



Trusted Software for Gaming

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News Release

For Immediate Release June 17, 2007

ESI Entertainment announces Fiscal 2008 Financial Results

BURNABY, B.C. June 17, 2008 - ESI Entertainment Systems Inc. ("ESI" or the "Company") (TSX: ESY) reported today its financial and operational results for the fiscal year ended February 29, 2008 ("fiscal 2008"). All amounts are in Canadian dollars unless otherwise stated.

Fiscal 2008 Financial Highlights

The highlights for ESI, on a consolidated basis, are:

- 85% decrease in consolidated revenues to \$3.25 million for fiscal 2008 from \$22.0 million for fiscal 2007;
- 96% decrease in consolidated gross profit to \$0.5 million for fiscal 2008 from \$13.5 million for fiscal 2007
- 44% increase in consolidated net loss before income taxes and non-controlling interest to a loss of \$7.2 million for fiscal 2008 from a loss of \$5.0 million for fiscal 2007.

ESI's revenues, which had increased during fiscal 2006 and 2007, were reduced significantly during fiscal 2008 consequent upon the cessation by Citadel of financial processing to the non-domestic internet gaming merchants for US based consumers. As of January 17, 2007, the Company ceased its financial processing business for non-domestic internet gaming merchants for US consumers. This has had a significant material impact on the revenues for Citadel in fiscal 2008, since 97% of the revenues generated by Citadel were from that market place. Revenues from ESI Integrity, although substantially smaller than those of Citadel in prior years, have continued to grow over the past three years. This is due to increased sales and marketing efforts and the stronger recognition of the ESI Integrity brand as the number of installations with government lotteries and pari-mutuel organizations has grown on a worldwide basis.

Consolidated gross profit which had increased steadily during fiscal 2006 and 2007 due to the growth of ESI's revenue base in its Citadel division, was reduced from \$13.5 million for fiscal 2007 to \$518,000 for fiscal 2008. This decrease was a direct result of cessation of financial processing for non-domestic internet gaming merchants for US consumers. Gross profit for ESI Integrity during fiscal 2008 increased from \$686,035 in fiscal 2007 to \$1.027 million in fiscal 2008, reflecting continued growth in that division.

During fiscal 2008 operating costs were impacted significantly by severances, contraction of rented premises, new product development and consequential marketing costs aimed into new markets. Additionally, the Company's costs were impacted during fiscal 2008 by the legal and auditing costs associated with negotiations with the Office of the United States District Attorney for the Southern District of New York ("USDA") in relation to the investigations being carried out by the Department of Justice ("DoJ") into internet gaming merchants.

Fiscal 2008 Business Highlights

Fiscal 2008 was a year for development of new business opportunities for Citadel Commerce Corp. by seeking out and developing applications for the Company's financial processing platform technology in new market segments as well as continuing to build the business base of ESI Integrity. In particular this has resulted in very limited growth in the provision of financial processing services to internet based gaming merchants in countries outside the USA and initial marketing of financial processing services to non-gaming related markets. Business highlights of the year include:

- Development and launch of the Citadel Rapid Bank transfer and Instant Bank transfer services, which are able to confirm bank transfers into merchants' accounts;
- Increase of the customer base and profitability of ESI Integrity;
- Establishment of many new business contacts in the worldwide marketplace for financial processing for internet-based merchants in non-iGaming business sectors;

In other respects, much of Management's time during fiscal 2008 was devoted to continuing negotiations with the DoJ which led, in early June, 2008, to resolution of the issues by entering into a Deferred Prosecution Agreement ("DPA") with the USDA, which was approved and ratified by the Court in New York in early June, 2008. Now that this negotiation has been completed Management will be able to devote all of its energies to building increased business on the Company's advanced technologies and resources.

