SMARTCOOL™

Smartcool Systems Inc. (TSX-V: SSC)
Condensed Consolidated Financial Statements

For the three months ended March 31, 2017 and 2016

Expressed in Canadian Dollars

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Smartcool Systems Inc.
Consolidated statements of financial position
(Expressed in Canadian dollars, unless otherwise stated)
(unaudited)

	March 31 2017	December 31 2016
	$	$
ASSETS		
Current assets		
Cash and cash equivalents	31,119	3,317
Available-for-sale securities	12,316	8,210
Trade and other receivables (note 3)	181,826	211,499
Inventory (note 4)	142,978	140,979
Prepaid expenses and deposits	50,311	50,772
	418,550	414,777
Property and equipment	3,960	3,728
Intangible assets (note 5)	1,004,907	1,142,519
Total assets	1,427,417	1,561,024
LIABILITIES		
Current liabilities		
Trade payables and accruals	801,296	908,881
Short-term loans (note 6)	455,463	485,191
Current portion of obligations under acquistion contracts (note 7)	296,935	292,292
Current portion of debentures (note 8)	259,068	280,574
	1,812,762	1,966,938
Obligations under acquisition contracts (note 7)	71,013	67,857
Deferred tax liability (note 10)	138,729	151,425
Total liabilities	2,022,504	2,186,220
SHAREHOLDERS' EQUITY		
Share capital (note 9(a))	31,931,190	32,081,862
Shares pending issue	-	-
Reserve for equity settled share based transactions (note 9(b))	7,185,021	6,643,640
Accumulated other comprehensive income	(321,370)	(321,719)
	38,794,841	38,403,783
Deficit	(39,389,928)	(39,028,979)
	(595,087)	(625,196)
Total liabilities and shareholders' equity (deficiency)	1,427,417	1,561,024

Approved and authorized for issue by the Board of Directors on May 30, 2017

"Theodore Konyi"	"Dalton Larson"
Theodore Konyi	Dalton Larson

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.

Consolidated statements of operations

(Expressed in Canadian dollars, unless otherwise stated)
(unaudited)

	Three months ended March 31	
	2017	**2016**
	$	$
Revenue	85,957	142,497
Cost of sales	26,143	34,017
Gross profit	59,814	108,480
Operating Expenses		
General and administrative expenses (note 15)	265,646	268,880
Amortization and depreciation (note 5)	138,186	142,124
Share-based compensation (note 9(b))	184	18,785
Research and development	-	-
	404,016	429,789
Operating loss	(344,202)	(321,309)
Finance expense	(33,247)	(30,657)
Foreign exchange gain (loss)	4,995	26,822
	(28,252)	(3,835)
Loss before income tax	(372,454)	(325,144)
Income tax recovery	11,505	12,696
Net loss for the period, net of tax	**(360,949)**	**(312,448)**
Net loss per share		
Basic	(0.00)	(0.00)
Diluted	(0.00)	(0.00)
Weighted average number of common shares outstanding (basic and diluted)	**144,620,515**	**122,848,848**

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Consolidated statements of comprehensive loss

(Expressed in Canadian dollars, unless otherwise stated)
(unaudited)

	Three months ended March 31	
	2017	**2016**
	$	**$**
Net loss for the period	**(360,949)**	**(312,448)**
Other comprehensive loss	350	1,614
Total comprehensive loss	**(360,599)**	**(310,834)**

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.
Consolidated statements of cash flows

(Expressed in Canadian dollars, unless otherwise specified)
(unaudited)

	Three months ended March 31	
	2017	**2016**
	$	$
Cash flows from operating activities		
Net loss for the period	(360,949)	(312,448)
Items not affecting cash:		
Depreciation of property and equipment	574	4,512
Amortization of intangible assets	137,612	137,612
Share-based compensation	184	18,785
Deferred tax liability	(12,696)	(12,696)
Foreign exchange (gain) loss	1,771	(36,351)
Accrued interest on short-term loans	16,704	8,100
Accrued interest on debentures	(21,506)	13,000
Accretion of obligation under acquisition contract	4,839	7,567
	(233,468)	(171,919)
Changes in non-cash working capital items:		
Trade and other receivables	29,673	45,125
Inventory	(1,999)	(96,833)
Prepaid expenses and deposits	461	56,030
Trade payables and accruals	(107,585)	112,102
Net cash flows used in operating activities	(312,918)	(55,495)
Cash flows from financing activities		
Shares and warrants issued for cash net of issue costs	390,525	-
Short-term loan	(46,049)	50,000
Net cash (used in) provided by financing activities	344,476	50,000
Net decrease in cash and cash equivalents	31,558	(5,495)
Effects of exchange rates changes on cash	(3,756)	(2,439)
Cash and cash equivalents, beginning of period	3,317	18,478
Cash and cash equivalents, end of period	31,119	10,544

