

NATIONAL CHALLENGE SYSTEMS INC.
2007 ANNUAL REPORT

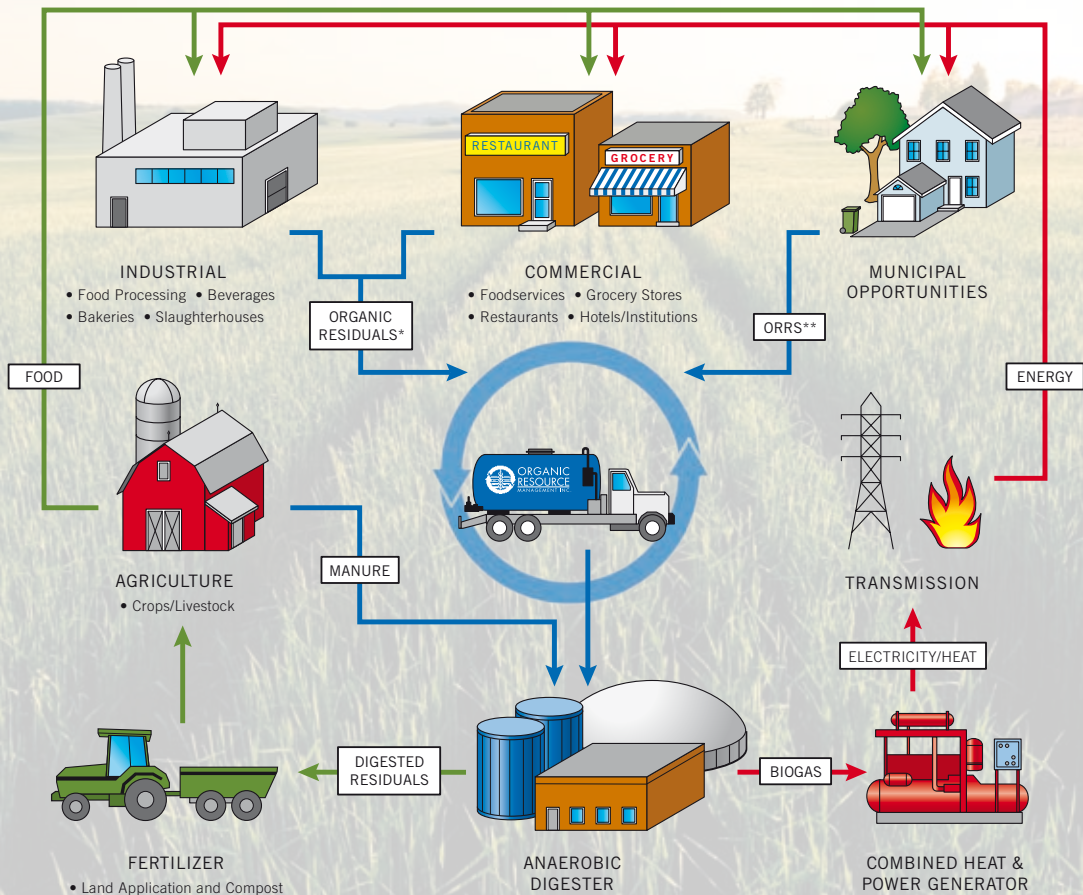
HOW IT WORKS

On-farm anaerobic digestion of manure creates biogas, which is a combination of methane and carbon dioxide that can be used to generate electricity and heat. The liquid organic residuals the Company collects provide 4 to 10 times the gas production of manure and are an ideal feedstock in conjunction with manure for anaerobic digesters. The combined digested material is a virtually odour-free, organic fertilizer that is used on farm fields. This technology is a clean renewable energy solution that is cost effective and environmentally beneficial.

BENEFITS

- + Renewable energy
- + Greenhouse gas reduction
- + Expands organic recycling capacity and reduces reliance on landfills
- + Major reduction in odour and pathogens in the digested material
- + Improves wastewater treatment and groundwater protection
- + Improves the nutrient availability in the digested material

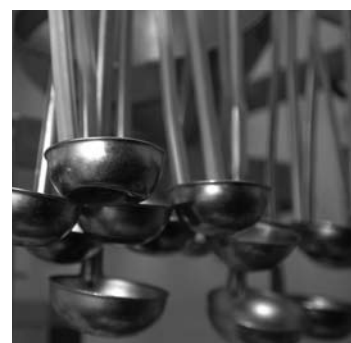
ORGANIC RESIDUALS TO RENEWABLE ENERGY COMING FULL CIRCLE



*Organic Residuals from wastewater (i.e. grease traps, DAF) and food waste

**ORRS (ORGANIC RESOURCE RECOVERY SYSTEM)

Organic Resource Management Inc., formerly National Challenge Systems Inc., is Canada's largest provider of vacuum truck services for the collection, treatment and recycling of organic and other non-hazardous liquid residuals. The Company provides services to more than 8,000 customers, mostly in the food service, processing, production and retail business. Organic Resource Management Inc. operates in Ontario and Quebec, and in the lower mainland of British Columbia through its wholly owned subsidiary A&A Anderson Tank Service (Vancouver) Ltd.



FINANCIAL HIGHLIGHTS

	2007	2006	2005	2004	2003
Total assets	\$ 11,368,028	\$ 11,747,603	\$ 13,278,384	\$ 13,534,106	\$ 14,506,492
Total liabilities	4,867,707	8,111,240	8,539,291	7,756,333	7,787,530
Long-term debt	742,290	899,435	1,348,455	1,106,270	1,486,005
Shareholders' equity	6,500,321	3,636,363	4,739,093	5,777,773	6,718,962
Net Book Value per Share	0.074	0.091	0.120	0.169	0.197
Revenue	15,418,215	16,031,828	14,494,091	13,677,228	14,053,175
Gross margin	4,649,577	4,049,693	3,614,654	3,351,773	3,682,907
Net loss	(1,243,650)	(1,195,838)	(1,129,874)	(1,691,352)	(2,140,194)
Loss per share basic and diluted	(0.03)	(0.03)	(0.03)	(0.05)	(0.06)
Cash flows from operating activities	998,107	739,061	701,422	359,562	345,442



MESSAGE TO SHAREHOLDERS

The year ended June 30, 2007 was a watershed year for our Company.

Several years of effort were rewarded in May of 2007 with the signing of the first long term feedstock supply agreement with a farm-based Anaerobic Digester (“AD”) for the production of renewable biogas energy from the Company’s organic residuals. Although the volume of residuals the farm currently receives is small, what is important is that this is the first Ontario on-farm AD to receive off-farm organic residuals and produce biogas energy.

I believe that this marks the end of a particularly challenging period for the Company. As the AD industry develops in Ontario and the rest of North America, the residuals that the Company collects will be converted from a difficult to manage recyclable waste to a valuable energy producing resource. As that happens, we will finally shed the constraints of limited recycling capacity that has plagued us for the past five years. And we will be firmly positioned to benefit from the expansion of the organics recycling industry that will inevitably follow.

In June 2007, we began executing an aggressive multi-step restructuring plan that we believe will simplify the Company’s management and organizational structure and make it a more profitable and dynamic company. We have now:

1. Converted all the outstanding preferred shares into common shares to improve the balance sheet, eliminate dividend expenses and simplify the Company’s share structure;
2. Amalgamated the Company with its largest subsidiary, and changed its name to Organic Resource Management Inc. to better reflect the Company’s core business;
3. Made a number of appointments and changes at the Board and executive level to streamline and augment the management and governance of the Company; and,
4. Acquired the proprietary software and patents the Company uses, thereby eliminating significant related party relationships, and allowing us to ultimately eliminate the complex US and Bermuda corporate structure.

We will also be seeking shareholder approval for a consolidation of the Company's common shares on the basis of one for twenty, in order to increase the Company's share price, thereby making it more attractive to a larger investor pool.

Simplifying the balance sheet and shedding the baggage of complex agreements and structures will allow the management team to focus on the Company's key business strategies; and potential investors and financiers to better understand the Company.

I am pleased to report that as all of this has been happening, our financial position has also continued to improve. Cash flows from operating activities increased by 35% to \$998,000 for 2007. And although total revenue was slightly down, concentration on the Company's core and more profitable business, its grease interceptor servicing, resulted in 10% growth in this area. Reduced residuals management costs combined with improved revenue quality generated a 15% increase in gross margin.

The elimination of preferred share dividends as a result of the restructuring combined with the end of intangible asset amortization related to the 2002 purchase of Organic Resource Management Inc. and A&A Anderson Tank Service (Vancouver) Ltd., will result in major expense reductions going forward. Including the write-down of patents, these items accounted for \$2,216,000 of non-cash expenses in 2007 that will not reoccur in 2008.

The Company continues to strive towards its mission to be the recognized leader in providing optimum solutions for the collection, transportation and recycling of organic and other non-hazardous liquid residuals through a team dedicated to service excellence and environmental responsibility. The Company has come through a difficult period that was exacerbated by the combination of a weak balance sheet and less than favorable government legislation and regulations with respect to disposal options. It is a tribute to our employees, our customer loyalty, and our systems and technologies, that we were able to persevere through it.

Although much is still to be done before AD becomes an industry in North America and a reality for the Company, we certainly welcome the challenges and look forward to the next twelve months.

On behalf of your executive team and the Board, I take this opportunity to thank our employees, our customers and our shareholders for their exemplary efforts, continued commitment and continued support.



Charles H. Buehler
Chief Executive Officer

THE FOUR FUNDAMENTALS

The Company's core business is the regularly scheduled **Collection** of non-hazardous liquid organic residuals. These residuals come from the excess organic material that is separated from wastewater discharges and accumulates in grease interceptors and dissolved air flotation systems. Using vacuum trucks dispatched by proprietary **Software**, the Company collects the liquid residuals from over 8,000 restaurants, grocery stores and other food processing facilities. The residuals are taken to the Company's facilities for **Processing** to remove excess water and the final processed residuals are transported to **Recycling** locations.



1 COLLECTION

Using a specialized fleet of vacuum trucks operated by expressly trained technicians, the Company picks up residuals in Ontario and the lower mainland of British Columbia. The trucks vary from small low-profile units that can fit into underground parking areas to tractor trailer units that can pickup 36,000 litres of material at a time.

In addition, the Company has a patent protected process for on-site collection of organic waste called the Organic Resource Recovery System ("ORRS"). Produce and other food related wastes are ground into slurry by a mill and discharged into a holding tank where it is stored until collected by our vacuum truck.



2 SOFTWARE

With over 8,000 customers, each with a specific volume of residuals and a unique time window to perform the pick up, logistics is extremely complex. The Company uses proprietary, sophisticated logistics software to affectively manage this problem. Our centralized customer service department uses map-based routing and dispatch software, coupled with technicians equipped with wireless handhelds and GPS tracking. The software results in a superior customer service, a highly productive fleet, and makes a labour intensive logistics function easily executable.

3 PROCESSING

Collected residuals are transported to local Company facilities. The Company operates transfer facilities where excess water is decanted in preparation for final use. This is our proprietary biological process that breaks down organic materials in the absence of oxygen. The decanted residual is then transported by the Company for recycling. Decanting is a very helpful pre-treatment process for enhancing the value of residuals for composting and anaerobic digestion. By reducing the water content and blending specific residuals, the Company will be able to maximize the performance of individual anaerobic digesters to ultimately produce biogas and the generation of clean renewable energy on an environmentally friendly and cost effective basis.



4 RECYCLING

Today most of the Company's residuals are taken to third party compost facilities for recycling. The Company is beginning to take a small amount of its residuals to the newly emerging anaerobic digestion industry. The Company believes that in the future, anaerobic digestion will be the most cost effective and environmentally beneficial organic waste recycling technology (see inside cover). The Company intends to partner with anaerobic digestion facilities through long term contractual relationships and through equity participation.

Our ORRS units, which liquify food organics, provide an end residual product ideal for anaerobic digestion and renewable energy production.



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FORWARD-LOOKING STATEMENTS

Certain statements made or incorporated by reference in this MD&A are forward-looking and relate to, among other things, anticipated financial performance, business projects, strategies, regulatory developments, new services, market forces, commitments and technological developments. By its nature, such forward-looking information is subject to various risks and uncertainties, including those discussed in this MD&A or in documents incorporated by reference in this MD&A, which could cause the Company's actual results and experience to differ materially from the anticipated results or expectations expressed. Readers are cautioned not to place undue reliance on this forward-looking information, and the Company undertakes no obligation to update publicly or revise any forward-looking information, whether as a result of new information, future events or otherwise, except in accordance with applicable securities laws.

MANAGEMENT DISCUSSION & ANALYSIS

The following Management's Discussion and Analysis ("MD&A") should be read in conjunction with National Challenge Systems Inc.'s ("NCS" or the "Company") fiscal 2007 consolidated financial statements and notes thereto.

Generally, all disclosure is made as of September 20, 2007, unless otherwise indicated. Financial information is presented as at June 30, 2007 in conformity with Canadian generally accepted accounting principles.

On July 1, 2007 the Company vertically amalgamated its largest wholly owned subsidiary, Organic Resource Management Inc. into National Challenge Systems Inc. and continued with its subsidiary's name. This change simplified the corporate structure and gave the Company a name more closely reflective of its core business. The Company's shares trade under the new name with a new TSX trading symbol of "ORI".

TABLE OF ACRONYMS

Acronym	Description	Acronym	Description
A&A	A&A Anderson Tank Service (Vancouver) Ltd.	NCS	National Challenge Systems Inc.
AD	Anaerobic Digestion	NCS ESL	NCS Environmental Services Ltd.
Company	National Challenge Systems Inc.	OII	Organic Resource Technologies International Inc.
DAF	Dissolved Air Flotation	ORMI	Organic Resource Management Inc.
DLAP	Direct Land Application Process	OIS	ORMI Information Systems Inc.
FOG	Fats, Oils & Grease	ORRS	Organic Resource Recovery System
GVRD	Greater Vancouver Regional District	ORTI	Organic Resource Technologies Inc.
IC&I	Industrial, Commercial & Institutional	Path	Path Information Systems Inc.
MD&A	Management Discussion & Analysis	SOP	Standard Offer Program
MOE	Ministry of Environment		

CORPORATE OVERVIEW

NCS is Canada's largest provider of vacuum truck services for the collection, treatment and recycling of organic and other non-hazardous liquid residuals. The vast majority of the residuals the Company collects are from customers in the food service, processing, production or retail business and include industrial, commercial and institutional ("IC&I") operations.

NCS services more than 8,000 customers in Canada through its two wholly-owned subsidiaries, Organic Resource Management Inc. ("ORMI") operating in Ontario and Quebec, and A&A Anderson Tank Service (Vancouver) Ltd. ("A&A") operating in the lower mainland of British Columbia.

NCS' core business is comprised of two distinct elements. The first is the regularly scheduled collection and transportation of organic and other non-hazardous liquid residuals. The primary source of these residuals is the food industry sectors. Within the food sectors the primary source is from the separation of excess organic residuals from wastewater discharges to prevent the adverse effect of discharging excessive organic materials to the drainage and sewer systems. These residuals accumulate on a predictable basis and require regular scheduled collection and removal. The second element of the Company's business is comprised of managing the disposal or recycling of the residuals it collects in the most cost effective and environmentally responsible manner. The Company does this through owned technologies and facilities, as well as through third-party relationships.

