INTERNATIONAL WATER-GUARD INDUSTRIES, INC. | **2010 ANNUAL REPORT**

BROADENING HORIZONS

FOR OVER 20 YEARS, INTERNATIONAL WATER-GUARD HAS BEEN IMPROVING THE QUALITY OF WATER ONBOARD AIRCRAFT - PROTECTING BOTH PASSENGERS AND CREW FROM THE RISK OF WATERBORNE ILLNESSES.

TODAY, WE ARE THE WORLD'S LEADING PROVIDER OF FLIGHT-CERTIFIED POTABLE WATER TREATMENT UNITS AND INNOVATIVE POTABLE WATER SYSTEM SOLUTIONS. FROM CORPORATE JETS TO PRIVATELY REGISTERED AIRLINERS AND MILITARY TRANSPORTS,

IWG DELIVERS CLEAR, SAFE, POTABLE WATER TO AIRCRAFT WORLDWIDE.

FINANCIAL HIGHLIGHTS

Fiscal year end September 30 (All items in dollars, except per share data)

Operations	**2010**	2009	2008
Total revenues	**$4,381,894**	$4,952,911	$4,156,469
Earnings (loss) before taxes	**189,323**	425,016	(148,044)
Net earnings (loss)	**135,423**	312,016	(97,044)
Cash flow from operations	**612**	500,668	88,264
Basic EPS	**0.3¢**	0.7¢	0.3¢
Fully diluted EPS	**0.3¢**	0.7¢	0.3¢

Financial position	**2010**	2009	2008
Capital expenditures	**$41,197**	$38,916	$96,075
Working capital	**2,289,382**	2,266,003	1,722,974
Total assets	**3,350,627**	3,249,308	2,941,421
Shareholder's equity	**2,910,449**	2,756,037	2,406,375
Common shares outstanding	**39,230,694**	39,340,694	39,310,694

Operating Results in thousands of dollars

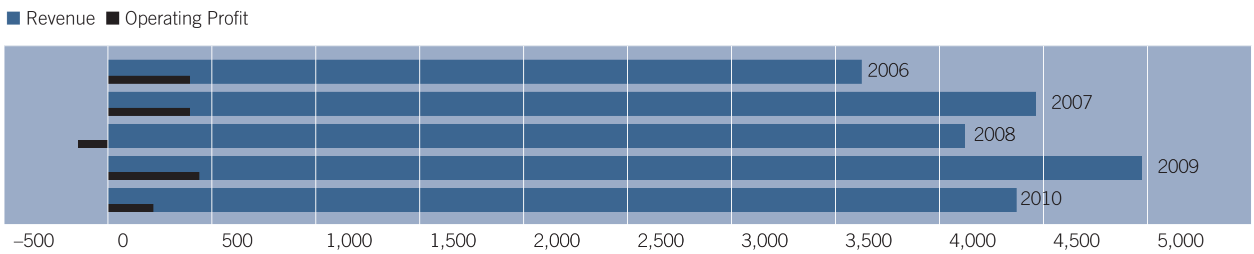


Table of Contents

PRESIDENT'S MESSAGE

International Water-Guard achieved a new milestone in fiscal 2010: the delivery of our 2000th water treatment unit.

We've come a long way from humble beginnings as a small commercial water treatment business in Vancouver. Today, we have a secure industry lead as an aviation systems company specializing in water. We are AS9100 approved and have a sterling track record of installations across leading business jet types and with VIP/ head-of-state airliners.

Our 2,000th unit, an IWG-A4 destined for a Dassault Falcon 2000LX, was shipped in what was otherwise a challenging year. We have been successful in maintaining profitability in the face of both adverse exchange rates and a flat business jet market. We took advantage of this time to position the company for an anticipated industry turnaround and made significant progress on a number of major initiatives. Most importantly, we continue our search for new opportunities to generate major growth for the company in the coming years.

IWG's successes this year were significant in the face of industry austerity. In particular our new IWG-A6 water treatment unit now flies on Gulfstream's four prototype G650's. This program is progressing well and is on target for entry into service in 2012 and revenue generating units are already being shipped. Also, for the fourth year in a row, we were honored as a Gulfstream Supplier of the Year.

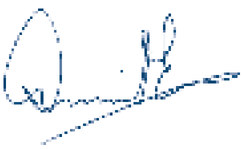
Taken together, our achievements underscore the maturity of the company as a successful and well-regarded specialty supplier to the world aerospace industry.

On the commercial aviation side, the move towards greater focus on aircraft water quality continues. The Environmental Protection Agency's Aircraft Drinking Water Rule is now in place in the United States, while here in Canada we are participating in a new initiative from the National Research Council focused on Aircraft Cabin Environment Technologies. We are also seeing the first signs of emerging competition for commercial aircraft applications. All this bodes well for our own eventual expansion into this broad market.

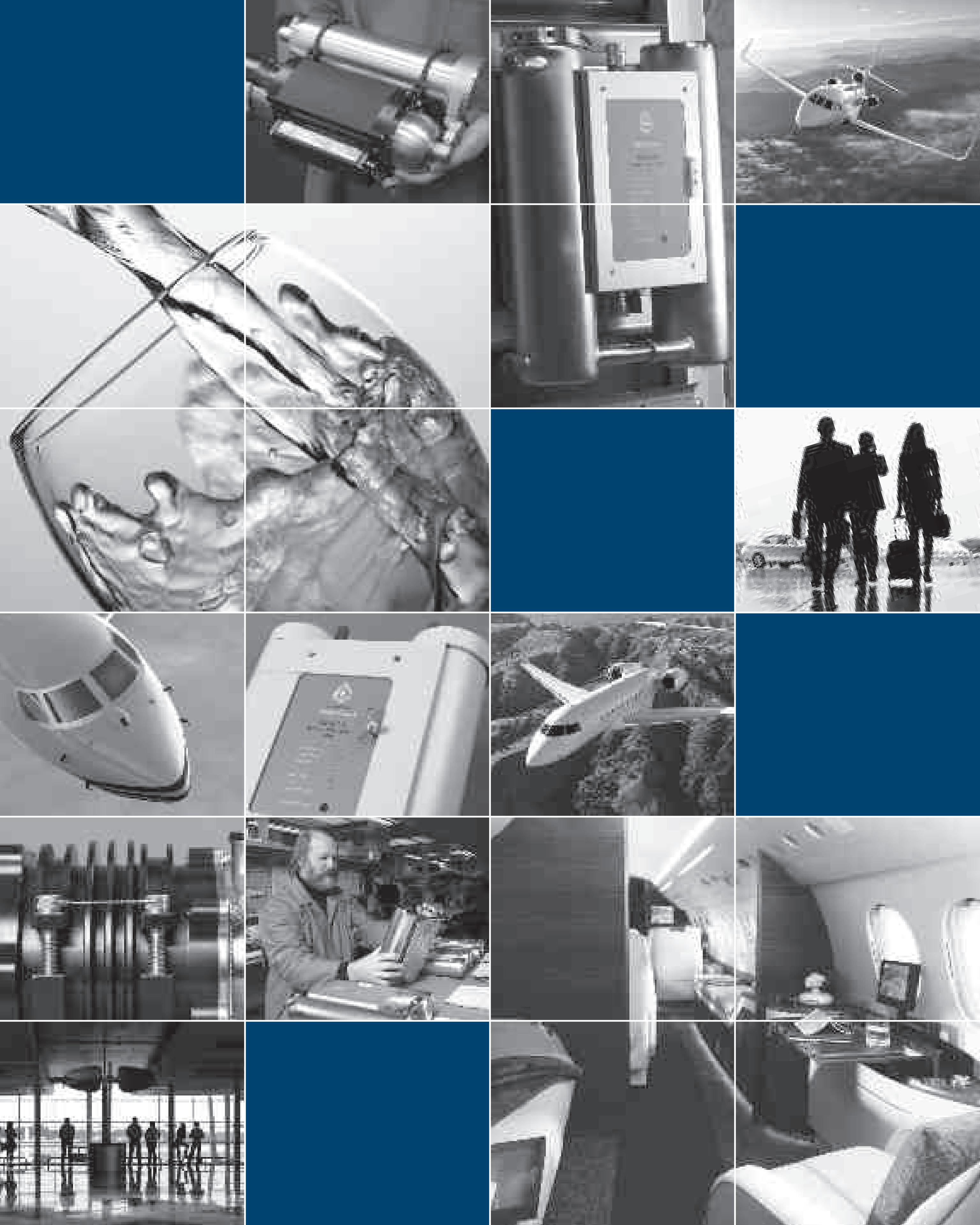
From a financial perspective, we achieved a strong cash balance of $1.1 million at year-end, only slightly down from 2009. We maintain these funds as our corporate "war chest," to take advantage of internal and external opportunities when they arise.