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Consolidated statements of shareholders' equity (deficiency)
(Expressed in Canadian dollars, unless otherwise stated)

(unaudited)

	Share capital	Reserve for equity settled share based transactions	Share pending issue	Accumulated other comrprehensive income	Deficit	Total Shareholders' Equity (Deficiency)
	$	$	$	$	$	$
Balance at January 1, 2016	**31,672,684**	**6,547,080**	**52,250**	**(380,654)**	**(37,362,221)**	**529,139**
Net loss					(312,448)	(312,448)
Available-for-sale securities unrealized loss				4,053		4,053
Foreign currency translation adjustment				(2,439)		(2,439)
Total comprehensive loss for the period				1,614	(312,448)	(310,834)
Shares issued for:						
Private placement	4,387	(4,387)				-
Warrants exercised						-
Shares subscribed						-
Warrants						-
Share issue costs	(612)					(612)
Share-based compensation		18,785				18,785
Balance at March 31, 2016	**31,676,459**	**6,561,478**	**52,250**	**(379,040)**	**(37,674,669)**	**236,477**
Net loss					(1,354,310)	(1,354,310)
Available-for-sale securities unrealized loss				12,002		12,002
Foreign currency translation adjustment				45,319		45,319
Total comprehensive loss for the period				57,321	(1,354,310)	(1,296,989)
Shares issued for:						
Private placement	366,375					366,375
Warrants exercise						-
Shares subscribed						
Warrants		64,424				64,424
Warrants pending issue	52,250		(52,250)			-
Share issue costs	(13,222)	(2,528)				(15,750)
Share-based compensation		20,266				20,266
Balance at December 31, 2016	**32,081,862**	**6,643,640**	**-**	**(321,719)**	**(39,028,979)**	**(625,196)**
Net loss					(360,949)	(360,949)
Available-for-sale securities unrealized gain				4,105		4,105
Transfer to statement of operations on sale of available-for-sale securites						-
Foreign currency translation adjustment				(3,756)		(3,756)
				349	(360,949)	(360,600)
Shares issued for:						
Private placements	255,400	145,840				401,240
Warrants						-
Warrants' term extension	(399,215)	399,215				-
Share issue costs	(6,857)	(3,858)				(10,715)
Share-based compensation		184				184
Balance at March 31, 2017	**31,931,190**	**7,185,021**	**-**	**(321,370)**	**(39,389,928)**	**(595,087)**

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Notes to the Consolidated Financial Statements
For the three months ended March 31, 2017
(expressed in Canadian dollars, except where otherwise indicated)

1. Nature of Operations and Going Concern

Smartcool Systems Inc. ("Smartcool" or the "Company"), was incorporated on August 31, 2000 under the Canada Business Corporations Act and changed its name to Smartcool Systems Inc. on July 20, 2004.

In 2004, the Company incorporated a wholly-owned subsidiary, Smartcool Systems (USA) Inc. ("Smartcool USA"), in Nevada. In 2006, a wholly-owned subsidiary Smartcool International Inc. ("Smartcool International") was incorporated in Barbados. In 2008, a wholly-owned subsidiary, Smartcool Systems (EMEA) Ltd. ("Smartcool EMEA"), was incorporated in England. In 2011, Smartcool EMEA acquired all of the outstanding shares of Smartcool Systems UK ("Smartcool UK"), also headquartered in England.

Smartcool EMEA and Smartcool UK were discontinued through voluntary liquidation in September 2014 and a new wholly-owned subsidiary, Lenten Street Limited ("Lenten Street"), was incorporated in England in October 2014.

The Company's shares are listed on the TSX Venture Exchange and the head office, principal address, and registered office is located at 2848 W. 22nd Avenue, Vancouver, B.C.

Smartcool and its subsidiaries are focused on acquiring, commercializing, and marketing energy saving technologies for commercial and retail businesses. Currently the Company has two principal revenue streams: the sale and installation of the ESM™ and ECO3™ to end customers and to distributors worldwide.

The ESM™ is manufactured by a third party in Australia and is designed specifically to reduce the electricity consumption and maximum demand of refrigeration and air conditioning compressors by improving their performance and maintaining temperature control. The ESM™ uses microprocessor technology and software algorithms.

