

Smartcool Systems Inc. (TSX-V: SSC) Management's Discussion and Analysis

2016 Annual Report



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Management’s Discussion and Analysis

The following is management’s discussion and analysis (“MD&A”) of the operating and financial results of Smartcool Systems Inc. for the year ended December 31, 2016. This information is provided as of May 1, 2017.

This MD&A should be read in conjunction with the Company’s audited consolidated financial statements for the years ended December 31, 2016 and 2015 together with accompanying notes. These documents and additional information about Smartcool can be located on the SEDAR website at www.sedar.com or the Company’s website at www.smartcool.net.

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Business Overview

Smartcool Systems Inc. is a clean technology company specializing in the development and distribution of energy efficiency solutions for air conditioning, refrigeration and heat pump systems (HVACR).

Smartcool was established in 2004, beginning as the North American distributor for the Energy Saving Module (ESM)™, a unique energy efficiency retrofit developed by Abbotly Technologies Pty Ltd of Australia. In 2006, Smartcool purchased the assets of Abbotly, including the intellectual property of the ESM™, and became the sole manufacturer and master distributor. In 2009, Smartcool’s research and development culminated in the delivery of the ECO³™ to market, a new product specifically designed to bring unprecedented energy efficiency to small scale HVACR systems. In late 2015, with the signing of the licensing agreement with Connected Holdings Llc., development began on the natural evolution of the product line, incorporating wireless communication. Beta versions of the new product have commenced to be tested in the market place with an expectation that a final product will be available to our customers and prospective customers in the 3rd Quarter of 2017.

While 2016 was an extremely challenging year for revenue generation, several new initiatives by the company combined with changing trends in the energy markets, give management optimism that the company will weather the challenges and provide shareholders with positive results in the near term. Generally, the company has a greater chance of success based on faster ROI’s (Returns on Investment) for the client. These ROI’s are directly impacted by both the company’s selling price and the cost of energy. Worldwide utility rates have been on the rise, with many geographic areas experiencing substantial hikes in energy costs. This raises the customers awareness of energy costs as a portion of their costs of operations resulting in increased interest in energy efficiency and faster ROI’s. Management believes that this will yield greater opportunities for the company.

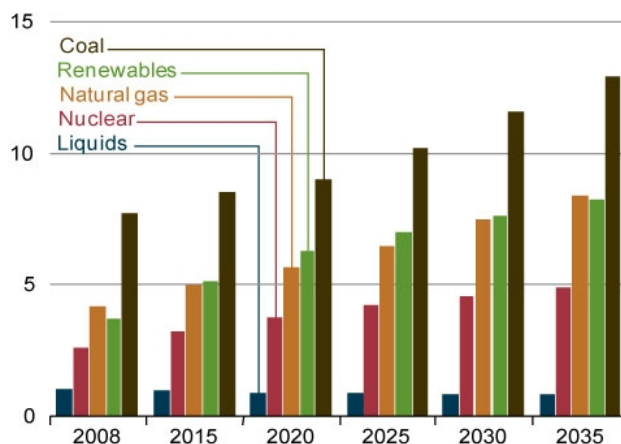
Management has also sought to add complimentary technologies to the product mix providing a more wholistic approach to energy efficiency solutions. To this end, the company’s distributor relationship with ATI Airtest Technologies Inc., has generated some sales of its CO2 sensors for the Demand Control Ventilation (DCV) protocol. Initial customer feedback has been very positive and Management believes this will generate additional follow on opportunities to grow this product revenue.

Other complimentary products and services are currently under review with some very promising possibilities. Management is continuing to evaluate some of these that could generate add on revenues and profitability from the existing client base.

Energy Issues

Smartcool has focused on developing energy efficiency solutions to address the critical energy issues facing the world today and in the future.

**EIA World Net Electricity Generation by Fuel
2008-2035**
(in trillion kWh)



Electricity is a crucial part of the global economy and our communities. The worldwide demand for electricity has increased by 5.4% since 2010, with developing countries averaging a 9.5% growth in demand. Coal continues to be the most widely used fuel for electricity generation, followed by natural gas. Electricity generated by these fossil fuels releases vast amounts of greenhouse gases into the atmosphere, contributing to climate change and general air pollution.

