuant to a demand by Holder.

6. Payment. Except as set forth herein, all payments shall be made in lawful money of the United States of America at the principal offices of the Holder. Payment shall be credited first to the accrued interest then due and payable and the remainder applied to principal.

7. Subordination. To the extent bankruptcy proceedings are initiated by the Company or a third party, the Holder shall receive the same percentage of ownership *pari passu* as the Holder would have under Section 3 hereof, regardless of any bankruptcy protection afforded to the Company.

8. Events of Default. The entire unpaid Outstanding Amount shall become immediately due and payable upon the occurrence of an Event of Default. An "Event of Default" shall be deemed to have occurred if:

(a) the Company shall: (i) be unable, or admit in writing its inability, to pay its debts as they mature; (ii) make a general assignment for the benefit of creditors; (iii) be adjudicated a bankrupt or insolvent; (iv) file a voluntary petition in bankruptcy, or a petition or answer seeking reorganization or an arrangement with creditors to take advantage of any insolvency law, or an answer admitting the material allegations of a bankruptcy, reorganization or insolvency petition filed against it; (v) take corporate action for the purpose of effecting any of the foregoing; or (vi) have an order for relief entered against it in any proceeding under the United States Bankruptcy Code;

(b) an order, judgment or decree shall be entered, without the application, approval or consent of the Company by any court of competent jurisdiction, approving a petition seeking reorganization of the Company or appointing a receiver, trustee or liquidator of the Company or of all or a substantial part of its assets, and such order, judgment or decree shall continue unstayed and in effect for any period of thirty (30) consecutive days; or

(c) the Company shall fail to pay as and when due any principal or interest hereunder and such nonpayment shall continue uncured for a period of ten (10) business days after written notice by the Holder thereof.

9. Transfer; Successors and Assigns. This Note may be transferred only upon surrender of the original Note for registration of transfer, duly endorsed, or accompanied by a duly executed written instrument of transfer in form satisfactory to the Company. Thereupon, a new note for the same principal amount and interest will be issued to, and registered in the name, of, the transferee. Interest and principal are payable only to the registered holder of this Note. The terms and conditions of this Note shall inure to the benefit of and binding upon the respective successors and assigns of the parties.

10. Governing Law. This Note and all acts and transactions pursuant hereto and the rights and obligations of the parties hereto shall be governed, construed and interpreted in accordance with the laws of the State of New York, without giving effect to principles of conflicts of law and choice of law that would cause the laws of any other jurisdiction to apply.

11. Notices. Whenever any notice is required to be given by the Company to a Holder, such notice shall be sent in writing via first class mail, postage prepaid, to the Holder at the Holder's last address appearing on the books maintained by the Company for registration, which notice shall be conclusively presumed to have been duly given, whether or not the Holder receives such notice. Whenever any notice is required to be given by the Holder of this Note to the Company, such notice shall be sent in writing via first class mail, postage prepaid, to the Company at the Company's address above.

12. Amendments and Waivers. This Note and any term hereof may be amended, waived, discharged or terminated only by an instrument in writing signed by the party against whom enforcement of such amendment, waiver, discharge or termination is sought. No waivers of any term, condition or provision of this Note, in any one or more instances, shall be deemed to be, or construed as, a further or continuing waiver of any such term, condition or provision.

13. Immunity of Members, Officers, Directors and Employees. No recourse shall be had for the payment of the principal or interest on this Note or for any claim based thereon or otherwise in any manner in respect thereof, to or against any subsidiary, member, officer, director or employee, as such, past, present or future, of the Company or any respective subsidiary, member, officer, director or employees, as such, past, present or future, of any predecessor or successor company, either directly or through the Company or such predecessor or successor company, whether by virtue of any constitutional provision or statute or rule of law, or by the enforcement of any assessment or penalty, or in any other manner, all such liability being expressly waived and released by the acceptance of this Note and as part of the consideration for the issuance thereof.

[Signatures on Following Page]

IN WITNESS WHEREOF, the Company has caused this Note to be duly executed and delivered by its authorized officer, as of the date first above written.