There are four major market drivers for the Company's services:

- **Protection of the municipal sewer infrastructure.** Municipalities regulate the amounts of organic residuals that can be discharged into the municipal sewer and as a result the Company's customers are required to capture, remove and properly dispose of these residuals. The Company provides the collection, transportation and recycling of these residuals. The Company's services help:
 - Prevent blockages and floods in the municipal sewer system.
 - Customers reduce the risk of exceeding sewer discharge limits and incurring expensive fines and remediation charges.
 - Improve the environmental quality of wastewater.
 - Increase the wastewater infrastructure capacity, allowing the same, existing physical infrastructure to service a greater customer base.
 - Limit the organic fats, oil and greases that are discharged into the sewer system and deposited in concrete sewer pipes accelerating corrosion of those pipes, thereby reducing infrastructure longevity.
- **Protection of the customer's physical drainage infrastructure.** The Company's services help prevent drain blockages at the customer's location that can result in costly backups, floods and business interruption.
- **Organic residuals diversion.** Municipalities are continuously looking for recycling and diversion from landfill options. The Company specializes in recycling organic residuals.
- **Renewable energy and greenhouse gas reduction.** The organic residuals the Company collects make excellent, high energy producing feedstock for biogas renewable energy production through anaerobic digestion. Biogas is a renewable energy that significantly reduces greenhouse gas emissions.

The organic and other non-hazardous liquid vacuum truck services industry is highly fragmented. It is estimated that approximately 52,000 companies operate in this industry in North America.¹ Management estimates that few of these companies have annual revenues in excess of \$1.5 million. There are no national operators, and therefore very few exit strategy options available for companies in this industry. The prime reason for this is the extremely complex logistics involved in delivering an intense customer service on a just-in-time basis.

At the heart of the Company are sophisticated, proprietary logistics and operational management software and systems, specifically designed for the Company's business, vision and growth plans. These systems allow it to deliver complex and intense customer services from its centralized call and logistics/dispatch center located in Woodbridge, Ontario. Although the Company currently operates only in Canada, its systems are ready for use in the US, a target market for future growth of the Company. Map-based GIS (Geographic Information System) routing and dispatch software, coupled with GPS (Global Positioning System) tracking and live, real-time handheld work order and data collection capabilities allow the Company to deliver superior customer service at extremely high productivity levels. The systems are easily scalable and have substantial inherent capacity. They were designed specifically to computerize otherwise labour-intense logistics decisions and administrative functions, and provide the Company with unique competitive advantages and a serious barrier to entry for potential competitors.

The Company's demonstrated success in obtaining, servicing and retaining customers has resulted in its ability to collect and be responsible for the management of large quantities of liquid organic residuals on an ongoing basis. A key corporate strategy has always been to control access to the lowest cost, most beneficial recycling alternatives in the markets the Company services. To date, the Company has achieved that through the development and deployment of proprietary processes as well as competitive arrangements with third-party organic recyclers such as composting facilities that are positively influenced by the Company's market dominance.

The Company believes that anaerobic digestion ("AD") of organic residuals to produce biogas and generating clean renewable energy will ultimately be the most cost effective and most environmentally beneficial organic waste recycling technology; capable of managing the largest variety of organic residuals. The Company also believes that it has a significant opportunity to participate in an emerging renewable energy industry in North America, and that the positive elements of combining organic recycling with energy production are a unique win-win opportunity.

The reason AD has not emerged previously in North America is the abundant supply of relatively low cost energy. It has been widely demonstrated in Europe and parts of Asia (where appropriately priced energy markets exist to support the purchase the electricity generated by AD) that AD is the lowest cost organic residuals recycling solution. Energy markets in North America, particularly Ontario (the Company's current largest market), are beginning to adopt pricing regimes and operational policies that are favourable to AD renewable energy development. The Company is extremely well positioned to take advantage of this trend.

The residuals the Company collects are ideal feedstock for ADs. Their high volatile organics content (particularly fat, oils and greases) results in their ability to provide 4 to 10 times the gas production of other typical agricultural AD feedstocks. As a result, the addition of even a relatively small quantity of the Company's residuals stream will result in at least a doubling of the energy production.

The Company's call center and communications infrastructure, its logistics and fleet management expertise, combined with the significant productivity gains to be achieved by co-digesting the Company's residuals with typical agricultural feedstock, makes it an ideal partner for AD facilities.

Footnote

¹ Tom Rulseh, Cole Publishing Inc., Three Lakes WI

The Company intends to partner with AD facilities through long term contractual relationships and through equity participation. In a long term contractual relationship, the delivery cost (“Tip Fee”) that the Company would pay will be adjusted based on the amount of biogas produced from ORMI’s feedstock, and ultimately could result in ORMI earning a rebate instead of paying a Tip Fee. Equity participation in an AD will require funding by the Company but will reflect ORMI’s contribution of its high energy feedstock and its ability to remotely monitor and benchmark day-to-day AD operations. In cases where the Company has an equity stake, it will receive a return on investment through renewable energy sales. In all cases ORMI will benefit by securing the lowest-cost recycling solution for the organic residuals it collects; thereby making it more competitive; thereby facilitating continued growth and improved profitability.

The Company believes the combination of increased low-cost residuals recycling capacity and the Company’s sophisticated logistics and fleet management systems will allow it to aggressively expand its business across Canada and into the United States as it begins consolidating the highly fragmented non-hazardous liquid waste services industry.

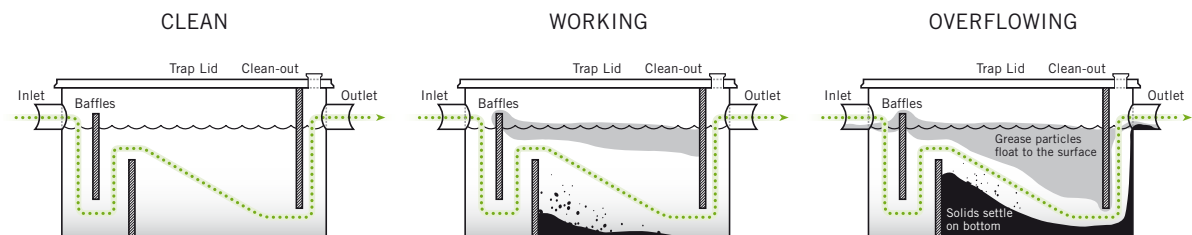
CORE BUSINESS

The core services the Company provides are:

Grease Interceptor Pumping

Grease interception devices are mandatory in all commercial, industrial and institutional facilities wherever fats, oils and grease (“FOG”) could be discharged into the sewer system. These facilities include restaurants, cafeterias, grocery stores, institutional kitchens, food processors, etc.

The grease interceptor captures and retains excess FOG and solids allowing only the cleaner wastewater to pass through to the sewer. As grease interceptors fill with captured FOG and solids, they progressively become less effective.



Grease interceptors must be periodically emptied in order to meet sewer discharge bylaws, prevent serious drain problems and protect the sewer and wastewater treatment systems.

The Company’s trained service crews use vacuum trucks to pump out grease interceptors and transport the liquid organics for processing and final recycling.

Provision of these services involves significant customer communications and care, which must be integrated with trucking logistics and residuals transportation.

Industrial Food Processing Wastewater Residuals

Industrial food and beverage processors typically generate large quantities of residuals that must be removed from

their wastewater prior to discharge to the municipal sewer system. This process is referred to as “pre-treatment”. In most cases, grease interceptors are not efficient enough and other pre-treatment technologies are required.

The most common technology deployed is dissolved air flotation (“DAF”). DAF is a clarification process for the separation of residuals from wastewater. It works by producing a stream of micro-fine air bubbles that attach to solids and float them to the surface, where they can be removed and stored in a holding tank for periodic collection. Industrial processors also have organic residual streams that are not wastewater related such as excess and off-spec product.

The Company’s trained service crews use vacuum trucks to collect and transport these residuals for processing and final recycling or disposal.

Liquification and Diversion of Food Residuals

The Company provides organics diversion services to the IC&I food industries sectors where the materials to be collected are liquid or semi-liquid and can therefore be collected using the Company’s vacuum truck fleet and can be managed through the Company’s organics recycling programs.

The Organic Resource Recovery System (“ORRS”) is a patent protected process for on-site collection of organic waste. Produce and other food related wastes are ground into slurry by a mill and discharged into a holding tank where it is stored until collected by a vacuum truck. Liquification of food organics provides an approximate five-fold volume reduction and makes these residuals ideally suited for use as a feedstock for renewable energy production in ADs. These residuals require no further pre-processing at the AD location prior to digestion.

Current efforts by the Company to deploy its ORRS have been focused on a few large industrial, commercial and institutional organics generators and have been effectively stalled by the severe lack of viable low-cost recycling alternatives that are cost competitive with landfill disposal in Ontario and British Columbia. The Company believes that the establishment of anaerobic digesters will make ORRS a more financially viable organic residuals handling technology.

Other Related Vacuum Truck Offerings

In addition to its two core services, Wastewater Residuals Management and Organic Residuals Diversion, the Company also provides related vacuum truck services such as: grease interceptor repairs and replacement, drain and sewer cleaning, off-spec product removal, septic and holding tank pumping; catch basin cleaning and sump and lift-station cleaning. These services help to ensure a fully integrated menu of offerings to customers, but they represent a secondary source of revenue and profitability to the Company.

ORGANIC RESOURCE MANAGEMENT INC.

ORMI, the Company’s Ontario based operating subsidiary, has been servicing the Ontario market and parts of Quebec for over 25 years.

ORMI provides primarily repeat, scheduled liquid organic waste removal services to the restaurant, foodservices and food retail industries.

ORMI operates three transfer facilities in Ontario, and is permitted to de-water residuals it collects (“Decant”). The Decant process removes excess water from the residuals the Company collects prior to delivery for final recycling/disposal.

Decanting is an especially advantageous pre-treatment process for AD’s. By reducing the water content of the residuals

and blending specific feed stocks, ORMI will be able to maximize the performance of individual AD's. This fuel blending process will increase the value-added status of our customer's residuals and positively impact operating margins for the Company.

During the past couple of years, ORMI has faced challenges with its Direct Land Application Process ("DLAP"). In light of the recent developments in Ontario, and the Company's knowledge of organic recycling options in general, the Company believes that an anaerobic digestion industry is emerging in Ontario, and that it will ultimately provide a low-cost, long-term recycling solution for all of the organic residuals the Company does and can collect. As a result, the Company has decided to suspend efforts to re-permit and expand its DLAP facilities in Ontario. In the interim, the Company continues to use higher cost recycling alternatives including transporting material out of province to third-party recycling sites.

In May 2007, ORMI signed an exclusive, 20-year contract to supply organic residuals as feedstock to a farm-based AD for the production of renewable biogas energy. The AD has obtained all necessary permits, including the Ontario Ministry of Environment ("MOE") Certificate of Approval for the use of off-farm organic residuals as feedstock to an on-farm AD. This was the first Ontario farm AD to receive off-farm organic residuals. ORMI has been delivering feedstock to the AD since July 2007. Although the volumes in the first stage of this two-stage contract are not material, the Company believes this is a watershed in the developments of AD's in Ontario.

ORMI services over 5,000 customer locations. Over the last several years the Company has increased rates to the Ontario customers in order to offset the erosion to the gross margin that had occurred from the increase in disposal costs.

ORMI's annual revenue for the year end June 30, 2007 was \$9,881,000 down 4% from the previous year's \$10,320,000. ORMI's core business (grease interceptor servicing) recorded an increase in revenue of 13% during the year; however, two of the Company's largest industrial accounts significantly reduced their service levels after making capital improvements to their wastewater handling system to reduce the amount of residuals they produce. The vast majority of the Company's customers do not have sufficient volumes of liquid organic waste to justify capital investments of this type and the lost revenue from these industrial customers does not have a significant impact on the gross margin of the Company.

A&A ANDERSON TANK SERVICE (VANCOUVER) LTD.

A&A, the Company's British Columbia based operating subsidiary, has been providing vacuum truck services in Vancouver and the Lower Mainland for over 30 years.

A&A's vacuum truck services vary from ORMI's in that a much smaller portion of its business is repeat scheduled service and with the larger portion being more responsive in nature. Over the last several years, A&A implemented a number of software enhancements designed specifically to manage the business requirements associated with a more responsive business model.

At present the major disposal option available in the Lower Mainland for non-hazardous liquid wastes, including FOG and a limited volume of food processing residuals, is delivery to municipal sewage treatment operated by the Greater Vancouver Regional District (the "GVRD"). The GVRD has continually increased prices at its liquid waste receiving facilities. There are no Decant facilities in the Lower Mainland. The Company believes there is a significant opportunity to establish a Decant facility in the GVRD and is actively pursuing a site. This opportunity will be driven by the introduction of ADs into British Columbia.

The British Columbia government acknowledges the lack of any significant organic diversion activity in the province as an embarrassment going into the 2010 Winter Olympics. The Company is recognized by the BC government for its leadership role in the development of ADs in Ontario. As a result, the Company was specifically recruited by the BC government to actively participate in the province's "Anaerobic Digester Feasibility Study Steering Committee". The committee's deliverables are identification and quantification of any potential regulatory barriers to AD deployment in the province, along with suggested remedies for these barriers. It is also tasked to review the available technology and make a recommendation for a site to establish a demonstration AD facility expressly capable of addressing both agricultural and urban organic wastes. The committee's report to the government is due before the end of 2007.

The momentum is building toward regulatory support for AD deployment. The Company is optimistic that it will begin realizing positive results in British Columbia from AD development during fiscal 2009.

A&A has over 3,000 customer locations. Annual revenue for the year end June 30, 2007 was \$4,892,000 down 4% from the previous year's \$5,090,000. The Company has been negatively impacted by the labour shortage in Western Canada and as a result has experienced a severe shortage of service technicians and a resulting drop in revenue without the labour available to do the work. The situation improved in the fourth quarter and A&A currently has a full compliment of technicians.

VISION AND STRATEGY

Wastewater Residuals Management

The Company's key focus is to collect, remove, transport and recycle residuals that are generated by its IC&I customers. Customers are often legally obliged to capture or prevent residuals from entering sewage collection and wastewater treatment networks. The provision of this service is vital to maintaining the physical infrastructure and business operations of customers, and ensures their compliance with municipal bylaws. It also strengthens the efficiency and longevity of municipal wastewater infrastructures.

The need for wastewater residuals collection/removal is driven by two factors:

- **Maintenance of Customer Drainage Infrastructure** – Food industry companies typically generate wastewaters that are high in FOG and other organic streams. These materials must be intercepted and prevented from entering the drainage system. If wastewaters containing FOG and other food solids are allowed to enter the drainage system, they accumulate on the walls of the drainpipes over time. These deposits eventually cause blockages and backups that can, in turn, cause serious floods – all of which are extremely costly to repair and may result in operational closures.
- **Municipal Regulations Protecting Wastewater Treatment Infrastructure** – Municipalities throughout Canada and the United States are actively mandating grease interceptor requirements, designed to reduce the discharge of excessive amounts of high-strength wastewaters into municipal sewer systems. In addition to the nearly universal application of bylaws mandating the installation of grease interceptors, more and more municipalities are implementing bylaws establishing maintenance schedules. Cost effective enforcement of these bylaws is a challenge that the Company is addressing through an adaptation of its sophisticated, proprietary logistics and operational management software.