An instinctive solution is to switch to renewable energy sources, not only for environmental reasons but also due to issues of energy security. Electricity generation by renewable resources such as hydro, wind, waves and solar is increasing by an average of 3% each year thanks to government incentives. However, as the Energy Information Administration explains, “Although renewable energy sources have positive environmental and energy security attributes, most renewable technologies other than hydroelectricity are not able to compete economically with fossil fuels during the projection period except in a few regions or in niche markets.”¹

On average, residential electricity rates around the globe have increased by 150% from 2005 to 2008.² Combined with environmental concerns surrounding fossil fuel generated electricity, it is clear that a solution to high energy consumption is urgently needed. Energy efficiency is the only option which is both cost effective and can be implemented rapidly.

Smartcool’s Energy Efficiency Solutions

Smartcool focuses on reducing the electricity used by refrigeration, air conditioning and heat pumps (HVAC). For target customer industries, such as supermarkets, these systems consume well over 50% of their total energy usage. Even for customers less dependent on HVAC, the systems still account for roughly 20% of their energy bill. The ability to save energy with Smartcool’s energy efficiency technology represents a major opportunity to cut operating expenses for any customer, typically giving them a return on their investment averaging 18 to 36 months. Electricity generated for buildings produces more greenhouse gases than any other source, so cutting HVAC energy consumption can also have a significant impact on the environment.

Smartcool’s ECO³™ and ESM™ are retrofit products, meaning that they are installed by wiring in between the existing thermostat and the compressor in the HVAC system, rather than replacing any expensive equipment. Once installed, the products immediately begin monitoring the cooling cycle of the compressor to identify inefficiencies and opportunities for saving energy. Even the most modern systems have pre-existing inefficiencies that can only be resolved by the intellectual property provided in Smartcool’s products. The ECO³™ and ESM™ dynamically adjust the cooling cycle to save customers energy without any impact to the temperature performance of the HVAC system.

The ECO³™



The ESM™



With the ECO³™ and ESM™, customers see all the benefits of energy efficiency, without any risks. The technology has undergone extensive independent third party testing by highly reputable organizations such as Oak Ridge National Laboratories,

¹Administration, *International Energy Outlook 2011*, Published Sept. 19, 2011

[ecasts/ieo/electricity.cfm](http://www.eia.gov/energy_outlook/energy_outlook/casts/ieo/electricity.cfm)

²Administration, *Electricity Prices for Households*, Updated June 10, 2010

<http://www.eia.gov/emeu/international/elecprh.html>

the University of Miami for Florida Power & Light, and the Los Angeles Department of Power & Water. These tests have proven unequivocally that the technology provides energy savings with no risks, as do over 30,000 installations worldwide.

For more information on Smartcool's technology, visit www.smartcool.net or for information specific to the ECO³™, visit www.smartcooleco3.com