Also related to corporate finance, the Board of Directors has taken special note of the trading patterns of IWG stock. As a result, a "Normal Course Issuer Bid" was set in place to buy back up to 5% of the company's stock since our share price may not adequately reflect the value of the underlying assets of the company.

As always, our Board has been very supportive of the company in the face of significant industry challenges and the general malaise of the worldwide economy. Our entire team has pushed hard for improved performance and achievements in every facet of our operation. I would like to thank everyone – including our shareholders - for the continuing dedication that allows IWG to prosper and grow.



David C. Fox
President & Chief Executive Officer



COMPANY OVERVIEW

International Water-Guard is an aerospace systems company specializing in the supply of water treatment equipment, systems and components to the world's large corporate jet manufacturers and VIP airliner conversions. The Company's mission is to improve the quality of aircraft potable water and water supply systems.

The Company has now delivered over 2,000 of its water treatment units to the aviation industry worldwide. The units are currently offered as standard installations or options by the three largest corporate jet manufacturers: Bombardier Aerospace, Dassault Falcon Jet, and Gulfstream Aerospace Corporation. Most VIP airliner conversions are equipped with IWG products. IWG also maintains its focus on the world's aircraft completion centers, where both new production aircraft and older models are modified for use in corporate aviation.

As well as corporate aviation, IWG has an ongoing focus on developing the commercial airline market where the move towards greater focus on aircraft water quality continues. For example, the U.S. Environmental Protection Agency's "Aircraft Drinking Water Rule" of 2009 sets guidelines that address increased water sampling requirements for commercial airliners and consequences for failing water tests. It is the view of IWG that on-board water treatment is the optimum way to deal with this issue.

COMPANY CAPABILITY

The Company's products and services are provided to its aviation customers in many countries. Its marketing, sales support and engineering design groups work directly with its network of Original Equipment Manufacturers (OEM's), aircraft completion centres and aircraft owners to provide the best water treatment solutions and support available. Our marketing and engineering support team engages the marketplace at the world's premier business and aircraft interiors tradeshows, demonstrating to existing and new customers that the Company's products are the best available to assure quality water to their customers.

International Water-Guard maintains its own product and system design team in house, and has experience in designing and certifying both water treatment products and potable water systems to appropriate aviation standards. IWG's extensive computer-aided design capability includes both Solid Works and CATIA systems. In addition, IWG's design team and quality assurance organization have a good working relationship and long history with Transport Canada as our national certifying agency, and with the US Federal Aviation Administration.

To assure ongoing support exists for its products and services, IWG is a Transport Canada approved manufacturing and maintenance organization, holding AS9100 aerospace quality management certification. The Company is also recognized by EASA (the European Aviation Safety Agency) as a certified maintenance organization. IWG operates from an 11,000 sq ft facility with the ability to expand as growth is required.

Primary manufacturing conducted by IWG includes both the production and test of its water treatment units and system components. This manufacturing process is supported by its procurement, quality assurance, testing and engineering staff, and underlying processes and procedures. IWG's customer service capability provides service to OEM's, completion centers and owner/operators worldwide. Currently, IWG supports more than 2,000 water treatment units on various aircraft types, and circulating potable water systems flying on five different aircraft types.

PRODUCTS

Aircraft Water Treatment Units

IWG's family of aircraft water treatment units were designed to address the problem of lack of assured water quality on aircraft. They can be installed by manufacturers as original equipment, or on existing aircraft as a retrofit. The units are fully flight-qualified for use on corporate and commercial aircraft, and meet or exceed the rigorous standards required for certified aviation products.

IWG's aviation products must undergo a rigorous, lengthy, and costly certification process resulting in the issuance of a "Supplemental Type Certificate," or "STC." IWG has been issued U.S. and Canadian STC's on its ultraviolet disinfection equipment, and on its circulating potable water system. The cost and difficulty of the certification process are significant barriers to entry for companies trying to compete in the highly regulated aviation market place.

The premier product, the NPS-A6, is a stainless steel product incorporating both ultraviolet disinfection and filtration which has now been joined by a companion product IWG-A6. The IWG-A6, to be standard on the Gulfstream G650, includes the controller concepts of the "intelligent" IWG-A4 and flow rate of the NPS-A6 but with new capabilities, in an all new package.

The IWG-A4 is the Company's first "intelligent" water treatment unit, and is a standard customer option on the Dassault Falcon Jet family and other aircraft as a "point of use" water treatment option. Ease of maintenance is a key feature of its new modular design. It is also equipped with enhanced self-monitoring capability that ensures adequate ultraviolet light is produced to disinfect the aircraft's water supplies, while scanning for a range of fault conditions which can be reported to a cabin management system through standard industry data protocols.

IWG's original product, the NPS-A2 was designed in the late 1970's. The NPS-A3 received its Transport Canada certification in 2000. The A3 was developed to meet customer needs for a lower flow rate than the newer A6 units and by fitting into smaller spaces while adding filtration to its disinfection capability.

Aircraft Water Systems

IWG has become a known source of comprehensive aircraft water systems solutions and engineering support. IWG's products include its patented Circulating Potable Water System (C-PWS) or custom water management systems for other specific aircraft applications, comprising a variety of third party and custom components, IWG design, and customer support.

Replacement Parts and Service

As the dominant provider of UV based water treatment to the business and 'head-of-state' aircraft markets, the Company supports its large install base with spare parts and overhaul and repair services for its equipment from its headquarters and a European depot.

TECHNOLOGY

IWG water treatment units are designed to provide optimum water treatment to aircraft potable water. Many technologies are available for disinfection and water filtration, and IWG looks at all options in developing its flight-certified products. The Company has found that the safest and most effective technology for on-aircraft disinfection is ultraviolet light. It is possible to develop lightweight, robust equipment that meets rigorous aviation equipment standards, uninterrupted service and a variety of monitoring and fail-safe design features.

Disinfection by Ultraviolet Light is Effective and Clean

Ultraviolet radiation is actually a form of high-energy light. At the proper dosage (intensity and exposure time), UV light is fatal to micro-organisms known to inhabit water. The ultraviolet spectrum ranges from 40 to 400 Nanometers (nm), with the most effective spectral region for germicidal purposes being between 250 and 265 nm.

Mercury arc lamps generate the ultraviolet radiation for water disinfection, with low-pressure lamps being the most common and effective type and are efficient producers of ultraviolet rays in the 254 nm germicidal range. This wavelength is very effective in the destruction of all known micro-organisms, including health threats like E. Coli, Cryptosporidium, and Giardia. IWG also employs high-intensity and amalgam ultraviolet lamps in specific applications.

Studies show that DNA molecules in the nucleus of the organism absorb ultraviolet light which is inactivated when sufficient dosage has been absorbed to modify the molecular structure in the DNA. The scrambling of the genetic code in the nucleus prevents reproduction, rendering it non-viable and harmless to humans.

Filtration alone does not destroy waterborne pathogens; it merely removes unwanted material suspended in the water, such as sediment and chemicals like chlorine. In fact filters can become a good breeding ground for micro-organisms if not changed regularly.

However, ultraviolet disinfection and filtration work extremely well together, since UV treatment is optimized by working on clear water to allow the light to penetrate to its maximum effect. The result of combining filtration with UV is water that is not only safe, but is clean and good-tasting.