Fiscal 2008 Financial Review

Consolidated Revenues

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

(\$ 000)	Year ended		% change
	Feb 29 2008	Feb 28 2007	
Citadel	875	19,976	(96%)
Integrity	2,373	2,036	17%
Other	-	11	(100%)
Total revenue	3,248	22,023	(85%)

Total revenue decreased by 85% to \$3,248 million in fiscal 2008 from \$22.0 million in fiscal 2007. This decrease was entirely due to the decrease in Citadel revenues consequent on the cessation of financial processing for non-domestic based internet gaming merchants for US consumers.

ESI Integrity revenues increased by 17% in fiscal 2008. The increase in ESI Integrity revenues was derived from continuing increasing sales within that division.

Consolidated Gross Profit

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

(\$ 000)	Year ended	
	February 29, 2008	February 28, 2007
Revenues	3,248	22,023
Direct costs	2,730	8,479
Gross profit	518	13,544
Gross profit margin	16%	61%

The decrease in gross profit margin in fiscal 2008 was due to the costs incurred in connection with the cessation of financial processing to internet based gaming merchants in the Citadel division, which resulted in costs being incurred in staff severance, rented premises reduction and legal and accounting costs, as well as the costs associated with development of new products and exploitation of new markets for the company's products and services

The gross profit margin by dollar and as a percentage of revenues for each subsidiary is listed below:

(\$ 000)	Year ended	
	February 29, 2008	February 28, 2007
	<u>GP%</u>	<u>GP%</u>
Citadel	(509) (58%)	12,853 64%
Integrity	1,027 43%	686 43%
Other	- -	5 45%
Total gross profit	518 16%	13,544 61%

Citadel's gross profit margin during fiscal 2008 was (58%), compared to 64% for the prior fiscal year, reflecting the significant change to its business consequent upon the cessation of financial processing for non-domestic internet based gaming merchants for US consumers. Integrity's gross profit increased by 43% over the prior fiscal period, reflecting increased business in that division.

Product Development

Product development expenses were \$1.24 million in fiscal 2008, a decrease of 1% compared to \$1.25 million for the prior period. These expenditures are principally related to software development since the Company no longer capitalizes those costs.

Sales, Marketing and Customer Service

Sales, marketing and customer service expenses were \$1.67 million for fiscal 2008, a decrease of 47% compared to \$3.16 million for the prior period. The decrease primarily related to the contraction of Citadel's sales and marketing forces, reduced travel, and reduction of marketing activities relating to trade shows and promotional activities.

General and Administrative

General and administrative expenses were \$5.41 million for fiscal 2008, a decrease of 29% compared to \$7.64 million for the prior period. This decrease resulted from reductions in the financial, human resources and information systems departments to manage the decreased activity within the Citadel division in particular. In addition, ESI contracted its rental space, but incurred additional professional fees and other general corporate expenses in fiscal 2008 consequent on the cessation of the financial processing business for non-domestic internet gaming merchants for US consumers. The Company had recorded a provision for bad debts totaling \$0.8 million for fiscal 2007, but this provision was retrospectively cancelled during fiscal 2008 related to actions taken by the DoJ against the on-line gaming payment processing industry in the U.S.

Included in general and administrative expenses was non-cash stock compensation expense of approximately \$423,588 for fiscal 2008, compared to approximately \$272,874 for fiscal 2007. Stock compensation expense increased during fiscal 2008 as a result of additional stock grants to the Company's employee base, reflecting agreement by employees to forego salary reviews and, in certain cases, accepting salary deferrals.

Amortization of Property and Equipment

Amortization expenses were \$776,706 for fiscal 2008, a decrease of 13% compared to \$887,783 for the prior period. The decrease is accounted for by the cut back in purchases of computer hardware and software, furniture and fixtures and leasehold improvements, consequent on the contraction of the Company's employee base.

Provision for Income Taxes

Provision for income tax expense was \$27,243 for fiscal 2008 compared to \$46,550 for the prior period. This decrease resulted from a net loss before income taxes in fiscal 2008, and other factors including adjustments made to reflect non-deductible expenses and losses as well as non-capital losses which have expired compared to net earnings before income taxes in fiscal 2006.