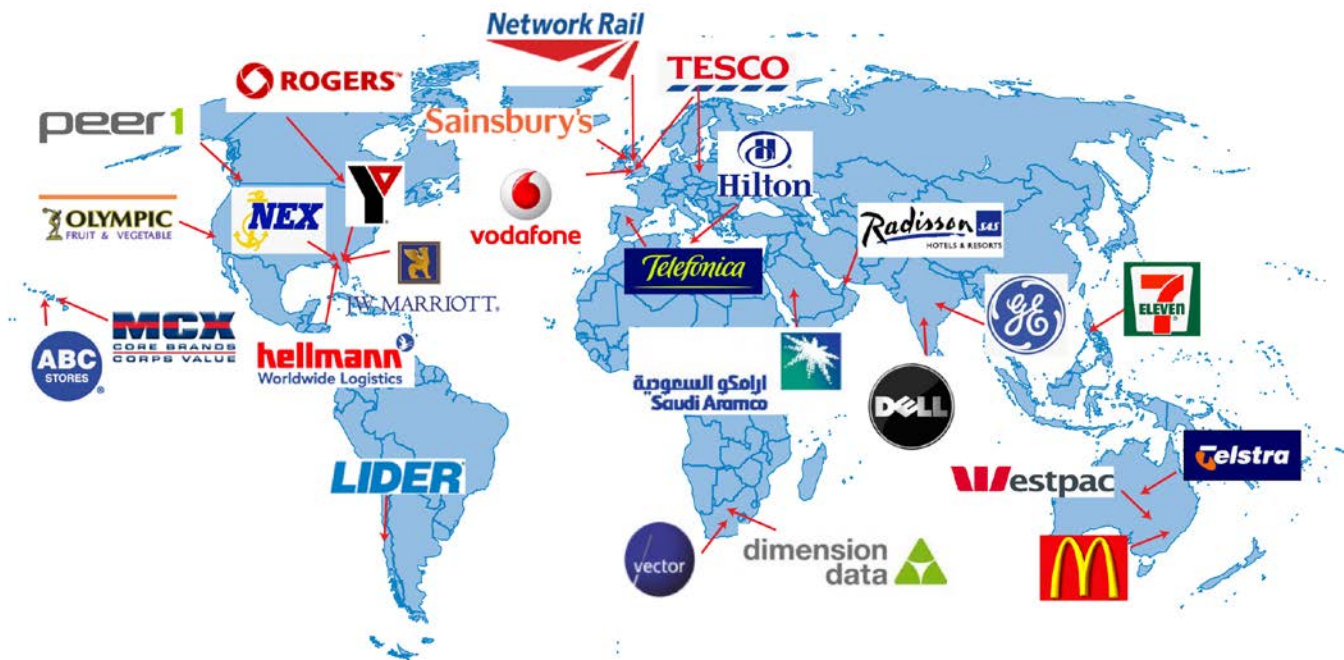
The Market Strategy

Smartcool's ECO³™ and ESM™ are cost effective energy efficiency solutions for any air conditioning, refrigeration or heat pump system. The few other energy efficiency products geared towards the HVAC market, do not offer the full package of benefits that the ECO³™ and ESM™ provide. Other products on the market do not provide the same degree of safety, and can cause temperature and humidity performance to be affected. They all lack the wide range of compatibility held by the ECO³™ and ESM™, which can be installed on any HVAC system. Perhaps most significantly, other products cannot easily prove consistent energy savings. Smartcool's energy savings can be instantly verified on the product display screens, letting customers monitor energy savings as they happen. This is a critical feature for utility rebate qualification, which Smartcool has already received from major utilities like Florida Power & Light, Southern California Edison and Con Edison. These factors give Smartcool exclusive access to an immense market.

Direct Sales

The company distributes its products directly to major clients, providing them with superior project management and service as they roll out Smartcool products to their facilities. For direct sales, Smartcool targets specific industries such as food retailers, telecommunications, commercial real estate and hospitality, where HVAC energy usage tends to represent a very high percentage of a client's operating budget. In Europe, Smartcool has built a strong portfolio of direct sales through major electrical wholesalers like Rexel, utilities like EON and facilities management companies like Matrix and EMCOR. They have introduced Smartcool to their customers for energy efficiency solutions such as Scottish and Southern Energy and Transport for London.

With the success in the UK of developing sales directly to end users, often through intermediaries such as Facilities Managers and Utility Companies, it became clear to management that this model should be deployed in the North American market place. These initiatives commenced late in 2016 and Management expects this strategy to begin impacting both revenues and profits starting in the 2nd Quarter of fiscal 2017. With the addition of Haiwen (Helen) Qian and Frank Lawrence in sales and marketing roles, early indications from the new team suggest that this will be a successful strategy.