MANAGEMENT'S DISCUSSION AND ANALYSIS

OVERVIEW

International Water-Guard Industries Inc. ("IWG") is engaged in the development, design, manufacture, sale and service of potable water treatment equipment and water systems for international aviation customers. The principal technology embodied in IWG's water treatment equipment is irradiation by ultraviolet ("UV") light, combined with filtration, ancillary systems and controls designed by the Company. Water systems may include tanks, water lines, pumps, valves, and electronic controls in addition to water treatment units.

This analysis should be read in conjunction with the Company's comparative audited financial statements and notes for the fiscal year ended September 30, 2010. The discussion and analysis in this report is based on information available to management as of December 8, 2010, and is intended to provide the reader with a further understanding of the Company's business and factors underlying its financial results.

Although the business aircraft industry has experienced a significant downturn during the recession of the last three years coupled with a weaker U.S. dollar, the Company has not been seriously impacted and has been generating positive cash flow from operations. It is generally felt that the bottom of the business jet market has now been seen. The Company held cash of $1,122,172 and had a $500,000 credit line unutilized at September 30th, 2010, enabling it to support its plans to pursue growth and investment in new products.

SELECTED ANNUAL FINANCIAL INFORMATION

($000's except per share amounts)

Fiscal year September 30th	2010	2009	2008
Total revenues	$4,382	$4,953	$4,156
Earnings (loss) from operations before taxes	$189	$425	($148)
Income tax recovery (expense)	($54)	($113)	$51
Net income (loss)	$135	$312	($97)
Earnings (loss) per share, basic and fully diluted	0.3¢	0.7¢	(0.3¢)
Dividends per share	Nil	Nil	Nil
Cash flow from operations	$1	$501	$88
Cash & cash equivalent	$1,122	$1,362	$940
Total assets	$3,351	$3,249	$2,941
Long term debt (1)	$12	$18	$45

(1) Excludes current portion

Additional information relating to the Company is also available under the Company's web site at www.water.aero or under its name on SEDAR at www.sedar.com.

REVIEW OF OPERATING RESULTS

While unit sales of IWG products increased by 7% over the previous year, revenue decreased by 12% due principally to the weakening of the United States dollar compared to the Canadian dollar. Control over expenses, the completion of the R&D phase of a new product, and use of foreign exchange contracts sustained profitability.

Revenue and margins

The Company's revenue in fiscal 2010 of $4,381,894 was a 12% decrease from the prior year's figure of $4,952,911. Sales to customers in Canada represented 22% of the Company's sales with 78% exported, primarily to United States.

The decrease in sales resulted in a lower gross margin percentage, reflecting the non-variable nature of some manufacturing expenses.

The Company now classifies its foreign exchange gains and losses as a separate item, rather than with sales and cost of sales, resulting in minor re-classifications of fiscal 2009 amounts.

Operating expenses

Selling expenses of $449,708 increased by 5% compared to the prior year. Most of this is attributable to increased presence at trade shows.

Engineering and product development expenses of $421,517 represent a 52% decrease from the prior year. This is the result of product development transitioning from the research stage to the development and pre-manufacturing stage, with capitalization of appropriate development costs.

General, administration, insurance, information technology and regulatory related expenses totaled $1,291,515, a small 2% increase compared to fiscal 2009, with increased consulting fees offsetting lower staffing costs.

Earnings

As a result of the various forgoing factors, fiscal 2010 net earnings were $135,423 compared to net earnings of $312,016 in the prior year. The Company's earnings per share were 0.3¢ in fiscal 2010 vs. earnings of 0.7¢ in fiscal 2009, both on a basic and fully diluted basis.

Income taxes

The Company's income tax expense represents the utilization of prior year Non-Capital Losses and other timing differences.

QUARTERLY INFORMATION

The Company's sales were $1,142,763 during the fourth quarter ended September 30th, 2010, compared to $1,127,720 for the same period a year earlier. Earnings from operations were $214,873, compared to $245,017 a year earlier.

The following summary information is taken from the Company's quarterly and annual financial reports covering the last two fiscal years.

Certain comparative figures have been reclassified to conform to the presentation adopted during the year. In particular, foreign exchange gains/losses previously included in revenue and in cost of goods sold have been reclassified with expenses. During fiscal 2010 the Company concluded it was appropriate to defer and then amortize certain product development costs. Such costs incurred during the first through third quarters were included with those deferred and such expenses for those quarters restated in the following table.

Fiscal year ended September 30 ($000's except per share amounts)

	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Year
Fiscal 2010:					
Sales	$1,030	$1,145	$1,064	$1,143	$4,382
Earnings before income taxes	58	77	(161)	215	189
Income tax expense	(17)	(23)	46	(60)	(54)
Net income	41	54	(115)	155	135
Earnings per share, basic and fully diluted	0.1¢	0.2¢	(0.2¢)	0.2¢	0.3¢
Fiscal 2009:					
Sales	$1,222	$1,340	$1,263	$1,128	$4,953
Earnings before income taxes	84	61	35	245	425
Income tax (expense) recovery	(24)	(22)	(12)	(55)	(113)
Net income (loss)	60	39	23	190	312
Earnings per share, basic and fully diluted	0.1¢	0.1¢	0.1¢	0.4¢	0.7¢

There are no significant factors which may be used to predict future performance in either sales or in net income on a quarter to quarter basis.

LIQUIDITY AND CAPITAL RESOURCES

The Company's liquidity and capital resource position remained unchanged during the year with cash provided from operations, enabling the Company to pursue new market opportunities and execute product development.

Cash position
Cash decreased by $240,191 to $1,122,172 from a year earlier, primarily due to regular operating activities including product development and an increase in customer receivables.

Cash flow from operations
Cash provided by operating activities, was $612 in 2010, effectively a break-even ($500,669 in 2009). This amount was from earnings before taxes and non-cash items, offset by a decrease of $297,069 in non-cash working capital changes.

Investing activities
Capital expenditures of $41,196 were incurred by the Company, $16,123 of which is leased. This total included leasehold improvement costs of $3,697, computer equipment and software purchases of $29,107 plus manufacturing and office equipment of $8,393. A further $178,170 was expended on the development of new products introduced to the market.

Cash provided from or utilized in financing activities
The Company utilized $8,375 to buy back 110,000 common shares and $29,184 to meet long-term debt obligations.

Working capital position
The Company completed its 2010 fiscal year with $2,289,382 in working capital, an improvement of $23,379 from the prior year. The Company completed fiscal 2010 with a cash reserve plus a credit facility available sufficient to finance future growth.

Contractual obligations
The Company's operating facility is subject to a lease agreement until November 2010, with one 3-year renewal option, currently under negotiation. Other obligations of the Company are the capital lease and royalty agreements described in the notes to the September 30th financial statements.

Share capital
The Company now has 38,460,694 common shares outstanding as at the date of this report. The Company

announced on September 22, 2010 its intention to make a Normal Course Issuer Bid to repurchase during the following 12 months up to 2 million of its outstanding shares for cancellation. A total of 110,000 shares were purchased to September 30 and a further 770,000 shares purchased to December 8, 2010.

There are 2,580,000 options outstanding under the Company's stock option plan and 5,000,000 warrants issued with the financing completed in August 2008.

FUTURE ACCOUNTING CHANGES

International Financial Reporting Standards

In February 2008, the CICA's Accounting Standards Board (AcSB) confirmed that publicly accountable enterprises would be required to adopt International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board for fiscal years beginning on or after January 1, 2011. The Company will be required to report under IFRS effective for interim and annual financial statements relating to its fiscal year beginning on October 1, 2011.

In the interim, the CICA have issued several accounting policy revisions which have served to conform Canadian GAAP with IFRS, which the Company has adopted when relevant. This serves to minimize any differences the Company must consider upon adoption of IFRS in 2011. These new policies included those affecting inventories, financial instruments, goodwill and intangible assets.

The Company commenced its preparation for transition to IFRS in fiscal 2009 with an initial awareness and assessment of the remaining potential areas of impact on its financial accounting policies and disclosure, determining how its systems and analysis might be impacted and then how changes, if any, might be implemented. This preparation continued into fiscal 2010 with a high level assessment of major differences between Canadian GAAP and IFRS. With these assessments it was determined the areas of accounting differences with the highest potential impact to the Company, and expected changes, are:

Accounting for property, plant and equipment, and impairment – under IFRS, fixed assets may be measured using the cost model, similar to GAAP, or a revaluation model only applied under IFRS. The Company expects to use the cost model with any impact expected to be not significant.