Net (loss) Earnings

Net loss for fiscal 2008 was \$7.2 million (\$0.42 loss per share – basic and diluted) compared to net loss of \$5.0 million (\$0.27 earnings per share- basic and diluted) for fiscal 2007. This decrease was largely driven by the costs incurred consequent upon the cessation of financial processing for non-domestic internet based gaming merchants for US customers, and the reductions in staffing and rented premises as well as the legal and auditing costs associated with the significant reduction of that portion of the Company's business.

Capital Expenditures

Capital expenditures for fiscal 2008 were \$103,811 compared to \$506,914 for fiscal 2007. The decrease in capital expenditures was primarily the result of reductions in acquisitions and consolidation of operations consequent upon the cessation of financial processing for non-domestic internet based gaming merchants for US based consumers in the Citadel division.

Deferred Start-Up Costs

The Company established PlayLine early in fiscal 2006 and the myCitadel division in fiscal 2004. Direct costs associated with the start up of these operations were being deferred until each commenced commercial operations, at which time the accumulated start up costs were to be amortized over a period not to exceed five years. Direct costs associated with the start up of the business operations for myCitadel and PlayLine were deferred until November 30, 2006, at which time the accumulated start up costs were reviewed in light of the passing of the UIGEA on October 13, 2006. During fiscal 2007, sales, marketing, business development and other direct expenses in the amount of \$185,787 and \$1.1 million were capitalized for PlayLine and myCitadel, respectively. Before the impairment of the asset, as at November 30, 2006, Start-up Costs for PlayLine

totalled \$813,698 and \$3,115,148 for myCitadel. With the enactment of the UIGEA, its impact on Citadel's market and the redeployment of resources from Playline to Citadel, management reassessed the carrying value of Deferred Start-up Costs. Management determined that the passing of the UIGEA and the redeployment of resources from Playline to Citadel would likely lead to reduced future revenue streams in the Citadel division. In fiscal 2007, Management took the view that the Company could no longer reasonably expect to recover the accumulated capitalized start up costs and hence wrote them off in that fiscal year. From the beginning of fiscal 2008 the Company has expensed and will recognize any revenues in future periods as these items occur.

Capitalized Development Costs

The Company had capitalized certain computer software production costs for PlayLine and myCitadel. Amortization of the software development costs would have commenced on reaching commercial operations using the straight line method over the useful life of the software. During fiscal 2007, software expenses in the amount of \$253,768 and \$354,024 were capitalized for PlayLine and myCitadel, respectively. Before the impairment of the asset, as at November 30, 2006, capitalized development costs for PlayLine totaled \$610,001 and \$1,266,415 for myCitadel.

As with Deferred Start-up Costs, with the enactment of the UIGEA, the redeployment of resources from Playline to Citadel, and its impact on Citadel's market, management reassessed the carrying value of Capitalized Development Costs in fiscal 2007 and determined that the passing of the UIGEA and the redeployment of resources from Playline to Citadel would lead to reduced future revenue streams in the Citadel division. Accordingly, Management determined that the Company could no longer reasonably expect to recover the accumulated capitalized development costs and hence wrote them off in fiscal 2007.

Citadel Processing Accounts and Liabilities

Citadel processing accounts as at February 29, 2008 totaled \$1.5 million compared to \$16.8 million as at February 28, 2007. The accounts are comprised of restricted 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. The processing account balances are also recorded as a liability because these funds represent amounts due to consumers and merchants. The decline in Citadel processing accounts and Citadel processing liabilities is due to cessation of the financial processing business for non-domestic internet gaming merchants for US consumers during fiscal 2007. The Company had also recorded a provision of allowance for bad debts totaling \$0.8 million for Citadel processing accounts due to the uncertainty created by actions taken by the DoJ against the on-line gaming payment processing industry in the U.S., but since this issue was clarified during fiscal 2008, the provision in 2007 was retrospectively reversed.

