ATI AIRTEST TECHNOLOGIES INC.

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2013

(Expressed in Canadian dollars)

DALE MATHESON CARR-HILTON LABONTE LLP
CHARTERED ACCOUNTANTS & BUSINESS ADVISORS

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INDEPENDENT AUDITOR'S REPORT

To the shareholders of ATI Airtest Technologies Inc.,

We have audited the accompanying consolidated financial statements of ATI Airtest Technologies Inc., which comprise the consolidated statements of financial position as at December 31, 2013 and 2012, and the consolidated statements of comprehensive loss, changes in shareholders' deficiency and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of ATI Airtest Technologies Inc. as at December 31, 2013 and 2012, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of matter
Without modifying our opinion, we draw attention to Note 1 to the financial statements which describes matters and conditions that indicate the existence of a material uncertainty that may cast significant doubt about ATI Airtest Technologies Inc.'s ability to continue as a going concern.

DMCL

April 30, 2014
Vancouver, Canada

DALE MATHESON CARR-HILTON LABONTE LLP
CHARTERED ACCOUNTANTS

ATI AIRTEST TECHNOLOGIES INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Expressed in Canadian dollars)

	Note	December 31, 2013	December 31, 2012
ASSETS			
Current			
Cash		$ -	$ 1,769
Trade receivables	4	539,243	505,593
Inventory	5	227,628	271,378
Prepaid expenses		4,859	9,708
		771,730	788,448
Non-current			
Equipment	6	8,306	10,532
		$ 780,036	$ 798,980
LIABILITIES			
Current			
Cash deficiency		$ 11,155	$ -
Trade payables and accrued liabilities	7	2,055,745	1,699,635
Customer deposits		-	12,960
Loans	8	1,511,598	1,418,876
Convertible debt notes	9	74,014	74,014
Due to related parties	11	437,567	312,273
		4,090,079	3,517,758
Non-current			
Derivative liability	10	43,057	-
		4,133,136	3,517,758
SHAREHOLDERS' DEFICIENCY			
Share capital	10	9,158,281	9,315,281
Subscriptions receivable	10	-	(157,000)
Share subscriptions received	10	100,000	-
Reserves	10	1,114,812	1,358,239
Deficit		(13,726,193)	(13,235,298)
		(3,353,100)	(2,718,778)
		$ 780,036	$ 798,980

Nature and continuance of operations (Note 1)

The accompanying notes are an integral part of these consolidated financial statements

APPROVED ON BEHALF OF THE BOARD

/s/ "George Graham"

/s/ "Darrel Taylor"

ATI AIRTEST TECHNOLOGIES INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Expressed in Canadian dollars)

		Years ended	
	Note	**December 31, 2013**	**December 31, 2012**
PRODUCT SALES		$ 2,681,844	$ 2,797,931
COST OF GOODS SOLD		1,715,851	1,699,273
GROSS PROFIT		965,993	1,098,658
EXPENSES			
General and administrative	12	555,928	688,812
Business development and marketing	12	518,998	516,799
Lending fees and finance charges		371,662	384,562
Research and development		10,300	47,000
		(1,456,888)	(1,637,173)
NET LOSS		$ (490,895)	$ (538,515)
OTHER COMPREHENSIVE INCOME			
Translation to presentation currency		(200,370)	-
COMPREHENSIVE LOSS		$ (490,895)	$ (538,515)
Loss per shares – basic and diluted		$ (0.02)	$ (0.02)
Weighted average number of common shares outstanding – basic and diluted		23,785,061	23,132,856

The accompanying notes are an integral part of these consolidated financial statements

ATI AIRTEST TECHNOLOGIES INC.
CONSOLIDATED STATEMENT OF CHANGES IN SHARHOLDERS' DEFICIENCY

(Expressed in Canadian dollars)