In the absence of proper grease interception, high-strength wastewaters pose a material risk to customer and community infrastructure. Without effective abatement, collection and removal of residuals, high-strength wastewaters emptying directly into drainage systems can have significant consequences, including the following:

- **Sewer Blockages and Floods** – Accumulation of residuals on the interior walls of sewer piping systems is akin to sclerotic deposits in blood vessels: over time, fluid pressures increase as blockages occur, causing inevitable failure of pipes and channels. The risk posed to municipal infrastructure has resulted in a well developed compliance function in most North American cities. Foodservice businesses face various monitoring, reporting, insurance and litigating risks given heightened bylaw enforcement. Increasingly, state and provincial jurisdictions are legislating compliance, given the regional and environmental protection impacts. For example, the State of California mandated (Chapter 533 of Statutes 2005) a process last year for documenting and tracking the transportation of kitchen grease to ensure proper disposal or recycling.
- **Capacity of Sewage Treatment** – Even in situations where the negative impact on sewer systems is slow to develop, the presence of residuals in wastewater treatment facilities is a costly and complex threat. Moreover, these challenges affect opportunities for municipal growth, since they impose a limit on sewer plant capacity and the effectiveness of wastewater infrastructure.
- **Increased Sewer System Operating and Maintenance Costs** – The impact on plant capital is high, given the difficulty in removing residual deposits from plant collection, pumping and treatment systems. To cope with operating and maintenance issues associated with removing residuals accumulation, municipal plant managers are increasingly forced to invest in customized equipment and handling processes. Lift station scum removal and pooling systems are some of the additional investments made by municipalities to contain the problem of residuals accumulation.
- **Reduced Life Expectancy of Sewer Infrastructure** – The low PH levels of FOG material causes accelerated deterioration of concrete sewer pipes. With underground and facility infrastructure failing at an accelerated rate, municipalities are facing significant cost pressures on replacement and repair.

As a result of the above consequences, municipalities seek to reduce the quantity of residuals that may be discharged into the sewer system. The focus of current municipal policy is to expand regulatory intervention, which includes increased fines and/or penalties for non-compliance to ensure excessive amounts of FOG and other organics are not discharged into the sewer systems. As a result, residual generators are increasingly required to improve their ability to capture these materials through the installation of additional or more efficient interception equipment and implement stringent maintenance (residual removal) programs in order to ensure compliance.

In the commercial and institutional sectors, grease interceptors are recognized as the best available technology to capture and prevent excess residuals from entering the sewer systems. Grease interceptors have been mandated by building codes throughout North America for decades. They must be installed wherever there is the potential for discharge of residuals to the drainage system. The standard for grease trap design, PDI-G101, has been in effect for more than 50 years. Design specifications were intended to ensure capture of FOG materials prior to discharge of commercial wastewaters to sewer systems.

In the industrial sector, numerous technologies and devices exist to facilitate the removal and capture of excess residuals from processed wastewater. Given the significantly larger wastewater volumes, and in many cases higher residuals concentrations in those wastewaters, technologies and devices tend to be more complex and capable of delivering significantly better residuals removal efficiencies, which in turn creates substantial residual volumes that must be managed.

Once captured, residuals must be periodically collected and removed from customers' premises. The core business of the Company is the deployment of a skilled workforce and a fleet of vacuum trucks and related equipment to collect captured residuals from customer locations and ensure they are recycled and/or disposed in an approved manner. Once removed, residuals are transported to owned and/or third-party facilities for either recycling or disposal.

Organic Waste Diversion

In addition to its core business in the wastewater services industry, the Company also believes it is uniquely positioned to participate in the collection, transportation and recycling/disposal of solid organic waste.

The collection, transportation and disposal of organic waste is a large, growing and under-serviced market. Sixty-seven percent² of North America's annually discarded waste is comprised of organic materials. At industrial, commercial and institutional waste generators, such as supermarkets, institutions, food processors and restaurants, organic materials can represent 55% to 90%³ of the total discarded waste stream. As of March 2001, only 2.6% of the 22 million tons of food scraps generated were recovered⁴ largely because collection is typically highly inefficient. Even if the recovery rate may have doubled to the present time, there is a huge volume of material remaining to be managed. Inefficient handling results in smelly waste that attracts vermin and flies. Further, organic residuals are heavy and bulky requiring excess floor space and smaller more frequent collections due to the many small tote bins on site to hold this material.

The US government is targeting to divert 35%⁵ of all waste from landfill. This is estimated to result in an increase in food waste recycling from the 2.6%⁶ to 14%, or 5.4 times the recycled mass. The Company can bring substantial proprietary efficiencies to this market and is participating in the development of AD solutions for these wastes.

Organic Residuals Recycling and Disposal

The Company has invested significant resources in the past 15 years to develop a comprehensive knowledge base of all types of organic recycling and disposal alternatives. Each of the Company's service territories have different drivers which dictate the practical recycling and/or disposal options that are available for collected residuals. The Company's over-riding strategy is to control the lowest cost recycling (or disposal) option in the markets that it does business by obtaining long-term contractual relationships and/or through direct equity participation.

The Company's market leadership in the collection, transportation and recycling of residuals has resulted in it being responsible for managing large volumes of organic residual streams. Historically, in Ontario the Company has recycled these organic residuals using aerobic methods such as composting and its own patented DLAP technology. In British Columbia the only option has, and continues to be, delivery to the municipally operated sewage treatment plant for de-watering and use in a mine-tailings reclamation project.

In Ontario, as in most markets, the composting industry has matured to the extent that revenue generating markets for end product are nearing saturation. In addition, odour management and truck traffic issues around both DLAP and composting facilities are making them increasingly difficult to site as the urbanization of rural areas continues to foster strong community opposition. The only answer is the application of increasingly complex and capital intensive technology which drives up costs. As a result, costs for composting large quantities of residuals are at an all-time high.

A particularly attractive recycling option for the Company is the AD process, a widely proven technology that has been in constant commercial use in Europe for many years. In the simplest terms, AD is a biological process that breaks down organic materials in the absence of oxygen. The primary by-products of AD are: stable organic matter, water, carbon dioxide and methane gas. The carbon dioxide/methane gas combination is what is commonly referred to as biogas.

Footnote

² US Environmental Protection Agency, 1998 Waste Generation Report

³ Cynthia Greene, US Environmental Protection Agency, unpublished report, March 14, 2001

⁴ Cynthia Greene, US Environmental Protection Agency, unpublished report, March 14, 2001

⁵ US Environmental Protection Agency, 1998 Waste Generation Report

⁶ US Environmental Protection Agency, 1998 Waste Generation Report

Biogas is combusted to create energy (see page 1). The high energy content of the Company's FOG residuals significantly improves both the quantity and quality of the AD's biogas output. This makes the Company's residual streams a highly desirable material to combine and co-digest with other AD organic inputs such as livestock manure and source separated organics from urban residential collection programs.

During the past decade, the Company has amassed a significant AD knowledge base, and has been a strong proponent of its introduction and development in Canada. The Ontario Government's two new programs have confirmed the Company's efforts:

1. The Standard Offer Program ("SOP") is encouraging the development of small generators of "clean", renewable electricity by allowing them to sell into the Ontario power grid at a fixed premium. The general terms of the SOP include a long-term fixed price (20 year) contract. A key goal of the SOP is to make AD for biogas energy production financially viable in Ontario.
2. The \$9 million Ontario Biogas Systems Financial Assistance Program will help farmers and rural businesses carry out feasibility studies for the installation of biogas systems as well as cover a proportion of construction and implementation costs. Applicants can receive up to \$400,000 in funding.

These programs in Ontario have made the province a leader in the promotion and development of the AD renewable energy industry in North America. British Columbia and Alberta are aggressively developing parallel programs. Many US States are moving forward in a similar manner that virtually ensures the deployment of AD facilities across North America over the next five years. There is no reason to doubt that the North American AD industry will eventually duplicate the market penetration experienced in Europe which is still aggressively expanding.

Other Canadian and US jurisdictions are watching closely as the Ontario experience unfolds over the next few years. The Company believes that co-digestion of the organic residuals it collects in AD systems with agricultural residuals will eventually be adopted by multiple North American jurisdictions, including British Columbia. The major policy driver in British Columbia is the high density of livestock in the Fraser valley, and the urgent need for better environmental stewardship of the vital ground water resource that are suffering from manure related nitrate and phosphate overload. In addition, British Columbia lacks any significant organic recovery and landfill diversion activity. Implementation of co-digested AD systems will address these factors.

AD recycling eliminates the challenges that both composting and DLAP face. In strategic terms, it offers a more environmentally sustainable approach in managing the recycling of residual streams. AD extracts the inherent energy from the residuals and at the same time reduces pathogens, odours and greenhouse gas emissions, and improves nutrient availability. AD processes create a more efficient and environmentally responsible solution.

AD facilities can be divided into two primary categories; both are ideal partners for the Company:

- **On-farm ADs** are located on the farms that have large numbers of livestock generating significant quantities of manure feedstock. Ontario regulations allow On-farm ADs to receive prescribed quantities of industrial, commercial and institutionally generated clean organics such as those collected by the Company.⁷ On-farm ADs will typically be able to utilize most or all of the digested material onsite in the fields where they grow crops for the livestock. The farm generated manures can be processed by the AD with very little additional effort or cost than traditional manure management. The processed digestate can be managed with similar efficiency.

Footnote

⁷ OMAFRA, On-Farm Mixed Treatment System Design and Operations Manual, October 12, 2005

- **Centralized ADs** are typically large facilities strategically located to harvest the vast quantities of heat energy coincidentally created by the biogas burning generator engines. Sometimes these facilities receive some of their residuals (AD feedstock) from the co-located heat consumer, but most or all of their feedstock could also come from off-site generators like source separated organics from an urban residential collection program, large industrial generators and livestock manure from multiple farms. Centralized facilities are typically larger than On-farm ADs and require significantly more transportation logistics as most if not all of the material to be digested must be transported in, and all of the residual digested material must be transported out from the digester for final use to a farm or a composter. This additional transportation requirement could be a positive opportunity for the Company to provide additional transportation services. However, the Company believes there is a significant hurdle to siting centralized ADs as they are designated as waste processing facilities and must be permitted and regulated by the MOE.

The implications of the advent of AD recycling are dramatic to the Company:

- **Lower Operating Cost Base** – AD recycling represents a significantly lower cost alternative to third-party disposal options like composting, especially out of province composting. The Company believes that as AD facilities multiply they will eventually attach a commercial value to the reliable delivery of its high-energy potential feedstocks. As ADs multiply across the Company's service areas, they reduce total residuals management costs by shortening the travel times for delivery.
- **Increased Volumes** – Increased business volumes can come in three areas:
 - **IC&I Customers** - AD recycling offers the Company a secure and long-term solution for larger volumes of organic residuals. This new capacity will enable the Company to increase its market by providing reliable collection services in Ontario to customers with large residual streams that the Company has not been able to service previously due to a lack of cost effective recycling capacity. For the first time the Company will be in position to offer large volume customers long term service contracts on the strength of the Company's long term delivery contracts with the ADs.
 - **Municipal Bylaw Enforcement** – The emergence of secure, long-term solutions for larger volumes of organic residuals will encourage many municipalities to enforce and/or improve their existing sewer use discharge bylaws. Mandated service will require all generators in the relevant municipality to establish service contracts, significantly expanding the Company's market.
 - **ORRS** - once Centralized AD operations appear, the Company believes it will have substantially expanded opportunities for utilizing its ORRS system, including the management of source separated organics on behalf of municipalities.
 - **AD Farm Residuals** – The Company will have new opportunities to utilize its fleet to transport farm manures to AD facilities and the digestate that results from AD processes back to neighbouring farms, where it will be used as a feedstock for land application or to composting operations for inclusion into wholesale and retail soil amendments.
- **Municipal Bylaw Compliance Software** – The Company is addressing the emerging municipal desire to enforce their existing and new sewer use bylaws through an adaptation of its sophisticated, proprietary logistics and operational management software. When completed, the proprietary Municipal Compliance Package will allow a licensed municipal user to access a web-based, automated compliance program for these bylaws. Grease trap service event information would be automatically uploaded to the municipality's central site. Non compliant generator sites stand out as exceptions and the system will automatically issue compliance warnings and even fines.

- **Renewable Energy Partnerships** – Direct participation in AD projects would convert a cost center into a revenue generating opportunity. AD's will desire the Company as a partner because of its:
 - **Residuals** - Reliable volumes of high-energy potential feedstocks and fuel blending initiatives.
 - **Knowledge** - Significant technical, operational and industry contact knowledge and on-going practical knowledge the Company will develop by participating in multiple AD's.
 - **Direct Land Application** - The Company believes it will have the opportunity to utilize its existing know-how, infrastructure and composting relationships for the management of digested organics coming from AD's.

The Company's strategy is to participate in AD projects through both long term exclusive contractual feedstock supply agreements and energy-side equity participation. The Company has a unique opportunity to directly participate in the development, ownership and operation of multiple ADs.

Integrated Strategy

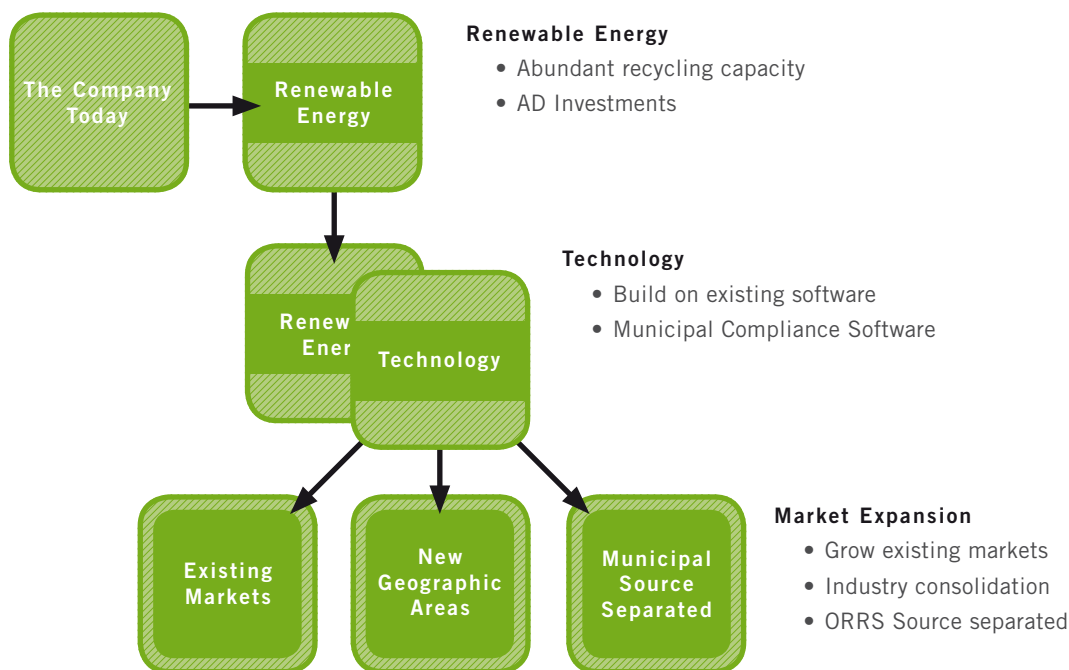
The Company's mission is:

"To be the recognized leader in providing optimum solutions for the collection, transportation and recycling of organic and other non-hazardous liquid residuals through a team dedicated to service excellence and environmental responsibility"

Six core values reflect the Company's quest for excellence:

- To provide customers with economic liquid residuals management solutions that are beneficial to society and the environment.
- To promote ethical and environmentally responsible business practices.
- To recognize the value and respect of employees, customers and neighbours.
- To foster innovation and individual commitment among employees.
- To continuously research and develop innovative residuals recycling and management technologies.
- To be a profitable, secure Company dedicated to continued growth.