Stock option compensation – under IFRS, the calculation includes as estimate of the number of options expected to vest and a more detailed calculation based on the individual options that vest. This change will be adopted by the Company but should not have a material impact on its financial results.

Share purchase warrants – under IFRS, the proceeds of an issue of common share units, that include share purchase warrants, would be allocated to common shares and to contributed surplus. The allocation would be performed by determining the fair value of the warrants issued recorded at contributed surplus with the residual amount allocated to the common shares.

In addition, the Company is currently evaluating the additional disclosures that may be required under IFRS.

The Company's operations are not overly complex so IFRS transition requirements are limited to a smaller list of policy issues unlike much larger more diversified organizations. As such, the awareness, design and implementation of any changes are also not as extensive as with many other companies. Having identified those areas of impact, key personnel have been and will continually be kept informed as to the impact of changes to the Company's financial reports. The audit committee has and will be provided with any recommendations for adoption of any changes to its policies and systems design during the ongoing review of such policy changes. No significant changes to systems processes have been identified to date. Changes required will be reviewed with the Company's external auditors for final implementation. This will include the development of parallel quarterly financial reports during fiscal 2011 outside the main accounting system to facilitate compilation of comparative IFRS data for its fiscal year 2011.

At this time, the Company is in the process of finalizing its elections under IFRS 1 "First-Time Adoption to IFRS" and expects to have its IFRS compliant opening balance sheets in place early in 2011. During the implementation phase leading up to the transition to IFRS on October 1, 2011, new IFRS updates will be monitored and any changes that are relevant to the Company will be identified and addressed. As such, the final impact of IFRS on the Company's financial statements will only be known once all such IRFSs applicable at the conversion date are known.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Financial statement preparation requires that the Company use estimates and assumptions that affect the reported amount of certain assets and liabilities as well as related revenues and expenses. Our accounting policies are described in note 2 to our financial statements. The following policies have a more significant impact on the Company's financial statements or are significantly impacted by judgments, assumptions and estimates used in the preparation of the Company's financial statements.

Revenue recognition and accounts receivable

Revenue is recognized when persuasive evidence of a contractual arrangement exists, the products and services have been delivered to the customer and there are no significant vendor obligations remaining, the price is fixed or determinable, and collectability is reasonably assured. Amounts received from customers in advance of satisfying all revenue recognition criteria are deferred.

The Company mitigates credit risk through regular credit assessment and collection policies. Trade receivable accounts are reviewed regularly and an allowance for doubtful receivables is recognized when we determine an account is not fully collectable.

Inventory

Inventory is valued at the lower of cost (determined on a first-in, first-out basis) and net realizable value. Raw materials inventory includes parts to be used in the manufacturing process. Work-in-process and finished goods inventory includes the cost of raw materials, direct labour, freight and other direct manufacturing costs including an allocation of indirect manufacturing costs. A provision is recognized to the extent that cost of inventory exceeds its net realizable value. Such provisions are reversed in subsequent periods if the net realizable value increases.

Income taxes

Income taxes are accounted for using the liability method. Future income tax assets and liabilities are determined based on temporary differences between the accounting and tax bases of existing assets and liabilities, and are measured using the tax rates expected to apply when these differences reverse. A valuation allowance based on the Company's best judgment on the recovery of tax losses carried forward and other timing differences is recorded against any future tax asset when such benefits are not expected to be realized.

Deferred product development costs

The Company has certain product development programs that meet the criteria for deferral and amortization of development costs. Such costs are capitalized for clearly defined, technically feasible technologies which management intends to produce and promote to an identified future market, and for which resources exist or are expected to be available to complete the project. Once the development activities have been completed and sales of the related product have commenced, the Company records amortization over a reasonable number of future deliveries, generally during a term of no more than five years.

RISKS AND UNCERTAINTIES

IWG recognizes that certain risks are inherent in its business plan, which requires the Company to manage its affairs to minimize the potential impact of such risks to its operations. The following are the more significant risks managed by the Company.

Financial & Economic Conditions

The worldwide economic downturn has continued to have the potential to impact the Company's performance, although it would seem that the corporate jet market has seen bottom. IWG monitors the situation carefully with a view to mitigating risk from any more significant downturns. The Canadian/U.S. dollar exchange rate is a key factor that the company reviews frequently to minimize adverse impact on the company's financial health.

Aircraft Markets

The Company's primary customers are business-use aircraft manufacturers, owners and operators. Such markets are cyclical over time, although often differing from the cycles for commercial aircraft. The well documented downturn in the corporate jet market has had only a moderate impact on IWG, as it operates in the large business jet and VIP airliner markets that have been less affected.

Sales are made on a standard or optional basis and are dependent upon the production rates and customization of new aircraft or the requirement for upgrading existing aircraft by owners. As a consequence, equipment and systems sales that are not subject to a production agreement will fluctuate from period to period.

Competition

Aviation - Potable Water Treatment Equipment

At this time, there are no other companies with significant sales of flight certified potable water disinfection equipment to the aircraft industry. The market is evolving, with the introduction of broadly competing products. IWG intends to remain the dominant player in this field because of its significant head start, and reputation for quality, service and product innovation. A variety of water filters are used by some airlines and operators, but these do not actively treat and disinfect the water.

Aviation - Potable Water Systems

Currently, IWG is aware of several major full water systems providers in addition to itself. Their focus tends to be on the airliner / regional jet markets, whereas the Company currently places most of its attention on the corporate / VIP jet market. At least one of the companies competes directly in the corporate / VIP market. A variety of companies provide components to aircraft manufacturers for inclusion in their potable water system designs, but IWG is one of the few companies offering aircraft manufacturers a full system solution as a kit.

Intellectual Property

The Company has several patents on its aviation products and water treatment systems. In order to properly protect its intellectual property, the Company from time to time must assert its intellectual property rights against those who appear to be infringing upon them. In this respect, the Company filed a Statement of Claim against Bombardier Inc. on June 26th, 2006, claiming infringement of a Canadian patent owned by the Company. This action is currently in progress.

Foreign Exchange

The Company reports its financial results in Canadian dollars. However, the Company's sales are invoiced in U.S. dollars, which are offset to some extent by the portion of its product costs that are also in U.S. dollars. Generally, fluctuations in the Canadian to U.S. dollar exchange rate are recorded as transactions occur and adjusted for gains or losses at the end of the period that financial results are reported. The details of the Company's foreign exchange policy are included in the notes to the financial statements.

Fluctuations in the Canadian to U.S. dollar foreign exchange rate will impact sales revenue, gross margins and net earnings reported by IWG. With the shift in Canadian to U.S. dollar exchange rate in recent periods, this is an area of risk that has impacted the financial results of IWG. This impact has been mitigated to some degree by entering into short-term foreign exchange contracts to hedge against the fluctuation in exchange rates for a portion of the Company's near term cash flow.

Financial Resources

The Company's operations and cash reserves have ensured that sufficient cash is available to fund the current level of operations, product development, and capital expenditures. Continuing growth in the aviation market may require additional capital beyond that generated from operations.

The notes to the Company's financial statements describe in more detail the credit, liquidity, and fair value risks that may impact the Company's financial instruments.

This is not an exhaustive list of the various risk factors that may be faced by the Company, but is a specific reference to the major risk factors addressed by the Company's management.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company maintains a system of internal controls and procedures over regular financial transactions and financial reports, to ensure management has confidence in the quality of its financial reporting. As such, although the Company has limited staff and consequent restraints on the segregation of duties normally required, conscious effort is made to assure optimum segregation of responsibilities associated with key processes. In addition, there exists amongst senior management familiarity with day to day transactions and mitigating controls consisting primarily of management review of financial information, approval of key transactions and open communication from and with employees. These procedures are deemed sufficient to support its conclusions that no material control weaknesses exist that would impact on the fair presentation of the Company's financial reports, noting that no material adverse control changes have been made during the year that would impact this conclusion.