Distribution Sales

Smartcool has developed an intricate network of distributors to target regional markets. Distributors are provided both technical and sales training by Smartcool and receive ongoing support. Distributors have the advantage of detailed regional knowledge, allowing them to build strong client portfolios across the residential sector as well as in industries like food retail, climate controlled storage, hospitality and commercial real estate. Smartcool’s distributors have continued to expand their businesses in Australia, India, UAE, Saudi Arabia, Eastern Europe, France, South Africa, and the US (particularly Florida, California and the Mid-West). Distributors have also proven instrumental in launching key accounts for Smartcool, like Telefonica, GE Healthcare, Dell, Saudi Aramco, 7-Eleven, JW Marriott and more.

Corporate Structure

Smartcool has gone through several phases of growth to reach its current structure. Smartcool Systems Inc. is the publicly traded parent company, with three wholly owned subsidiaries: Smartcool International Inc., Smartcool Systems USA Inc. and Lenten Street Ltd. DBA Smartcool. Smartcool International holds the intellectual property and is the master distributor of Smartcool’s product line. Smartcool Systems USA distributes the technology within the United States, using a network of local distributors to deliver the products to market. Lenten Street distributes the technology in Europe, the Middle East, Africa and the Indian Sub-Continent with a focus on direct sales.

Financial Overview

Significant reduction of operating expenses was achieved as a result of effective cost management though revenue has not yet responded to tremendous marketing effort conducted during 2016.

Revenue decreased to \$325,976 from \$785,498 for the previous year, a decrease of \$459,522. Operating expenses decreased to \$1,887,132 from \$2,242,494 for the previous year, a decrease of \$355,362.

Total assets decreased to \$1,561,024 from \$2,437,023 at the end of the previous year. The Company had \$3,317 in cash and cash equivalents at the end of the year, compared to \$18,478 at the end of the previous year.

Current liabilities at the end of the year were \$1,966,938 (2015 - \$1,549,708) which includes current portion of acquisition obligations and debentures totaling \$572,866 (2015 - \$513,269). Long-term liabilities were \$219,282 (2015 - \$358,176), consisting of acquisition obligations \$67,857 and deferred tax liability of \$151,425.

All the fiscal quarters below have been prepared using IFRS.

	Mar 2016	Jun 2016	Sep 2016	Dec 2016
	(\$)	(\$)	(\$)	(\$)
Total revenues	142,497	26,854	81,547	75,078
Net income (loss)	(312,449)	(403,029)	(373,180)	(578,100)
Income (loss) per share – basic & diluted	(0.00)	(0.00)	(0.00)	(0.00)

	Mar 2015	Jun 2015	Sep 2015	Dec 2015
	(\$)	(\$)	(\$)	(\$)
Total revenues	189,666	181,855	126,602	287,375
Net income (loss)	(356,703)	(593,017)	(469,146)	(257,606)
Income (loss) per share – basic & diluted	(0.00)	(0.01)	(0.00)	(0.00)

Selected Annual Information

The following is selected information on Smartcool's financial performance for the past three years. This financial information is derived from the audited financial statements of the Company and has been prepared using IFRS.

	Dec. 31, 2014* (\$)	Dec. 31, 2015* (\$)	Dec 31, 2016* (\$)
Revenue	738,121	785,498	325,976
Selling, General & Administrative	1,367,476	1,449,091	1,277,676
Net Income (Loss)	(849,400)	(1,676,473)	(1,666,758)
Net income (loss) – per share (basic and diluted)	(0.01)	(0.00)	(0.00)
Total assets	2,525,695	2,437,023	1,561,024
Total long term liabilities	443,515	358,176	219,282
Cash dividends	-	-	-

* Continuing operations only

Summary of Operating Results

Revenue

Smartcool sells its products both directly to major customers and through a network of independent distributors.

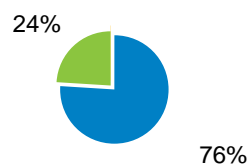
Distribution sales were \$93,362 or 29% of total revenue for the year, compared to \$668,281 or 85% of total revenue for 2015. Direct sales for the year were \$ 232,614 or 71% of total revenue compared to \$117,217 or 15% of total revenue for 2015.