Three integrated strategies flow from the mission and values of the Company. These strategies, illustrated below, represent a prudent and consistent approach to growing the Company's business based on its current operations and future opportunities:



• **Renewable Energy**

- Secure abundant recycling capacity through long term exclusive contracts with AD's to deliver the Company's feedstock.
- Invest in AD's through equity participation.

• **Technology**

- Continue to focus on efficiency improvements that build on the technologies, expertise and systems developed by the Company.
- Address the emerging municipal desire to enforce sewer use bylaws with Municipal Bylaw Compliance Software adapted from the Company's sophisticated, proprietary logistics and operational management software.

• **Market Expansion**

- Increase volumes in existing markets as a result of an abundant AD recycling capacity, and increased municipal bylaw enforcement.
- Expand into new geographic markets through a targeted program of industry consolidation and acquisition of customer lists within the Company's core business.
- Leveraging ORRS plus the Company's operational logistics and management capabilities, increase large volume organics collection including source separated organics markets.

The three strategies are connected. The Company believes that expansion into renewable energy will lower the cost of recycling, and abundant capacity will allow it to accelerate growth in existing markets. Combining this with the Company's continually improving technology will have a compounding positive affect on the Company's financial performance. Improved results will position the Company to secure additional financing for its strategy of industry consolidation through acquisition of customer lists in its core business. The Company may then apply its systems and expertise to its long-term goals of penetrating related industries for non-hazardous liquid organic services, such as municipal source separated organics.

RISKS & UNCERTAINTIES

Technology and Competition

The Company's success depends on remaining competitive in the development of systems, technologies and services in its area of expertise. Environmental technology is an evolving field in which new developments are expected to continue at a rapid pace. Competition in the non-hazardous liquid waste services industry is intense and expected to increase, both from within the industry and from those diversifying into the field. Some of the Company's competitors and potential competitors may have greater development, financial or personnel resources.

The Company is subject to the risks generally associated with new systems development and deployment, including lack of acceptance, delays in development and failure of systems to function properly. The market growth potential is subject to certain risks, including costs to develop and deploy such systems, the cost and feasibility of development, introduction of competing technologies and regulatory forces.

The Company believes there are two major constraints to the advancement of the ORRS program. First, the capital cost of installed ORRS equipment as compared to containerized collection alternatives, and second, the lack of readily available, low-cost organic recycling alternatives in Canada and the United States.

The Company has offset the erosion to the gross margin that occurred from the increase in Ontario recycling costs by increasing rates several times to Ontario based customers. The Company has successfully increased customer rates in the past, but with any price increase there is a risk that accounts could be lost. The price increases should have a long-term positive impact on the Company's gross margin, subject to the amount of lost business.

Government Regulation

Over the past few years ORMI has been impacted by a number of government regulatory changes that directly affect the way liquid organic waste is handled and processed in Ontario. As a result of these changes, most of the third-party disposal facilities in Ontario that receive and process liquid organic waste significantly reduced their capacity, or closed down altogether. This had a major impact on the cost of recycling/disposal. As part of the regulatory changes, the Company had to close most of its DLAP sites during 2005 and commence a re-permitting process. This was an extensive undertaking and the Company had limited success, with only one of the smaller Ontario DLAP sites being re-permitted. The only option the Company was left with was to transport a large portion of the waste to alternative third-party recycling sites located in Quebec. This resulted in a dramatic increase in the Company's transportation expense. In addition, the actual cost of recycling is significantly more expensive than using ORMI's DLAP facilities.

At the same time, anaerobic digestion began to evolve as a superior competitive recycling alternative. After extensive study, the Company concluded that this alternative will ultimately provide a low-cost, long-term recycling solution for all of the organic residuals it collects. Therefore, the Company decided to suspend efforts to re-permit and expand its DLAP facilities in Ontario and to focus its efforts on anaerobic digestion.

In May 2007, the Company signed an exclusive, 20-year contract to supply organic residuals as feedstock to an On-farm AD for the production of renewable biogas energy. The AD has obtained all necessary permits, including the Ontario MOE Certificate of Approval for the use of off-farm organic residuals as feedstock in an on-farm AD. This is the first Ontario farm AD to receive off-farm organic residuals. ORMI has been delivering feedstock to the AD since July 2007.

The delivery cost (“Tip Fee”) that ORMI will pay is significantly less than current recycling alternatives. However, the first stage of the two-stage contract is only for 700 tonnes per year of ORMI residuals, and therefore will not have a material financial impact. Stage two of the Contract provides an option to the AD until December 31, 2008, to expand the contracted volume to a maximum of 5,000 tonnes per year. The contract Tip Fee will be adjusted based on the amount of biogas produced by ORMI feedstock. Ultimately during the term of the contract this could result in ORMI earning a rebate instead of paying a Tip Fee feedstock delivered.

The Company believes this contract and the associated MOE Certificate of Approval are fundamental accomplishments to achieving the Ontario Ministry of Energy’s goal of developing renewable energy from biogas on Ontario farms. Using high-energy-potential off-farm organic residuals in Ontario farm-based ADs mirrors successful and long established European practices.

Although initially the volumes for this site are not material, the Company believes that this contract signals the advent of anaerobic digestion, making DLAP obsolete and no longer a long term cost effective method of disposal. Therefore the net loss for the year includes an impairment charge of \$991,667 (2006 - \$ Nil) to write-off the balance of the carrying value of the Company’s DLAP patent license agreements.

The Company is actively working on additional potential AD sites that, if successfully funded and permitted, would result in an Ontario in-province solution. This additional capacity would allow ORMI to pursue a number of long-term contracts that it is unable to acquire today because of a lack of secure and competitively priced disposal options. In most cases, the waste generated by these potential customers is being transported outside the Province at much higher costs.

The development of AD is subject to government regulations for bringing off-farm waste (the Company’s residuals) onto a farm for co-digestion as well as the ability of the AD to access the power transmission grid. The growth of AD’s in Ontario will be positively impacted by two Ontario government programs, the SOP and the Ontario Biogas Systems Financial Assistance Program (discussed previously herein).

The Company has been forced to transport a large part of its Ontario residuals out of province in the last two years at great cost. During the first half of fiscal 2007 the Company had some temporary relief and began delivering more of its Ontario residuals to third-party sites in Ontario, thereby saving significant transportation costs. However, in the second half of the year the Company had to again revert to transporting large volumes out of province. Other than the small Klaesi AD, the Company has no long-term contracts with these third-party Ontario disposal sites and therefore cannot predict with certainty its cost of disposal. The Company’s profitability can be materially impacted by the volume of residuals these Ontario sites receive.

Risk Associated With Acquisitions

The Company is seeking acquisitions that are a good fit for its strategic direction. The Company does not have control over the market conditions prevailing or likely to prevail in the future, which may impact the ability to finance and execute this strategy. These variables include market valuations of potential targets and the Company’s stock price volatility. There can be no assurances that the Company will be able to identify suitable acquisition candidates

available for sale at reasonable valuations, consummate any acquisition or successfully integrate any acquired business into its operations. However, the Company continues to believe that with its technologies, systems and experienced management team, it is uniquely positioned to capitalize on a substantial opportunity.

Compactors

Prior to March 31, 2002, the Company's primary business was the ownership, rental and distribution of waste compactor equipment. In March 2002, the Company sold the vast majority of its compactor fleet to Canadian Waste Services Inc., but retained 195 compactors located in Western Canada. The remaining compactors were rented to a major retail grocery chain under a five year contract which expired on September 30, 2006. Rental of compactors has continued on a monthly basis with the grocery chain while it replaces compactors with its own units and the Company sells off its excess equipment.

The annual rental revenue from the compactors for 2007 was \$590,000 (2006 - \$518,000). During the year the Company sold or disposed of more than half of the rental compactors. The Company expects to dispose of the remaining compactors prior to June 30, 2008 and does not anticipate recovering any value for the remaining machines other than outstanding purchase commitments. As a result, the net loss for the year includes an impairment charge of \$235,000 (2006 - \$190,000).

Labour

ORMI's hourly employees at its Toronto operation are represented by the Universal Workers Union Local 183. In October 2006 a new three year contract was ratified that runs from October 1, 2006 to September 30, 2009. The agreement includes a harmonization of pay scales over 24 months, improvements to benefits and a 3% wage increase in each of the three years.

In July 2007 the hourly employees at A&A ratified a new three year collective agreement with the Service Employees Union from May 1, 2007 to April 30, 2010. The agreement includes a 3% wage increase in each of the three years, some minor inflationary increases and a small improvement in the union pension plan.

Dependence on Key Personnel

The Company's success will depend to a significant extent upon its management group. The loss of the services of key executive personnel could have a material adverse effect on the Company.

RESULTS OF OPERATIONS

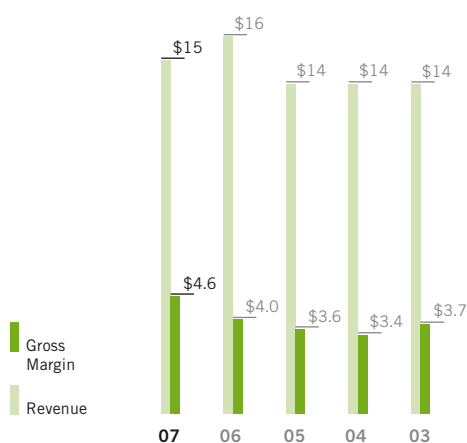
Annual Information

The following table sets out certain selected financial information prepared in conformity with Canadian generally accepted accounting principles for the fiscal years ended June 30 from 2003 to 2007:

FIVE-YEAR COMPARATIVE FINANCIAL INFORMATION

	2007	2006	2005	2004	2003
Revenue	\$15,418,215	\$16,031,828	\$14,494,091	\$13,677,228	\$14,053,175
Gross margin	4,649,577	4,049,693	3,614,654	3,351,773	3,682,907
Operating expenses	5,265,654	4,541,352	4,095,197	4,555,413	4,527,338
Non-cash expenses before taxes	3,158,477	2,116,891	2,231,930	1,827,366	3,003,702
Future income tax (recovery) expense	(1,135,000)	(4,000)	(142,000)	197,000	(252,500)
Net loss	(1,243,650)	(1,195,838)	(1,129,874)	(1,691,352)	(2,140,194)
Cash flows from operating activities	998,107	739,061	701,422	359,562	345,442
Working capital deficiency	(171,445)	(810,124)	(1,291,947)	(960,088)	(1,682,267)
Total assets	11,368,028	11,747,603	13,278,384	13,534,106	14,506,492
Total liabilities	4,867,707	8,111,240	8,539,291	7,756,333	7,787,530
Long-term debt	742,290	899,435	1,348,455	1,106,270	1,486,005
Obligations under capital lease	982,711	251,495	267,357	365,698	237,706
Shareholders' equity	6,500,321	3,636,363	4,739,093	5,777,773	6,718,962
Loss per share basic and diluted	(0.03)	(0.03)	(0.03)	(0.05)	(0.06)

Revenue &
Gross Margin
\$ millions



Revenue

The Company's core business (grease interceptor servicing) recorded an increase in revenue of 10% during 2007 compared to 2006 as a result of both volume and price increases. However, the Company's two largest industrial accounts, both food processing facilities, significantly reduced their service levels after making capital improvements to their wastewater handling system to reduce the amount of residuals they produce. The vast majority of the Company's customers do not have sufficient volumes of liquid organic waste to justify capital investments of this type. The lost revenue from these two industrial customers was very competitively priced and did not have a significant impact on the gross margin of the Company. The net result was a reduction in revenue of 4% or \$614,000 from \$16,032,000 for fiscal 2006 to \$15,418,000 for 2007.

Gross Margin & Operating Expenses

The Company's single largest operating expense, residuals management, was 23% lower in 2007 compared to 2006 for two reasons. First, the volume of waste collected in Ontario was down 21% largely because of the loss of the two major industrial accounts. Second, the Company was able to take more residuals to third-party recycling sites in Ontario instead of transporting them out of province. Primarily as a result of reduced residuals management costs, the total gross margin continued to improve in 2007 increasing \$600,000 or 15% from \$4,050,000 in 2006 to \$4,650,000 in 2007. As a percentage of revenue, gross margin was 30.2% in 2007 compared to 25.3% in 2006.

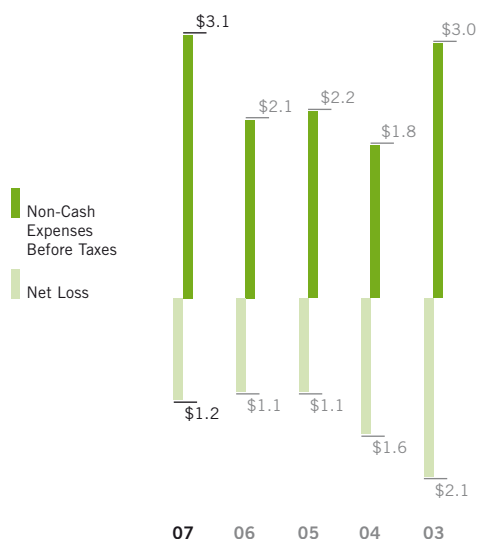
The increase in operating expenses is mainly due to higher selling, general and administrative expenses which were up \$719,000 or 25%, from \$2,933,000 in 2006 to \$3,652,000 in 2007. \$280,000 of the increase pertains to a severance expense that was recorded in the fourth quarter of 2007 for two long term employees that were terminated. In addition, there were legal and accounting fees of approximately \$200,000 for the multi-step restructuring program the Company has undertaken that includes the conversion of all the outstanding preferred shares into common shares, the amalgamation of the Company with its largest subsidiary and concurrent name change to Organic Resource Management Inc., and the proposed elimination of related party relationships. The balance of the increase in selling, general and administrative expenses relates to general cost increases and costs incurred in relation to the Company's involvement in anaerobic digestion.

The Company continued to have large non-cash expenses including amortization of intangible assets related to the acquisition of ORMI and A&A. The five year amortization of intangible assets related to software and customer lists was completed on May 31, 2007 and as a result, amortization expense was down \$72,000 from \$969,000 in 2006 to \$897,000 in 2007. The balance of \$992,000 related to the DLAP patent licence agreement was written off in June 2007. Also included in non-cash expenses for 2007 is the \$235,000 (2006 - \$190,000) write-down of property, plant and equipment related to compactors.

NON-CASH EXPENSES

	2007	2006	2005	2004	2003
Amortization of property, plant & equipment	\$ 695,907	\$ 606,859	\$ 606,531	\$ 591,743	\$ 585,218
Amortization of intangible assets	896,642	969,064	969,064	969,064	1,170,334
Share based compensation	20,958	55,348	110,431	152,384	-
Foreign exchange loss (gain)	453	(22,747)	(59,854)	(8,088)	(152,778)
Gain on disposal of property, plant and equipment	(9,212)	-	-	(66,929)	(101,043)
Write-down of property, plant & equipment	234,755	189,514	322,460	-	-
Write-down of intangible assets	991,667	-	-	-	-
Write-down of goodwill	-	-	-	-	1,261,971
Dividends accrued on preferred shares	327,307	318,853	283,298	189,192	240,000
Non-cash expenses before taxes	\$ 3,158,477	\$ 2,116,891	\$ 2,231,930	\$ 1,827,366	\$ 3,003,702
Future income taxes	(1,135,000)	(4,000)	(142,000)	197,000	(252,500)
Non-cash expenses	\$ 2,023,477	\$ 2,112,891	\$ 2,089,930	\$ 2,024,366	\$ 2,751,202

**Net Loss/
Non-Cash Expenses Before Taxes**
\$ millions



Income Taxes & Net Loss

The net loss for the year was \$1,244,000, an increase of \$48,000 from \$1,196,000 in 2006. The future income tax recovery increased by \$1,131,000, from \$4,000 in 2006 to \$1,135,000 in 2007. The future income tax recovery is the result of changes in timing differences plus the recognition of future tax assets. The increase is the result of future tax assets in the Company that management has assessed are now more likely than not to be realized, on the basis that the Company has generated a taxable income in 2006 and 2007 and the probability that it will continue to have taxable income in the future.