FORWARD-LOOKING STATEMENTS

The Company's financial reports contain forward-looking statements that involve risks and uncertainties. These forward-looking statements are based on current expectations of management and actual events may differ materially from current expectations.

BUSINESS OUTLOOK

Development activity pursued by IWG in recent years has assured that its water treatment products and systems are at the leading edge of aviation market requirements. The long term business outlook on the aviation sector after coming out of recession is strong, and potable water quality is being perceived as an increasingly important issue.

With its base in the aviation industry firmly established, a solid infrastructure in place and a robust balance sheet, IWG's objective is to significantly grow its business both within current markets, and through exploration of new opportunities that will lever off its industry expertise, corporate structure and financial strength.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The financial statements of International Water-Guard Industries Inc. for the fiscal years ended September 30, 2010 and 2009 and all other information in the annual report are the responsibility of management and have been approved by the Board of Directors.

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. When alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly in all material respects. Management has also prepared the financial information presented elsewhere in the Annual Report and Annual Information Form and has ensured that it is consistent with that in the financial statements.

The Company maintains a system of internal control designed to provide reasonable assurance that financial information is reliable and accurate and that assets are safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting, and is ultimately responsible for reviewing and approving the financial statements. The Board carries out this responsibility, principally through its Audit Committee. The Board appoints the Audit Committee, and all of its members are outside directors. The Audit Committee meets periodically with management, as well as the external auditors, to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues, to satisfy itself that each party is properly discharging its responsibilities, and to review the Annual Report, the financial statements and the external auditors' report.

KPMG LLP, the Company's external auditors, have audited the financial statements in accordance with Canadian generally accepted auditing standards on behalf of the shareholders to provide reasonable assurance that the financial statements are presented fairly, in all material respects, in accordance with Canadian generally accepted accounting principles. KPMG LLP have full and unrestricted access to the Audit Committee to discuss their audit and related findings as to the integrity of the Company's financial reporting.

President, CEO and Director   Chief Financial Officer

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the balance sheets of International Water-Guard Industries Inc. as at September 30, 2010 and 2009 and the statements of net income, comprehensive income and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 2010 and 2009 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Vancouver, Canada
December 8, 2010

BALANCE SHEETS

September 30, 2010 and 2009	2010	2009
Assets		
Current assets:		
Cash and cash equivalents	$ 1,122,172	$ 1,362,363
Accounts receivable	880,150	672,010
Inventory (note 3)	569,976	577,993
Prepaid expenses	75,696	42,807
Future income tax asset (note 9)	70,000	86,000
	2,717,994	2,741,173
Furniture and equipment (note 4)	213,363	229,135
Future income tax assets (note 9)	241,100	279,000
Deferred product development costs	178,170	–
	$ 3,350,627	$ 3,249,308
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 409,381	$ 449,413
Current portion of capital lease obligations and loan payable (note 6)	19,231	25,757
	428,612	475,170
Capital lease obligations and loan payable (note 6)	11,566	18,101
	440,178	493,271
Shareholders' equity:		
Share capital (note 7(b))	8,103,112	8,111,487
Contributed surplus (note 7(c))	227,528	200,164
Deficit	(5,420,191)	(5,555,614)
	2,910,449	2,756,037
Contingencies and commitments (note 8)		
Subsequent event (notes 7(b) and 8(b))		
	$ 3,350,627	$ 3,249,308

See accompanying notes to financial statements.
Approved on behalf of the Board:

David C. Fox
Director

Bruce W. Gowan
Director

STATEMENTS OF NET INCOME, COMPREHENSIVE INCOME AND DEFICIT

Years ended September 30, 2010 and 2009	2010	2009
Sales	$ 4,381,894	$ 4,952,911
Cost of goods sold	2,000,349	1,827,070
Gross profit	2,381,545	3,125,841
Expenses:		
Selling expenses	449,708	427,924
Engineering and product development	421,517	875,219
General, administrative and occupancy	1,291,515	1,266,085
Amortization	56,969	60,389
Foreign exchange loss (gain)	(47,202)	54,754
Interest	19,715	16,454
	2,192,222	2,700,825
Income before taxes	189,323	425,016
Future income tax expense (note 9)	(53,900)	(113,000)
Net income and comprehensive income	135,423	312,016
Deficit, beginning of year	(5,555,614)	(5,867,630)
Deficit, end of year	$ (5,420,191)	$ (5,555,614)
Income per share amounts:		
Basic and diluted	$ 0.003	$ 0.007
Weighted average shares outstanding (note 2(k)):		
Basic and diluted	39,340,069	39,340,283

See accompanying notes to financial statements.

STATEMENTS OF CASH FLOWS

Years ended September 30, 2010 and 2009	2010	2009
Cash flows from (used by):		
Operations:		
Net income	$ 135,423	$ 312,016
Items not involving cash:		
Future income tax expense	53,900	113,000
Amortization	56,969	60,388
Change in value in forward contract	24,024	(47,688)
Stock based compensation	27,364	35,396
	297,680	473,112
Changes in non-cash operating working capital:		
Accounts receivable	(232,164)	86,448
Inventory	8,017	(81,658)
Prepaid expenses	(32,889)	22,600
Accounts payable and accrued liabilities	(40,032)	166
	612	500,668
Financing:		
Repayment of capital lease obligations	(25,038)	(37,795)
Repayment of loan payable	(4,146)	(4,146)
Issuance (repurchase) of capital stock (note 8)	(8,375)	2,250
	(37,559)	(39,691)
Investments:		
Purchase of furniture and equipment	(25,074)	(38,916)
Product development costs incurred	(178,170)	–
	(203,244)	(38,916)
Increase (decrease) in cash and cash equivalents	(240,191)	422,061
Cash and cash equivalents, beginning of year	1,362,363	940,302
Cash and cash equivalents, end of year	$ 1,122,172	$ 1,362,363
Supplementary information:		
Interest paid	$ 19,715	$ 16,454
Non-cash transactions:		
Furniture and equipment purchased using capital lease obligations	16,123	–

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

Years ended September 30, 2010 and 2009

1. OPERATIONS:

The Company is incorporated under the Business Corporations Act (British Columbia). The Company's principal business operations relate to the development, manufacture, and sale of aircraft water treatment equipment and water systems.

2. SIGNIFICANT ACCOUNTING POLICIES:

(a) Basis of presentation and operations:

The Company's financial statements are prepared in accordance with Canadian generally accepted accounting principles and, except where otherwise indicated, are expressed in Canadian dollars. These principles require management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenue and expenses during the reporting period. Significant estimates used in the preparation of these financial statements primarily relate to the assessment of the valuation of accounts receivable, the net realizable value of inventory, the future recoverability of deferred product development costs, and the realizability of future income tax assets. Actual results could differ from these estimates.

(b) Cash and cash equivalents:

Cash equivalents are highly liquid investments, such as term deposits with major financial institutions, having a term to maturity of three months or less at acquisition that are readily convertible to specified amounts of cash.

(c) Inventory:

Inventory is valued at the lower of cost (determined on a first-in, first-out basis) and net realizable value. Raw materials inventory includes parts to be used in the manufacturing process. Work-in-process and finished goods inventory includes the cost of raw materials, direct labour, freight and other direct manufacturing costs as well as an allocation of indirect overhead costs and depreciation. A provision is recognized to the extent that cost of inventory exceeds its net realizable value. Such provisions are reversed in subsequent periods if the net realizable value increases.

(d) Furniture and equipment:

Furniture and equipment is stated at cost. Amortization using the declining-balance method on tooling and equipment is provided at a rate of 20% per annum and on computer equipment at 25% per annum. Leasehold improvements are amortized over the term of the lease on a straight-line basis.

(e) Impairment of long-lived assets:

The Company tests long-lived assets, such as furniture and equipment and deferred product development costs, for impairment when events or circumstances indicate that impairment may exist. Long-lived assets are impaired if the undiscounted cash flows expected to be earned from their use is less than their carrying amount, at which time long-lived assets are written down to their fair value.

