

Consolidated Financial Statements

Coastal Contacts Inc.

October 31, 2006 and 2005

AUDITORS' REPORT

To the Shareholders of
Coastal Contacts Inc.

We have audited the consolidated balance sheets of **Coastal Contacts Inc.** as at October 31, 2006 and 2005 and the consolidated statements of income (loss) and retained earnings (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 October 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Vancouver, Canada,
January 24, 2007.

Chartered Accountants

Coastal Contacts Inc.

CONSOLIDATED BALANCE SHEETS

As at October 31

	2006 \$	2005 \$
ASSETS		
Current		
Cash and cash equivalents <i>[note 3]</i>	24,272,912	13,609,739
Accounts receivable <i>[note 4]</i>	7,126,537	4,809,216
Income taxes receivable	—	3,598
Inventory	12,262,134	7,020,637
Prepaid expenses	701,970	949,662
Due from related parties <i>[note 16]</i>	610,359	322,250
	44,973,912	26,715,102
Property, equipment and leasehold improvements <i>[note 8]</i>	2,773,274	1,446,029
Intangible assets <i>[note 9]</i>	13,631,468	5,466,712
Goodwill <i>[note 10]</i>	6,697,221	5,479,147
	68,075,875	39,106,990
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Bank indebtedness	—	328,157
Accounts payable and accrued liabilities <i>[note 4]</i>	11,866,546	10,259,818
Income taxes payable	211,779	308,447
Deferred revenue	205,457	77,502
Current portion of lease inducement	26,333	24,337
Current portion of long-term debt <i>[note 11]</i>	—	379,257
	12,310,115	11,377,518
Long-term lease inducement	86,209	114,177
Future income tax liability <i>[note 15]</i>	4,226,504	1,646,676
	16,622,828	13,138,371
Commitments and contingent liabilities <i>[note 18 and note 19]</i>		
Share capital and deficit		
Share capital <i>[note 12]</i>		
Authorized:		
Unlimited common shares without par value		
Unlimited Class A preferred shares without par value		
Issued and outstanding:		
74,681,712 common shares [2005 – 51,632,951]	53,515,222	26,263,656
Shares held in Treasury		
42,700 common shares [2005 – nil]	(41,005)	—
Contributed surplus <i>[note 13]</i>	530,417	593,083
Cumulative foreign currency translation adjustment	(2,135,856)	(1,808,808)
Retained earnings (deficit)	(415,731)	920,688
	51,453,047	25,968,619
	68,075,875	39,106,990

See accompanying notes

On behalf of the Board:

Roger V. Hardy

Murray McBride

Director

Director

Coastal Contacts Inc.

**CONSOLIDATED STATEMENTS OF INCOME (LOSS)
AND RETAINED EARNINGS (DEFICIT)**

Years ended October 31

	2006	2005
	\$	\$
Sales	81,013,951	67,527,885
Cost of sales	60,708,922	49,663,779
Gross profit	20,305,029	17,864,106
Selling, general and administration expenses	20,837,063	14,077,713
Stock-based compensation	268,470	175,632
Amortization on property, equipment and leasehold improvements	552,651	230,056
Amortization on intangible assets	758,178	602,775
Foreign exchange losses (gains)	(836,419)	408,893
Interest on long-term debt	42,973	99,001
Interest income	(932,685)	(206,930)
Income (loss) before income taxes	(385,202)	2,476,966
Income tax expense - current <i>[note 15]</i>	579,840	474,596
Income tax expense (recovery) - future <i>[note 15]</i>	371,377	(93,703)
Net income (loss)	(1,336,419)	2,096,073
Retained earnings (deficit), beginning of year	920,688	(1,175,385)
Retained earnings (deficit), end of year	(415,731)	920,688
Basic earnings (loss) per share	(0.02)	0.05
Diluted earnings (loss) per share	(0.02)	0.04
Weighted average number of commons shares outstanding – basic <i>[note 14]</i>	68,018,799	44,887,816
Weighted average number of common shares outstanding – diluted <i>[note 14]</i>	68,018,799	54,665,592

See accompanying notes

Coastal Contacts Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended October 31