Introduced in early 2009, the ECO3™ is manufactured in China and is a simple retrofit product that can be installed on any air conditioning, heat pump or refrigeration unit with one or two compressors, achieving the same energy efficiency gains as the ESM™ for these smaller systems.

During the three months ended March 31, 2017, the Company had a net loss of $360,949 compared to $312,448 for the same period of the previous year.
The company had a deficit of $39,389,928 as at March 31, 2017 (December 31, 2016 - $39,028,979). As at March 31, 2017, the Company had negative working capital of $1,394,212 (December 31, 2016 - $1,552,161). This increase in working capital was attributable to equity financing obtained through a non-brokered private placement in March 2017, partially offset by operating loss. To ensure that the Company continues to be a going concern over the next twelve months a new commission-based sales

network in North America has been established to generate recurring revenue. The Company also announced a second private placement to raise additional capital of $300,000 in April 2017 (note 17).

The Company's ultimate success and the recoverability of its assets will depend on the Company's ability to successfully execute its business plan which includes a growing market for its products, achieving profitable operations, meeting its business acquisition obligations, the continued support of the Company's shareholders and employees, and the continued support from creditors with whom negotiations have been made and waivers obtained.

Management is aware, in making its assessment, that these material uncertainties are related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. These consolidated financial statements do not reflect adjustments to the carrying value of assets and liabilities which may be required should the Company be unable to raise adequate financing or meet current obligations and therefore be unable to continue as a going concern.

2. Significant Accounting Policies

Basis of Presentation and Statement of Compliance

The condensed consolidated interim financial statements of the Company for the three month ended March 31, 2017 comprise the Company and its subsidiaries. These condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards 34, Interim Financial Reporting. They do not include all the necessary annual disclosures as prescribed by International Financial Reporting Standards and should be read in conjunction with the annual audited consolidated financial statements as of December 31, 2016.

The Company's condensed consolidated interim financial statements have been prepared on the historical cost basis except for certain financial instruments which are measured at fair value, as explained in Note 15, and are presented in Canadian dollars except where otherwise indicated.

Significant Accounting Judgments, Estimates and Assumptions

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:

- The determination of sales and related costs used in the cash flow projections for the purpose of assessing the carrying amount of the intangible assets.

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.

Basis of Consolidation

The Company consolidates subsidiaries controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of the subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Smartcool USA, Smartcool International and Lenten Street. They also include the accounts of Smartcool EMEA from April 2008 and Smartcool UK from February, 2011, until they were discontinued through voluntary liquidation in September 2014. All inter-company transactions, balances, revenues and expenses, have been eliminated. The financial statements of the subsidiaries are prepared for the same reporting period as the parent Company, using consistent accounting policies, in all material aspects.

Revenue Recognition

Revenue from the sale and installation of the ESM™ and ECO3™ is recognized when the ESM™ and ECO3™ 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 ESM™ and ECO3™ 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

a. ***Research and development***

Research costs are expensed as incurred. Development costs are expensed as incurred unless they can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Company intends to and has sufficient resources to complete development and to use the asset.

b. ***Goodwill***

Goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognized in the statement of operations.

c. ***Other 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 on a periodic basis. 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.

Impairment

a. *Property, equipment and intangible assets with a finite useful life*

Property, equipment and intangible assets with a finite life are assessed for indications of impairment at the end of each reporting period. If such indications exist, then the recoverable amount of the asset or cash-generating unit ("CGU") is estimated.

An impairment loss is recognized when the carrying amount of the asset or CGU exceeds its recoverable amount. A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of cash inflows from other assets or groups of assets. The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and risks specific to the asset or CGU.

Impairment losses recognized in respect to CGU's are first allocated to reduce the carrying amount of any goodwill allocated to the CGUs, and then to reduce the carrying amount of the other assets in the unit on a pro-rata basis. Impairment losses are recognized in profit or loss for the period they are identified.

b. *Intangible assets with an indefinite useful life*

Intangible assets with an indefinite life are reviewed and tested for impairment annually, or more frequently, if events or changes in circumstances indicate that the asset might be impaired. The asset is written down when the carrying amount exceeds its recoverable amount. The ESM™ brand is considered to have an indefinite life as the Company has a global market and there is no direct competition for its instinctive green technology.

c. *Financial assets*

Financial assets, other than those at fair value through profit and loss ("FVTPL"), are assessed for indicators of impairment at each period end. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Impairment of financial assets carried at amortized cost, is the difference between the asset's carrying amount and the present value of the estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of all financial assets, excluding trade and other receivables, is directly reduced by the impairment loss. Uncollectible amounts in trade and other receivables are written off against the allowance account.

