

TOTALLY HIP TECHNOLOGIES INC.
Form 51-102F1

MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

MARCH 1, 2005

For the three months ended December 31, 2004, Totally Hip Technologies Inc. ("Totally Hip" or the "Company") has prepared this management discussion following the requirements of new National Instrument 51-102 ("NI-51-102"). NI 51-102 outlines more detailed and comprehensive requirements for management discussion and analysis. This Management Discussion and Analysis of the results of operations as of March 1, 2005 provides information on the operations of Totally Hip for the three months ended December 31, 2004 and subsequent to the quarter end and should be read in conjunction with the audited financial statements and accompanying notes for the years ended September 30, 2004 and 2003.

FORWARD LOOKING STATEMENTS

Certain information included in this discussion may constitute forward-looking statements. Forward-looking statements are based on current expectations and entail certain risks and uncertainties. The risks and uncertainties could cause or contribute to actual results that are materially different than those expressed or implied. The Company disclaims any obligation or intention to update or revise any forward-looking statement, whether as a result of new information, future events, or otherwise.

DESCRIPTION OF BUSINESS AND PRODUCTS

Totally Hip Technologies Inc. ("Totally Hip"), founded in 1995 is an award winning developer of convergent media technologies and one of the leading QuickTime developers in the world. Totally Hip's products allow users to create content with the highest levels of interactivity combined with video and other digital media integration. Totally Hip develops software, enterprise solutions and services to effectively produce and deliver convergent media solutions and to ensure its software products are compatible with and complement established media file formats, platforms, and standards.

Totally Hip currently focuses its engineering, sales and marketing resources on its present QuickTime based products. Totally Hip began developing products based on QuickTime in 1998 and is recognized as one of the leading QuickTime software developers in the world. QuickTime has risen to become a leading technology for the delivery and integration of rich media content over the Internet and one of the most popular media players. Quick Time is also used for Apple's popular iPod portable music player. Totally Hip's principal products focus on allowing Totally Hip's customers to create compelling and interactive content that deliver a quality viewing experience that improve brand awareness, message comprehension, web site retention and recall by their viewers.

The current target market of Totally Hip's products is primarily the content creation, production and delivery segment of the interactive video and digital media integration markets. The majority of the current customer base can be categorized into three distinct groups comprising professional multimedia developers, communications and production companies and educators and educational institutions and developers. The largest segment of the client base is located in North America, with the second largest customer group situated in Europe. Service based clients are mainly looking to implement major media integration or interactive QuickTime delivery solutions and tend to not have in-house capability or availability of expert, qualified or trained staff.

Totally Hip generates awareness and demand for its products through its websites, developer network, community discussion lists, public relations activities, email notifications or offers, press articles and reviews.

Totally Hip continues to mainly sell its products direct to customers with limited marketing and sales resources. Totally Hip also sells its software products through other specialty resellers.

LiveStage Professional gives users the combination of an industrial strength media integration and authoring tool at

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an affordable price including the added VR editor and MindAvenue Axel 3D support, a completely new support site and features to greatly improve workflow, productivity and learning time.

LiveStage Professional also uncovers a whole set of QTVR features rarely accessible before. Supporting 360° panoramic, cubic or object movies, it allows users to quickly and easily create interactive QTVR presentations. LiveStage also introduced FastTracks that allow users to simply add a map, compass and directional sound to a QTVR without any scripting via a new scriptless VR editor that is easy and fast to learn.

LiveStage Professional also includes support for MindAvenue's Axel. Axel is the award winning 3D software for publishing interactive 3D content for the web. Users can combine the benefits of two great tools to create some truly amazing interactive 3D content.

LiveStage Professional's user interface emphasizes working in a distinctly visual environment for greater productivity. It includes dozens of productivity features that allows experienced developers to work faster and more efficiently, and new users to create powerful content quickly. The latest release fully supports all of the new features in QuickTime. The Company continues to strive towards developing new and enhanced products.