	2006 \$	2005 \$
OPERATING ACTIVITIES		
Net income (loss)	(1,336,419)	2,096,073
Non-cash items:		
Amortization	1,310,829	832,831
Amortization of deferred lease inducement	(25,972)	(19,676)
Accrued interest	(27,360)	(189,333)
Stock-based compensation	268,470	175,632
Future income taxes	371,377	(222,679)
Unrealized foreign exchange gains on loans	(835,812)	—
Changes in non-cash working capital:		
Accounts receivable	(1,556,422)	(2,056,153)
Inventory	(5,058,882)	(3,285,210)
Prepaid expenses	275,222	(775,936)
Accounts payable and accrued liabilities	1,090,697	5,466,888
Income taxes payable	(138,355)	566,208
Deferred revenue	128,048	(259,837)
Due from related parties	(288,109)	(214,699)
Cash provided (used in) by operating activities	(5,822,688)	2,114,109
INVESTING ACTIVITIES		
Business acquisition, net of cash acquired	(3,947,019)	(955,369)
Acquisition of property, equipment and leasehold improvements	(1,508,739)	(773,569)
Acquisition of intangible assets	(1,383,421)	(573,672)
Cash used in investing activities	(6,839,179)	(2,302,610)
FINANCING ACTIVITIES		
Issuance of share capital	3,417,300	14,138,984
Issue of Special Warrants	22,500,000	—
Bank indebtedness	(328,157)	(355,706)
Loan payments	(378,672)	(606,662)
Share issue costs	(1,580,775)	(931,903)
Cash provided by financing activities	23,629,696	12,244,713
Effect of exchange rate changes on cash	(304,656)	(66,829)
Increase in cash and cash equivalents	10,663,173	11,989,383
Cash and cash equivalents, beginning of year	13,609,739	1,620,356
Cash and cash equivalents, end of year	24,272,912	13,609,739
Income taxes paid in cash	650,814	11,315
Interest paid in cash	42,973	99,001

See accompanying notes

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

1. NATURE OF OPERATIONS

Coastal Contacts Inc. (the “Company”) is a global on-line retailer of contact lenses sold through internet sites created and operated by the Company. The Company has operations in North America, Europe and Asia.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany transactions and balances have been eliminated.

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Revenue recognition

Revenue from product sales is recognized when the product has been shipped to the customer. At this point, the amount of sales revenue is determinable, no significant vendor obligations remain and the collection of the revenue is reasonably assured. A provision is made for product returns.

Deferred revenue includes revenue collected in advance of the product being shipped to the customer.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Foreign currency translation

The reporting currency of the Company is the Canadian dollar. Assets and liabilities of non-domestic subsidiaries with functional currencies other than the Canadian dollar are translated into Canadian dollars at the rates of exchange at the balance sheet date; income and expenses are translated at the average rates of exchange prevailing during the year. The resultant translation adjustments are reported as cumulative foreign currency translation adjustment in shareholders' equity.

Monetary assets and liabilities denominated in currencies other than the functional currency are translated into the functional currency at the exchange rate prevailing at the balance sheet date. Revenues and expenses denominated in currencies other than the functional currency are translated at the date prevailing on the transaction date. Foreign currency translation gains or losses are recorded in income in the period in which they occur.

Short-term investments

Short-term investments consist of money market funds and fixed income securities and are carried at cost plus accrued interest. The Company has a restriction of \$196,834 (1,265,000 Swedish Krona) against certain short term investments. This restriction is required by the Norwegian government as security against Value added tax payments.

Inventory

Inventory is valued at the lower of cost (determined on a first-in first-out basis) and net realizable value.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Property, equipment and leasehold improvements

Property, equipment and leasehold improvements are recorded at cost less accumulated amortization. Amortization is calculated over the estimated useful life of the assets at the following rates:

Leasehold improvements	Over the remaining term of the lease
Furniture and fixtures	20% declining balance
Computer hardware	30% declining balance
Computer software	50% declining balance
Customized ERP software	20% straight-line

Intangible assets

Finite life intangible assets are recorded at cost less accumulated amortization. Amortization is calculated over the estimated useful life of the assets at the following rates:

Website development	5 years straight-line basis
Customer lists	5 years straight-line basis

The Company intends to keep the brand names and brands it acquires intact. All future sales and marketing efforts in Europe and Asia will be conducted using these names. As a result, trade names are considered to have an indefinite life and will not be amortized. Their values will be reviewed for possible impairments annually or more frequently if events or changes in circumstances indicate possible impairment, based on the profitability and cash flows of the underlying business. Based on this testing the Company has determined that no impairment charge is required as at October 31, 2006.