During fiscal 2008 approximately US\$ 9.1 million of funds which had been on deposit in the USA, principally Merchant funds, were seized by the DoJ. Throughout fiscal 2008 the Company was engaged in negotiations with the DoJ and the USDA; subsequent to the end of fiscal 2008 a resolution was reached with the USDA.

Liquidity and Capital Resources

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

During fiscal 2008, cash used in operating activities was (\$7.05) million compared to cash provided by operating activities of \$2.6 million during fiscal 2007, a decrease of \$ 9.65 million from the prior period. Non-cash operating items in fiscal 2008 were lower than in fiscal 2007, principally as a result of less provision being taken for assets written off.

Cash provided by investing activities totaled \$997,092 during fiscal 2008 compared to cash used in investing activities of (\$3.1) million during fiscal 2007. This difference is accounted for

principally by re-allocation of restricted cash, in the amount of \$1,100,903, and reduced costs of property and equipment acquisitions, at \$103,811 in fiscal 2008 compared to \$362,644 in fiscal 2007.

Cash used in financing activities totaled \$361,588 during fiscal 2008 compared to cash provided by financing activities on \$7,488,883 in fiscal 2007. The financing activities in fiscal 2007 included the Company's IPO which raised \$8.9 million.

Overall, the net cash used in fiscal 2008 was \$6.4 million compared to cash provided of \$7 million in fiscal 2007.

Consolidated Financial Statements

NOTE TO READER: The following financial statements are extracted from the complete audited financial statements of the Company which have been filed together with the Management's Discussion and Analysis and Annual Information Form with the Company's documents on www.sedar.com to which the reader is referred.

Consolidated Balance Sheets
(expressed in Canadian dollars)

Years Ended	February 29 2008	February 28, 2007
Assets		
Current		
Cash and cash equivalents	\$ 3,042,463	\$ 9,453,701
Accounts receivable	1,111,215	558,291
Prepays	444,575	472,910
	4,598,253	10,484,902
Restricted cash	-	1,100,903
Citadel processing accounts	1,219,205	16,075,768
Property and equipment	718,869	1,391,764
Deferred contract costs	1,116,461	502,596
	\$ 7,652,788	\$ 29,555,933
Liabilities		
Current		
Accounts payable and accrued liabilities	\$ 820,492	\$ 1,237,547
Capital lease obligations	214,715	348,671
Software license obligation	-	9,917
Deferred revenue	706,773	539,198
	1,741,980	2,135,333
Citadel processing liabilities	1,530,705	16,883,268
Deferred revenue	1,923,472	1,080,247
Capital lease obligations	30,684	245,399
	5,226,841	20,344,247
Shareholders' Equity		
Capital stock	9,957,959	13,226,702
Warrants	5,926	84,634
Contributed surplus	4,092,247	330,134
Deficit	(11,630,185)	(4,429,784)
	2,425,947	9,211,686
	\$ 7,652,788	\$ 29,555,933

Consolidated Statements of Operations and Comprehensive Income (Deficit) and Retained Earnings

(expressed in Canadian dollars)

Years Ended	February 29, 2008	February 28, 2007
Revenues	\$ 3,248,630	\$ 22,023,110
Direct costs	<u>2,730,208</u>	<u>8,478,676</u>
Gross profit	<u>518,422</u>	<u>13,544,434</u>
Operating expenses		
Product development	1,241,378	1,250,584
Sales, marketing and customer service	1,671,003	3,164,733
General and administrative	5,410,952	7,639,875
Amortization of property and equipment	776,706	887,783
Cost recovery	<u>(2,055,430)</u>	<u>-</u>
	<u>7,044,609</u>	<u>12,942,975</u>
(Loss) earnings before under noted items	(6,526,187)	601,459
Other expenses (income)		
Impairment of intangibles and other assets	57,192	6,211,465
Foreign exchange loss (gain)	837,685	(272,973)
Interest income	(297,751)	(527,564)
Interest expense	<u>49,845</u>	<u>134,822</u>
Loss before income taxes	<u>(7,173,158)</u>	<u>(4,944,291)</u>
Provision for income taxes	<u>27,243</u>	<u>46,550</u>
Net loss and comprehensive loss	<u>\$ (7,200,401)</u>	<u>\$ (4,990,841)</u>
Loss per share		
Basic and diluted	\$ (0.42)	\$ (0.27)
(Deficit) retained earnings, beginning of year	\$ (4,429,784)	\$ 561,057
Net loss	<u>(7,200,401)</u>	<u>(4,990,841)</u>
Deficit, end of year	<u>\$ (11,630,185)</u>	<u>\$ (4,429,784)</u>