(f) Revenue recognition:

Revenue is recognized when persuasive evidence of a contractual arrangement exists, the products and services have been delivered to the customer and there are no significant vendor obligations remaining, the price is fixed or determinable, and collectibility is reasonably assured. Amounts received from customers in advance of satisfying all revenue recognition criteria are deferred.

(g) Government assistance:

The Company receives payments from time to time under various government assistance programs. These payments are recorded in the period during which the amounts are received or receivable. Payments received in respect of operating expenditures are deducted from expenses and in respect of capital expenditures are applied to reduce the cost of such additions. Under certain government assistance programs, the Company is required to pay future royalties to the government as a condition of receiving the grant (note 9(a)). Royalty payments are recognized and expensed when incurred.

(h) Engineering and product development:

Engineering costs are expensed as incurred. Product development costs are expensed as incurred unless certain specified criteria for deferral have been met. The Company applies a stringent interpretation of these criteria, with the result that only costs associated with completing specific technologically feasible product applications having a continuing identifiable market with best estimates of net cash flows in excess of the carrying value of the costs incurred are deferred. Once development activities have been completed and sales of the related product have commenced the Company records amortization over a reasonable number of future deliveries, generally during a term of not more than five years. Routine alterations to existing products are expensed as incurred.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED) :

(i) Income taxes:

Income taxes are accounted for using the liability method. Future income tax assets and liabilities are determined based on temporary differences between the accounting and tax bases of existing assets and liabilities, and are measured using the tax rates expected to apply when these differences reverse. A valuation allowance is recorded against any future tax asset when such benefits are not expected to be realized.

(j) Stock-based compensation:

The Company has a stock-based compensation plan, which is described in note 8(c).

The Company recognizes stock-based compensation related to stock options granted to employees and directors based on the fair value of the options on the grant date and recognizes such stock-based compensation in results from operations over the vesting period. Options granted to consultants are measured at fair value and the related compensation is recognized over the period that the services are delivered. The measurement date for options granted to consultants is the date on which the services are substantially completed and changes in fair value between the grant date and measurement date are recognized in stock-based compensation during the period.

(k) Income per share:

Income per share amounts has been calculated based on the weighted average number of shares outstanding. Fully diluted per share amounts have been calculated using the treasury stock method, which takes into account the dilutive effect of outstanding warrants and options. Securities such as stock options and warrants are included in the calculation of diluted per share amounts only if the market price of the underlying common shares exceeds the exercise price. All of the Company's outstanding options and warrants were excluded from the calculation of diluted earnings per share for the years ended September 30, 2010 and 2009 as they were anti-dilutive.

(l) Foreign exchange translation:

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rates of exchange in effect at the balance sheet date. Revenue and expenses are translated into Canadian dollars at the rates of exchange in effect at the dates of the transactions. Gains or losses arising from foreign exchange translation are included in the results of operations.

(m) Comprehensive income:

Comprehensive income, comprising net income and other comprehensive income, is defined as the change in shareholders' equity from transactions and other events from non-owner sources. Cumulative changes in other comprehensive income are included in accumulated other comprehensive income which is presented as a separate component in shareholders' equity. For both years presented, net income is equal to comprehensive income. Accordingly, no amounts are required to be recognized as a separate component of shareholders' equity.

(n) Financial instruments:

Financial assets and liabilities are initially recognized and subsequently measured based on their classification as held-for-trading, available for sale, held-to-maturity, loans and receivables, or other financial liabilities.

The Company classifies cash and cash equivalents as "held-for-trading", measured at fair value. Accounts receivable are classified as "loans and receivables", and measured at amortized cost.

Accounts payable and accrued liabilities, capital lease obligations and loan payable are classified as other financial liabilities and are measured at amortized cost.

The Company enters into foreign currency forward contracts from time to time to protect itself against fluctuations in the U.S. dollar exchange rate. The Company does not use hedge accounting. Accordingly, the foreign currency forward contracts are recognized at fair value on the balance sheet and changes in fair value are recognized under expenses in the statement of operations.

The fair value disclosure for such financial instruments (assets or liabilities) includes a three-level hierarchy classification that reflects the significant inputs used in making such fair value measurement. Those assets or liabilities included in Level I are determined by active market quotations of similar items, those in Level II are determined by other observable market data and Level III items are those determined by inputs not based on quoted or observable data. The fair value classifications are included in note 11(d).

(o) Future changes to accounting policies:

In February 2008, the CICA's Accounting Standards Board (AcSB) confirmed that publicly accountable enterprises would be required to adopt International Financial Reporting Standards (IFRS) as issued by the International Accounting

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED) :

Standards Board for fiscal years beginning on or after January 1, 2011. The Company will be required to report under IFRS effective for interim and annual financial statements relating to its fiscal year beginning on October 1, 2011.

In the period leading up to the changeover, the International Accounting Standards Board may continue to issue new standards. As such, the final impact of IFRS on the Company's financial statements will only be known once all such IFRSs applicable at the conversion date are known. Currently, the Company expects the most significant impact of IFRS to be on the measurement and presentation of stock-based compensation and share purchase warrants.

(p) Comparative figures:

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

3. INVENTORY:

	2010	2009
Raw materials and work-in-process	$ 412,139	$ 443,505
Finished goods	157,837	134,488
	$ 569,976	$ 577,993

4. FURNITURE AND EQUIPMENT:

	2010	2009
Tooling	$ 7,779	$ 7,779
Manufacturing and distribution equipment	103,671	95,278
Furniture and office equipment	426,536	397,429
Leasehold improvements	104,769	101,072
	642,755	601,558
Accumulated amortization	(429,392)	(372,423)
Net book value	$ 213,363	$ 229,135

As at September 30, 2010, furniture and equipment with a cost of $68,529 (2009 - $92,831) and a net book value of $39,688 (2009 - $50,495) is held under capital lease.

5. BANK CREDIT LINES:

The Company has a $500,000 operating loan credit facility with The Toronto-Dominion Bank. Amounts drawn on the facility bear interest at bank prime rate plus 1.5% and are secured by a general security agreement on the Company's assets with normal covenants and margin requirements. At September 30, 2010, no amounts have been drawn on this facility.

6. CAPITAL LEASE OBLIGATIONS AND LOAN PAYABLE:

	2010	2009
Obligations under capital leases	$ 22,505	$ 31,420
Loan payable	8,292	12,438
	30,797	43,858
Current portion	19,231	25,757
	$ 11,566	$ 18,101

The Company has entered into several capital lease agreements for equipment. These lease obligations have terms from 10 to 30 months, with interest rates ranging from 2.3% to 10.5% and averaging 6.1%. Each lease includes a purchase option approximating 10% of the equipment cost exercisable prior to the completion of the lease period. The present value of the lease obligations are recorded as a liability, with the current portion included in current liabilities.

The capital lease obligations require the following minimum annual payments during respective fiscal years:

2011	$ 16,457
2012	5,724
2013	2,222
	24,403
Less: amount representing interest	1,898
Principal amount of capital lease obligation	$ 22,505

During 2002, the Company received funds from Industry Canada's Industrial Technology Office (ITO). The loan outstanding is non-interest bearing, repayable in equal annual installments until December 2011. Interest at ITO's prescribed rates plus 300 basis points is charged on late payments.

7. SHARE CAPITAL:

(a) Authorized:

Unlimited number of common shares without par value

Unlimited number of preference shares without par value

(b) Issued common shares:

	2010		2009	
Common shares	Shares	Amount	Shares	Amount
Balance at beginning of year	39,340,694	$ 8,111,487	39,310,694	$ 8,108,202
Issued for cash on exercise of options	–	–	30,000	3,285
Repurchased under a Normal Course Issuer Bid	(110,000)	(8,375)	–	–
Balance at end of year	39,230,694	$ 8,103,112	39,340,694	$ 8,111,487

The Company announced on September 22, 2010 its intention to make a Normal Course Issuer Bid to repurchase during the following 12 months up to 2 million of its outstanding common shares for cancellation. A total of 110,000 shares were purchased at an average price of $0.075 to September 30, 2010. These shares had not been cancelled at that date.

Subsequent to this date and until December 8, 2010, a further 770,000 shares have been purchased at an average price of $0.073 for a total of 880,000 common shares purchased for cancellation.