Goodwill

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired. Goodwill is not amortized and is reviewed for possible impairment annually or more frequently if events or changes in circumstances indicate possible impairment, based on the profitability and cash flows of the reporting units to which the goodwill relates. Based on this testing, the Company has determined that no goodwill impairment charge is required as at October 31, 2006.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Income taxes

Income taxes are accounted for using the liability method of tax allocation. Under this method future income tax assets and liabilities are recognized for the tax consequences of temporary differences by applying substantively enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities.

The effect on future taxes for a change in tax rates is recognized in income in the period that includes the substantive enactment. In addition, future tax assets are recognized to the extent their realization is more likely than not.

Financial instruments

The Company's financial instruments consist of cash, bank indebtedness, accounts receivable, short-term investments, accounts payable, loans, and amounts due from related parties. The fair value of these financial instruments approximate their carrying value with the exception of certain related party advances. The fair value of such advances that are non-interest bearing and have no fixed repayment terms cannot be reliably estimated. It is management's opinion that the Company is not exposed to significant interest, currency or credit risk arising from these financial instruments.

The Company has not used derivative instruments to reduce its exposure to currency risk. Purchases from U.S. suppliers offset sales in U.S. dollars and purchases from European suppliers offset sales primarily in Euros, Norwegian Krona and Swedish Krona in the normal course of business and consequently, reduce the Company's exposure to currency risk.

Stock-based compensation

The Company follows the recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3870, *Stock-Based Compensation and Other Stock Based Payments* which requires the use of the fair value method of accounting for all stock options granted.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Earnings per share

The Company calculates basic earnings per share using the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated by the treasury stock method. Under the treasury stock method, the weighted average number of common shares outstanding for the calculation of diluted earnings per share assumes that the proceeds to be received on the exercise of dilutive stock options and warrants are applied to repurchase common shares at the average market price for the period. Stock options and warrants are dilutive when the Company has income from continuing operations and when the average market price of the common shares during the period exceeds the exercise price of the options and warrants.

3. CASH AND CASH EQUIVILENTS

	2006	2005
	\$	\$
Cash	3,975,864	2,985,600
Guaranteed investment certificates	19,939,570	10,401,481
Other cash investments	357,478	222,658
	24,272,912	13,609,739

The investments mature 30-90 days from the date of investment with an average interest rate of 4.6% (2005 – 3.3%).

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

4. ACCOUNTS RECEIVABLE, ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts receivable

	2006	2005
	\$	\$
Accounts receivable	7,280,868	4,104,580
Allowance for doubtful accounts	(606,836)	(259,980)
Value added tax receivable	452,505	964,616
	7,126,537	4,809,216

Accounts payable and accrued liabilities

	2006	2005
	\$	\$
Accounts payable - trade	9,095,679	8,902,550
Accrued liabilities	2,475,182	1,095,294
Value added tax payable	295,685	261,974
	11,866,546	10,259,818

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

5. ACQUISITION OF YOURLENSES

On May 4, 2005 through the Company's wholly owned subsidiary, Lensway AB (now named Lens Logistics AB), the Company completed the acquisition of all of the shares of Yourlenses Scandinavia AB, ("Yourlenses"), a European retailer of contact lenses. The consideration paid consisted of cash of \$949,032 (5,380,000 Swedish Krona) and the assumption of debt in the amount of \$156,167, with fifty percent of the cash paid upon signing on May 4, 2005 and the remaining fifty percent held in escrow, payable eighteen months from such date.

The acquisition was accounted for using the purchase method whereby assets acquired and liabilities assumed were recorded at their fair market values as of the date of the acquisition

The following sets forth the purchase price and its allocation to the tangible and intangible assets acquired.

	\$
Cash	949,032
Direct acquisition costs	111,193
Total consideration	1,060,225
Cash	33,988
Other current assets	240,942
Property and equipment	5,865
Yourlenses customer list	735,000
Yourlenses trade name	514,500
Website development	134,750
Current liabilities	(313,440)
Long-term debt	(85,361)
Future income tax liability	(387,590)
Net assets acquired	878,654
Goodwill	181,571

Goodwill has been allocated to the Swedish reporting unit and is not deductible for income tax purposes.