		Share capital			Reserves				
	Note	**Number of shares**	**Amount $**	**Subscriptions receivable $**	**Share based payment $**	**Foreign currency translation $**	**Subscriptions received $**	**Deficit $**	**Total shareholders' deficiency $**
Balance, December 31, 2011		20,432,176	8,879,407	(157,000)	1,303,271	-	-	(12,696,783)	(2,671,105)
Shares issued for cash:						-			
Private placement	10	3,352,885	435,874	-	-	-	-	-	435,874
Stock options granted	10	-	-	-	32,775	-	-	-	32,775
Stock options repriced	10	-	-	-	22,193	-	-	-	22,193
Comprehensive loss		-	-	-	-	-	-	(538,515)	(538,515)
Balance, December 31, 2012		23,785,061	9,315,281	(157,000)	1,358,239	-	-	(13,235,298)	(2,718,778)
Subscriptions received	10	-	-	-	-	-	100,000	-	100,000
Write-off subscriptions receivable	10	-	(157,000)	157,000	-	-	-	-	-
Derivative liability	10	-	-	-	(43,057)	-	-	-	(43,057)
Comprehensive loss		-	-	-	-	(200,370)	-	(490,895)	(691,265)
Balance, December 31, 2013		23,785,061	9,158,281	-	1,315,182	(200,370)	100,000	(13,726,193)	(3,353,100)

The accompanying notes are an integral part of these consolidated financial statements

ATI AIRTEST TECHNOLOGIES INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in Canadian dollars)

	Years ended	
	December 31, 2013	**December 31, 2012**
CASH PROVIDED BY (USED IN):		
Operating Activities:		
Net loss	$ (490,895)	$ (538,515)
Items not involving cash:		
Amortization	2,226	2,938
Bad debt	74,931	-
Stock based compensation	-	54,968
Foreign exchange gain	(200,370)	-
Changes in non-cash working capital items:		
Trade receivables	(108,581)	(53,204)
Inventory	43,750	(29,686)
Interest payable	144,202	106,692
Prepaid expenses	4,849	55,418
Trade payables and accrued liabilities	356,110	58,614
Customer deposits	(12,960)	-
Cash used in operating activities	(186,738)	(342,775)
Financing Activities:		
Proceeds from share issuance	-	435,878
Share subscriptions received	100,000	(416,000)
Loan (repayments) proceeds	(51,480)	206,949
Advances from related parties	125,294	83,167
Cash from financing activities	173,814	309,994
Decrease in cash	(12,924)	(32,781)
Cash, beginning of year	1,769	34,550
Cash (Cash deficiency), end of year	$ (11,155)	$ 1,769

The accompanying notes are an integral part of these consolidated financial statements

1. Nature and continuance of operations

ATI Airtest Technologies Inc. (the “Company”) was incorporated in British Columbia on March 13, 1996. The primary business activity is the manufacture and sale of air testing equipment and related services in Canada and the United States. The Company’s shares are traded on the TSX Venture Exchange (“TSX-V”).

The Company’s head office is located at Unit 9-1520 Cliveden Ave, Delta, British Columbia, V3M 6J8.

These consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business. As at December 31, 2013, the Company is not able to finance day to day activities through operations and has a significant working capital deficiency. A significant portion of the amounts owed to the Company’s creditors are past due. The Company’s continuation as a going concern is dependent upon its ability to obtain additional financing, continued support of existing creditors and lenders, continued financial support from related parties, and ultimately attaining profitable operations. These factors indicate the existence of a material uncertainty that may cast significant doubt about the Company’s ability to continue as a going concern.

Management intends to finance operating costs over the next twelve months through equity financing, sales growth, loans from related parties, and bridge financing. Should the Company be unable to continue as a going concern, the net realizable value of its assets may be materially less than the amounts on its consolidated statement of financial position.

2. Basis of presentation

The financial statements were authorized for issue on April 30, 2014 by the directors of the Company.

The consolidated financial statements of the Company comply with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and interpretations of the International Financial Reporting Interpretations Committee (“IFRIC”).

The consolidated financial statements of the Company have been prepared on an accrual basis and are based on historical costs, modified where applicable. The consolidated financial statements are presented in Canadian dollars unless otherwise noted.

3. Significant accounting policies

Basis of consolidation
These consolidated financial statements include the accounts of the Company and each of its wholly owned inactive subsidiaries: Airwave Environmental Technologies Inc. (Canada), Airtest Technologies Corp. (US), and Clairtec Inc. (US). Inter-company transactions and balances have been eliminated upon consolidation.