Live Stage Professional Version 4.5

During the year ended September 30, 2004, the Company announced the release of LiveStage Professional 4.5. LiveStage Professional 4.5 expands market opportunities for development professionals and uncovers a whole new set of functionality that was not accessible before, with the introduction of the QScript Extension Essentials (QSXE) QuickTime component.

Livestage professional has become an indispensable cross-platform media integration tool used in developing compelling cross-platform interactive content. This latest version represents a significant advancement for both the LiveStage Professional production environment and the multi-media industry.

LiveSlideShow 3

On August 31, 2004, Totally Hip Technologies Inc. announced the release of LiveSlideShow 3 for both Windows and Macintosh computers.

LiveSlideShow is one of the easiest to use slide show creation applications available on the market today. LiveSlideShow 3 has a host of powerful new features to enable customers to easily transform their digital photos into dazzling and professional looking presentations and to create effective multimedia learning products.

LiveSlideShow 3 is an easy to use product that allows customers to simply add professional transitions and dazzling effects such as music, captions and media skins to bring their digital pictures to life. LiveSlideShow 3 includes some compelling new features such as a timeline for ordering photos and multiple soundtracks. Customers can add their own voiceovers, sound effects, sound tracks and interactive elements to create the ideal presentation. With LiveSlideShow 3's background music tracks, slideshows are now a powerful presentation tool perfect for deployment on the Web, CD-ROM, or via email. Scrolling captions can easily be added to any digital picture as an added touch. LiveSlideShow includes a media skins feature that allows customers to present their slideshows inside uniquely shaped themed players.

LiveSlideShow 3 works with most of the popular digital cameras available on the market today. Because LiveSlideShow 3 utilizes the industry leading QuickTime multimedia technology from Apple Computer, it supports more digital image and sound formats than any other similar product available to consumers today on both the Macintosh and Windows platforms.

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OTHER PRODUCTS

Development on other products has been limited to minor upgrades to support new operating systems and versions of Quick Time due to limited development, marketing and sales capacity and budgets.

SELECTED FINANCIAL DATA

The following table presents selected financial information for the three months ended December 31, 2004, and the last three audited fiscal years ended September 30, 2004, 2003 and 2002:

	Three months ended December 31, 2004 \$	2004 \$	2003** \$	2002* \$
OPERATIONS:				
Revenues	48,711	257,648	485,121	685,256
Net Income (Loss)	(66,565)	(524,108)	(214,503)	(345,416)
Basic and diluted income (loss) per share	(0.01)	(0.08)	(0.03)	(0.13)
BALANCE SHEET:				
Working capital (deficiency)	(462,698)	(398,383)	(371,786)	(301,906)
Total assets	123,670	96,597	131,068	244,153

* As at September 30, 2002, management of the Company disputed certain charges. During the year ended September 30, 2003, the matter was resolved and the Company agreed to pay an additional \$41,521 interest and legal fees owing at September 30, 2002 and accordingly, restated its operations for the year then ended. (Refer to the Company's audited consolidated financial statements as at September 30, 2003);

** The Company has determined that \$12,094 of professional fees expensed during the year ended September 30, 2003 were incurred for completion of a private placement and should have been recorded as share issue costs and accordingly, has restated its operations for the year then ended. As a result, for the year ended September 30, 2003, professional fees were restated to \$188,469 from \$200,563 and the net loss was restated to \$214,503 from \$226,597. As at September 30, 2003, the deficit ending was restated to \$7,624,283 from \$7,636,377 and share capital were restated to \$6,511,584 from \$6,523,678.