Consolidated Statements of Cash Flows

(expressed in Canadian dollars)

Years Ended	February 29, 2008	February 28, 2007
Cash flows provided by (used in)		
Operating activities		
Net loss	\$ (7,200,401)	\$ (4,990,841)
Items not affecting cash:		
Stock-based compensation	423,588	272,874
Amortization of property and equipment	776,706	887,783
Impairment of intangibles and other assets	57,192	6,211,465
Net changes in non-cash operating items		
Accounts receivable	(460,152)	159,033
Inventory	-	(205,250)
Prepays	(65,047)	13,072
Accounts payable and accrued liabilities	(479,564)	(976,240)
Allowance for bad debts	(496,000)	807,500
Deferred revenue	1,010,801	367,311
Deferred contract costs	(613,865)	35,226
	<u>(7,046,742)</u>	<u>2,581,933</u>
Investing activities		
Restricted cash	1,100,903	(1,100,903)
Acquisition of property and equipment	(103,811)	(362,644)
Deferred start up cost	-	(1,253,151)
Capitalized development cost	-	(398,685)
	<u>997,092</u>	<u>(3,115,383)</u>
Financing activities		
Capital lease payments	(348,671)	(294,889)
Software license obligation	(9,917)	(109,616)
Cancellation of common share costs	(3,000)	-
Issuance of common shares	-	8,893,388
Loan payable	-	(1,000,000)
	<u>(361,588)</u>	<u>7,488,883</u>
(Decrease) Increase in cash and cash equivalents	(6,411,238)	6,955,433
Cash and cash equivalents, beginning of year	<u>9,453,701</u>	<u>2,498,268</u>
Cash and cash equivalents, end of year	<u>\$ 3,042,463</u>	<u>\$ 9,453,701</u>

Consolidated Statements of Cash Flows (Continued)

(expressed in Canadian dollars)

Years Ended	February 29 2008	February 28 2007
Non-cash investing and financing transactions not included in cash flows		
Cancellation of common shares	\$ 3,341,525	\$ -
Fair value of expired Agent's warrants	\$ 78,708	\$ -
Conversion of preferred shares into common shares	\$ -	\$ 2,706,941
Share issue costs incurred in prior fiscal year	\$ -	\$ 936,987
Future income tax on share issue costs	\$ -	\$ 258,000
Fair value of options exercised	\$ -	\$ 519
Agents' warrants included in share costs	\$ -	\$ 78,708
Purchase of property and equipment funded by obligations under capital lease	\$ -	\$ 144,270
Cash and cash equivalents comprises		
Cash	\$ 3,042,354	\$ 4,943,585
Cash equivalents	109	4,510,116
	<u>\$ 3,042,463</u>	<u>\$ 9,453,701</u>
Supplemental information		
Interest received	\$ 71,977	\$ 527,535
Interest paid	\$ 25,432	\$ 134,822
Income taxes paid	\$ 27,243	\$ 57,109

Forward- looking Statements

This news release 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. 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. The Toronto Stock Exchange does not accept responsibility for this press release.

About ESI Entertainment Systems Inc.

ESI Entertainment Systems Inc. ("ESI") (TSX: ESY) provides products and services to the international gaming and e-commerce industries through its three principal subsidiaries, Citadel Commerce Corp., ESI Integrity Inc. and PlayLine Inc. ESI's products and services, which primarily consist of payment processing, transaction monitoring and turnkey gaming platforms, are deployed in the online and land based gaming and e-commerce markets.

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