Inventory
Inventories include raw materials, work in process and finished goods, all of which are stated at the lower of weighted average cost and net realizable value. Cost includes the cost of direct material, direct labour and other overhead costs. Labour costs are allocated to items based on actual labour rates. Fixed and variable overhead are allocated to production activities in converting materials to finished goods.

Revenue recognition
Product sales revenue is recognized when evidence of a contractual arrangement exists, prices are fixed, and the risks of ownership or title pass to the customer. This is normally when products are shipped from the warehouse, provided collection is reasonably assured.

Service revenue is recognized when the service has been completed to the customer’s specification and collection is reasonably assured.

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3. Significant accounting policies (continued)

Warranty provision

The Company accrues for estimated warranty obligations under a warranty provision at the time sales are recognized and any changes in estimates are recognized prospectively through the provision. The Company provides its customers with a limited right of return for defective products. All warranty returns must be authorized by the Company prior to acceptance. Warranty provisions are estimated based on the Company's experience and to date have been insignificant

Equipment

Equipment is stated at historical cost less accumulated depreciation and accumulated impairment losses. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of comprehensive loss during the financial period in which they are incurred.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in the statement of comprehensive loss.

Amortization is calculated on a declining-balance method to write off the cost of the assets to their residual values over their estimated useful lives. The amortization rates applicable to each category of equipment are as follows:

Class of equipment	Rate
Computer hardware	30%
Office furniture and fixtures	20%
Assembly equipment	20%
Testing equipment	30%

Research and development

Research and development costs are expensed as incurred unless development costs meet the criteria for capitalization:

- The technical feasibility of completing the intangible asset so that it will be available for use or sale;
- The intention to complete the intangible asset and use or sell it;
- The ability to use or sell the intangible asset;
- How the intangible asset will generate probable future economic benefits;
- The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- The ability to measure reliably the expenditure attributable to the intangible asset during its development.

The Company amortizes costs, commencing with commercial production, over the expected future benefit period based upon quantities delivered compared to expected levels contracted to be delivered.

Loss per share

Basic loss per share amounts are calculated by dividing net loss by the weighted average number of common shares outstanding during the year.

Diluted loss per share amounts are computed similarly to basic loss per share except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of additional options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire shares of common stock at the average market price during the year.

3. Significant accounting policies (continued)

Significant estimates and assumptions
The preparation of financial statements in accordance with IFRS requires the Company to make estimates and assumptions concerning the future. The Company's management reviews these estimates and underlying assumptions on an ongoing basis, based on experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to estimates are adjusted for prospectively in the period in which the estimates are revised.

Estimates and assumptions where there is significant risk of material adjustments to assets and liabilities in future accounting periods include the useful lives of equipment, recoverability of trade receivables, net realizable value of inventory, fair value measurements for financial instruments, stock-based compensation and other equity-based payments, warranty accruals, cost allocations, and the measurement of deferred tax assets and liabilities.

Significant judgments
The preparation of financial statements in accordance with IFRS requires the Company to make judgments, apart from those involving estimates, in applying accounting policies. The most significant judgments in applying the Company's financial statements include the assessment of the Company's ability to continue as a going concern and whether there are events or conditions that may give rise to significant uncertainty.

Income taxes
Current income tax assets and liabilities for the period and as at the year end are measured at the amount expected to be recovered from or paid to taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date, in the countries where the Company operates and generates taxable activities.

Current income tax relating to items recognized directly in other comprehensive income or equity is recognized in other comprehensive income or equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred income tax is provided using the asset and liability method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and recognized only to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred income tax assets and deferred income tax liabilities are offset only if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Share-based payments
The Company operates a stock option plan. Share-based payments to employees are measured at the fair value of the instruments issued and amortized over the vesting periods. Share-based payments to non-employees are measured at the fair value of goods or services received or the fair value of the equity instruments issued, if it is determined the fair value of the goods or services cannot be reliably measured, and are recorded at the date the goods or services are received. The corresponding amount is recorded to the share-based payment reserve. The fair value of options is determined using the Black–Scholes Option Pricing Model. The number of shares and options expected to vest is reviewed and adjusted at the end of each reporting period such that the amount recognized for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest.