For the three months ended December 31, 2004 gross revenue was \$48,711 compared to \$51,542 for the same period in 2003 (5.1% decrease). For the year ended September 30, 2004 revenues (net of packaged software) was \$257,648 compared to \$485,121 in 2003 (46% decrease). These variations in revenue are due to a number of factors some of which are not under the control of the Company and the amount of variation can not be directly attributable thus it would be misleading to attempt to define. Revenue in the Company's business/market varies due to conditions such as timing of current releases, promotion of QuickTime by Apple and the Company, new releases of QuickTime, delays in Apple's approval of Totally Hip's custom QuickTime component, cash flow constraints and employee absence. In addition the Company is exposed to a fluctuation in currency exchange, mostly U.S. dollars. Approximately 89% of the Company's total sales are sales in foreign currencies. In 2004 the average annual exchange rate for U.S. dollar posted by the Bank of Canada was approximately 10% lower than the average annual exchange rate for 2003. The average exchange rate for the quarter ended December 31, 2004 was 7.22% lower than the average exchange rate for the same period in 2003. Company sales figures presented in Canadian dollars were affected accordingly.

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The Company's net loss for the fiscal year ended September 30, 2004 was \$524,108 compared to the loss of \$214,503 in the fiscal 2003. The 2003 net loss was affected by a \$139,860 gain on the write-off of accounts payable which was also offset by a \$31,370 loss on the write-off of advances receivable and \$21,431 loss on foreign exchange with net gain of \$87,059.

RESULTS OF OPERATIONS

Current Quarter and Year-to-Date

During the three months ended December 31, 2004, Net sales/gross profit before expenses were \$48,711 as compared to \$51,542 for the comparable period in 2003.

On an overall basis the net loss for the three months ending December 31, 2004 is \$66,565 comparable to a net loss of \$66,574 for the same period in the previous year resulting in a net loss of \$0.01 per share for the current quarter compared to a loss of \$0.04 per share for the same quarter in 2003.

Administrative expenses for the three months ending December 31, 2004 were \$109,517, compared to \$104,577 in the previous year. Major expense reductions occurred in office and miscellaneous expenditures (\$4,698) and salaries and consulting fees (\$2,942), which were offset by a \$10,518 increase in professional fees, and \$2,073 in office rent. Research and development salaries of \$45,000 incurred by the Company during the quarter were at comparable level with \$45,000 incurred by the Company in the same period in 2003.

Gross profit from sales for the three months ended December 31, 2004 was \$43,022 or 88.32% of gross sales compared to a gross profit from sales of \$42,599 or 82.65% in 2003. Cost of goods sold does not include labor costs to generate sales, service or training revenue that is included in expenses under salaries and consulting fees.

Gross sales were adversely impacted by about 7% overall due to the exchange rate between the Canadian and US dollar as the majority of sales were in US dollars.

The geographical distribution of sales revenues for the quarter ended December 31, 2004 is USA 54.20%, Europe 31.74%, Canada 4.33%, Australia and New Zealand 3.48%, Asia 6.25%.

Totally Hip continues to look at avenues of increasing sales and diversifying into more services revenue.

Totally Hip continues to work on achieving a positive cash flow and streamlining operations to reduce expenditures in the year ended September 30, 2005.

SUMMARY OF QUARTERLY RESULTS

The following table presents unaudited selected financial information for each of the last eight quarters:

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	Years ended September 30,							
	<u>2005</u>	<u>2004</u>				<u>2003</u>		
	Q1	Q1	Q2	Q3	Q4	Q2	Q3	Q4
	\$	\$	\$	\$	\$	\$	\$	\$
Revenue	48,711	51,542	82,157	86,527	79,799	128,074	137,451	96,972
Net income (loss)	(66,565)	(66,574)	(97,832)	(254,594)	(105,108)	29,509	(4,108)	(217,433)
Basic/diluted loss per share	(0.01)	(0.04)	(0.03)	(0.02)	(0.01)	0.00	0.00	(0.03)

During the three months ended December 31, 2004, gross sales were \$48,711 as compared to \$51,542 for the comparable period in 2003, and the net loss was \$66,565 compared to the net loss of \$66,574 for the comparable period in 2003. The current cash flow is limiting the increase in total sales. As reflected in the above table revenues are usually high in the first quarter ending December 31, and second quarter ending March 31, corresponding with holiday seasons. Sales gradually decrease during the rest of the year. These seasonal fluctuation affect the quarterly results of operations along with other factors such as foreign currency exchange, overall market conditions, etc.

