



**Third Quarter Report
and Management's Discussion and Analysis**

For the Three and Nine Months Ended

November 30, 2009

February 1, 2010

ESI Entertainment Systems Inc.

1018 - 4720 Kingsway Ave

Burnaby, BC V5H 4N2

Facsimile 604-299-3984

Telephone 604-299-6922

TO OUR SHAREHOLDERS

For the Quarter Ended November 30, 2009

Dear Shareholder:

We are pleased to present our results for the third quarter ended November 30, 2009.

Revenues for the three months and nine months ended November 30, 2009 decreased 30% and 7% respectively to \$832,284 and \$2,618,546, compared to \$1,196,471 and \$2,808,153 during the comparative periods in the prior year. Net loss after tax was \$525,232 for the three months and \$1,583,032 for the nine months ended November 30, 2009, compared with net loss after tax of \$1,106,477 and \$3,965,574 in the comparative periods in the prior year.

In November 2009, Citadel was audited by FTI Consulting to provide assurance to the USA Department of Justice (DOJ) that it is adhering to the terms of the Deferred Prosecution Agreement (DPA) signed in June 2008. The final audit and report to the DOJ were completed successfully and subsequent to the end of this quarter, on December 16, 2009, the Company received a copy of the *Nolle Prosequi* filed by the US Attorney's Office, which disposed of the prosecution in its entirety. The Company had complied with all terms of the DPA without exception, and will no longer be subject to oversight by the independent Monitor that was appointed pursuant to the DPA.

In January 2010, the terms of the USD \$2 million loan obtained in June 2008 were amended so that the outstanding US\$ 2 million loan facility is no longer repayable on a fixed date; all other terms of the loan are unchanged.

The Lender's agreement to amend the terms of the Loan is indicative of their support of the Company's progress to-date, including the ongoing profitability of its wholly-owned subsidiary ESI Integrity as well as the increasing revenue stream and reduced costs of Citadel Commerce.

The Company has reviewed several offers for the purchase of ESI Integrity, but in light of the new terms for the loan has decided it will retain ownership and continue to grow its business in the regulated lottery and pari-mutuel markets.

On December 11, 2009, the Company held its AGM-SGM and all matters placed before shareholders were approved.

On December 16, 2009, ESI and Citadel moved its offices to an adjacent office tower in the same complex and ESI Integrity moved to new offices several kilometers away to complete the operational separation of the companies.

We are continuing to review the expenses and grow the revenues in the subsidiaries.

ESI Integrity has decreased its resource levels due to lower than expected third quarter revenues however it continues to be profitable and has built a strong funnel of business for 2010.

Citadel Commerce has re-structured to significantly reduce its costs while retaining a core team of individuals with the ability to function well in multiple roles and retain the experience and expertise developed by the Company.

The statements show that Citadel has not only reduced costs but is now achieving notable growth in its revenues driven mainly by the accelerating adoption of its Instant Internet Banking service. Many major merchants have signed agreements to use this service and have been integrating to the Citadel servers. Much of this work is now complete and is reflected in the growth of Citadel's revenues as the merchants begin to switch transactions to our service. Management believes that it is reasonable to expect this growth to continue.

There are now good indicators of a successful renewal and the Board and employees remain committed to bringing the Company through the final stages of the turnaround and doing everything possible to ensure a successful outcome.

"Anthony Greening"
Chairman & CEO

"Michael Meeks"
President

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management discussion and analysis ("MD&A") relates to our interim unaudited financial statements for the three and nine month periods ended November 30, 2009. The MD&A should be read in conjunction with the Company's February 28, 2009 year-end audited consolidated financial statements and related notes therein that are prepared in accordance with Canadian generally accepted accounting principles. All financial information is stated in Canadian dollars, unless otherwise stated. Additional information regarding ESI Entertainment Systems Inc ("ESI" or "the Company"), including our Annual Information Form ("AIF") and MD&A and audited consolidated financial statements for the financial year ended February 28, 2009 can be found on the System for Electronic Document Analysis and Retrieval (SEDAR) at www.sedar.com.

Forward Looking Information

This MD&A contains forward-looking statements concerning ESI Entertainment Systems Inc. which statements can be identified by the use of forward-looking terminology such as "expect", "proposed", "may", "plan", "intend", "will", "would" or the negative thereof or any other variations thereon or comparable terminology referring to future events or results. Forward-looking statements are statements about the future and are inherently uncertain, and the actual events or results could be materially different than those anticipated in those forward-looking statements as a result of numerous factors discussed more fully in this document. These risks include risks related to revenue growth, operating results, industry growth, changes in regulation and legislation, products, technology, financing, competition, personnel and other factors affecting the Company and its business, any of which could cause actual events or results to vary materially from ESI's anticipated future results. Forward-looking statements are based on beliefs, opinions and expectations of ESI's management at the time they are made, and ESI does not assume any obligation to update its forward-looking statements if those beliefs, opinions or expectations, or other circumstances should change. Investors are expected to refer to the "Risks & Uncertainties" section of this MD&A for a discussion of risk factors that could affect the Company's performance.