(c) Stock options:

The Company, from time to time, grants stock options to employees, directors, officers and certain consultants under the Company's stock option plan. The maximum amount of options available for issue is 3,503,000 common shares. These stock options are granted at the discretion of, and have terms and conditions as directed by, the Board of Directors. Stock options generally vest over a period of eighteen months following the date of grant.

A summary of the status of the Company's stock option plan as at September 30, 2010 and 2009 and changes during the years ending on those dates is presented below:

	2010		2009	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding, beginning of year	2,582,500	0.13	2,197,500	$ 0.14
Granted	530,000	0.09	767,000	0.10
Exercised	–		(30,000)	(0.08)
Cancelled or expired	(532,500)	(0.10)	(352,000)	(0.11)
Outstanding, end of year	2,580,000	0.13	2,582,500	0.13
Options exercisable, end of year	2,302,000	0.14	2,131,500	$ 0.14

Stock options outstanding and exercisable at September 30, 2010:

Number of stock options outstanding	Options exercisable	Exercise price	Weighted average remaining contractual life
580,000	580,000	$ 0.21	19.5 months
150,000	150,000	0.15	22.3 months
320,000	320,000	0.13	27.7 months
280,000	280,000	0.12	10.8 months
720,000	720,000	0.10	37.8 months
530,000	252,000	0.09	49.9 months
2,580,000	2,302,000		31.1 months

7. SHARE CAPITAL (CONTINUED) :

During the year ended September 30, 2010, the Company recognized $27,364 (2009 - $35,396) in stock-based compensation related to options granted.

The fair value of options granted during the year ended September 30, 2010 was calculated using the Black-Scholes option pricing model assuming a weighted average risk-free interest rate of 2.65% (2009 - 1.62%), a dividend yield of 0.0%, a weighted average expected volatility of 54.6% (2009 - 53.1%) and expected life of stock options of 3 years (2009 - 4 years). The weighted average grant date fair value of options granted during the year ended September 30, 2010 was $0.03 (2009 - $0.04).

Changes in contributed surplus related to stock-based compensation are as follows:

Contributed surplus	2010	2009
Balance at beginning of year	$ 200,164	$ 165,803
Stock-based compensation reclassified to share capital on exercise of options	–	(1,035)
Stock-based compensation recognized	27,364	35,396
Balance at end of year	$ 227,528	$ 200,164

(d) Stock purchase warrants:

There are 5,000,000 warrants outstanding exercisable at $0.17 until August 28, 2011. These warrants were issued in connection with the private placement of common shares in August 2008. In August 2010, the expiry date was extended by one year.

8. CONTINGENCIES AND COMMITMENTS:

(a) The Company entered into an agreement with the National Research Council of Canada (NRC/IRAP) in 2002, whereby NRC/IRAP assisted in the funding to further develop the Company's potable water systems for certain aircraft (C-PWSTM) in the amount of $495,000. As a condition of this agreement, the Company agreed to pay NRC/IRAP a royalty of 2% of the Company's gross revenue earned for the quarters ended June 30, 2005 and September 30, 2007 and then from January 1, 2009 for every quarter thereafter through December 31, 2014 up to a maximum amount of $742,500. Royalty payments have been made as required with accumulated royalties paid or payable to September 30, 2010 totaling $239,832 (2009 - $151,956).

(b) The Company entered into a long-term operating lease for premises expiring November 30, 2010, subsequently renewed to November 30, 2013. The annual lease payments, exclusive of property taxes and expenses directly payable by the Company, are:

2011	$ 105,300
2012	112,612
2013	116,513
2014	19,500
	$ 353,925

9. INCOME TAXES:

Income tax expense differs from the amounts computed by applying the combined Canadian federal and provincial income tax rate of 28.88% (2009 - 30.25%) to earnings before income taxes as follows:

	2010	2009
Income before taxes	$ 189,323	$ 425,016
Expected income tax expense	$ (54,667)	$ (128,567)
Tax effect of:		
Change in valuation allowance	351,497	271,342
Change in tax rate	(14,430)	(47,576)
Expired tax losses	(319,696)	(199,119)
Other	(16,604)	(9,080)
Income tax expense	$ (53,900)	$ (113,000)

The tax effects of temporary differences that give rise to future tax assets are presented below:

	2010	2009
Future income tax assets:		
Non-capital losses carried forward	$ 285,003	$ 660,731
Furniture and equipment	100,117	88,816
Scientific research and development expenditures	90,788	90,788
Share issue costs	4,094	7,171
Total gross future income tax assets	480,002	847,506
Valuation allowance	(115,360)	(466,857)
	364,642	380,649
Future income tax liabilities:		
Forward contracts	(8,144)	(15,649)
Deferred development costs	(45,398)	–
Net future income tax assets	$ 311,100	$ 365,000

9. INCOME TAXES (CONTINUED) :

Future income tax assets are classified on the balance sheet as follows:

	2010	2009
As current asset	$ 70,000	$ 86,000
As long-term asset	241,100	279,000
	$ 311,100	$ 365,000

The ultimate realization of the future tax assets is dependent on the generation of taxable income during periods in which the temporary differences reverse. As at September 30, 2010, evidence does not yet exist to support a conclusion that it is more likely than not that all future income tax assets will be realized. Accordingly, a valuation allowance has been recorded against those future tax assets for which realization is not certain. In its determination of the valuation allowance, the Company considered forecasted future earnings and taxable income in the period during which losses are expected to expire or other temporary differences are expected to reverse.

The Company has non-capital loss carry forwards of approximately $1,097,000 which will expire as follows:

2014	$ 991,000
2028	106,000

The Company also has Scientific Research and Development expenditures of approximately $363,000 which are available to offset taxable income indefinitely.

10. FINANCIAL INSTRUMENTS:

(a) Foreign currency risk:

A foreign currency risk will exist where the future cash flows of financial instruments will fluctuate because of changes in foreign currency exchange rates. The Company conducts a significant portion of its business activities in United States dollars (USD). Cash and cash equivalents, accounts receivable and accounts payable that are denominated in USD will be affected by changes in the exchange rate between the Canadian dollar and the USD.

The USD carrying amount subject to exposure to such foreign currency risk at September 30, 2010 is as follows (USD amounts):

	2010	2009
Cash and cash equivalents	$ 125,303	$ 284,710
Accounts receivable	777,998	563,320
Accounts payable	50,543	29,328

The Company periodically uses foreign currency forward contracts to fix the rate of exchange for Canadian dollars (CAD) at future dates in order to reduce a portion of the Company's exposure to foreign currency fluctuations on USD sales. At September 30, 2010, the Company had open forward currency contracts with a total commitment to sell USD$2,300,000 at an average rate of CAD$1.047 to August 2011.

A 100 basis point change in the foreign exchange rate as at September 30, 2010 would have changed net results by approximately $31,770 (2009 - $21,926).

(b) Credit risk:

The Company's exposure to credit risk will relate to uncertainties as to the timing and collectability of accounts receivable. The Company mitigates credit risk through regular credit assessment and collection policies. The Company reviews its trade receivable accounts regularly and will recognize an allowance for doubtful receivables should it be determined an account is not fully collectable. All amounts due are from long term regular customers who generally pay within agreed payment terms.

The carrying amount of financial assets represented by accounts receivable of $880,150 (2009 - $672,010) represents the maximum credit exposure. At September 30, 2010, six customers (2009 - nine) represented approximately 96% (2009 - 94%) of accounts receivable.

The Company's cash and cash equivalents are held by a Canadian Schedule 1 bank.

(c) Liquidity risk:

Liquidity risk is the risk that the Company would not be able to meet its financial obligations as they fall due. The Company's cash flows have enabled it to satisfy its financial commitments for its current and long-term debt, financial and operating leases, royalties, and lease commitments. The Company maintains up-to-date budgets and/or forecasts of sales, costs, and expenses related to its current and future products and the sales value impacted by fluctuations in the value of the U.S. dollar to enable the Company to manage its future operating cash position.

10. FINANCIAL INSTRUMENTS (CONTINUED) :

The following contractual maturities of financial obligations exist as at September 30, 2010.