QUARTERLY REVIEW

FINANCIAL INFORMATION - EIGHT QUARTER SUMMARY

	2007	2006	2007	2006	2006	2005	2006	2005
(in 000's except earnings per share)	Fourth Quarter Ending June 30		Third Quarter Ending March 31		Second Quarter Ending Dec 31		First Quarter Ending Sept 30	
Revenues	\$3,834	\$ 3,955	\$ 3,928	\$ 4,103	\$ 3,810	\$ 4,008	\$ 3,846	\$ 3,966
Net income (loss)	(836)	(268)	(264)	(398)	(155)	(305)	11	(225)
Cash flows from operating activities	132	192	297	395	96	(237)	473	389
Loss per share, basic and fully diluted	(0.01)	(0.01)	(0.01)	(0.01)	(0.00)	(0.01)	0.00	(0.00)

Total revenue levels have remained fairly level through the last eight quarters. However, the mix of revenue has changed in the last five quarters as the Company has replaced large volume, low margin industrial business with small volume, higher margin core grease trap business.

The increasing loss through the first three quarters of 2006 reflects the ongoing increasing costs of recycling organic residuals. In the fourth quarter of 2006 this trend reversed as the revenue quality improved with additional rate increases, and lower disposal costs resulting from the Company's ability to take some of its waste to third-party facilities in Ontario. This situation changed again in the second quarter of fiscal 2007 as the Ontario sites were impacted by colder weather and they reduced the volume of residuals they received. In the fourth quarter of 2007 the Ontario sites marginally increased the volume they received.

The net loss of \$836,000 for the fourth quarter of 2007 includes the write down of the DLAP patent for \$992,000, the write-down of property, plant and equipment related to compactors for \$235,000, severance expense of \$280,000, legal fees of \$173,000 related to restructuring, the \$125,000 MOE fine and the future income tax recovery of \$1,135,000.

Adjusted net earnings excluding non-cash expenses as displayed in the table below is a non-GAAP measure and does not have any standardized meaning prescribed by GAAP and is therefore unlikely to be comparable to similar measures presented by other issuers. It should not be construed as an alternative to net earnings or cash flow from operating activities determined in accordance with GAAP.

Adjusted net earnings excluding non-cash expenses is a measure of the Company's ability to earn cash and is intended to be a measure that is representative of its operating performance. Adjusted net earnings excluding non-cash expenses appears on the Consolidated Statement of Cash Flows as a subtotal and is the sum of the net earnings and items not involving cash.

ADJUSTED NET EARNINGS EXCLUDING NON-CASH EXPENSES

	2007	2006	2007	2006	2006	2005	2006	2005
(in 000's)	Fourth Quarter Ending June 30		Third Quarter Ending March 31		Second Quarter Ending Dec 31		First Quarter Ending Sept 30	
Net income (loss)	(836)	(268)	(264)	(398)	(155)	(305)	11	(225)
Non-cash expenses	520	701	547	473	493	478	464	461
Adjusted net earnings excluding non-cash expenses	(316)	433	283	75	338	173	475	236
Changes in operating assets and liabilities	448	(241)	14	320	(242)	(410)	(2)	153
Cash flows from operating activities	132	192	297	395	96	(237)	473	389

Fourth Quarter 2007

Revenue for the fourth quarter of 2007 was \$3,834,000 down \$121,000 or 3% from \$3,955,000 in the fourth quarter of 2006. The Company's core business (grease interceptor servicing) recorded an increase in revenue of 12% for the fourth quarter 2007 compared to the same period last year as a result of both volume and price increases. However, this was offset by the lost revenue from the low margin high volume industrial accounts.

The gross margin for the fourth quarter of 2007 was \$879,000 down \$335,000 or 28% from \$1,215,000 in the fourth quarter of 2006. The gross margin was affected by higher disposal costs with increased volumes going out of province. In addition, during the fourth quarter the Company recorded a \$125,000 expense for a fine from the Ontario MOE related to the Company's one remaining DLAP site. Although the ministry inspectors reported that the waste storage facility appeared to be well operated and well maintained, the Company failed to submit financial assurance or annual reports as required. The ministry requires financial assurance to ensure adequate funds are available for environmental activities, including site remediation. On July 10, 2007 the Company pleaded guilty to these charge and was given six months to pay. The Company has submitted the required financial assurance and annual reports.

The net loss for the fourth quarter of 2007 was \$836,000 compared to a net loss of \$268,000 in the fourth quarter of 2006. The net loss for the quarter includes the write-down of the DLAP patent for \$992,000 (2006 - \$ Nil), the write-down of property, plant and equipment related to compactors for \$235,000 (2006 - \$190,000), severance

expense of \$280,000 (2006 - \$ Nil) and the future income tax recovery of \$1,135,000 (2006 - \$4,000). Also impacting the fourth quarter were legal fees related to the restructuring of \$173,000 and the \$125,000 MOE fine.

Cash Flow
From Operations
\$ millions



Balance Sheet & Cash Flow

Accounts receivable increased \$185,000 or 8% from \$2,227,000 at June 30, 2006 to \$2,412,000 at June 30, 2007. The increase is a temporary surge and not indicative of the normal stable level of receivables. Prepaid expenses increased \$80,000 from \$146,000 to \$226,000 as a result of deposits provided to the Ontario MOE for financial assurance on various facilities. Accounts payable and accrued liabilities increased \$475,000 from \$1,983,000 at June 30, 2006 to \$2,458,000 at June 30, 2007 as a result of accruals pertaining to severance and the MOE fine.

Total capital leases increased by \$731,000 from \$251,000 at June 30, 2006 to \$983,000 at June 30, 2007, as a result of replacing seven old vacuum trucks with new vehicles and adding one new truck to the fleet, thereby improving the age of the fleet.

Cash flows from operating activities increased by \$259,000 or 35% from 739,000 for 2006 to \$998,000 for 2007.

On June 1, 2007 National Challenge Systems Inc. converted all of the outstanding Class A and Class B preferred shares into common shares.

As at June 1, 2007 there were a total of 4,086,650 class A and B shares outstanding. Under the terms of these shares, the conversion into common shares was calculated by dividing the redemption value of the preferred shares at \$1.00 per share by the amount per common share, equal to the lesser of:

1. \$0.40; or
2. \$0.0852, the average weighted market price over the 15-day period immediately prior to June 1, 2007 when the conversion notice was given.

As a result of the conversion, 47,965,376 million additional common shares were issued bringing the total of issued and outstanding common shares to 88,098,949. The preferred share account was reduced by \$4,086,650 to nil and the common share account was increased by the same amount from \$11,743,933 to \$15,830,583. With the conversion of the preferred shares the Company has eliminated the associated annual dividends (\$327,000 in 2007 and \$319,000 in 2006).

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's consolidated financial statements are prepared in conformity with Canadian generally accepted accounting principles. The preparation of these consolidated financial statements requires the Company to make estimates and assumptions that affect the reported amount of assets and liabilities that are inherently uncertain. These estimates and assumptions can affect the reported amounts of assets and liabilities, revenues and expenses. The Company bases its estimates on historical experience and other assumptions which it believes to be reasonable in the circumstances. The significant accounting policies are described in Note 2 of the consolidated financial statements. The following items in the consolidated financial statements involve significant estimation or judgement.

Goodwill and Intangible Assets

The Company accounts for all business combinations using the purchase method, under which it allocates the excess of the purchase price of business acquisitions over the fair value of identifiable net assets acquired to intangibles and goodwill. Purchase price allocations are derived from a formal valuation by an independent third-party valuation expert. Any goodwill or intangible assets with indefinite useful lives acquired in a business combination are not amortized to income over their useful lives but are assessed annually for any potential impairment in value. All other intangibles assets are amortized over their estimated useful life.

Intangible assets are identified and recorded at estimated values based on the valuations of customer relationships, software license agreements and patent license agreements relating to the Company's business acquisitions in 2002. The Company must make assumptions regarding estimated future cash flows, market conditions and other factors to determine the fair value of the assets. If these estimates or related assumptions change in the future, the Company may be required to record impairment charges for these assets. Over the past few years ORMI has been impacted by a number of government regulatory changes that directly affect the way liquid organic waste is handled and processed in Ontario. As a result of these changes, most of the third-party disposal facilities in Ontario that receive and process liquid organic waste have significantly reduced their capacity, or have closed down altogether. This has had a major impact on the cost of recycling/disposal. As part of the regulatory changes, the Company had to close most of its DLAP sites during 2005 and commence a re-permitting process. This was an extensive undertaking and the Company had limited success, with only one of the smaller Ontario DLAP sites being re-permitted. In the interim, a large portion of the waste was trucked to alternative third-party disposal sites located in Ontario and Quebec, with a large portion going to Quebec. In 2007 the Company was able to locate additional third-party disposal capacity in Ontario thus impacting the incremental savings compared to Quebec disposal.

In the last two years, anaerobic digestion has been evolving as a superior competitive disposal alternative. The Company believes that this alternative will ultimately provide a low-cost, long-term recycling solution for all of the organic residuals the Company collects. As a result, the Company has decided to suspend efforts to re-permit and expand its DLAP facilities in Ontario and to focus its efforts on anaerobic digestion. In May 2007, the Company signed an exclusive, 20-year contract to supply organic residuals as feedstock to a farm-based anaerobic digester for the production of renewable biogas energy. Although initially the volumes for this site are not material, the Company believes that this contract signals the advent of anaerobic digestion, effectively making DLAP obsolete and no longer a long term cost effective method of disposal.

In fiscal 2007 the Company recorded an impairment charge of \$991,667 (2006 - \$ Nil) to write-off the balance of the carrying value of the Company's patent license agreements.

The Company has goodwill arising from business acquisitions, which are comprised of the excess of amounts paid over the fair value of net identifiable assets acquired. The Company performs an annual assessment of the fair value of the businesses to which this goodwill relates. In assessing the fair value of the businesses, the Company must

make assumptions regarding estimated future cash flows, market conditions and other factors to determine the fair value of the business. If the estimates or their related assumptions change in the future, the Company could be required to record impairment charges for these assets.

In fiscal years 2007 and 2006, the Company did not record an impairment charge related to goodwill.

Impairment of Long-Lived Assets

Long-lived assets held and used by the Company are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If changes in circumstances indicate that the carrying amount of an asset that the Company expects to hold and use may not be recoverable, future cash flows expected to result from the use of the asset and its disposition must be estimated. If the undiscounted value of the future cash flows is less than the carrying amount of the asset, impairment is recognized.

During 2007 the Company recorded an impairment loss of \$235,000 (2006 - \$190,000) in the carrying value of its rental compactors based on quoted market prices.

Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable or recoverable for the current year. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized.

The Company has future income tax assets, which are subject to periodic recoverability assessments. Realization of the Company's future income tax assets is largely dependent upon its achievement of projected future taxable income and the continued applicability of ongoing tax planning strategies. The Company's judgements regarding future earnings or losses may change due to future market conditions, changes in tax legislation and any other factors that could adversely affect the ongoing value of future income tax assets. These changes, if any, may require the material adjustment of these future income tax asset balances. This adjustment would reduce the future income tax asset to the amount that is considered to be more likely to be realized and would be recorded in the period such a determination was to be made. Conversely, in the event that the Company's assessments were to determine that it is more likely than not to be able to realize future income tax assets in excess of the recorded amount, an adjustment to the income tax asset that would increase income would be made in the period such a determination was made.

During 2007 the Company recorded a future tax recovery of \$1,135,000 (2006 - \$4,000).

LIQUIDITY & CAPITAL RESOURCES

The Company's main sources of capital are cash flow generated from operations, a revolving loan and long-term debt. Cash flows from operating activities increased by \$259,000 or 35% from 739,000 for 2006 to \$998,000 for 2007.

On June 14, 2005 the Company entered into a \$2 million revolving credit facility for a 3-year term with Textron Financial. The Textron loan was reduced by \$534,000 from \$1,218,000 at June 30, 2006 to \$684,000 at June 30, 2007. The Company's cash position remained virtually unchanged at \$227,000 at June 30, 2007 compared to \$206,000 at June 30, 2006.

ORMI's Toronto facility (net book value \$913,000) has a first mortgage on the property having a principal balance of \$579,000, bearing interest at 8%, repayable in monthly instalments of principal and interest of \$5,136 and matures in November 2009.

The financing of trucks and equipment is primarily through capital leases. The funding of the software development, \$71,000 in 2007 and \$77,000 in 2006 is through cash generated from the operations. The Company's contractual obligations due over the next five years are summarized below:

CONTRACTUAL OBLIGATIONS

	Less than 1 year	1-3 years	4-5 years	After 5 years	Total
Long-term debt	\$ 100,948	\$ 620,496	\$ 20,846	\$ -	\$ 742,290
Capital lease obligations	308,898	541,243	327,904	-	1,178,045
Operating leases	263,381	264,591	90,173	-	618,145
	\$ 673,227	\$ 1,426,330	\$ 438,923	\$ -	\$ 2,538,480

Based on current operating levels, management expects cash flow generated from operations along with the available borrowing capacity under the Company's credit facility to be sufficient to meet its working capital needs and debt service requirements for the next fiscal year. The Company has the ability to reduce capital spending to fund debt requirements if necessary; however, a long-term decline in capital expenditures may negatively impact its growth strategy.

There can be no assurance that operating levels will not deteriorate over the ensuing fiscal year, which could result in the Company being unable to meet its current working capital and debt service requirements. In addition, other factors, not presently known to management, could materially and adversely affect the Company's future cash flow. In such events, the Company would be required to obtain additional capital as is necessary to satisfy working capital and debt service requirements from other sources. Alternative sources of capital could result in increased dilution to shareholders and may be on terms that are not favourable to the Company.

OUTSTANDING SHARE DATA

As of September 20, 2007 the following is the outstanding share data:

	Issued	Stated Capital
Common shares	88,098,949	\$ 15,830,583

DIVIDENDS

The Class A preferred shares provided for the payment of the 12% dividend at the Company's discretion to be either (i) in cash or (ii) in additional Class A preferred shares. The Class A preferred shares have paid no dividends since December 31, 2003. On January 31, 2007 the Company issued \$1,016,823 of Class A shares representing the amount of dividends accrued to that date. On May 31, 2007 the Company issued a further \$121,827 of Class A shares for dividends accrued in the four months ending May 31, 2007. On June 1, 2007 the Company converted all issued and outstanding Class A and Class B shares into 47,965,376 common shares with a book value of \$4,086,650 based on a weighted average market price of \$.0852 per share. As a result, there were no cumulative dividends in arrears on the Class A preferred shares as at June 30, 2007 (2006 - \$811,343).

The financial liability for the preferred shares reflected in the June 30, 2006 consolidated financial statements included accrued dividends though they had not been declared as payable by the Board of Directors.