Revenue by Channel



■ Distribution ■ Direct Channels

Revenue by Region



■ EMEA ■ Americas ■

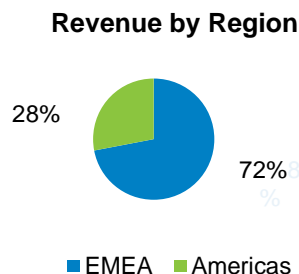
Revenue from the Americas for the year was \$76,735 or 24% of total revenue, compared to \$557,196 or 71% of total revenue for 2015. Revenue from the Europe, Middle East, and Africa for the year was \$249,241 or 76% of total revenue compared to \$228,302 or 29% of total revenue for 2015.

For the fourth quarter, distribution sales were \$26,883 or 36% of total revenue, compared to \$274,691 or 96% of total revenue for the same period of 2015. Direct sales were \$48,195 or 64% to total revenue, compared to \$12,684 or 4% of total revenue for the same period of 2015.

Revenue by Channel



■ Distribution ■ Direct ■



During the fourth quarter, the Americas contributed \$6,962 or 9% of total revenue compared to \$226,690 or 79% of total revenue for the same period of 2015. The EMEA (Europe, Middle East, and Africa) region contributed \$68,116 or 91% of total revenue compared to \$60,685 or 21% of total revenue for same period of 2015.

Gross profit

Gross profit for the year was \$239,736 compared to \$634,176 for 2015, a decrease of \$394,440 or 62%. Profit margin for the year was 74%, compared to 81% for 2015; both were within the expected range.

Gross profit for fourth quarter was \$52,889 compared to \$228,195 for the same quarter of 2015. Profit margin for the quarter was 70%, compared to 79% for the same quarter of 2015.

Though all margins were within the expected range, 2016 margins were lower than that of the previous year due to the smaller contribution of distribution sales to total revenue in 2016.

General and administrative expenses

General and administrative (“G & A”) expenses for the year were \$1,277,676, compared to \$1,449,091 for 2015, a decrease of \$171,415. The decrease was primarily attributable to the reduction of consulting fees, brought about by the termination of SmartACR consulting agreement in November 2015, along with broad improvement in other cost areas. Consulting fees decreased to \$336,777 from \$618,811 for the previous year, travel expenses decreased to \$73,127 from \$112,713, professional fees decreased to \$68,070 from \$98,902, and filing and listing fees decreased to \$28,515 from \$42,511. A large allowance for bad debts was recorded for the year, however, due to doubtful receivables.

	2016	2015
Advertising and promotion	\$2,185	\$11,927
Bad debts (recoveries)	162,350	(113,663)
Commissions	6,467	10,524
Consulting and management fees	336,777	618,811
Filing and transfer fees	28,515	42,511
Insurance	14,216	21,030
Interest	4,333	725
Investor relations	12,113	29,783
Product certification	4,869	6,832
Professional fees	68,070	98,902
Office and supplies	28,009	45,053
Rent	25,373	52,388
Salaries and benefits	493,055	490,946
Telephone	18,217	20,608
Travelling	73,127	112,713
Total general and administrative expenses	\$1,277,676	\$1,449,091

Total operating expenses for the year decreased to \$1,887,132 from \$ 2,242,494 for the previous year, a reflection of reduced business activities and lower share-based compensation costs.

	Three months ended December 31, 2016	Three months ended December 31, 2015
Advertising and promotion	\$943	\$1,762
Bad debts	162,350	(97,769)
Commissions	64	10,524
Consulting & management fees	93,452	137,288
Filing and transfer fees	2,760	1,055
Insurance	3,521	6,768
Interest	19	453
Investor relations	4,788	4,316
Product certification	1,638	2,238
Professional fees	49,085	40,399
Office and supplies	6,085	12,683
Rent	3,908	13,616
Salaries and benefits	105,887	123,564
Telephone	5,030	8,436
Travelling	26,396	27,677
Total general & administrative expenses	\$465,925	\$293,010

General and administrative (“G & A”) expenses for the fourth quarter were \$465,925, compared to \$293,010 for the same quarter of 2015, an increase of \$172,915. The increase does not indicate cost ineffectiveness as the previous year’s expenses included debt recoveries while a significant amount of bad debts was recorded for the current year. On the contrary, major expenses in the fourth quarter of the year decreased thanks to cost cutting measures. Salaries decreased to \$105, 887 from \$123,564 for fourth quarter of 2015 and consulting fees decreased to \$93,452 from \$137,288.