SHARE CAPITAL

Authorized:

100,000,000 common shares without par value
100,000 preferred shares without par value

Common shares issued:

		<u>Number</u>	<u>Amount</u>
Balance, September 30, 2002		6,441,874	\$ 6,388,678
Issued for cash:			
Pursuant to a private placement	– at \$0.1725	579,710	100,000
Less: share issue costs		-	(12,094)
Issued for debt settlement agreements	– at \$0.25	<u>140,000</u>	<u>35,000</u>
Balance, September 30, 2003		7,161,584	6,511,584
Consolidation of shares 4 for 1		(5,371,190)	-
Escrow shares returned to treasury		(129,998)	(127,400)
Issued for cash:			
Pursuant to a private placement	– at \$0.10	1,200,000	120,000
Pursuant to a private placement	– at \$0.05	10,000,000	500,000
Less: share issue costs		<u>-</u>	<u>(55,159)</u>
Balance, September 30, 2004 and March 1, 2005		<u>12,860,399</u>	<u>\$ 6,949,025</u>

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SHARE CAPITAL – CONT'D

Escrow:

During the year ended September 30, 2004, 129,998 (520,000 pre-consolidated) escrow shares with a cost of \$127,400 were returned to treasury and cancelled. As at September 30, 2004, and December 31, 2004, there were no shares held in escrow.

Commitments:

Share Purchase Options

Share purchase options have been granted to directors, officers and employees of the Company. The options were granted with an exercise price equal to the market price of the Company's shares on the date of the grants and fully vest when granted.

A summary of the share purchase options is as follows:

	Three months ended December 31, 2004		2003	
	<u>Number of Shares</u>	<u>Weighted Average Exercise Price</u>	<u>Number of Shares</u>	<u>Weighted Average Exercise Price</u>
Options outstanding and exercisable at the beginning and end of period	37,489	\$8.00	37,489	\$8.00

As at December 31, 2004, 37,489 share purchase options were outstanding as follows:

<u>Number of Options</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
18,750	\$5.20	February 1, 2005
4,250	\$26.00	May 12, 2005
2,700	\$11.20	November 20, 2005
11,789	\$5.20	December 27, 2005
37,489		

Subsequent to December 31, 2004, 18,750 share purchase options expired unexercised.

Share Purchase Warrants

A summary of the Company's outstanding share purchase warrants is as follows:

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SHARE CAPITAL – CONT'D

Share Purchase Warrants:

At December 31, 2004, 11,200,000 share purchase warrants were outstanding entitling the holders thereof the right to purchase one common share for each warrant held as follows:

<u>Number of Warrants</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
1,200,000	\$0.10	April 13, 2005
<u>10,000,000</u>	\$0.05	April 15, 2005
<u><u>11,200,000</u></u>		

RELATED PARTY TRANSACTIONS

The Company incurred the following transactions with a director, officers of the company and a company controlled by a director of the company:

	Three months ended December 31,	
	<u>2004</u>	<u>2003</u>
Research and development salaries	\$ 45,000	\$ 45,000
Salaries and consulting fees	<u>13,500</u>	<u>18,000</u>
	\$ <u>58,500</u>	\$ <u>63,000</u>

These transactions were measured by the exchange amount, which is the amount agreed upon by the transacting parties

At December 31, 2004 accounts receivable included \$Nil (2003: \$26,705) due from a company with a common director.

LIQUIDITY AND SOLVENCY

At December 31, 2004, the Company held cash on hand of \$12,748 (2003: \$32,160) and liabilities totalled \$562,201 (2003: \$468,563).

Totally Hip expenses its research and technology development. Accordingly Totally Hip's total assets are \$123,670 as of December 31, 2004 compared with \$131,730 as of December 31, 2003.