3. Significant accounting policies (continued)

Financial Instruments
The Company classifies its financial instruments in the following categories: at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale and financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of financial instruments at initial recognition.

Financial assets are classified at fair value through profit or loss when they are either held for trading for the purpose of short-term profit taking, derivatives not held for hedging purposes, or when they are designated as such to avoid an accounting mismatch or to enable performance evaluation where a group of financial assets is managed by key management personnel on a fair value basis in accordance with a documented risk management or investment strategy. Such assets are subsequently measured at fair value with changes in carrying value being included in profit or loss.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are subsequently measured at amortized cost. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period.

Held-to-maturity investments are non-derivative financial assets that have fixed maturities and fixed or determinable payments, and it is the Company's intention to hold these investments to maturity. They are subsequently measured at amortized cost. Held-to-maturity investments are included in non-current assets, except for those which are expected to mature within 12 months after the end of the reporting period.

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or are not suitable to be classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments and are subsequently measured at fair value in current assets. Unrealized gains and losses are recognized in other comprehensive income, except for impairment losses and foreign exchange gains and losses.

Financial liabilities (excluding financial guarantees that are derivatives) are subsequently measured at amortized cost.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. At each reporting date, the Company assesses whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a significant and prolonged decline in the value of the instrument is considered to determine whether impairment has arisen.

Impairment of assets
The carrying amount of the Company's long term assets are reviewed at each reporting date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. An impairment loss is recognized whenever the carrying amount of an asset, or the asset's cash generating unit, exceeds its recoverable amount. Impairment losses are recognized in the statement of comprehensive loss.

The recoverable amount of an asset is measured at the greater of its fair value less cost to sell and its value in use. In assessing value in use, the estimated attributable future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset.

For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount, however, a reversal cannot exceed the carrying amount that would have been determined had no impairment loss been recognized in previous years.

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment.

3. Significant accounting policies (continued)

Foreign currency translation
The functional currency of each entity is measured using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in Canadian dollars. The Company's functional currency is the United States dollar.

Transactions and balances:

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the period-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined.

Exchange differences arising on the translation of monetary items or on settlement of monetary items are recognized in the statement of comprehensive loss in the period in which they arise, except where deferred in equity as a qualifying cash flow or net investment hedge.

Exchange differences arising on the translation of non-monetary items are recognized in other comprehensive income in to the extent that gains and losses arising on those non-monetary items are also recognized in other comprehensive income. Where the non-monetary gain or loss is recognized in profit or loss, the exchange component is also recognized in profit or loss.

Translation to presentation currency:

The financial results are translated from the functional currency to the Company's presentation currency as follows:

- assets and liabilities are translated at period-end exchange rates prevailing at that reporting date; and
- income and expenses are translated at average exchange rates for the period.

Exchange differences arising on translation are recognized in other comprehensive income and recorded in the Company's foreign currency translation reserve in equity.

Accounting standards issued but not yet applied
At the date of authorization of these financial statements, IFRS 9 "Financial Instruments" has not been early adopted and is not expected to have a material effect on the Company's future results and financial position. The effective date of IFRS 9 has not yet been determined.

(Expressed in Canadian dollars)

4. Trade receivables

	December 31, 2013	December 31, 2012
Trade receivables	$ 74,888	$ 33,124
Trade receivables factored (Note 9(a))	471,542	477,825
Allowance for doubtful amounts	(7,187)	(5,356)
	$ 539,243	$ 505,593

5. Inventory

	December 31, 2012	December 31, 2012
Finished goods	$ 105,787	$ 135,634
Work in progress	17,104	3,135
Raw materials and component parts	104,737	132,609
	$ 227,628	$ 271,378

For the year ended December 31, 2013, inventory recognized as an expense in cost of sales amounted to $1,509,380 (2012 - $1,502,305) with write downs of $10,876 (2012 - $Nil).