The results of operations have been included in the accompanying consolidated financial statements since May 4, 2005.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

6. ACQUISITION OF MYLENSES

On August 11, 2006 through the Company's wholly owned subsidiary, Lensco Holdings AB, the Company completed the acquisition of all of the shares of Eye-1 B.V., Eye-2 B.V. and Condis B.V., ("Mylenses"), a European retailer of contact lenses. The consideration paid consisted of cash of \$3,358,582 (2,350,000 Euros) and 1,650,000 common shares of the Company. The shares issued are subject to a voluntary pooling restriction. Under the terms of the agreement, 40% of the shares will be released on August 11, 2007 with the remaining 60% released in equal six month increments over the next 2 years.

The acquisition was accounted for using the purchase method whereby assets acquired and liabilities assumed were recorded at their fair market values as of the date of the acquisition. For purposes of computing the purchase price, the value of the restricted common shares was determined by taking the closing price of the Company's common stock as quoted on the TSX Exchange for the five days before, the day of and the five days following the date of acquisition. This average price was then reduced by a 15% discount due to the restriction provisions associated with the common shares issued. This discount is consistent with the discount applied to previous transactions with the same restrictions.

The following sets forth the preliminary purchase price and its allocation to the tangible and intangible assets acquired translated at the currency exchange rates prevailing on the day of acquisition. The final allocations may differ significantly from the preliminary allocations presented below.

	\$
Cash	3,358,582
Restricted common shares	1,702,635
Direct acquisition costs	319,920
Total consideration	5,381,137
Cash	25,920
Accounts receivable	566,396
Property, equipment and leasehold improvements assets	244,188
Mylenses customer list	1,258,656
Mylenses trademarks and tradenames	4,872,218
Website development	186,768
Current liabilities	(491,193)
Future income tax liability	(1,870,022)
Net assets acquired	4,792,931
Goodwill	588,206

Following the acquisition, Mylenses purchased inventory in the amount of \$736,590, from its former parent.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

6. ACQUISITION OF MYLENSES (cont'd.)

The Companies operate two websites and each has its own trademarks and tradenames. Goodwill has been allocated to the Dutch reporting unit and is not deductible for income tax purposes. The results of operations have been included in the accompanying consolidated financial statements since August 12, 2006.

7. ACQUISITION OF ASIANZAKKA

On October 13, 2006 the Company completed the acquisition of all of the shares of Asianzakka PTE. Ltd. ("Asianzakka"), an Asian retailer of contact lenses. The consideration paid consisted of cash of \$588,077 (817,000 Singapore Dollars) and 1,041,428 common shares of the Company. The shares issues are subject to a voluntary pooling restriction. Under the terms of the agreement, 40% of the shares will be released on October 13, 2007 with the remaining 60% released in equal six month increments over the next 2 years.

Under the terms of the agreement, the Company will make contingent payments of 778,000 Singapore Dollars and 389,000 Singapore Dollars on October 11, 2008 and April 11, 2009. The payments are contingent on Asianzakka meeting specified revenue and net income margin targets. Since the outcome of the contingency cannot be determined without reasonable doubt, the contingent payments have not been accrued. Should the contingent payments be made at a later date they will be accounted for as an adjustment of the purchase price of the acquired enterprise.

The acquisition was accounted for using the purchase method whereby assets acquired and liabilities assumed were recorded at their fair market values as of the date of the acquisition. For purposes of computing the purchase price, the value of the restricted common shares was determined by taking the closing price of the Company's common stock as quoted on the TSX Exchange for the five days before, the day of and the five days following the date of acquisition. This average price was then reduced by a 15% discount due to the restriction provisions associated with the common shares issued. This discount is consistent with the discount applied to previous transactions with the same restrictions.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

7. ACQUISITION OF ASIANZAKKA (cont'd.)

The following sets forth the preliminary purchase price and its allocation to the tangible and intangible assets acquired translated at the currency exchange rates prevailing on the day of acquisition. The final allocations may differ significantly from the preliminary allocations presented below.