Business Overview

The Company has two independently operated and controlled subsidiaries: Citadel Commerce Corp. and ESI Integrity Inc. A third subsidiary, PlayLine Inc., is presently dormant. The two active subsidiaries are located in separate physical locations and operated autonomously with completely separate management, personnel and infrastructure.

ESI has approximately 14 Citadel employees and 15 Integrity employees located in Burnaby, British Columbia, Canada from where each company markets its products and services globally.

ESI Integrity provides software solutions for real-time auditing of transaction processing systems to businesses requiring high levels of security, integrity, and trust, including government regulated lotteries and pari-mutuel (horse tracks) betting.

Citadel provides on-line payment processing services including Bank Transfer, Instant Credit (an instant form of Bank Transfer), electronic cheques and paper cheques. Transactions are processed with concurrent transactional fraud detection services including full identity pre-authorization via in-house and third party databases and validation of previous transaction history.

A detailed overview of ESI's business, including a summary of our core business, vision and strategy is provided in our MD&A and AIF for the financial year ended February 28, 2009.

Critical Accounting Policies and Estimates

The Company's accounting policies are outlined in Note 2 of the audited consolidated financial statements for the year ended February 28, 2009.

Additionally, the preparation of the consolidated financial statements in conformity with Canadian Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses for the period. Actual results could differ from these estimates.

Basis of consolidation and financial statement preparation

The unaudited interim Consolidated Financial Statements dated November 30, 2009, have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP) on a basis consistent with those followed in the most recent audited annual financial statements for the year ended February 28, 2009. The unaudited interim Consolidated Financial Statements do not include all note disclosures required by GAAP for annual consolidated financial statements. Accordingly, these statements should be read in conjunction with the Company's annual audited financial statements for the year ended February 28, 2009.

Financial Highlights for the Three and Nine Months ended November, 2009

The highlights for ESI, on a consolidated basis, compared to the same period last year, are:

- Revenue for the three months to November 30, 2009, decreased from \$1,196,471 to \$832,284, 30% decrease over the comparative period in the prior year;
- Revenue for the nine months to November 30, 2009 decreased from \$2,808,153 to \$2,618,546, 7% decrease over the comparative period in the prior year;
- Gross profit for the three months to November 30, 2009 decreased from \$619,634 to \$198,591, 68% decrease over the comparative period in the prior year;
- Gross profit for the nine months to November 30, 2009, decreased from \$721,754 to \$713,327, 1% decrease over the comparative period in the prior year;
- Net loss for the three months to November 30, 2009 decreased by 53% to \$525,232 from \$1,106,477 in the comparative period in the prior year;
- Net loss for the nine months to November 30, 2009 decreased by 60% to \$1,583,032 from \$3,965,574 in the comparative period in the prior year;

Results of Operations

Consolidated Revenues

The following table provides a breakdown of the Company's revenues from its subsidiaries for the reported periods:

(\$ 000)	Three months ended November 30			Nine months ended November 30		
	2009	2008	% Change	2009	2008	% Change
Integrity	546	1,022	(47%)	1,832	2,388	(23%)
Citadel	286	174	64%	786	420	87%
Total Revenue	832	1,196	(30%)	2,618	2,808	(7%)

Approximately 65% of ESI's revenues were generated by ESI Integrity during the three months ended November 30, 2009 compared to 85% for the same period in the prior year.

Total revenue decreased by 30% to \$832,284 for the three months ended November 30, 2009 from \$1,196,471 for the three months ended November 30, 2008.

Integrity Revenues

ESI Integrity provides software solutions for real-time auditing of transaction processing systems to businesses requiring high levels of security, integrity, and trust, including government regulated lotteries and pari-mutuel (horse tracks) betting.

Integrity Revenues are generated from long term customer license and support contracts where it charges a fixed license fee for the use of its audit and risk management software, as well as an annual support fee. Revenue is typically earned over a two to five year period, depending on a contract's respective term.

Citadel Revenues

Citadel revenues are generated from its on-line payment processing which include electronic cheques and paper cheques but its main focus is its two online banking services: Bank Transfer, and Instant Credit (an instant form of Bank Transfer). All of Citadel's services are based on a fee per transaction charged to its merchants.

Consolidated Gross Profit

The following table provides a summary of the Company's gross profit for the reported periods:

(\$ 000)	Three months ended Nov 30		Nine months ended Nov 30	
	2009	2008	2009	2008
Revenues	832	1,196	2,618	2,808
Direct Costs	634	577	1,905	2,086
Gross profit	198	619	713	722
Gross profit margin (%)	24%	52%	27%	26%

Product Development

Product development expenses were \$56,794 and \$179,682 during the three and nine months ended November 30, 2009 respectively, a decrease of 5% and 33% respectively compared to \$59,986 and \$267,764 for the three and nine months ended November 30, 2008.