6. Equipment

	Office furniture and fixtures	Computer hardware	Testing equipment	Assembly equipment	Total
Cost					
At December 31, 2012 and 2013	$ 39,765	$ 73,255	$ 17,967	$ 5,793	$ 136,780
Amortization					
At December 31, 2011	31,419	69,461	16,999	5,431	123,310
Charge for the period	1,628	946	291	73	2,938
At December 31, 2012	33,047	70,407	17,290	5,504	126,248
Charge for the period	1,303	663	203	57	2,226
At December 31, 2013	34,350	71,070	17,493	5,561	128,474
Net book value					
At December 31, 2012	6,718	2,848	677	289	10,532
At December 31, 2013	$ 5,415	$ 2,185	$ 474	$ 232	$ 8,306

7. Trade payables and accrued liabilities

	December 31, 2013	December 31, 2012
Trade payables	$ 1,599,990	$ 1,323,294
Due to government agencies	216,568	92,013
Payroll accrual and vacation payable	8,544	48,522
Accrued liabilities	230,643	235,806
	$ 2,055,745	$ 1,699,635

(Expressed in Canadian dollars)

8. Loans

	December 31, 2013	December 31, 2012
Loan, secured against receivables	$ 429,935	$ 486,914
Loans and advances, unsecured, due on demand:		
Non-interest bearing	40,000	25,000
Interest at 10% per annum	9,328	18,828
Interest at 18% per annum	785,669	681,467
Interest at 20% per annum	246,666	206,667
	$ 1,511,598	$ 1,418,876

Loan, secured against receivables

During July 2004, the Company entered into a lending arrangement whereby the Company borrowed up to 80% of its trade receivables that are less than 90 days overdue. In addition, the Company could request loans or advances against purchase orders. The specified trade receivables were pledged as security for the arrangement, with full recourse against the Company. The loans bear interest at 1.5% per month for the first 60 days outstanding, 3.5% per month for the period outstanding greater than 61 days and up to 90 days, and 5% per month for the period outstanding greater then 90 days. There is a 3% processing charge for all trade receivables factored and advances received. The agreement was terminated in October 2013.

During October 2013, the Company entered into a lending arrangement whereby the Company may borrow up to 85% of its trade receivables that are less than 90 days overdue. In addition, the Company may request loans or advances against purchase orders received from customers. The specified trade receivables are pledged as security for the arrangement, with full recourse against the Company. The loans bear interest at 1.5% per month for the first 30 days outstanding, and 0.05% per day after that until the invoice is paid to the lender. The amount due to the lender at December 31, 2013 includes current purchase orders for orders in progress.

The Company does not record a sale of the trade receivable or offset factored trade receivables to the related liability as the Company retains all the risks and rewards of ownership.

9. Convertible debt notes

The Company issued convertible debt instruments in 2004 and 2005. The debt instruments are unsecured and are non-interest bearing. Each of the instruments matured and are now repayable on demand.

10. Share capital

Authorized:

Unlimited common shares without par value

Issued

23,785,061 common shares issued and outstanding

2,700,000 shares held in treasury

Private placements

During the year ended December 31, 2013, management determined that $157,000 in subscriptions receivable are uncollectible and wrote-off the entire amount with a corresponding decrease to share capital.

On March 13, 2012, the Company entered into a private placement of 3,352,885 share units at $0.13 per unit for total gross proceeds of $435,875. Each unit consists of one common share and one share purchase warrant. Each warrant entitles the holder to acquire three quarters of an additional common share of the Company at a price of $0.20 per share for a period of 60 months from March 13, 2012.

As at December 31, 2013, the Company has received $100,000 in subscriptions for a future financing.

(Expressed in Canadian dollars)

10. Share capital (continued)

Stock options

The Company's Board of Directors may, from time to time, grant stock options, subject to regulatory terms and approval, to employees, officers, directors and consultants. The exercise price of each option can be set at no less than the closing market price of the common shares on the TSX-V on the date of grant. Options terminate 30 days following the termination of employment. Vesting and the option terms are set at the discretion of the Board of Directors at the time the options are granted.