The Company has never paid cash dividends on its common shares and does not anticipate paying any cash dividends in the foreseeable future. Subject to approval from Textron Financial, there are no other restrictions that prevent the Company from paying dividends.

RELATED PARTY TRANSACTIONS

On August 29, 2007 the Company announced that it had reached an agreement for three related party transactions which would eliminate the existing related party relationships for software and patents. These transactions closed on September 19, 2007. The three related party transactions resulted in the Company purchasing: (i) 100% of the shares of ORMI Information Systems Inc. formerly Path Information Systems Inc. (“OIS/Path”); (ii) the Canadian patents for DLAP and ORRS from Organic Resource Technologies Inc. (“ORTI”); and (iii) the 30% equity interest in NCS Environmental Services Limited (“NCS ESL”) that it did not already own from Organic Resource Technologies International Inc. (“OII”). The Company has now eliminated all material related party transactions with the exception of the repayment of the loan relating to the purchase of OIS, as noted below.

ORMI Information Systems Inc.

On September 19, 2007, Path changed its name to ORMI Information Systems Inc. and the Company purchased 100% of the issued and outstanding shares of OIS/Path for \$700,000. Charles Buehler, the Company’s Chairman, CEO and control block holder, owned a majority of the shares of OIS/Path. \$100,000 of the purchase price was paid in cash on closing and the remainder will be paid over six years with interest at 7% per annum. The shares of OIS/Path were pledged to the vendors as security until the balance has been paid. Also as part of the transaction, the vendors retained the Path name and obtained a perpetual and exclusive license, including access to the source code, for use of the software outside of the liquid organic industry.

OIS/Path owns proprietary route optimization and management information software (“Software”). Prior to the acquisition of OIS, the Company had a perpetual and exclusive license for use of the Software in the non-hazardous liquid waste industry in Canada. In addition, the Company, through its Bermuda subsidiary, NCS ESL, had a perpetual licence from OIS/Path exclusive to the non-hazardous liquid waste industry for the worldwide (excluding Canada) use of the Software. In addition, NCS ESL had a marketing agreement with Path for the Software which gave NCS ESL the right to market Software licenses to third-parties for use in its industry worldwide (excluding Canada).

Although the Company did have a perpetual license to the software, it did not own the source code and was required by the terms of the license to use Path programmers to do maintenance, perform upgrades and do development work on the software. The software is a critical element of the Company’s operational success and a key component to its future. The Company must continually develop and upgrade the software in order to remain competitive. Consequently, there would be on-going charges paid to OIS/Path for software support and development, and the potential for an on-going conflict of interest in the determination of the appropriate market charges for those services. By purchasing OIS/Path and thereby the software, this issue is permanently resolved because the Company will be able to maintain and develop its own software.

Canadian DLAP and ORRS Patents

DLAP is a patent protected solution for recycling high-fat content organic waste that uses the natural digestion ability of microbes found in soil to convert organic waste into stable soil organic matter.

ORRS is a patent protected process for on-site collection of organic waste. Produce and other food related wastes are ground into slurry by a mill and discharged into the holding tank where it is stored until collected by a vacuum truck. Current efforts by the Company to deploy its ORRS have been focused on a few large industrial, commercial

and institutional organics generators and have been effectively stalled by the severe lack of viable low-cost recycling alternatives in Ontario and British Columbia. The Company believes that the establishment of anaerobic digesters will make ORRS a more financially viable organic residuals handling technology.

On September 19, 2007 the Company purchased the Canadian patents for DLAP and ORRS from ORTI, a company owned as to one third by Mr. Buehler, and one third by Douglas Carruthers, an officer and director of ORMI, for \$15,000 cash. As part of the terms of this transaction, a note payable from the Company to ORTI, with 24 blended monthly installments of principal and interest of \$4,292 maturing in December 2008 which had a current outstanding balance of \$65,729, was also paid in full on closing.

Prior to the purchase, the Company had an arm's-length exclusive licensing agreement until 2017 with ORTI for exclusive use of DLAP in Canada. The license required the payment of \$25,000 per year plus royalties on waste processed using DLAP outside of the province of Ontario. (The Company has always had perpetual rights to DLAP in the province of Ontario at no cost or royalty; the Company inherited these rights through its purchase of ORMI in 2002). As at the date of purchase, no royalties have ever been paid and ORTI has always waived the requirement to pay the annual license fee.

Purchasing the ORRS and DLAP patents has eliminated any requirement for the Company to pay royalties on new ORRS locations and royalties or the annual license fee for the DLAP.

30% Equity Interest in NCS Environmental Services Ltd. ("NCS ESL")

NCS Holdings and NCS ESL are inactive Bermuda companies that were originally incorporated as a tax strategy which is no longer applicable. In March 2000, NCS ESL entered into an intangible asset purchase and sale agreement ("APSA") whereby it purchased the ORRS and DLAP United States patents and certain other assets from OII. In consideration for these assets, OII received 30% of the common shares of NCS ESL.

On September 19, 2007, the Company purchased the 30% equity interest in NCS ESL that it did not own from OII, a company owned as to one third by Mr. Buehler and one third by Mr. Carruthers, for \$10,000 cash.

The Company now owns 100% of NCS ESL and intends to transfer the US patents into the parent company and wind-up both Bermuda companies thereby simplifying its corporate structure.

Approvals for Elimination of Related Party Relationships

Other than Mr. Buehler and Mr. Carruthers, all other ORMI directors are independent. The transactions described above were assessed in detail and negotiated on behalf of the Company by a committee of all seven independent directors, and all resolutions approving these transactions were passed unanimously. Negotiations were extensive and lasted a number of months and finally concluded on August 21, 2007 when a purchase agreement for Path was signed.

Total fair market value of all three transactions, including the early repayment of the ORTI note, was \$790,729 or 9% of the Company's market capitalization determined in accordance with Ontario Securities Commission Rule 61-501 ("OSC Rule 61-501"). Accordingly, pursuant to section 5.5-2 of OSC Rule 61-501, the Company was exempt from a requirement for a formal valuation because the total fair market value of these transactions was not more than 25% of the market capitalization of the Company and, as a result, minority approval was also not required under OSC Rule 61-501 section 5.7(1)-2.

Eliminating related party relationships was part of a multi-step restructuring program that included simplifying the Company's balance sheet and organizational structure and strengthening its management. The restructuring program

began on June 1, 2007 with the conversion of all the outstanding preferred shares into common shares. It continued on July 1, 2007 with the amalgamation of the Company with its largest subsidiary and concurrent name change to Organic Resource Management Inc., and on August 20, 2007 with the appointment of Charles Buehler as Chairman & CEO, Ian Kelland as President and Edward Dreher as Vice President of Finance.

Related Party Transactions and Balances

During the year, the Company incurred charges from directors or companies and/or individuals related to them. These amounts have been recorded at their exchange amount, being the amount agreed to by all parties, for amounts approximately as follows:

RELATED PARTY CHARGES

	2007	2006
Dividends on preferred shares	\$ 199,194	\$ 318,853
Interest expense	9,253	12,776
Consulting fees	4,500	-
Software development cost	-	9,234

Accounts payable as at June 30, 2007 includes amounts payable to certain directors and/or companies controlled by them totalling \$103 (2006 - \$52,251). Long-term debt includes a note payable to a related party for \$20,933 (2006 - \$104,662). The note is repayable in 36 equal monthly instalments of \$6,977, the last of which is due September 1, 2007. Long-term debt also includes a note payable to a company owned by certain directors for \$73,568 (2006 - \$93,636) repayable in 24 blended monthly instalments of principal and interest of \$4,292 commencing January 2007 and maturing 2008.

ADDITIONAL INFORMATION

Additional information relating to the Company, including the Annual Information Form has been filed and is available on SEDAR at www.sedar.com.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements and other financial information for this annual report were prepared by the management of National Challenge Systems Inc., reviewed by the Audit Committee and approved by the Board of Directors.

Management is responsible for the preparation of the consolidated financial statements and believes that they fairly present the Company's financial position, the results of its operation and its cash flows in accordance with Canadian generally accepted accounting principles. Management has included amounts in the Company's consolidated financial statements based on estimates, judgements and policies that it believes reasonable in the circumstances.

In fulfilling its responsibilities for financial reporting and the safeguarding of assets, management has designed such internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of these financial statements. There are no changes in the Company's internal control over financial reporting that occurred during the Company's most recent interim period that has materially affected, or is reasonably likely to materially affect, the Company's control over financial reporting.

The Company has a formal policy on Corporate Disclosure approved by the Board on September 1, 2005. The Chief Executive Officer and the Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures as at June 30, 2007. They have concluded that the Company's disclosure controls and procedures were effective, at a reasonable assurance level, to ensure that material information relating to the Company would be made known to them by others within the Company, particularly during the period in which the management discussion and analysis and the consolidated financial statements contained in this report were prepared.



Charles H. Buehler
Chairman & CEO



Ian R. Kelland, CA
President & CFO

AUDITORS' REPORT

TO THE SHAREHOLDERS OF NATIONAL CHALLENGE SYSTEMS INC.

We have audited the consolidated balance sheets of NATIONAL CHALLENGE SYSTEMS INC. as at June 30, 2007 and 2006 and the consolidated statements of operations 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 consolidated financial statements present fairly, in all material respects, the financial position of the Company as at June 30, 2007 and 2006 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

The logo for Grant Thornton LLP is written in a green, cursive script font.

Grant Thornton LLP

Chartered Accountants

Toronto, Ontario

September 7, 2007, except as to Note 18.B, which is as of September 19, 2007

CONSOLIDATED BALANCE SHEETS

JUNE 30, 2007 AND 2006

	2007	2006
ASSETS		
CURRENT		
Cash	\$ 206,771	\$ 227,302
Accounts receivable (note 3)	2,412,263	2,226,910
Inventory	143,209	151,667
Prepaid expenses	225,839	145,734
Current portion of future income taxes (note 7)	315,000	-
	3,303,082	2,751,613
PROPERTY, PLANT AND EQUIPMENT (note 4)	2,892,911	2,724,391
INTANGIBLE ASSETS (note 5)	-	1,888,309
GOODWILL (note 6)	3,817,849	3,817,849
FUTURE INCOME TAXES (note 7)	1,325,000	505,000
DEFERRED FINANCING COSTS, net of accumulated amortization	29,186	60,441
	\$ 11,368,028	\$ 11,747,603
LIABILITIES		
CURRENT		
Revolving loan (note 8)	\$ 684,324	\$ 1,217,865
Accounts payable and accrued liabilities (note 15.B)	2,458,382	1,983,102
Current portion of long-term debt (note 9)	100,948	228,495
Current portion of obligations under capital lease (note 10)	230,873	132,275
	3,474,527	3,561,737
LONG-TERM DEBT (note 9)	641,342	670,940
OBLIGATIONS UNDER CAPITAL LEASE (note 10)	751,838	119,220
	1,393,180	790,160
REDEEMABLE PREFERRED SHARES (note 11)	-	3,759,343
	1,393,180	4,549,503
SHAREHOLDERS' EQUITY		
COMMON SHARES (note 12)	15,830,583	11,743,933
CONTRIBUTED SURPLUS (note 13)	211,338	190,380
DEFICIT	(9,541,600)	(8,297,950)
	6,500,321	3,636,363
	\$ 11,368,028	\$ 11,747,603

Commitments (note 14)

Subsequent events (note 18)

See accompanying notes to consolidated financial statements.

On behalf of the Board of Directors:



Charles H. Buehler
Director



Matthew Gaasenbeek
Director

CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

YEARS ENDED JUNE 30, 2007 AND 2006

	2007	2006
REVENUES		
Non-hazardous vacuum services	\$ 14,772,654	\$ 15,409,763
Compactor rental income	589,971	518,005
Compactor sales, service and other	55,590	104,060
	15,418,215	16,031,828
COST OF SALES	10,768,638	11,982,135
GROSS MARGIN	4,649,577	4,049,693
OPERATING EXPENSE (INCOME)		
Selling, general and administrative	3,651,694	2,932,828
Amortization of property, plant and equipment	695,907	606,859
Amortization of intangible assets	896,642	969,064
Share based compensation	20,958	55,348
Foreign exchange loss (gain)	453	(22,747)
	5,265,654	4,541,352
LOSS BEFORE THE UNDERNOTED	(616,077)	(491,659)
OTHER EXPENSE (INCOME)		
Gain on disposal of property, plant and equipment	(9,212)	-
Write-down of property, plant and equipment (note 4)	234,755	189,514
Write-down of intangible assets (note 5.C)	991,667	-
Interest on long-term debt and obligations under capital lease	120,229	103,617
Other interest	97,827	96,195
Dividends on preferred shares	327,307	318,853
	1,762,573	708,179
LOSS BEFORE INCOME TAXES	(2,378,650)	(1,199,838)
FUTURE INCOME TAXES (note 7)	(1,135,000)	(4,000)
NET LOSS	(1,243,650)	(1,195,838)
DEFICIT, BEGINNING OF YEAR	(8,297,950)	(7,102,112)
DEFICIT, END OF YEAR	\$ (9,541,600)	\$ (8,297,950)
LOSS PER SHARE, BASIC AND DILUTED (note 16)	\$ (0.03)	\$ (0.03)

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30, 2007 AND 2006

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss for the year	\$ (1,243,650)	\$ (1,195,838)
Add (deduct) items not involving cash:		
Amortization of property, plant and equipment	695,907	606,859
Amortization of intangible assets	896,642	969,064
Share based compensation	20,958	55,348
Foreign exchange loss (gain)	453	(22,747)
Gain on disposal of property, plant and equipment	(9,212)	-
Write-down of property, plant and equipment	234,755	189,514
Write-down of intangible assets	991,667	-
Dividends accrued on preferred shares	327,307	318,853
Future income taxes	(1,135,000)	(4,000)
	779,827	917,053
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable, net	(185,353)	70,009
Decrease in inventory	8,458	27,578
(Increase) decrease in prepaid expenses	(80,105)	61,052
Increase (decrease) in accounts payable and accrued liabilities	475,280	(336,631)
CASH FLOWS FROM OPERATING ACTIVITIES	998,107	739,061
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of property, plant and equipment	(382,197)	(203,997)
Proceeds on disposal of property, plant and equipment	277,551	-
	(104,646)	(203,997)
CASH FLOWS FROM FINANCING ACTIVITIES		
(Repayment) advance of revolving loan	(533,541)	92,370
Repayment of long-term debt	(157,598)	(426,273)
Repayment of capital lease obligation	(222,853)	(116,427)
Payment of deferred financing costs	-	(4,514)
	(913,992)	(454,844)
(DECREASE) INCREASE IN CASH DURING THE YEAR	(20,531)	80,220
CASH BEGINNING OF YEAR	227,302	147,082
CASH END OF YEAR	\$ 206,771	\$ 227,302
Supplemental cash flow information:		
Interest paid	\$ 218,056	\$ 199,812
Non-cash transactions:		
Capital assets acquired through capital leases	\$ 954,069	\$ 90,508
Conversion of preferred shares to common shares	\$ 4,086,650	\$ -

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS

National Challenge Systems Inc. (the “Company” or “NCS”) is incorporated under the Canada Business Corporations Act. The primary operations of the Company consist of operating vacuum truck fleets that provide collection, treatment and disposal services for non-hazardous liquid waste and other related services.