VALIDIAN CORPORATION

By:__________________________________
Name: Bruce Benn
Title: Chief Executive Officer

By:__________________________________
Name: Ronald I. Benn
Title: Chief Financial Officer

AGREEMENT

This Agreement entered into on the ___ day of _______ 2006, between Validian Corporation, a Nevada corporation (together with its successors and assigns, the "Company"), with an address at 30 Metcalfe Street, Ottawa, Ontario, Canada K1P 5L4, and __________ (the "Holder") with an address at ____, agree as follows:

WHEREAS, on the date hereof, the Company issued a Senior 10% Convertible Note pursuant to which the Company promised to pay the Holder a principal amount of _____________($_______) and to pay interest thereon at a rate of 10%;

NOW THEREFORE, BE IT RESOLVED, that the Company and Holder, intending to be legally bound, hereby agree as follows:

1. Grant of Common Stock

1.1. In consideration of the Holder's investment in the Company, the Company hereby agrees to grant ________________ (__________) shares of the Company's common stock, par value $0.001 (the "Common Stock") to the Holder.

1.2 Unless a registration statement under the Securities Act of 1933, as amended, with respect to the shares of Common Stock granted pursuant to Section 1.1 hereof has been filed with the Securities and Exchange Commission, each share granted pursuant to Section 1.1 hereof shall be restricted and stamped or otherwise imprinted with a legend substantially in the following form:

> "THIS SECURITY HAS NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 ACT"), OR APPLICABLE STATE SECURITIES LAWS AND MAY NOT BE TRANSFERRED OR OTHERWISE DISPOSED OF UNLESS IT HAS BEEN REGISTERED UNDER THE 1933 ACT AND SUCH LAWS OR AN EXCEPTION FROM REGISTRATION IS AVAILABLE."

2. Governing Law. This Agreement and all acts and transactions pursuant hereto and the rights and obligations of the parties hereto shall be governed, construed and interpreted in accordance with the laws of the State of New York, without giving effect to principles of conflicts of law and choice of law that would cause the laws of any other jurisdiction to apply.

[Signatures on the Following Page]

IN WITNESS WHEREOF, the parties hereby cause this Agreement to be duly executed and delivered by its authorized officers, as of the date first above written.

VALIDIAN CORPORATION

By:___________________________
Name: Bruce Benn
Title: Chief Executive Officer

By:___________________________
Name: Ronald I. Benn
Title: Chief Financial Officer

HOLDER

By:___________________________
Name: _______________

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Bruce Benn, certify that:

(1) I have reviewed this report on Form 10-QSB of Validian Corporation;
(2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
(3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operation and cash flows of the small business issuer as of, and for, the periods represented in this report;
(4) The small business issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
    (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    (b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
    (c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonable likely to materially affect, the small business issuer's internal control over financial reporting; and
(5) The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
    (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
    (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: November 24, 2006

By : /s/ Bruce Benn

Bruce Benn
Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Ronald Benn, certify that:

(1) I have reviewed this report on Form 10-QSB of Validian Corporation;
(2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
(3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operation and cash flows of the small business issuer as of, and for, the periods represented in this report;
(4) The small business issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   (b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   (c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonable likely to materially affect, the small business issuer's internal control over financial reporting; and
(5) The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: November 24, 2006

By : /s/ Ronald Benn

Ronald Benn
Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C., SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), I, the undersigned Chief Executive Officer of Validian Corporation (the “Company”), hereby certify that, to the best of my knowledge, the Quarterly Report on Form 10-QSB of the Company for the period ended September 30, 2006 (the “Report”) fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company as of, and for, the periods presented in the Report. A signed original of this written statement required by Section 906 has been provided to the registrant and will be retained by it and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished as an exhibit to the Form 10-QSB pursuant to Item 601(b)(32) of Regulation S-B and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of the Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-QSB for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

Date: November 24, 2006

By : /s/ Bruce Benn

Bruce Benn
Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C., SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350 (as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002), I, the undersigned Chief Financial Officer of Validian Corporation (the “Company”), hereby certify that, to the best of my knowledge, the Quarterly Report on Form 10-QSB of the Company for the period ended September 30, 2006 (the “Report”) fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operation of the Company as of, and for, the periods presented in the Report. A signed original of this written statement required by Section 906 has been provided to the registrant and will be retained by it and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished as an exhibit to the Form 10-QSB pursuant to Item 601(b)(32) of Regulation S-B and Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of the Title 18, United States Code) and, accordingly, is not being filed as part of the Form 10-QSB for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

Date: November 24, 2006

By: /s/ Ronald Benn

Ronald Benn
Chief Financial Officer