Sales, Marketing and Customer Service

Sales, marketing and customer service expenses were \$39,423 and \$117,702 during the three and nine months ended November 30, 2009 respectively, a decrease of 78% and 82% respectively compared to \$181,946 and \$658,789 for the three and nine months ended November 30, 2008.

General and Administrative

General and administrative expenses were \$699,865 and \$1,970,403 during the three and nine months ended November 30, 2009 respectively, representing a decrease of 29% and 33% respectively compared to \$985,757 and \$2,957,975 for the three months and nine months ended November 30, 2008.

Amortization of Property and Equipment

Amortization expenses were \$28,710 and \$160,212 during the three month and nine month periods ended November 30, 2009 respectively, a decrease of 66% and 58% respectively compared to \$85,186 and \$379,313 for the corresponding periods ended November 30, 2008. The decrease in amortization expense mainly relates to very few new assets being purchased and amortization being reduced on older equipment.

Net Loss

Net loss for the three and nine month periods ended November 30, 2009 was \$525,232 (\$0.04 net loss per share) and \$1,583,032 (\$0.11 net loss per share), respectively, compared to net loss of \$1,106,477 (\$0.07 net loss per share) and \$3,965,574 (\$0.28 net loss per share) for the prior comparative periods.

The decrease in all expense categories and Net Loss is due to the Company's ongoing efforts to minimize its operating expenses.

Citadel Processing Accounts and Liabilities

Citadel processing accounts as at November 30, 2009 totaled \$8.2 million compared to \$2.9 million as at February 28, 2009. These accounts are comprised of cash, which are segregated bank funds arising from the processing of deposits and payments for Citadel merchants and consumers, and accounts receivable relating to Citadel processing accounts for funds in transit from merchants and consumers.

Summary of Quarterly Results

The following Table sets out comparative information in respect of the past eight Quarters to November 30, 2009 derived from unaudited statements prepared by Management.

<i>(\$000)</i> <i>except for per share data</i>	30-Nov	31-Aug	31-May	28-Feb	30-Nov	31-Aug	31-May	29-Feb
	2009	2009	2009	2009	2008	2008	2008	2008
Consolidated Revenue	832	952	834	1,147	1,196	742	869	1,029
Consolidated Gross Profit	198	355	160	251	619	(60)	161	145
% of revenues	24%	37%	19%	22%	52%	-8%	19%	14%
Total Operating Expenses	825	752	851	1,297	1,313	1,474	1,476	2,042
% of revenues	99%	78%	102%	113%	110%	198%	170%	198%
Consolidated Net Income (Loss)	(525)	(535)	(522)	(1,103)	(1,106)	(1,547)	(1,312)	225
% of revenues	-63%	-56%	-63%	-96%	-92%	-208%	-151%	22%
Earnings (Loss) per share								
Basic	(\$0.04)	(\$0.04)	(\$0.04)	(\$0.09)	(\$0.07)	(\$0.08)	(\$0.07)	(\$0.02)

Liquidity and Capital Resources

ESI has historically financed its operations through the sale of equity and through cash generated by its operations.

During the three month period ended November 30, 2009, cash provided in operating activities was \$32,262 and during the nine months ended November 30, 2009, cash used in operating activities was \$366,006, compared to cash used in operating activities of \$1,062,935 and \$4,429,792 during the comparative periods ended November 30, 2008, respectively.

Cash used in financing activities totaled \$51,987 and \$433,752 during the three months and nine months ended November 30, 2009 respectively. These activities related to the funding of capital lease obligations and to the loan payable.

Certain employees have voluntarily deferred part of their compensation. The unpaid deferred amounts are being accrued with interest and are recorded in the Company's financial statements. The salary deferrals are payable upon termination or when the Company's economic conditions have strengthened to accommodate for the repayment. As at November 30, 2009, the total amount of the deferred salaries is \$765,686.

As at November 30, 2009, the Company had cash and cash equivalents of \$105,544, compared to \$887,278 on November 30, 2008.

For the three month period ending November 30, 2009 the Company incurred a loss from operations of \$525,232 with a decrease of operating cash flow of \$29,410. In addition, the Company has incurred significant operating losses and net utilization of cash in operations in all prior periods. Accordingly, the Company will require continued financial support from its shareholders and creditors and/or new debt or equity financing until it is able to generate sufficient cash flow from operations on a sustained basis.