	\$
Cash	588,077
Restricted common shares	811,182
Direct acquisition costs	81,255
Total consideration	1,480,514
Cash	128,124
Asianzakka customer lists	440,878
Asianzakka Trademarks and Tradenames	836,768
Future income tax liability	(255,529)
Other assets and liabilities	(32,712)
Net assets acquired	1,117,529
Goodwill	362,985

The Company operates under several websites and has several trademarks and tradenames. Goodwill has been allocated to the Singapore reporting unit and is not deductible for income tax purposes. The results of operations have been included in the accompanying consolidated financial statements since October 14, 2006.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

8. PROPERTY, EQUIPMENT AND LEASEHOLD IMPROVEMENTS

	Cost	Accumulated	Net Book
	\$	Amortization	Value
		\$	\$
2006			
Leasehold improvements	915,570	199,687	715,883
Computer hardware	735,256	258,105	477,151
Computer software	310,595	143,733	166,862
Customized ERP Software	1,183,672	248,805	934,867
Furniture and fixtures	687,630	209,119	478,511
	3,832,723	1,059,449	2,773,274
2005			
Leasehold improvements	465,094	70,667	394,427
Computer hardware	500,506	120,134	380,372
Computer software	51,899	22,782	29,117
Customized ERP Software	512,138	90,379	421,759
Furniture and fixtures	292,488	72,134	220,354
	1,822,125	376,096	1,446,029

As at October 31, 2006, capital projects in progress not subject to amortization was \$647,000.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

9. INTANGIBLE ASSETS

	Cost \$	Accumulated Amortization \$	Net Book Value \$
2006			
Website creation	1,929,929	295,454	1,634,475
Brand names and Trademarks acquired	8,799,551	—	8,799,551
Customer lists acquired	4,236,363	1,038,921	3,197,442
	14,965,843	1,334,375	13,631,468
2005			
Website creation	800,167	119,954	680,213
Brand names and Trademarks acquired	2,933,508	—	2,933,508
Customer lists acquired	2,418,360	565,369	1,852,991
	6,152,035	685,323	5,466,712

During the current year, the Company terminated the Pharmalens agreements and the value attributed to the agreements was written down to nil. The write-down of \$15,000 has been included in amortization of intangible assets.

10. GOODWILL

	October 31, 2005	Additions	Currency Impact	October 31, 2006
Acquisition of Lensway	5,326,397	—	256,932	5,583,329
Acquisition of Yourlenses	152,750	—	7,412	160,162
Acquisition of MyLenses	—	588,206	1,984	590,190
Acquisition of Asianzakka	—	362,985	555	363,540
Total Goodwill	5,479,147	951,191	266,883	6,697,221

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

11. LONG-TERM DEBT

	2006	2005
	\$	\$
<hr/>		
Vancity Capital		
Loan #1: Repayable in monthly instalments of \$8,378, blended principal and interest at 13%. The loan matured on March 15, 2006.	—	170,690
Loan #2: Repayable in monthly instalments of interest only at an interest rate of 13%. Beginning November 15, 2003 monthly payments are \$26,250 blended principal and interest at a fixed interest rate of 13.0%. The loan matured on June 15, 2006.	—	68,412
Handelsbanken Loan: Repayable in monthly instalments of \$38,266, consisting of blended principal and interest at 7.45%. The loan is denominated in Swedish Krona (SEK 3,611,106) matured on February 28, 2006.	—	140,155
	—	379,257
Less current portion	—	379,257
	—	—
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All of the Vancity Capital loans were collateralized by a general security agreement over all the assets of the Company and certain personal guarantees by shareholders. These Vancity Capital loans were subordinate to any other loan facilities that the Company might obtain in the future. These loans also gave VanCity the option of participating in equity offerings undertaken by the Company by converting the debt outstanding at the date of such offering into the equity offered.

The Handelsbanken loan was collateralized by a floating charge on the assets of Lensway, to a maximum of 7,500,000 krona (\$1,291,500), depending on the amount of outstanding loan.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

12. SHARE CAPITAL

[a] Issued and outstanding common shares

Authorized share capital comprises an unlimited number of common shares without par value and an unlimited amount of Class A preferred shares without par value. Common shares are issued and outstanding as follows:

	2006		2005	
	Number of Common Shares #	\$	Number of Common Shares #	\$
Balance - beginning of year	51,632,951	26,263,656	33,874,860	11,569,500
Issued in private placement	9,000,000	21,069,671	2,500,000	1,762,560
Issued in private placement	—	—	11,200,000	10,901,871
Issued on exercise of warrants	3,164,965	3,479,928	1,646,775	1,903,516
Issued on exercise of options	8,192,368	188,150	2,371,166	86,059
Issued in purchase of Pharma Lens	—	—	40,150	40,150
Issued in purchase of MyLenses [note 6]	1,650,000	1,702,635	—	—
Issued in purchase of Asianzakka [note 7]	1,041,428	811,182	—	—
Balance - end of year including shares held in treasury	74,681,712	53,515,222	51,632,951	26,263,656
Shares repurchased not cancelled	(42,700)	(41,005)	—	—
Balance - end of year	74,639,012	53,474,217	51,632,951	26,263,656