During the year ended December 31, 2012, 1,000,000 stock options were granted to employees and directors. The fair value of the options was estimated to be $32,775 using the Black-Scholes Option Pricing Model with volatility of 184%, dividend yield of 0%, expected life of 5 years at a risk free rate of 1.37%.

During the year ended December 31, 2012, the Company repriced and extended the terms of 1,216,617 stock options. The incremental fair value of the modification was estimated at $22,193 using the Black-Scholes Option Pricing Model with a volatility of 184%, dividend yield of 0%, expected life of 5 years and a risk free rate of 1.37%.

A continuity of the Company's options is as follows:

	December 31, 2013			December 31, 2012		
	Number of options		Weighted average exercise price	Number of options		Weighted average exercise price
Outstanding, beginning of year	2,383,334	$	0.10	1,566,667	$	0.60
Exercised	-		-	1,000,000		0.10
Cancelled	-		-	(183,333)		0.60
Outstanding, end of period	2,383,334	$	0.10	2,383,334	$	0.10

As at December 31, 2013, stock options outstanding have a weighted average life remaining of 3.62 years.

Warrants

	December 31, 2013			December 31, 2012		
	Number of options		Weighted average exercise price	Number of options		Weighted average exercise price
Outstanding, beginning of year	4,914,331	$	0.14	3,333,000	$	0.60
Exercised	-		-	2,514,664		0.20
Cancelled	(2,399,666)		0.60	(933,333)		0.60
Outstanding, end of period	2,514,664	$	0.20	4,914,331	$	0.16

As at December 31, 2013, warrants outstanding have a weighted average life remaining of 3.2 years.

Share base payment reserve
The share-based payment reserve records items recognized as stock-based compensation expense and other share-based payments until such time that the stock options or warrants are exercised, at which time the corresponding amount will be transferred to share capital.

Foreign currency translation reserve
The foreign currency translation reserve records unrealized exchange differences arising on translation from the Company's functional currency to its presentation currency.

(Expressed in Canadian dollars)

10. Share capital (continued)

Derivative liability

The derivative financial liability consists of the fair value of share purchase warrants that have exercise prices that differ from the functional currency of the Company and are within the scope of IAS 32 “Financial Instruments: Presentation”.

The fair values of these warrants as at December 31, 2013 were estimated using the Black-Scholes Option Pricing Model using the following inputs; expected life of warrants: 3.25 years; volatility: 115%; risk-free interest rate: 1.2% and dividend yield: 0%.

11. Related party transactions

During the year ended December 31, 2013, the Company paid or accrued professional and management fees to directors of $36,000 (2012 - $26,000).

At December 31, 2013, $437,567 (December 31, 2012 - $312,273) is payable to directors for accrued services and advances.

Amounts due to related parties are non-interest bearing, unsecured, and without specified terms of repayment.

Key management personnel compensation

The Company’s key management personnel have authority and responsibility for overseeing, planning, directing and controlling the activities of the Company and consist of the Company’s Board of Directors and the Company’s Executive Leadership Team. The Executive Leadership Team consists of the CEO and President, and Chief Financial Officer (CFO).

	Year ended			
		December 31, 2013		December 31, 2012
Salaries	$	288,000	$	280,000
Stock-based compensation		-		54,968
Total	$	288,000	$	334,968

(Expressed in Canadian dollars)

12. Supplementary information

Presentation of the Company's operating expenses by nature versus function for the years ended December 31, 2013 and 2012 is as follows:

	Years ended	
	December 31, 2013	**December 31, 2012**
OPERATING EXPENSES		
General and administrative:		
Amortization	$ 2,226	$ 2,938
Automotive	18,873	19,136
Bad debts	74,931	-
Bank charges and interest	-	44,126
Foreign exchange (gain) loss	(147,498)	(9,300)
Freight	37,754	46,740
Office and general	47,734	45,840
Professional and management fees (Note 11)	89,510	83,195
Regulatory fees	15,868	24,315
Rent and property tax	56,356	55,350
Salaries, benefits and stock-based compensation	360,174	360,750
Total general and administrative	$ 555,928	$ 688,812
Business development and marketing:		
Advertising	$ 2,375	$ 13,520
Auto	13,939	14,085
Business promotion	6,998	12,301
Meals and entertainment	6,577	3,795
Office and general	8,182	9,263
Salaries and benefits	446,720	438,250
Trade shows	7,295	11,573
Travel	26,912	14,012
Total business development and marketing	$ 518,998	$ 516,799

13. Financial Instruments

The Company's financial instruments are exposed to certain financial risks, including currency risk, credit risk, interest rate, liquidity and funding risk.