Available-for-sale financial assets are impaired if the cost (net of any principal payment and amortization) is greater than the current fair value, less any impairment previously recognized.

Reversal of Impairment

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized. An impairment loss with respect to goodwill is never reversed.

For all other financial assets carried at amortized cost in which impairment was previously recognized, if subsequent measurement indicates that the recorded impairment has decreased, and the decrease can be related objectively to an event occurring after the impairment was recognized, then the reversal of the impairment is recognized in the statement of operations. On the date of the impairment reversal, the carrying value of the financial asset cannot exceed its amortized cost had impairment not been recognized.

Financial Instruments

a. ***Financial assets***

The Company classifies its financial assets in the following categories: FVTPL, held to maturity investments, available-for-sale financial assets, and loans and receivables. The classification depends on the nature and purpose for which the financial assets were acquired. Management determines the classification of financial assets at initial recognition.

i. **Financial assets at FVTPL**

Financial assets are classified as FVTPL when the financial asset is held for trading or is designated as FVTPL on initial recognition.

A financial asset is classified as held for trading when it is purchased and incurred with the intention of generating profits in the near term, part of an identified portfolio of financial instruments that the Company manages and has an actual pattern of short-term profit-taking, or is a derivative that is not designated and effective as a hedging instrument.

Financial assets classified as FVTPL are stated at fair value with any resulting gain or loss recognized in profit or loss. Transaction costs are expensed in the period in which the costs are incurred.

The Company's only financial asset classified as FVTPL is cash and cash equivalents.

Cash and cash equivalents consist of cash on deposit and highly liquid investments that are readily convertible into cash with maturities of three months or less when purchased. The Company did not hold any cash equivalents as at March 31, 2017 and December 31, 2016.

ii. Held to maturity investments

Held to maturity investments are measured at amortized cost using the effective interest rate method. Transaction costs are added and amortized to the statement of operations over the life of the financial instrument on an effective yield basis.

The Company classifies short-term investments of interest bearing term deposits with maturity dates of more than three months as held to maturity investments. Interest on these term deposits is recognized in the statement of operations using the effective interest method.

The Company did not hold any held-to-maturity investments as at March 31, 2017 and December 31, 2016.

iii. Available-for-sale financial assets

Financial assets classified as available-for-sale are carried at fair value (where determinable based on market prices of actively traded securities) with changes in fair value (being unrealized gains or losses) recorded as a component of accumulated other comprehensive income. On disposal of, or if there is an other-than-temporary impairment of, an available for sale financial asset, the deferred cumulative amount included in accumulated other comprehensive income relating to that particular financial asset is recognized in gain or loss in the statement of operations.

As at March 31, 2017, the Company held common shares of ATI Airtest Technologies Inc., a venture company traded on the TSX Venture exchange with market value of $12,316 (December 31, 2016 – $8,210).

iv. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortized cost using the effective interest method, less any impairment.
The Company classifies trade and other receivables as loans and receivables.

v. Derecognition of financial assets

A financial asset is derecognized when the contractual right to the asset's cash flows expires or if the Company transfers the financial asset and substantially all risks and rewards of ownership to another entity.

b. *Financial Liabilities*

Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

i. **Other financial liabilities**
Other financial liabilities are initially measured at fair value, net of transaction costs, and subsequently measured at amortized cost, with any resulting premium or discount from the face value being amortized to income or expense using the effective interest method.

The Company classifies trade payables and accruals, loans and advances, obligations under acquisition contracts and debentures as other financial liabilities.

ii. **Derecognition of financial liabilities**
The Company derecognizes financial liabilities when, and only when, the Company's obligations are discharged, cancelled, or expired. A substantial modification of the terms of a financial liability or a part of it is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount of the financial liability extinguished and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognized in profit or loss.

Share Purchase Warrants

The Company issues common shares and share purchase warrants as a unit as well as units of debenture and share purchase warrants. The unit price is allocated to common shares and warrants based on their relative fair values. The residual method is used to allocate the value of debentures and warrants. The fair value of common shares is the market price on the date of issue and the fair value of warrants is determined using the Black-Scholes Option Pricing Model. Because the Black-Scholes Option Pricing Model requires the input of highly subjective assumptions, including the volatility of share price, changes in subjective input assumptions can materially affect the fair value estimate.