Totally Hip's liabilities at December 31, 2004 comprised of accounts payable and accrued liabilities totalling \$420,353, (2003: \$429,891), loans payable of \$108,094 (2003: \$Nil), and amounts due to shareholders of \$33,754 (2003: \$33,754)

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LIQUIDITY AND SOLVENCY – CONT'D

Totally Hip's ability to continue as a going concern is dependent upon its ability to generate profitable operations, sell technology assets and/or to obtain additional financing to meet its obligations and repay liabilities arising from normal business operations when they come due.

During the three months ended December 31, 2004, Totally Hip has not issued any stock options or received any proceeds from the exercise of existing stock options or warrants. Totally Hip intends to implement a stock option plan as an incentive to employees and contractors.

CRITICAL ACCOUNTING POLICIES

Management has prepared the consolidated financial statements of the Company in accordance with Canadian generally accepted accounting principles and are stated in Canadian dollars. The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The financial statements have, in management's opinion, been properly prepared using careful judgement with reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

a) Principles of Consolidation

These consolidated financial statements include the accounts of Totally Hip Technologies Inc. and its wholly-owned active subsidiary Totally Hip Software (B.C.) Inc. and its wholly-owned inactive subsidiary 614604 B.C. Ltd. All significant inter-company transactions and balances have been eliminated.

b) Revenue Recognition

Revenues are recognized when there are no significant obligations remaining, the fees are fixed and determinable, persuasive evidence of an arrangement exists and collectibility is reasonably assured. Packaged software sales sold directly to the end-user are either shipped or directly downloaded and revenues are recognized when delivered. Sales, other than packages downloaded, are subject to a one day return policy. Packaged software sales made by resellers is recognized when delivered to the end user. Revenue from consulting and training services is recognized when the services are completed.

c) Foreign Currency Translation

Monetary items denominated in a foreign currency are translated into Canadian dollars at exchange rates prevailing at the balance sheet date and non-monetary items are translated at exchange rates prevailing when the assets were acquired or obligations incurred. Foreign currency denominated revenue and expense items are translated at exchange rates prevailing at the transaction date. Gains or losses arising from the translations are included in operations.

d) Stock-based Compensation

Stock-based compensation is accounted for at fair value as determined by the Black-Scholes option pricing model using amounts that are believed to approximate the volatility of the trading price of the Company's shares, the expected lives of awards of stock-based compensation, the fair value of the Company's stock and the risk-free interest rate, as determined at the grant date. The estimated fair value of awards of stock-based compensation are charged to expense over their vesting period, with offsetting amounts recognized as contributed surplus. Upon exercise of share purchase options, the consideration paid by the option holder,

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CRITICAL ACCOUNTING POLICIES – CONT'D

together with the amount previously recognized in contributed surplus, is recorded as an increase to share capital.

e) Research and Development

The Company incurs costs on activities that relate to research and development of new products. Research costs are expensed as they are incurred. The Company has also expensed development costs incurred because the costs do not meet generally accepted criteria for deferral and amortization.

FINANCIAL INSTRUMENTS

The Company's financial instruments consist of cash, accounts receivable, accounts payable and accrued liabilities, due to shareholders and obligations under capital leases. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial statements. The fair value of these financial instruments approximates their carrying values.

- a) The Company provides credit to its clients in the normal course of operations. It carries out, on a continuing basis, credit checks on its clients and maintains provisions for contingent credit losses. For other debts, the Company estimates, on a continuing basis, the probable losses, and provides a provision for losses based on the estimated realized value.
- b) The Company is exposed to fluctuations in foreign currency through its sales to United States customers. The Company monitors this exposure, but had no hedge position at December 31, 2004 or September 30, 2004.

RISK AND UNCERTAINTIES

The Company competes with other software companies, some of which have greater financial resources and technical facilities. The Company is focused on expanding its business through the development and marketing of new products such as the LiveStage professional products. Future results will depend on the ability to successfully complete these product offerings and the resulting adoption rate of customers to implement these products into their systems.