Foreign exchange risk
Foreign currency risk is the risk that the fair values of future cash flows of a financial instrument will fluctuate because they are denominated in currencies that differ from the respective functional currency. The Company is exposed to currency risk as it incurs expenditures that are denominated in Canadian dollars while its functional currency is the United States dollar. The Company does not use hedges or derivative instruments to reduce its exposure to currency risk.

The following is an analysis of of financial assets and liabilities that are denominated in Canadian dollars:

	December 31, 2012	December 31, 2011
Cash deficiency	$ 7,729	$ 2,505
Trade receivables	134,863	97,936
Trade payables	614,616	780,256
Loans	105,591	120,387
Convertible debt notes	74,014	74,014
Due to related parties	437,567	312,273
	$ 1,374,380	$ 1,387,371

Based on the above net exposures, as at December 31, 2012, a 10% change in the Canadian dollar to United States dollar exchange rate would impact the Company's net loss by $130,000.

Liquidity risk
Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company has a planning and budgeting process in place to help determine the funds required to support the Company's normal operating requirements on an ongoing basis. At present, the Company does not have sufficient funds to pay its existing creditors or meet its short-term business requirements.

Historically, the Company's main sources of funding have been the issuance of equity securities for cash, debt instruments and bridge financing. The Company's access to financing is always uncertain. There can be no assurance of continued access to significant equity funding. Liquidity risk is considered to be high.

Credit risk
Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is exposed to moderate credit risk due to concentration of the majority of its trade receivables with a small number of customers. As at December 31, 2013, there are two customers that represent approximately 20% and 9% of its revenue. Four customers represent approximately 63% of trade receivables. Management performs a periodic assessment of the credit worthiness of customers to reduce exposure to credit risk.

Fair value
The fair value of the Company's financial assets and liabilities approximates the carrying amount.

14. Capital Management

The capital structure of the Company consists of equity and debt obligations, net of cash. The Company manages its cash, trade receivables and loans in conjunction with budgeted or expected capital needs. The Company's objective when managing capital is to maintain sufficient liquidity to continue to meet ongoing expenditure and operational needs.

The Company is not subject to externally imposed capital requirements other the loan arrangement as described in Note 8.

There were no changes in the Company's approach to capital management during the year.

(Expressed in Canadian dollars)

15. Segment Disclosure

During the year ended December 31, 2013, $1,604,035 (2012 - $2,200,088) of the Company's revenue was earned from customers domiciled in the USA.

16. Income Taxes

Income tax recovery attributable to net loss before income tax recovery differs from the amounts computed by applying the combined Canadian federal and provincial income tax rate of 25.0% to income before income taxes as follows:

		2013		2012
Net loss for the year	$	(490,895)	$	(538,515)
Statutory tax rate		25.0%		25.0%
Expected income tax recovery	$	(122,724)	$	(134,629)
Tax effect on:				
Permanent differences and other		-		(94,033)
Impact of tax rate changes		-		(92,162)
Change in valuation allowance		122,724		214,920
Income tax recovery	$	-	$	-

The Company has the following deductible temporary differences for which no deferred tax asset has been recognized:

		December 31, 2013		December 31, 2012
Non-capital loss carry-forwards	$	1,858,000	$	1,736,000
Equipment		45,000		44,000
	$	1,903,000	$	1,780,000

The tax pools relating to these deductible temporary differences expire as follows:

		Canadian non-capital losses
2014	$	695,000
2015		596,000
2026		778,000
2027		318,000
2028		736,000
2029		488,000
2030		1,127,000
2031		962,000
2032		500,000
2033		490,000
	$	6,690,000