The Company also issues warrants to agents as compensation for services. The fair value of these warrants is determined to be the difference between agent's standard all-cash compensation and compensation with warrants. Warrants are also issued as non-cash consideration for business acquisitions. The fair value of these warrants is determined based on Black-Scholes Option Pricing Model.

Changes in Accounting Policies

As of January 1, 2017, the Company adopted the following IFRS standards and amendments:

Standard	Title
IAS 1 (Amendments)	Presentation of financial statements (amendments)

Accounting Standards Issued but not yet Effective

At the date of authorization of these consolidated financial statements, the IASB and IFRIC have issued new and revised standards and amendments which are not yet effective. Below is a list of new standards that are likely to be relevant to the Company. However, management has yet to assess the impact of these standards on the Company's operations:

Standard	Title	Applicable for financial years beginning on/after
IFRS 9	Financial instruments	January 1, 2018
IFRS 15	Revenue from contracts with customers	January 1, 2018
IFRS 16	Leases	January 1, 2019

3. Trade Receivables

	March 31, 2017	**December 31, 2016**
Trade receivables, net of allowances for doubtful accounts	$ 171,909	$ 196,219
Other receivables	9,917	15,280
	$ 181,826	**$211,499**

As at March 31, 2017, the allowance for doubtful accounts was $156,539 (US$117,504) (2016 - $157,772).

Other receivables includes $5,000 (2016 - $5,000) from the former President of the Company relating to an advance for travel expenses.

4. Inventory

	March 31, 2017	**December 31, 2016**
ESM™ ECO3™	$139,819	$ 137,820
Other products	3,159	3,159
	$ 142,978	**$140,979**

During the three months ended March 31, 2017, total inventories of $3,339 were recognized as costs of sales (March 31, 2016 - $3,652).

5. Intangible Assets

Indefinite Lives

As at March 31, 2017, ESM™ brand (b) had a carrying value of $56,100 (2016 - $56,100) and is not subject to amortization due to having an indefinite useful life.

Definite Lives

Cost

	North American distribution rights	Intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1, 2015	**$ 286,718**	**$124,100**	**$1,861,742**	**$113,651**	**$5,152,218**	**$1,211,369**	**$8,749,798**
Acquisition	-	25,000	-	-	-	-	25,000
Effect of change in foreign exchange rates	40,302	-	-	-	-	-	40,302
Balance at December 31, 2015	**327,020**	**149,100**	**1,861,742**	**113,651**	**5,152,218**	**1,211,369**	**8,815,100**
Effect of change in foreign exchange rates	(7,434)	-	-	-	-	-	(7,434)
Balance at December 31, 2016	**$ 319,586**	**$149,100**	**$ 1,861,742**	**$113,651**	**$5,152,218**	**$1,211,369**	**$ 8,807,666**
Effect of change in foreign exchange rates	(1,890)						(1,890)
Balance at March 31, 2017	**$ 317,696**	**$149,100**	**$ 1,861,742**	**$113,651**	**$5,152,218**	**$1,211,369**	**$8,805,776**

Accumulated Amortization and Impairment

	North American distribution rights	Intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1, 2015	**$286,718**	**$93,074**	**$1,399,027**	**$85,243**	**$3,758,735**	**$955,435**	**$6,578,232**
Amortization	-	8,291	119,706	5,680	374,834	51,188	559,699
Effect of change in foreign exchange rate	40,302	-	-	-	-	-	40,302
Balance at December 31, 2015	**327,020**	**101,365**	**1,518,733**	**90,923**	**4,133,569**	**1,006,623**	**7,178,233**
Amortization	-	8,708	119,812	5,684	365,056	51,188	550,448
Effect of change in foreign exchange rate	(7,434)	-	-	-	-	-	(7,434)
Balance at December 31, 2016	**$319,586**	**$110,073**	**$ 1,638,545**	**$ 96,607**	**$4,498,625**	**$ 1,057,811**	**$7,721,247**
Amortization	-	2,177	29,953	1,421	91,264	12,797	137,612
Effect of change in foreign exchange rate	(1,890)						(1,890)
Balance at March 31, 2017	**$317,696**	**$112,250**	**$1,668,498**	**$98,028**	**$4,589,889**	**$1,070,608**	**$7,856,969**

Carrying Value								
	North American distribution rights		Intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1, 2015	**$**	-	$31,026	$462,715	$28,408	$1,393,483	$255,934	$2,171,566
Balance at December 31, 2015	$	-	$47,735	$343,009	$22,728	$1,018,649	$204,746	$1,636,867
Balance at December 31, 2016	$	-	**$39,027**	**$223,197**	**$17,044**	**$653,593**	**$153,558**	**$1,086,419**
Balance at March 31, 2017	$	-	**$36,850**	**$193,244**	**$15,623**	**$562,329**	**$140,761**	**$948,807**

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.