Net loss

Net loss for year was \$1,666,758 compared to net loss of \$1,676,473 for the previous year.

The loss per share (basic and diluted) for the year was \$0.013, compared to the loss per share \$0.015 for the previous year.

Loss per share is calculated based on the weighted average number of common shares outstanding throughout the year.

The fourth quarter recorded net loss of \$578,100 compared to net loss of \$257,606 for the same quarter of the previous year. The increase was attributable to allowance for bad debts.

Comprehensive loss

Comprehensive loss for the year was \$1,607,823 (2015 - \$1,671,321) consisting of net operating loss \$1,666,758 (2015 - \$1,676,473) and positive foreign currency translation adjustment \$58,935. (2015 - \$5,152). As the functional currencies of Smartcool USA and Lenten Street are different from the reporting currency (Canadian dollar), their monetary assets and liabilities as well as non-monetary assets and liabilities in the consolidated financial statements must be translated into the reporting currency based on December 31, 2016 exchange rate under IFRS. This method of foreign currency translation resulted in the above adjustment which is classified as a component of equity.

Comprehensive loss for the fourth quarter was \$548,330 compared to comprehensive loss of \$261,544 for the same quarter of 2015.

Amortization and depreciation

Amortization and depreciation expenses for the year were \$568,429 compared to \$586,173 for the previous year. Amortization on property and equipment was \$17,981 (2015 - \$26,474) and amortization of intangible assets was \$550,448 (2015 - \$559,699).

Amortization and depreciation expenses for the fourth quarter were \$142,176 compared to \$136,223 for the same quarter of 2015. Depreciation of property and equipment was \$4,564 (2015 - \$5,308) and amortization of intangible assets was \$137,612 (2015 - \$130,915).

Share-based compensation

Share-based compensation costs for the year was \$39,051, compared to \$206,253 for the previous year, a decrease of \$167,202. There were only 75,000 stock options granted during the year while 8,070,000 were granted in the previous year.

Share-based compensation costs for the fourth quarter were \$2,068, compared to \$5,136 for the same quarter of 2015, a decrease of \$3,068.

Capital expenditures

During the year, the Company made computer equipment purchases of \$2,943. Capital expenditures for the previous year were \$700.

Liquidity and Capital Resources

As at December 31, 2016, the Company had \$3,317 in cash and cash equivalents (December 31, 2015 - \$18,478). Negative working capital at December 31, 2016 was \$1,552,161 compared to \$824,492 at December 31, 2015.

The Company used net cash flow of \$661,456 during the year to finance operations and used \$1,176,010 in the previous year. The decrease in net cash used was primarily attributable to the collection of accounts receivable and increase in accounts payable.

The Company was unable to make debenture and acquisition obligation payments as scheduled. Debenture payments consist of monthly interest payments totaling \$35,650 and principal payments totaling \$244,924 (scheduled for March 31, 2016). Acquisition obligation payments consist of installments totaling \$233,553 (£141,000) scheduled for April 30-June 30, 2014 (£25,000), December 15,

2014 (£26,000), June 15, 2015 (£26,000), December 15, 2015 (£19,000), June 15, 2016 (£26,000), and December 15, 2016 (£19,000).

To ensure that Smartcool continues to be a going concern with adequate working capital in the next 12 months, the Company completed two private placements in June and September 2016 raising additional capital of \$455,000. The Company has revitalized its marketing strategy with the addition of a commission-based sales team. The closing of pending installation projections in the UK should provide adequate cash flow and financing will be contemplated if additional working capital is needed.