Contingent Off-Balance Sheet Arrangements

The Company did not have any contingent off-balance sheet arrangements during the three month or nine month period ending November 30, 2009. (November 30, 2008 – nil)

Outstanding Share Data

ESI's outstanding share data is listed in the table below as at the dates indicated:

	Nov 30/09	Nov 30/08	Date of this Report
Weighted average shares used in computation of basic earnings per share	14,324,726	14,324,726	14,324,726

During the three month period ended November 30, 2009, 145,000 stock options were granted and a total of 82,000 were forfeited or expired unexercised. (November 30, 2008, nil and 169,500 respectively).

As at November 30, 2009, and at the date of these unaudited financial statements, there were 2,000,000 options outstanding, (November 30, 2008 – 1,417,500) exercisable at a Weighted Average Price of \$0.60. (November 30, 2008 - \$0.64).

Disclosures, Controls and Procedures

The Company maintains a set of disclosure controls and procedures designed to ensure that information required to be disclosed in filings made pursuant to Multilateral Instrument 52-109 is recorded, processed, summarized and reported within the time periods specified in the Canadian Securities Administrators rules and forms. During the three month and nine months ended November 30, 2009, the Company did not make any changes to its internal control over financial reporting that would have materially affected, or would likely materially affect, such controls. The Chief Executive Officer and Chief Financial Officer have evaluated the Company's disclosure controls and procedures as of November 30, 2009 and concluded that the Company's current disclosure controls and procedures are effective.

Risks & Uncertainties

A detailed explanation of risk factors which ESI faces is provided in its Annual Information Form listed on www.sedar.com. Although not exhaustive, the following list summarizes some of the key risks the Company faces, as well as, strategies the Company employs to manage these risks:

Market, Operating and Competitive Risks

The market opportunity for ESI's products is dependent upon external factors such as the continued growth in the use of the Internet, the growth of consumers' disposable income, consumer interest in gaming and regulatory and legislative matters. As well, the Company has larger competitors who have larger customer bases and more significant financial and operating resources, which may make it more difficult for ESI to compete in the marketplace. Additionally, ESI also has fewer customers for Citadel business since cessation of the financial processing business for non-domestic internet gaming merchants. If ESI were not able to grow its customer base, ESI's business would be materially negatively impacted. To manage this risk, ESI has invested significant resources in product development, sales, marketing and customer service to ensure that it delivers products and services that are competitive and valuable to its customers and that are attractive to potential new customers. It also mitigates some of the market risk by aiming at a diversified customer base in different markets.

Technology Risks

ESI has invested significant resources in its products to ensure that they provide customers with a competitive offering relative to other suppliers in its industry. If ESI has not protected its intellectual property adequately or if it infringes third party intellectual property rights, it may lose its competitive advantage and incur significant costs and loss of reputation that could materially negatively impact its business. To manage this risk, ESI has invested significant resources in product development and professional assistance to protect its intellectual property and avoid to the extent possible infringement of third party intellectual property rights.

Financial Risk

ESI is undertaking an expansion strategy to new markets and new geography. This strategy requires significant capital to achieve its long term strategic plan. If the Company is unable fund its strategic plan through operating cash flow, debt and equity financing, its future prospects would be materially negatively impacted. In order to mitigate this risk, the Company has employed a disciplined budgeting approach to manage its expenditures relative to the achievement of its strategic plan so that appropriate measures can be put in place to reduce the Company's exposure to financial risk.

Regulatory Risk

The Company is subject to anti-money laundering (“AML”) legislation in jurisdictions in which it operates or has operated in. Management has implemented controls and procedures that it believes makes the Company compliant with all applicable AML rules and regulations. It is possible that regulatory authorities may audit the Company systems and processes and assess monetary penalties for non-compliance which could be material.

Foreign currency risk

A significant component of the Company's transactions, particularly revenues, is undertaken in US dollars, Euros, and other foreign currencies. The Company maintains significant deposits in foreign currencies denominated accounts. Fluctuations in exchange rates between those foreign currencies could have a material effect on the business, results of operations and financial condition of the Company. The Company does not use hedging instruments to manage its exposure to foreign currency exchange risk.

Key Personnel Risk

The future success of ESI is heavily dependent upon the Company's ability to retain, recruit and train senior management, technical, sales and managerial personnel. Competition for qualified employees is intense and it may be possible that the Company is unable to retain and recruit qualified personnel in the future. If this were to occur, this would have a material negative impact on the Company. To manage this risk, the Company has implemented employee training programs, recognition programs and competitive compensation.

For further information please refer to the unaudited financial statements for the nine months ending November 30, 2009, the audited year end financial statements as at February 28, 2009 and February 29, 2008, the Management's Discussion and Analysis as at February 28, 2009 and the Annual Information Form for February 28, 2009. All information presented here is filed by the company on SEDAR, (System for Electronic Document Analysis and Retrieval) and can be viewed at www.sedar.com.

Dated February 1, 2010.