2. SIGNIFICANT ACCOUNTING POLICIES

A. Principles of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, after the elimination of all material inter-company transactions and balances, as follows:

(i) Active

- Organic Resource Management Inc. (“ORMI”)
- A&A Anderson Tank Service (Vancouver) Ltd. (“A&A”)

(ii) Inactive

- National Organic Resources Inc.
- NCS Holdings Limited, which in turn controls 70% of NCS Environmental Services Limited (“NCS ESL”). NCS ESL holds certain patents, software licenses and marketing agreements applicable to planned expansion outside of Canada (see note 5).

B. Cash and cash equivalents

Cash and cash equivalents include cash on hand and balances with banks and highly liquid temporary money market instruments with original maturities of three months or less. Bank borrowings are considered to be financing activities.

C. Inventory

Inventory is valued at the lower of cost and replacement cost.

D. Property, plant and equipment

Property, plant and equipment are recorded at cost. Amortization of property, plant and equipment is provided at rates designed to write off the assets over their useful lives as follows:

Building	5% declining balance
Compactor rental machines	Straight-line over 15 years
Vehicles	30% declining balance
Vehicles under capital lease	30% declining balance
Office furniture, equipment and computers	20% declining balance
Office equipment under capital lease	20% declining balance
Software	Straight-line over 5 years
Machinery and equipment	20% declining balance
Leasehold improvements	Straight-line over the term of the lease
Farm storage units	Straight-line over 10 years

If property, plant and equipment are subject to permanent impairment, a write-down will be provided.

E. Goodwill and long-lived intangible assets

The Company does not amortize goodwill and recognized intangible assets are amortized over their useful life to the Company unless the life is determined to be indefinite. When an intangible asset is determined to have an indefinite life, it is not amortized until its life is considered to be no longer indefinite. Goodwill is subject to an annual impairment test. If intangible assets or goodwill are subject to permanent impairment, a write-down will be provided.

Intangible assets are identified and recorded at cost. Cost is based on valuations of certain assets relating to the Company's business acquisitions in 2002. Amortization of intangible assets is provided at rates to write-off the assets over their estimated useful life as follows:

- (i) Customer relationships - straight-line over 5 years
- (ii) Software license agreement - straight-line over 5 years
- (iii) Patent license agreements - straight-line over 15 years

F. Impairment of long-lived assets and intangibles

Long-lived assets and intangibles held and used by the Company are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If changes

in circumstances indicate that the carrying amount of an asset that an entity expects to hold and use may not be recoverable, future cash flows expected to result from the use of the asset and its disposition must be estimated. If the undiscounted value of the future cash flows is less than the carrying amount of the asset, impairment is recognized and the asset will be written down to its fair value.

During 2007 the Company recorded an impairment loss of \$234,755 (2006 - \$189,514) in the carrying value of its compactor rental machines, as described in Note 4, and an impairment loss of \$991,667 (2006 - \$ Nil) in the carrying value of its patent license agreements, as described in Note 5. As at June 30, 2007, the Company has no intangible assets remaining and management believes that there has been no impairment in the value of any other of the Company's long-lived assets.

G. Income taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable or recoverable for the current year. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized.

H. Deferred financing costs

Deferred financing costs are amortized on a straight-line basis over the repayment period of a revolving loan agreement which expires on June 14, 2008.

I. Revenue recognition

- (i) Revenue from non-hazardous vacuum services is recognized when the service is performed and collection is reasonably assured.
- (ii) Compactor rental income which is derived from a month to month agreement is recognized monthly providing that collection is reasonably assured.
- (iii) Compactor sales and service revenue is recognized when goods are delivered and services are performed and collection is reasonably assured.

J. Loss per share

Basic loss per share is calculated based on the weighted average number of shares outstanding during the year. Diluted per share amounts are calculated using the treasury stock method whereby loss per share is calculated as if common share equivalents such as convertible preferred shares, stock options and warrants are converted or exercised at the beginning of the year and funds received were used to purchase the Company's own stock. The effect of potential issuances of common shares under preferred share conversions, options and warrants would be anti-dilutive, and accordingly basic and diluted loss per share are the same.

K. Stock-based compensation plan

The Company has a stock option plan, as described in Note 12.E, which allows for the issuance of stock options to employees and directors. All stock-based awards made by the Company are recognized using the fair value method, whereby the fair value of options granted is recorded as compensation expense in the financial statements in the period the options are vested or expected to vest.

L. Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and 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 estimates and assumptions include those related to the valuation of goodwill and intangibles, estimated useful lives of intangibles, property, plant and equipment and recoverability of future income tax assets. Actual results could differ from those estimates.

M. Pending accounting pronouncements

In 2005, the CICA issued three new standards: Financial Instruments – Recognition and Measurement, Hedges and Comprehensive Income. These Sections will become effective for the Company on July 1, 2007 and require the following:

- (i) In Section 1530 “Comprehensive Income”, certain gains and losses arising from changes in fair value will be temporarily recorded outside the income statement in comprehensive income. The Company does not expect the implementation of this Section to have a material impact on its consolidated financial statements.
- (ii) In Section 3855 “Financial Instruments – Recognition and Measurement” and Section 3865 “Hedges”, all financial instruments including derivatives are to be included on a company’s balance sheet and measured either at their fair value or, in limited circumstances, when fair value may not be considered most relevant, at cost or amortized cost. These Sections specify when gains and losses, as a result of changes in fair value, are to be recognized in the income statement. The Company does not expect the implementation of these Sections to have a material impact on its consolidated financial statements.

3. ACCOUNTS RECEIVABLE

	2007	2006
Trade	\$ 2,376,789	\$ 2,193,633
Other	54,789	49,954
	2,431,578	2,243,587
Less allowances for doubtful accounts	(19,315)	(16,677)
	\$ 2,412,263	\$ 2,226,910

4. PROPERTY, PLANT AND EQUIPMENT

	2007			2006		
	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Land	\$ 263,500	\$ -	\$ 263,500	\$ 263,500	\$ -	\$ 263,500
Building	729,815	79,851	649,964	656,623	47,568	609,055
Rental machines	1,354,906	1,322,367	32,539	2,514,904	1,919,404	595,500
Vehicles	2,459,565	2,272,368	187,197	2,905,484	2,733,739	171,745
Vehicles under capital lease	1,554,042	531,867	1,022,175	530,535	313,115	217,420
Office furniture, equipment and computers	1,032,377	829,990	202,387	998,374	783,154	215,220
Office equipment under capital lease	87,407	43,089	44,318	79,913	33,883	46,030
Software	831,792	534,977	296,815	760,962	384,884	376,078
Machinery and equipment	713,510	551,808	161,702	693,673	513,862	179,811
Leasehold improvements	22,866	22,866	-	22,866	20,862	2,004
Farm storage units	157,145	124,831	32,314	157,145	109,117	48,028
	\$9,206,925	\$6,314,014	\$2,892,911	\$9,583,979	\$6,859,588	\$2,724,391

During the year, the Company sold or disposed of more than half of its rental compactors following the expiration of its long-term contract with a major retailer. Due to the expectation that the Company will dispose of the remaining compactors prior to June 30, 2008 and does not anticipate recovering any value for these machines, other than machines for which there are outstanding purchase commitments at quoted market prices, the net loss for the year includes an impairment charge of \$234,755 (2006 - \$189,514).

Amortization of property, plant and equipment includes \$227,958 (2006 - \$83,137) relating to assets under capital lease.

5. INTANGIBLE ASSETS

	2007			2006		
	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Software license agreement	\$ 3,000,000	\$ 3,000,000	\$ -	\$ 3,000,000	\$ 2,450,000	\$ 550,000
Customer relationships	1,550,000	1,550,000	-	1,550,000	1,303,358	246,642
Patent license agreements	1,500,000	1,500,000	-	1,500,000	408,333	1,091,667
	\$6,050,000	\$6,050,000	\$ -	\$6,050,000	\$4,161,691	\$1,888,309

A. Software license agreement

The software license agreement represents the value attributed to the Company's perpetual license for use of a proprietary route optimization and management information software ("Software") in Canada from Path Information Systems Inc. ("Path"), a company partially owned by a director of the Company. The Company has exclusive use of the Software in its industry.

In addition to this agreement, on February 14, 2002, NCS ESL obtained a perpetual non-exclusive license for the worldwide (excluding Canada) use of the Software from Path ("Worldwide License"). On November 11, 2003, NCS ESL entered into a marketing agreement ("Marketing Agreement") for the Software which: (1) gives NCS ESL the right to market Software licenses to third parties for use in its industry worldwide (excluding Canada); and (2) makes the Software exclusive to NCS ESL for its industry. Licenses marketed by NCS ESL under the Marketing Agreement are at no charge from Path and do not restrict NCS ESL in any way with respect to the fees it can charge to third party licensees. This Marketing Agreement was provided by Path at no cost to NCS ESL. The Software and Marketing Agreement will be applicable to the Company as it pursues its expansion plan outside of Canada. The value attributed to the software license agreement includes only the value of the license in Canada and no value has been attributed to either the Marketing Agreement or the Worldwide License.

Subsequent to year end, the Company reached an agreement to purchase 100% of the issued and outstanding shares of Path, as described in Note 18.B.

B. Customer relationships

Customer relationships acquired as a result of the acquisition of ORMI and A&A are net of an impairment charge of \$160,334, recorded in 2003.

C. Patent license agreements

On February 20, 2002, the Company signed an exclusive licensing agreement (the "License") with Organic Resource Technology Inc. ("ORTI"), a company partially owned by two directors of the Company, for ORTI's Canadian patented Direct Land Application/Organic Soil Conditioning Process ("DLAP"), with a 15-year, fixed price option to purchase all of the outstanding shares of ORTI (the "Option"). The Option was granted at no cost to the Company. The License is for a 15-year period and is exclusive to the Company for use of the DLAP throughout Canada. The Company has perpetual rights to DLAP in the province of Ontario at no cost or royalty.

Over the past few years ORMI has been impacted by a number of government regulatory changes that directly affect the way liquid organic waste is handled and processed in Ontario. As a result of these changes, most of the third party disposal facilities in Ontario that receive and process liquid organic waste have significantly reduced their capacity, or have closed down altogether. This has had a major impact on the cost of recycling/disposal. As part of the regulatory changes, the Company had to close most of its DLAP sites during 2005 and commence a re-permitting process. This was an extensive undertaking and the Company had limited success, with only one of the smaller Ontario DLAP sites being re-permitted. In the interim, a large portion of the waste was trucked to alternative third party disposal sites located in Quebec. In 2007, the Company was able to locate additional third party disposal capacity in Ontario thus impacting the incremental savings compared to Quebec disposal that the one Ontario DLAP site provided.

In the last two years, anaerobic digestion has been evolving as a superior competitive disposal alternative. The Company believes that this alternative will ultimately provide a low-cost, long-term recycling solution for all of the organic residuals the Company collects. As a result, the Company has decided to suspend efforts to re-permit and

expand its DLAP facilities in Ontario and to focus its efforts on anaerobic digestion. In May 2007, the Company signed an exclusive, 20-year contract to supply organic residuals as feedstock to a farm-based anaerobic digester for the production of renewable biogas energy. Although initially the volumes for this site are not material, the Company believes that this contract signals the advent of anaerobic digestion, making DLAP obsolete and no longer a long term cost effective method of disposal. Therefore the net loss for the year includes an impairment charge of \$991,667 (2006 - \$ Nil) to write-off the balance of the carrying value of the Company's patent license agreements.

Subsequent to year end, the Company reached an agreement to purchase the Canadian patent for DLAP and another patent, Organic Resource Recovery System ("ORRS"), for \$15,000 cash, as further described in Note 18.B. Purchasing the DLAP patent eliminates the requirement for the Company to pay an annual fee of \$25,000 under the existing license.

6. GOODWILL

	2007	2006
ORMI, cost	\$ 2,434,793	\$ 2,434,793
A&A, cost net of cumulative provision for impairment of \$1,261,971, recorded in 2003	1,383,056	1,383,056
	\$ 3,817,849	\$ 3,817,849

The annual goodwill impairment test indicated no impairment loss for either 2007 or 2006.

7. INCOME TAXES

A. Provision for taxes

The income tax recovery included in the consolidated statements of operations differs from the statutory income tax rate as follows:

	2007	2006
Combined Federal and Ontario income tax rate	36.12%	36.12%
Income tax recovery based on the statutory income tax rate	\$ (859,000)	\$ (433,000)
Tax effect of non-deductible and other items	540,000	263,000
Effect of tax rate changes	15,000	143,000
Valuation allowance (recovery)	(831,000)	23,000
Provision for income taxes	\$ (1,135,000)	\$ (4,000)

B. Future tax asset

Future income tax assets consist of the following:

	2007	2006
Excess of capital cost for tax purposes over net book value of capital assets at statutory tax rate	\$ 1,637,000	\$ 1,130,000
Loss carryforwards at statutory tax rate	1,192,000	1,395,000
	2,829,000	2,525,000
Deduct valuation allowance	(1,189,000)	(2,020,000)
Future income tax asset	\$ 1,640,000	\$ 505,000
Less current portion	315,000	-
	\$ 1,325,000	\$ 505,000

Management believes that realization of a portion of the net future income tax assets is more likely than not. The ultimate realization of future income tax assets is dependent upon the generation of future taxable income during the periods in which temporary tax and accounting differences become deductible. Management considered projected future taxable income and tax planning strategies in making their assessment.

C. Non-capital losses

The right to apply non-capital losses of approximately \$3,496,000 against taxable income of future years, inclusive of those for which a benefit has been recognized, expires as follows:

2007	\$ 36,000
2008	26,000
2009	855,000
2010	2,272,000
2014	22,000
2015	94,000
2027	191,000
	\$ 3,496,000

8. REVOLVING LOAN

The Company has access to a revolving credit facility with Textron Financial Canada Ltd. to a limit of \$2,000,000; advances bearing interest at the Royal Bank of Canada's prime commercial lending rate plus 2% (8.0% at June 30, 2007). In addition, there is an annual fee of 1% of the \$2,000,000 credit line limit. The term of the agreement is for three years commencing June 14, 2005.

Security is provided by:

- a continuing security interest against the accounts receivables of ORMI and A&A; and
- unlimited guarantees of the parent and subsidiary companies.

The Company has provided covenants whereby:

- it maintain at all times, adjusted tangible net worth, equal to the sum of shareholders' equity and redeemable preferred shares less prepaid expenses, intangible assets, goodwill, future income taxes and deferred financing costs, of not less than \$500,000;
- it shall not have accounts receivable turnover of more than sixty days; and
- it shall not purchase, make or enter into any commitment to make non-financed capital expenditures in an amount not to exceed an aggregate of \$250,000 during the fiscal year.

At June 30, 2007 the Company was in compliance with the above covenants.