The timing of future payments related to financial liabilities is outlined in the table below:

	Total	1 year	1-2 years
Trade payables and accruals	\$ 837,349	\$ 837,349	\$-
Short-term loans	485,191	485,191	-
Obligations under acquisition contracts	360,149	292,292	67,857
Debentures	280,574	280,574	-
Total	1,963,263	\$1,895,406	\$ 67,857

Outstanding Share Data

The authorized share capital of the Company is an unlimited number of common shares without par value. As at December 31, 2016 the Company had 140,842,737 (2015 – 122,097,737) common shares outstanding. The weighted average number of common shares outstanding for the year was 131,864,244 (2015- 113,644,118). The weighted average number of common shares outstanding for the fourth quarter was 140,842,737 (2015 – 119,863,063).

As at April 28, 2017 the outstanding shares are 160,842,737 and diluted are 231,735,737.

Warrants and Stock Options

As at December 31, 2016, there were 43,175,000 (2015 – 45,845,000) share purchase warrants and 11,945,000 (2015 – 12,415,000) stock options outstanding which collectively could result in the issuance of 55,120,000 common shares if these warrants and stock options are exercised. The outstanding options have a weighted average exercise price of \$0.05. The outstanding warrants have weighted average exercise price of \$0.07.

As at December 31, 2016 there were 11,901,250 (2015 - 11,140,000) exercisable options with a weighted average exercise price of \$0.05 (2015 - \$0.05). During the year, 75,000 options were granted.

As at April 28, 2017, there are 59,423,000 outstanding warrants and 11,470,000 outstanding options. The outstanding options have weighted average exercise price of \$0.05.

Intangible Assets

a. *ESM™ Intellectual Property and worldwide distribution rights*

The Company acquired intangible assets in relation to the acquisition of Abbotly Technologies Inc. in March 2006.

During the year ended December 31, 2014, management performed a review of the carrying value of these assets. As discrepancies between revenue projections and actual operating results in 2014 resulted in significant uncertainty in future cash generation of these assets, an impairment loss of \$175,313 was recorded based on cash flow projections as at December 31, 2014.

b. *Distribution Rights from TECC Services*

In July 2008, the Company acquired the exclusive rights to distribute the ESM™ in the United Kingdom, Spain, Portugal, and the Middle East from T.E.C.C. Services Ltd. (“TECC”) (note 7).

c. *Intangible Assets from Smartcool UK*

In February 2011, the Company acquired intangible assets in relation to the acquisition of Smartcool UK. These intangible assets include the distribution rights of the ESM™ in the United Kingdom, the distribution right related to sales to a major customer and a customer relationship.

During the year ended December 31, 2014, management performed a review of the carrying value of these assets. As discrepancies between revenue projections and actual operating results in 2014 resulted in significant uncertainty in future cash generation of these assets, an impairment loss of \$528,716 (\$344,251 for distribution rights and \$184,465 for a customer relationship) was recorded based on cash flow projections as at December 31, 2014.

d. *SmartACR Intellectual Property and Customer Relationship*

In February 2015, the Company acquired \$25,000 of intangible assets in relation to the termination of a license agreement (note 12). These intangible assets include intellectual property (\$25,000) and a customer relationship (\$Nil).

Critical Accounting Policies & Estimates

Revenue Recognition

Revenue from the sale and installation of the ESMTM and ECO3TM is recognized when the ESMTM and ECO3TM have been installed, significant risks and rewards of ownership of the equipment have been transferred to the customer, the Company does not retain continuing managerial involvement or effective control over the equipment, the sales price can be determined and collection is probable, and the cost of the transaction can be measured reliably.

Revenue from the international distribution of the ESMTM and ECO3TM is recognized when the equipment has been shipped, title has been transferred, the sales price has been determined and the cost of the equipment can be measured reliably. Revenue is also recognized when equipment has been ordered and laid away as instructed by the customer, the sales price has been determined and a significant portion of it has been paid. Provisions are established for estimated warranty costs at the time revenue is recognized. The Company records deferred revenue when cash is received in advance of the above revenue recognition criteria being met.