On February 22, 2005, the Company, through its newly incorporated subsidiary Coastal Pharma Lens Inc. entered into a purchase and sale agreement with Marlin Financial Group Inc. The Company acquired the Pharma Lens trademark application, the Distributorship Pilot Agreement between Ahold USA Inc. and Marlin Financial Group Inc. and the supply contract between Ralphs Grocery Company and Marlin Financial Group Inc. for 40,150 shares valued at \$1.00 per share and cash of \$14,850. The shares are subject to a voluntary pooling agreement of three years with tranches released at six month intervals.

On March 10, 2005, the Company undertook a private placement issuing 11,200,000 shares at \$1.10 per share. The underwriters received a commission of 6.5% of gross proceeds and "Compensation Warrants" of 9.5% of the total number of shares sold. These warrants are exercisable at \$1.10 per warrant and are exercisable for up to 18 months after closing. Net proceeds were \$11,380,671 after underwriters commission and other share issue costs. In addition, the "Compensation Warrants" were valued at \$478,800 and offset against the proceeds with a corresponding increase in contributed surplus.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

12. SHARE CAPITAL (cont'd.)

On January 31, 2006, the Company closed on an underwritten bought deal 9,000,000 special warrants by way of private placement, at a price of \$2.50 per special warrant, for gross cash proceeds of \$22.5 million. The Company paid underwriters a commission equal to 6% of the gross proceeds and up to \$30,000 for underwriters' expenses and fees related to the offering. Net proceeds were \$21,069,671 after underwriters' commission and other underwriting costs. The special warrants and common shares issuable upon exercise of the special warrants were subject to resale restrictions for a period of four months from the closing date. Each special warrant is exercisable to acquire one common share of the Company for no additional consideration. These warrants were exercised on March 30, 2006 into common shares.

On October 16, 2006, the Toronto Stock Exchange accepted the Company's notice of intention to make a normal course issuer bid for its common shares through the facilities of the exchange. Effective, October 18, 2006, the Company may commence making purchases of up to a maximum of 4,933,641 common shares. Any shares acquired will be purchased at the market price for the common shares at the time of acquisition and will be cancelled. The bid will terminate on the earlier of the date determined by the Company and October 17, 2007. As at October 31, 2006, 42,700 shares had been repurchased under a Normal Course Issuer Bid for which the shares had not yet been cancelled. The shares were cancelled in November, 2006.

As at October 31, 2006, 6,667,995 shares were subject to voluntary pooling restrictions of which 2,691,428 were subject to regulatory trading restrictions.

[b] Stock options

The shareholders of the Corporation have adopted a stock option plan (the "Option Plan") for its directors, officers and employees. The Option Plan provides that options to purchase common shares may be granted to eligible persons on terms determined within the limitations set out in the Option Plan. The maximum number of common shares to be reserved for issuance anytime under the Option Plan and any other employee incentive plan is 10% of the issued and outstanding common shares. The exercise price for an option granted under the Option Plan may not be less than that permitted by applicable regulatory authorities. Options granted may be subject to vesting requirements. Non-assignable options will be granted for a period which may not exceed five years from the date of the grant and will expire within 90 days upon the participant ceasing to be a director, officer or an employee of the Company. The Option Plan is administered by the Company's Compensation and Corporate Governance Committee. The Option Plan is subject to the rules and policies of the TSX Exchange.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

12. SHARE CAPITAL (cont'd.)

The following table contains information with respect to Company stock options:

	#	\$
Options outstanding, October 31, 2004	11,302,241	0.005 – 1.00
Granted	243,089	1.00
Exercised	(2,371,165)	0.005 – 1.00
Options outstanding, October 31, 2005	9,174,165	0.005 – 1.00
Granted	150,000	1.37
Exercised	(8,192,368)	0.005 – 1.00
Options outstanding, October 31, 2006	1,131,797	0.125 – 1.37

The following table summarizes information about company stock options outstanding as at October 31, 2006:

Options Outstanding			Options Exercisable	
Shares #	Weighted Average Contractual Life (years)	Exercise Price \$	Shares #	Exercise Price \$
550,000	2.33	0.125	467,500	0.125
54,000	3.26	1.00	54,000	0.275
182,339	3.26	1.00	116,059	1.00
195,458	2.75	1.00	117,958	1.00
150,000	4.68	1.37	15,000	1.37
1,131,797	2.91	0.62	770,517	0.48

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October 31, 2006 and 2005

12. SHARE CAPITAL (cont'd.)

On March 1, 2005, 198,840 options were issued to employees of Lensway. These options are exercisable at \$1.00 each and vest equally on March 31, 2005, 2006 and 2007. Using the Black-Scholes option-pricing model, the Company estimated the fair value of this option grant to be \$143,165. Compensation of \$41,057 has been recognized as expense in the year ended October 31, 2006 (2005 - \$90,990). A further \$9,544 will be expensed in 2007.