9. LONG-TERM DEBT

	2007	2006
(a) 48-month note payable with interest paid monthly on the outstanding principal at the current bank prime lending rate (6.0% at June 30, 2007). Repayment of principal is due in 36 monthly instalments of \$6,977 maturing in September 2007. Certain vehicles with a net book value of \$34,033 have been provided as security.	\$ 20,933	\$ 104,662
(b) 6.25% unsecured note payable in 24 blended monthly instalments of principal and interest of \$4,292 maturing in December 2008.	73,568	93,636
(c) 8% per annum calculated half-yearly mortgage payable in blended monthly instalments of principal and interest of \$5,136 maturing in 2009, secured on the building and land with a net book value of \$913,464.	579,403	594,772
(d) 1.90% note payable in 48 blended monthly instalments of principal and interest of \$610 maturing in December 2010. Certain vehicles with a net book value of \$22,675 have been provided as security.	24,770	-
(e) 6.90% note payable in 60 blended monthly instalments of principal and interest of \$913 maturing in February 2012. Certain vehicles with a net book value of \$56,064 have been provided as security.	43,616	-
(f) 10% USD promissory note payable in blended monthly instalments of principal and interest of \$23,160 USD maturing in October 2006. Compactor rental equipment and the assignment of certain rental revenue receipts have been provided as security.	-	101,179
(g) 8.63% notes payable in blended monthly instalments of principal and interest of \$886, maturing in December 2006.	-	5,186
	742,290	899,435
Less current portion	(100,948)	(228,495)
	\$ 641,342	\$ 670,940

Long-term debt due in each of the next five years is as follows:

2008	\$	100,948
2009		59,102
2010		561,394
2011		13,726
2012		7,120
	\$	742,290

10. OBLIGATIONS UNDER CAPITAL LEASE

Future minimum payments, in aggregate and for each of the next five years, together with the balance of the obligation under capital leases are as follows:

2008	\$	308,898
2009		273,083
2010		268,160
2011		248,617
2012		79,287
Total minimum lease payments		1,178,045
Less amount representing interest at rates from 6.2% to 10.4%		(195,334)
Balance of obligation		982,711
Less current portion		(230,873)
	\$	751,838

11. REDEEMABLE PREFERRED SHARES

A. Authorized

An unlimited number of Class A and Class B preferred shares.

An unlimited number of preferred shares issuable in series.

B. Class A preferred shares

Non-voting, non-participating, entitled to a 12% cumulative dividend per annum to be paid quarterly, redeemable at any time and convertible on or after June 1, 2007 into common shares at the option of either the Company or the preferred shareholder. The conversion into common shares is to be calculated by dividing the redemption value of the preferred shares at \$1.00 per share by an amount per common share, which would be equal to the lesser of:

- (i) \$0.40; or
- (ii) the average weighted market price over the 15-day period immediately prior to the date upon which conversion notice is given.

The provision for a 12% dividend on Class A preferred shares is cumulative and can be paid in cash or in additional Class A preferred shares at the Company's discretion. No dividends may be paid on any other class of shares until these shares have been redeemed.

C. Class B preferred shares

Non-voting, non-participating, with no entitlement to dividends, redeemable at any time and convertible on or after June 1, 2007 into common shares at the option of either the Company or the preferred shareholder. The conversion into common shares is to be calculated by dividing the redemption value of the preferred shares at \$1.00 per share by an amount per common share, which would be equal to the lesser of:

- (i) \$0.40; or
- (ii) the average weighted market price over the 15-day period immediately prior to the date upon which conversion notice is given.

D. Issued

	2007	2006	2007	2006
	Number of Shares		Book Value	
Class A shares:				
Balance beginning of year	2,048,000	2,048,000	\$ 2,048,000	\$ 2,048,000
Accrued dividends	-	-	-	811,343
Issued in the year	1,138,650	-	1,138,650	-
Conversion to common shares	(3,186,650)	-	(3,186,650)	-
Balance end of year	-	2,048,000	-	2,859,343
Class B shares:				
Balance beginning of year	900,000	900,000	900,000	900,000
Conversion to common shares	(900,000)	-	(900,000)	-
Balance end of year	-	900,000	-	900,000
	-	2,948,000	\$ -	\$ 3,759,343

On January 31, 2007 the Company issued \$1,016,823 of Class A shares representing the amount of dividends accrued to date. On May 31, 2007 the Company issued a further \$121,827 of Class A shares for dividends accrued in the four months ending May 31, 2007. On June 1, 2007 the Company converted all issued and outstanding Class A and Class B shares into 47,965,376 common shares with a book value of \$4,086,650 based on a weighted average market price of \$0.0852 per share. There were no cumulative dividends in arrears on the Class A preferred shares as at June 30, 2007 (2006 - \$811,343).

The specific conversion provisions of the Class A and B preferred shares, which allowed the holder to receive a number of common shares which varied based on the redemption value and accrued dividends of the preferred shares, resulted in classification of the preferred shares as a financial liability in 2006. The financial liability included accrued dividends.

12. COMMON SHARES

A. Common shares

Authorized 100,000,000; issued as follows:

	2007	2006	2007	2006
	Number of Shares		Book Value	
Balance beginning of year	40,133,573	39,642,323	\$ 11,743,933	\$ 11,681,173
Conversion of preferred shares	47,965,376	-	4,086,650	-
Employee share compensation	-	300,000	-	45,000
Directors' compensation	-	191,250	-	17,760
Balance end of year	88,098,949	40,133,573	\$ 15,830,583	\$ 11,743,933

B. Employee share compensation

In 2006 as per an employment contract the Company paid one of the executives in common shares. The number of shares was calculated by dividing the salary payable by \$0.15. Salary was based on an annual amount of \$120,000 pro-rated for the amount of time devoted to the Company.

C. Directors' compensation plan

Non-management directors are compensated for Board and Committee meetings in cash or through the issuance of common shares at the Company's discretion. The number of shares to be issued is based on a weekly average closing price of the shares each quarter with a minimum price of \$0.20 per share.

D. Warrants outstanding

		2007	2006
Expiry Date	Exercise Price	Number of Shares	
June 29, 2007	\$ 0.20	-	100,000
		-	100,000

On June 29, 2007 100,000 warrants expired without exercise.

E. Stock option plan

The Company has an incentive stock option plan for certain employees and directors as determined by the Board of Directors. The maximum number of options that can be granted under the plan is 5,200,000 and no one person can be issued options which, when exercised, exceed 5% of the issued and outstanding common shares. The Board of Directors determines the number of options granted and their exercise price and vesting period. However, the minimum exercise price of a stock option is the weighted average trading price of the Company's shares for the five days preceding the award date. As of June 30, 2007 there were 5,155,000 options outstanding with exercise prices ranging from \$0.10 to \$0.30, and average remaining life of 3.8 years. Of the 3,470,000 options granted in 2007, 1,050,000 vest over a three year period, 420,000 vested immediately on grant and 2,000,000 options vest subject to certain performance conditions. The 475,000 options granted in 2006 vest over a three year period.

Option activity for each of the years ending June 30, 2007 and 2006 is as follows:

	2007		2006			
	Weighted Average Exercise Price		Number of Options			
Balance beginning of year	\$	0.19	\$	0.21	4,023,000	4,265,000
Granted		0.10		0.14	3,470,000	475,000
Expired		0.19		0.27	(2,338,000)	(717,000)
Balance end of year	\$	0.13	\$	0.19	5,155,000	4,023,000

Weighted average characteristics of options outstanding at June 30, 2007 are as follows:

Range of Exercise Prices	Outstanding Options		Exercisable Options		Weighted Average Remaining Life Years
	Number at June 30, 2007	Weighted Average Exercise Price	Number at June 30, 2007	Weighted Average Exercise Price	
\$0.10	3,050,000	\$ 0.10	-	\$ -	5.0
\$0.11-\$0.20	1,655,000	0.15	1,605,000	0.15	2.6
\$0.21-\$0.30	450,000	0.30	450,000	0.30	0.5
	5,155,000	\$ 0.13	2,055,000	\$ 0.18	3.8

F. Fair value of stock options granted to employees, directors and non-employees

The fair value of each option granted during the year is estimated on the date of grant using the Black-Scholes option pricing model based on the following weighted average assumptions:

	2007	2006
Number of options granted	3,470,000	475,000
Fair value	\$0.05	\$0.07
Assumptions:		
Risk free interest rate	4.6%	3.6%
Average expected life in years	4.7	3.6
Expected dividend yield	0%	0%
Volatility	60%	70%

13. CONTRIBUTED SURPLUS

	2007	2006
Balance beginning of year	\$ 190,380	\$ 160,032
Value of stock-based compensation	20,958	30,348
Balance end of year	\$ 211,338	\$ 190,380

14. COMMITMENTS

A. Operating leases

Future minimum payments under operating leases for the next five years and in aggregate for premises, automotive and office equipment are approximately as follows:

2008	\$ 263,381
2009	173,476
2010	91,115
2011	83,237
2012	6,936
	\$ 618,145

In addition, the Company is required to pay its share of maintenance, taxes and other costs of the premises leased.

B. Patent license agreement

Pursuant to a patent license agreement for a Direct Land Application Process with a company related to two directors, the Company is committed to a minimum annual license fee of \$25,000 to 2017.

Subsequent to year end, the Company reached an agreement to purchase the Canadian patent for DLAP, as described in Note 18.B.

15. RELATED PARTY TRANSACTIONS

A. Related party charges

During the year, the Company incurred charges from directors or companies and/or individuals related to them.

These amounts have been recorded at their exchange amount, being the amount agreed to by all parties, for amounts approximately as follows:

	2007	2006
Dividends on preferred shares	\$ 199,194	\$ 318,853
Interest expense	9,253	12,776
Consulting	4,500	-
Software development cost	-	9,234

B. Accounts payable and accrued liabilities

Includes amounts payable as at June 30, 2007 to certain directors and/or companies controlled by them totaling \$103 (2006 - \$52,251).

C. Long-term debt

Includes a note payable to a related party for \$20,933 (2006 - \$104,662). The note is repayable in 36 equal monthly instalments of \$6,977, the last of which is due September 1, 2007. Long-term debt also includes a note payable to a company owned by certain directors for \$73,568 (2006 - \$93,636), repayable in 24 blended monthly instalments of principal and interest of \$4,292, which commenced January 2007 and matures in December 2008.

D. Patent license agreement

Pursuant to patent license agreements with companies related to directors of the Company as described in Note 5.C, the Company has use of patent products at a minimum annual patent license fee of \$25,000. The charges for 2007 and 2006 were waived by the licensor.

Subsequent to year end, the Company reached an agreement to purchase the Canadian patent for DLAP, as described in Note 18.B.

16. LOSS PER SHARE

Basic loss per share is based on the weighted average common shares outstanding during the year. Weighted average common shares used in computation of basic loss per share were 44,075,933 and 39,789,250 for the years ended June 30, 2007 and 2006, respectively.

17. FINANCIAL INSTRUMENTS

A. Interest rate risk

The Company's exposure to interest rate risk is as follows:

Accounts receivable	Non-interest bearing
Revolving loan	Floating rate
Accounts payable and accrued liabilities	Non-interest bearing
Long-term debt	Fixed and floating rates
Obligations under capital lease	Fixed rates

B. Credit risk

The Company's exposure to credit risk is indicated by the carrying value of its financial assets. The Company does not have a significant exposure to any individual customer. An allowance for doubtful accounts is established based upon factors surrounding the credit risk of specific customers, historical trends and other information.

C. Currency risk

The Company's exposure to market risks associated with changes in foreign currency exchange rates is substantially limited to its long-term debt with one party. As at June 30, 2007 there was no debt payable to this party (2006 - \$90,743 USD).

D. Fair value

The following summarizes the major methods and assumptions used in estimating fair values of financial instruments.

Short-term financial instruments are valued at their carrying amounts, which are reasonable estimates of fair value due to the relatively short period to maturity. This approach applies to accounts receivable, the revolving loan and accounts payable and accrued liabilities.

The carrying value of long-term debt and obligations under capital lease approximates fair value since the terms and interest rates are consistent with current market terms and rates for such borrowings. The fair value of redeemable preferred shares was not readily determinable in 2006 because instruments with similar characteristics were not readily available for comparison.

18 SUBSEQUENT EVENTS

A. Vertical amalgamation

On July 1, 2007 the Company vertically amalgamated with its largest and wholly owned subsidiary Organic Resource Management Inc. and also assumed its subsidiary's name. This change simplifies the Company's corporate structure and gives the Company a name more closely reflective of its core business, the provision of vacuum truck services for the collection, treatment and disposal of non-hazardous liquid waste.

B. Related party transactions

On August 29, 2007 the Company announced that it had reached an agreement for three related party transactions (see Note 5) which will eliminate the existing related party relationships for software and patents. These transactions were unanimously approved by a committee of all seven independent directors on June 25, 2007 and closed on September 19, 2007. The three related party transactions resulted in the Company purchasing:

- (i) 100% of the issued and outstanding shares of ORMI Information Systems Inc., formerly Path Information Systems Inc. ("OIS/Path"), a company controlled by one of the Company's directors, for \$700,000. \$100,000 of the purchase price was paid in cash on closing and a six year promissory note with interest at 7% per annum to be paid in blended equal monthly instalments will be issued for the balance. The shares of OIS/Path have been pledged to the vendors as security until the balance has been paid. Also as part of the transaction, the vendors retained the the Path name and obtained a perpetual and exclusive license, including access to the source code, for use of the software outside of the liquid organic industry.
- (ii) Canadian patents for DLAP and ORRS from Organic Resource Technologies Inc., a company partially owned by two directors, for \$15,000 cash. Purchasing the DLAP patent eliminates the requirement for the Company to pay royalties on new ORRS locations and the annual fee of \$25,000 under the existing license.
- (iii) The remaining 30% equity interest in NCS ESL that it does not already own from Organic Resource Technologies International Inc, a company partially owned by two directors of the Company, for \$10,000 cash.

CORPORATE DIRECTORY

Board of Directors

Charles H. Buehler

Chairman and CEO, National Challenge Systems Inc.

Donald R. Carse, Jr.¹

Former CFO, National Challenge Systems Inc.

Douglas M. Carruthers

Vice President Corporate Development, National Challenge Systems Inc.

Frank Facto^{2,3}

Senior Human Resources Consultant, City of Toronto
Former President and Director, Toronto Municipal Credit Union

Martin Fallick^{2,3}

Former President, Fairway Canadian Express

Matthew Gaasenbeek^{1,2}

Chairman, Northern Crown Capital
Former Chairman, Ontario Development Corporation
Former Senior Vice President and Director, Midland Doherty Limited

Gary Kain

Former Chairman & CEO, Regional Cablesystems Inc.
Former COO and CFO Canadian Satellite Communications Inc. (Cancom)

Ian London^{1,3}

Vice President, Corporate Development,
Avalon Ventures Ltd.
Former CEO, Process Products Limited
Former President & CEO, Ontario Hydro International

Executive Officers

Charles H. Buehler

Chairman & CEO

Ian R. Kelland

President & CFO

Douglas M. Carruthers

Vice President Corporate Development

Edward Dreher

Vice President Finance

¹Member Audit Committee

²Member Compensation Committee

³Member Corporate Governance Committee

CORPORATE INFORMATION

Independent Auditors

Grant Thornton LLP
350 Burnhamthorpe Road W.
Suite 401
Mississauga, Ontario L5B 3J1

Legal Counsel

McMillan Binch Mendelsohn LLP
BCE Place, Suite 4400
Bay Wellington Tower
181 Bay Street
Toronto, Ontario M5J 2T3

Transfer Agent

Equity Transfer & Trust Company
200 University Avenue
Suite 400
Toronto, Ontario M5H 4H1

Stock Information

Shares of Organic Resource Management Inc.
(formerly National Challenge Systems Inc.) are
traded on the Toronto Stock Exchange under the
symbol ORI.

Investor Inquiries

Inquiries should be directed to:

Investor Relations
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3700 Steeles Avenue West, Suite 601
Woodbridge, Ontario L4L 8K8
Email: info@ormi.com

Also visit the Company's IR HUB at
http://www.ormi.com/ORMI_Investor.asp

Annual Meeting of Shareholders

The Annual Meeting of the Shareholders will be held
on October 24, 2007 at 4:00 p.m. at:

The offices of McMillan Binch Mendelsohn LLP
BCE Place, Suite 4400
Bay Wellington Tower
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PRINCIPAL OFFICES

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