Share-based Payments

The fair value of all stock options granted to employees is determined using the Black-Scholes Option Pricing Model, and the resulting value is charged to operations over the vesting period. Volatility rate is determined based on the trading history of the Company’s shares for the relevant period and interest rate is based on Canadian bond rates.

The fair value of options granted to non-employees is determined using the fair value of the goods or services received. The resulting value is charged to operations when a performance commitment is made or the options are fully vested and non-forfeitable, whichever is earliest, and the expense is recognized over the period in which the goods or services from the non-employees are received. To estimate the fair value of options granted to non-employees, management considers primarily the fees management would be willing to pay in cash for the service if no options were granted.

A corresponding increase in equity, the reserve for equity settled share-based transactions, is recorded when stock options are expensed. When stock options are exercised, share capital is credited by the sum of the consideration paid and the related portion previously recorded in the reserve is reversed. At the time of grant, the expense is determined based on estimated forfeiture rate. The expense will be adjusted to recognize the effect of actual forfeitures as they occur. The fair value of warrants issued to agents for their finder’s fee is based on the fair value of the services provided and charged to share issuance costs.

When the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based payment arrangement or is otherwise beneficial to the employee as measured at the date of modification.

Intangible assets

Intangible assets are recorded at cost and include the ESM™ brand, ESM™ intellectual property, distribution rights, distribution agreements, supplier agreements and customer relationships. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The ESM™ brand has been determined to have an indefinite life and is not amortized. The remaining intangible assets with finite lives are amortized on a straight-line basis. The useful lives of the intangible assets have been assessed as follows:

Intellectual property - ESM™	13.5 years
Intellectual property - SmartACR	10 years
Distribution rights - North American	10 years
Distribution rights - TECC and United Kingdom	9.5 - 12 years
Distribution agreements	13.5 - 15 years
Supplier agreements	13.5 years
Customer relationship	12 years

Residual value and estimated useful lives are reviewed annually. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates.

Use of estimates and judgments

The preparation of these consolidated financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from these estimates. It also requires management to exercise judgement in applying the Company's accounting policies. These consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout these consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and further periods if the revision affects both current and future periods.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the consolidated statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

- Allowance for doubtful accounts – as at December 31, 2015, approximately \$186,000 in trade receivables was outstanding for more than 120 days. This balance is primarily receivable from one customer. It is management's opinion, based on an assessment of the customer's business, the payment plan in place and payment received subsequent to year end that this balance will be received in full.

Critical judgments in applying the Company's accounting policies relate to, but are not limited to, the following:

- Useful lives of intangible assets with finite lives – the determination that there are no indicators suggesting that the useful lives and/or that the method of calculating amortization require revision;
- Unlimited life of the ESM brand – the determination that useful life of the ESM brand remains unlimited;
- Impairment of intangible assets – the determination that there are no indicators of impairment indicating that the carrying amount exceeds the recoverable amount;
- Analysis of the functional currency for each entity of the Company; and
- Ability to continue as a going concern – the determination that the Company will continue as a going concern for the next year.

Off-balance sheet arrangements

The Company has no off-balance sheet arrangements that would require disclosure.

Forward-looking statements

This MD&A contains forward-looking information and statements regarding the future results of operations and marketing activities. Forward-looking statements generally can be identified by the use of forward-looking terminology such as “may”, “will”, “expect”, “intend”, “anticipate”, “plan”, “foresee”, “believe” or similar terminology. Although these forward-looking statements are based on what management believes to be current and reasonable assumptions, they involve known and unknown risks, uncertainties and other factors that may cause the actual results and performance to differ materially from those stated, anticipated, or implied in these forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking information as no assurances can be given to future results, performances, or achievements.

The forward-looking statements included in this MD&A speak only as of the date of this document. The Company does not undertake any obligation to publicly update or revise any of these forward-looking statements to reflect events or circumstances after this date except when required by applicable legislation.

Additional Information

Additional information relating to the Company, including the Company’s latest Annual Financial Statements and news releases can be located on the Company’s website at www.smartcool.net or on the SEDAR website at www.sedar.com.