On March 1, 2005, 54,000 options were issued to directors of the Company. These options are exercisable at \$1.00 per share. 30,000 of these options vested on February 18, 2005 while the remaining options vested on February 18, 2006. Using the Black-Scholes option-pricing model, the Company estimated the fair value of this option grant to be \$38,880. Compensation of \$4,960 has been recognized as expense in the year ended October 31, 2006 (2005 - \$31,500).

On July 6, 2006, 150,000 options were issued to officers of the Company. These options are exercisable at \$1.37 per share. 15,000 of these options vested immediately while the remaining options vest in equal six month increments over 3 years. Using the Black-Scholes option-pricing model, the Company estimates the fair value of this option grant to be \$98,025. Compensation of \$32,910 has been recognized as expense in the year ended October 31, 2006. A further \$43,542 will be expensed in 2007 and \$21,573 in 2008.

On January 31, 2006, an employee entered into a call option agreement with a principal shareholder for 300,000 options. These options are exercisable at \$1.00 per share. 120,000 of these options will vest on January 31, 2007 while the remaining options vest in equal six month increments over 2 years. Using the Black-Scholes option-pricing model, the Company estimates the fair value of this option grant to be \$335,944. Compensation of \$172,906 has been recognized as expense in the year ended October 31, 2006. A further \$120,764 will be expensed in 2007, \$38,131 in 2008 and \$4,141 in 2009.

The fair value of the option grants are estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2006	2005
Dividend yield	0%	0%
Expected volatility	59%	70%
Risk free interest rate	4.0%	3.10%
Expected lives	2.7 years	3 years

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

12. SHARE CAPITAL (cont'd.)

[c] Warrants

The following table contains information with respect to all warrants:

	#	\$
Warrants outstanding, October 31, 2004	3,871,490	0.80 - 1.50
Granted	1,064,000	1.10
Exercised	(1,646,775)	0.80 - 1.50
Warrants outstanding, October 31, 2005	3,288,715	0.80 - 1.10
Exercised or expired	(3,288,715)	0.80 - 1.10
Warrants outstanding, October 31, 2006	—	—

13. CONTRIBUTED SURPLUS

	2006	2005
	\$	\$
Balance - beginning of year	593,083	105,898
Stock-based compensation	268,470	175,632
Compensation warrants	—	478,800
Reclassification to share capital on exercise of warrants	(331,136)	(167,247)
Balance - end of year	530,417	593,083

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

14. EARNINGS PER SHARE

	2006	2005
	\$	\$
Weighted average number of common shares outstanding - basic	68,018,799	44,887,816
Stock options	—	8,720,949
Warrants	—	1,056,827
Weighted average number of common shares outstanding - diluted	68,018,799	54,665,592

The diluted average number of common shares is calculated using the Treasury method.

15. INCOME TAXES

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future tax liabilities are as follows:

	2006	2005
	\$	\$
Future tax assets		
Non-capital loss carryforwards	1,979,803	194,376
Net book value of capital assets in excess of tax value	(219,854)	(139,617)
Share issue costs	865,453	708,430
Other	158,897	46,260
Total future tax assets	2,784,299	809,449
Valuation allowance	(2,784,299)	(809,449)
Total future tax assets	—	—
Future tax liabilities		
Expense recognized for tax purposes in foreign jurisdictions	370,737	260,680
Net book value of capital assets in excess of tax value	306,127	—
Carrying value of intangible assets in excess of tax basis	3,549,640	1,385,996
	4,226,504	1,646,676

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

15. INCOME TAXES (cont'd.)

The potential income tax benefits relating to the future tax assets have not been recognized in the consolidated financial statements where their realization did not meet the requirements of "more likely than not" under the liability method of tax allocation.