	Carrying amount	Contractual cash flows	Within 1 year	2 to 4 years	5 years and over
Accounts payable and accrued liabilities	$ 409,381	$ 409,381	$ 409,381	$ –	$ –
Loan payable	8,292	8,292	4,146	4,146	–
Obligations under capital lease	22,505	24,403	16,457	7,946	–
Operating lease commitments	–	353,925	105,300	248,625	–
Royalty payments	–	502,668	104,640	249,598	148,430
	$ 440,178	$ 1,298,669	$ 639,924	$ 510,315	$ 148,430

(d) Fair values:

Financial instruments include cash and cash equivalents accounts receivable, accounts payable and accrued liabilities, the carrying values of which are considered by management to approximate their fair values due to their ability for prompt liquidation and short-term to maturity, and loan payable and capital lease obligations, the fair value of which is not materially different from its carrying value based on market rates of interest. Cash and cash equivalents are recognized at fair value which is classified within Level 1 of the fair value hierarchy.

The fair value of foreign currency forward contracts was an asset of $30,164 at September 30, 2010 (2009 - $54,188). This asset has been included in accrued receivables on the Company's balance sheet, and is classified as Level II in the fair value hierarchy.

11. MANAGEMENT OF CAPITAL:

As at September 30, 2010, the Company's capital is composed of share capital.

The Company's objectives when managing capital are as follows:

(a) to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders; and

(b) to have sufficient cash, cash equivalents, short-term investments and marketable securities on hand to fund the Company's business plans.

The Company's primary uses of capital are to finance product development, market development, working capital, capital expenditures, and operating losses. The Company currently funds these requirements from internally generated cash flows, amounts drawn against its line of credit and proceeds from the offering of debt or equity securities. There were no changes to the Company's approach to capital management during the year ended September 30, 2010. The Company is not subject to externally imposed capital requirements.

12. SEGMENTED INFORMATION:

The Company's principal business operations relate to the development, manufacturing, and sale of aircraft water treatment equipment and water systems and, accordingly, the Company has only one reportable segment. In 2010, sales to five customers (2009 - five customers) represent approximately 82% (2009 - 85%) of total revenue. All of the Company's furniture and equipment is located in Canada. In 2010, approximately 22% (2009 - 25%) of sales revenue was generated by customers in Canada and 78% (2009 - 75%) by customers in other countries, primarily the United States.

DIRECTORS & OFFICERS

Bruce W. Gowan – Chairman of the Board
Mr. Gowan, a Chartered Accountant, is the former Chief Financial Officer at Magellan Aerospace, and continues as a member of the company's Board of Directors where he chairs it's Governance & Nominating Committee and the Pension Committee and serves on the Audit Committee and the Human Resources and Compensation Committee. He is also a director of Radiant Energy Corporation, a provider of airport de-icing systems, chairing its Audit Committee. Mr. Gowan is also a director and past-chairman of the Board for Lakeland Holdings Ltd., a power generation and power distribution company, and of several community organizations.

David C. Fox – President and CEO
Mr. Fox has many years of business development and aerospace experience and holds both an Aeronautical Engineering Degree from the University of London and an MBA from the London Business School. From 1989 to 1995, he was Vice President and General Manager of Airshow Canada, a major international aerospace tradeshow. He served as IWG's Vice President, Aerospace Business from 1996 to 1998. Until May 2004, Mr. Fox was Vice President, Business Development for Vortek Industries Ltd., a supplier of high-energy optical systems to the aerospace /materials testing and semiconductor industries.

Michael A. Evans – Director
Mr. Evans is a Principal of Evans & Evans, Inc., a leading Canadian boutique investment banking firm with offices in Canada, the U.S. and Asia. Since 1990 He has raised millions of dollars for numerous clients through private placements, public offerings, and debt issuances. He has also advised on many merger and acquisition transactions and has originated transactions both for purchasers and sellers. He holds a Bachelor of Business Administration degree from Simon Fraser University, a Master's degree in Business Administration from the University of Portland, and the professional designations of Chartered Financial Analyst (CFA), Chartered Business Valuator (CBV) and Accredited Senior Appraiser (ASA). He is a member of the Association of Investment Management and Research, the Canadian Institute of Chartered Business Valuators and the American Society of Appraisers. Mr. Evans is also a Director of Weifei Capital Inc. and Bastion Resources Ltd.

John J.D. Lawson – Director
Mr. Lawson began his aviation career with 18-years in the Canadian Armed Forces, where he was a Flight Instructor, Fighter Pilot, and Test Pilot. He is a graduate of the Royal Military College and the University of Toronto, where he received an Honours BASc in electrical engineering. He left the Air Force in 1975 with the rank of Lieutenant Colonel to pursue a career in business. He retired in 2001 as President of Bombardier Business Aircraft Sales with responsibility for the worldwide marketing and sales of all Learjet and Bombardier corporate jets. Previous to that, Mr. Lawson held several positions within the Bombardier group, including President of Canadair Business Aircraft, Vice-President, Marketing and International Sales, and Vice-President of Challenger Product Support. Mr. Lawson is currently a Director of NAV CANADA.

Bruce G. MacCoubrey – Director
Mr. MacCoubrey completed a highly successful career with Air Canada as Vice-President, Strategic Business Services and Chief Purchasing Officer in 2003. He is now consulting in the aviation industry. He is a member of the Order of Engineers of Quebec and holds a Masters Degree in Business Administration from McGill University. He joined Air Canada in 1969, held senior positions in Cargo, Airport Operations Planning, Purchasing & Supply, and Component Maintenance and in 2000 was appointed a Vice-President and Chief Purchasing Officer. He has also been Chairman of the Board for AeroXchange, and Board Member for Airliance Materials, and Acetec. Mr. MacCoubrey was also Chairman of the Star Alliance Purchasing Committee, and Chairman of the Air Transport Association Materials Management Committee.

Michael J. Piscatella – Director
Mr. Piscatella has over thirty-five years of aerospace business experience. He currently is the Senior Vice President of Business Development for Tailwind Technologies Inc. and its subsidiary Hartzell Propeller Inc. His previous experience includes president positions at Industrial Tube Corporation and Electrofilm Manufacturing Company, also subsidiaries of Tailwind Technologies Inc. Previously he spent nine years with Goodrich Corporation, a period in which he rose to become Group President, Aerostructures & Aviation Technical Services, and twenty-five years with Textron Lycoming, culminating with the position of Director, International Business. Mr. Piscatella is also a member of the President's Advisory Board for Embry-Riddle Aeronautical University.

Gerald P. Eiers – Vice-President & General Manager
Mr. Eiers' experience with both large and small manufacturing firms gives him a strong background in marketing and sales. In addition, he provides leadership to IWG's procurement and manufacturing teams and oversees the company's administrative functions, including: human resources, information technology and facility development. Mr. Eiers' joined IWG in 1997, and until September 2001 was responsible for the company's accounting and administrative functions.

Brian Ulrich – VP, Engineering
Mr. Ulrich brings to IWG an extensive background in project and product management. He has provided strong business and technical leadership for complex engineering projects in the power electronics, opto-electro-mechanical print prepress, space robotics and aerospace industries. Past positions have included Product Manager with Xantrex Technologies of Burnaby, BC, Product Manager with CreoScitex Inc. of Burnaby, BC, Senior Robotics Engineer with Davion Systems, St Bruno, PQ and Rocket Propulsion Design Engineer with Bristol Aerospace Ltd, of Winnipeg, MB.

C. Edward Butterfield – Chief Financial Officer and Corporate Secretary
Mr. Butterfield is a Chartered Accountant with a career in managing the financial and business operations of public companies. Prior to joining IWG in year 2000, he served as CFO and Corporate Secretary with a major public aerospace component manufacturer he had joined in 1989. Mr. Butterfield has also served as the senior financial officer of several other public and private companies in the manufacturing, distribution and financial sectors.

CORPORATE INFORMATION

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Capital Structure
(as at January 4, 2011)
Authorized: an Unlimited number of Common Shares and an Unlimited number of Preference Shares
Issued: 38,185,694 Common Shares

Stock Exchange
TSX Venture Exchange
Trading Symbol: "IWG"

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