Additional risks and uncertainties that pertain to the growth of the Company are:

Product Development and technological Change

The software industry is characterized by rapid technological change, competition and many new product introductions. The ability of the Company to continue to achieve market success and maintain its competitive advantage will depend on its capability to maintain a competent R & D staff that is current with all technological advances as it pertains to evolving computer hardware, software platforms and operating environments.

Foreign Exchange Exposure

The largest segment of the Company's client base is located in North America with 55% of revenues been generated in the United States while corresponding expenses are incurred in Canadian dollars. This means the Company is exposed to exchange rate fluctuations between the Canadian and US dollar. To date, the Company has not engaged in hedging currency risk in the commodity markets.

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OUTLOOK

In 2004 Totally Hip's plan to update LiveStage Professional and incorporate OpenGL technology has been completed on MacIntosh, and is now being updated for Windows. This will dramatically increase the speed and capability of the graphics interface of the authoring stage. Future releases building upon this foundation will be able to incorporate 3D visualization in the development of interactive media projects.

Totally Hip is developing an application for its recently developed custom wired action handler that extends the capabilities of QuickTime in principle areas of business interest: data storage and communication capabilities, file manipulation, real-time audio monitoring and display, printing, encryption and dynamic media within QuickTime VR panoramas using LiveStage Professional. Component technology enables Totally Hip to create functionality independent of QuickTime's basic wired action handler. This initial component release has the potential of opening up entirely new markets for LSP developers. The component coupled with the rising tide of QuickTime adoption widens the appeal of Totally Hip's development platform and reaffirms the continuing advancement of interactive media. Totally Hip is still waiting for Apple's approval of its QuickTime component and has been given no definitive date for approval. Totally Hip is also reviewing and developing other technology and technology based applications including working to develop a solution to deploy DVD quality video over the Internet utilizing QuickTime and LiveStage Professional technology.

Totally Hip having acquired, extensive insights and experience in the online learning area through its interactive tools and consulting business is now planning to take the technology it has developed and release it into the expanding online delivery market.

Totally Hip Technologies is developing an online learning technology that would utilize its latest online and interactive rich media technologies to produce turnkey systems that can be quickly deployed. The Totally Hip solution uses existing content in almost any format and allows the content to remain in a non-proprietary format. These systems will be targeted at small to medium sized companies and schools looking for fast economical online learning solutions incorporating DVD quality video. The Totally Hip online learning system's capabilities are designed to be expandable to grow with the clients' requirements using the modular component design.

Currently the online training and learning market is still in a development stage. Totally Hip Technologies deduces that many post high school institutions and most companies have initiated research projects with the hope of deploying their own system at some point in the future. Many companies are looking for innovative ways to utilize their existing content to educate their staff and customers online.

With many companies reducing overhead they find themselves trying to meet the challenge of today's ever shrinking budgets while finding economical, low capital learning solutions. Most of these companies and educational institutions have been looking at online solutions to help them attain their goals and are now starting to implement solutions. Trainers and educators can now make full use of the Internet or their own intranets to deploy low cost high quality learning experiences.

Online learning technology provides many advantages over traditional methods of delivery including uniformity of delivery, instantaneous updates, high availability, minimal overhead, on-demand delivery and location independence. The technology also now allows the online delivery mechanism to deliver in a DVD style and quality.

Large IT vendors such as IBM have their own proprietary systems meant for large deployments and that usually have extensive implementation and media formatting schedules. These systems are costly, require long-term commitments and usually require the content to be formatted into a proprietary format limiting future use and require ongoing technology payments. As a result, there is little available for the small to medium sized companies

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or schools who want to participate in the online learning revolution. The cost of entry capital, extended implementation schedules and long-term technology commitment are simply too high.

Totally Hip is basing this new offering on its cross platform based interactive media engine used in its award winning tools while deploying content via the widely distributed QuickTime player. QuickTime has risen to become a leading technology for the delivery and integration of DVD quality video and rich media content over the Internet and one of the most popular media players. QuickTime is also used for Apple's popular iPod portable music player available for both Windows and OS X operating systems.