Significant components of the income tax expense attributable to continuing operations are as follows:

	2006	2005
	\$	\$
Current income tax expense	579,840	474,596
Future income tax recovery relating to the utilization of previously unrecognized losses	—	(168,941)
Future income tax recovery relating to reversal of taxable temporary differences	371,377	75,238
	951,217	380,893

The reconciliation of income taxes attributable to continuing operations computed at the statutory income tax rates to income tax expense, at the statutory tax rate of 34.75% [2005 - 35.12%] is as follows:

	2006	2005
	\$	\$
Income tax expense (recovery) at statutory tax rates	(133,858)	869,910
Expenses not deductible for income tax purposes	98,365	60,736
Financing costs deductible for income tax purposes	(318,347)	(210,421)
Non-capital losses generated	1,959,729	—
Non-capital losses utilized	—	(179,187)
Foreign tax rate differential	(574,762)	(113,514)
Other	(79,910)	(46,631)
	951,217	380,893

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

15. INCOME TAXES (cont'd.)

As at October 31, 2006, the Company has non-capital loss carryforwards of \$6.378 million for Canadian income tax purposes that expire as follows:

	\$
2010	304,000
2014	435,000
2016	5,639,000
	<u>\$6,378,000</u>

16. RELATED PARTY TRANSACTIONS

	2006 \$	2005 \$
Promissory notes receivable	376,033	115,000
Advances to officers	234,326	167,559
CMP Medical Inc.	—	39,691
	<u>610,359</u>	<u>322,250</u>

The amounts due from related parties includes (1) nine promissory notes from officers ranging in value from \$12,500 to \$100,000. These loans are payable on demand and bear interest at 5% per annum; (2) The advances to officers are non interest bearing with no fixed terms of repayment; and (3) \$39,691 from CMP Medical Inc., a company controlled by an officer and shareholder of the Company.

During the year, the Company issued loans covered by promissory notes to officers and employees in the amount of \$360,100. Interest is accrued at a rate of 5% per annum. During the year, payments were made on the loans in the amount of \$99,067.

During the year, the Company made other advances to officers in the amount of \$66,767.

During the year, CMP Medical Inc. ceased to operate and as a consequence the loan amount of \$39,691 advanced in 2002 was written off and included in selling, general and administration expenses on the income statement.

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

17. SEGMENTED INFORMATION

The Company operates in one business segment, the sale of contact lenses. The Company ships product from North America and Europe to Customers in North America, Europe and Asia.

Geographical information is based on the location of the customers in which the Company sells contact lenses and accessories. Intercompany revenues have been excluded from the revenues in the country of shipment. Certain comparative figures have been adjusted to reflect this reporting.

	United States	Sweden	Norway	Other	Total
	\$	\$	\$	\$	\$
Revenue					
Year Ended:					
October 31, 2006	25,665,453	21,638,068	12,634,034	21,076,396	81,013,951
October 31, 2005	29,411,272	19,198,995	9,108,422	9,809,196	67,527,885
Property, equipment and leasehold improvements					
October 31, 2006	-	1,438,687	-	1,334,587	2,773,274
October 31, 2005	-	703,778	-	742,251	1,446,029
Goodwill					
October 31, 2006	-	5,743,472	-	953,749	6,697,221
October 31, 2005	-	5,479,147	-	-	5,479,147

Included in "Other" are revenues to non-related customers in the Company's home domicile of \$1,412,718 for the year ended October 31, 2006 (2005 - \$827,849) and Property, equipment and leasehold improvements located in the Company's home domicile of \$1,118,381 (2005 - \$742,251).

Coastal Contacts Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

October 31, 2006 and 2005

18. COMMITMENTS

The Company is committed to minimum annual payments, primarily related to lease costs on its warehouse and office premises, as follows:

	\$
2007	630,020
2008	768,912
2009	861,967
2010	455,597
2011	105,432
	<u>2,821,928</u>

Operating costs on leases have been excluded.

19. CONTINGENT LIABILITIES

Under the terms of the agreement to acquire the shares of Asianzakka PTE. Ltd., the Company will make contingent payments of 778,000 Singapore Dollars (\$540,000) and 389,000 Singapore Dollars (\$272,000) on October 11, 2008 and April 11, 2009. The payments are contingent on Asianzakka meeting specified revenue and net income margin targets for 2007 and 2008. The liability has not been accrued in the financial statements as the amount of the liability cannot be determined at this time.

20. COMPARATIVE FIGURES

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