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.

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 10). These intangible assets included intellectual property ($25,000) and a customer relationship ($Nil).

6. Loans and Advances

Advances

To finance its operations, the Company has received advances from investors:

1. During 2015, the Company received advances totaling $262,000 from an investor. These advances bear interest at 1% per month and are secured by promissory notes that were due on October 31, 2015. The principal balance outstanding at December 31, 2016 can be converted into shares of the Company, by the investor, at the conversion price of $0.06 per share.

2. In February 2016, the Company received another advance of $48,000 from the investor in 1. This advance is secured by a promissory note and bears interest of $2,000 from February 1, 2016 to the repayment date on March 5, 2016. Any unpaid balance after maturity bears interest at 2% per month.

3. In September 2016, the Company received an advance of $46,368 (US $35,000) from an investor. This advance is secured by a promissory note and bears interest at 1% from September 27, 2016 to

the repayment date on November 27, 2016. Any unpaid balance after maturity bears interest at 2% per month.

4. In November 2016, the Company received an advance of $20,000 from an investor. This advance is secured by a promissory note and bears interest of $4,000 from November 22, 2016 to the repayment date on March 22, 2017. Any unpaid balance after maturity bears interest at 2% per month.

5. In December 2016, the Company received another advance of $20,000 from the investor in 4. This advance is secured by a promissory note and bears no interest from December 28, 2016 to the repayment date on March 28, 2017. Any unpaid balance after maturity bears interest at 2% per month. This advance was repaid on February 23, 2017.

These advances are summarized as follows:

	Repayment Date	Funds Advanced	Prepaid Interest	Accrued Interest	Foreign Exchange	Balance
Loan 1	October 31, 2015	$262,000	$8,000	$46,950	$-	$316,950
Loan 2	March 5, 2016	48,000	2,000	12,839	-	62,839
Loan 3	November 27, 2016	46,368	-	4,801	245	51,414
Loan 4	March 22, 2017	20,000	-	4,107	-	24,107
		$376,368	$10,000	$68,697	$245	$455,310

At March 31, 2017, the carrying amount of these advances was as follows:

Funds advanced in 2015	$262,000
Discount, beginning prepaid interest withheld	8,000
Accrued interest	6,450
Foreign exchange	-
Balance, December 31, 2015	**276,450**
Funds advanced	134,368
Discount, beginning prepaid interest withheld	2,000
Accrued interest	45,543
Foreign exchange	628
Balance, December 31, 2016	**$458,989**
Payment	(20,000)
Accrued interest	16,704
Foreign exchange	(383)
Balance, March 31, 2017	**455,310**

Secured Short-Term Loan

In December 2016, the Company entered into a lending arrangement with a factoring firm whereby the Company pledged a specific trade receivable as security and received an advance of $26,202 (GBP 14,200), with full recourse against the Company. The factoring fee was set at GBP 9,600 per annum, as a minimum.

At March 31, 2017, the loan balance was $153. The interest charged during the three months ended March 31, 2017 was $4,352.98 (March 31, 2016 - $Nil) and is recorded within finance expense in the statement of operations.

7. Obligations Under Acquisition Contracts

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 TECC. Consideration of $1,738,750 (£1,035,000) was payable in cash and $532,067 (£265,000) was payable in common shares of the Company. As at December 10, 2013, the balance of $886,714 (£508,217), including accrued interest of $145,181 (£83,217), was outstanding. The Company negotiated a debt reduction and the outstanding obligation was extinguished and replaced with two new obligations (TECC 1 and TECC 2). The fair values of TECC 1 and TECC 2 were determined by discounting the future payments at 16%.

Smartcool UK

In February 2011, the Company acquired the business of Smartcool UK for total cash consideration of $4,410,745 (£2,840,438) and some non-cash consideration (note 6). As at December 10, 2013, the principal balance of $1,744,600 (£1,000,000), including accrued interest of $285,274 (£163,517), was outstanding. The Company negotiated a debt reduction and the outstanding obligation was extinguished and replaced with two new obligations (UK 1 and UK 2). The fair values of UK 1 and UK 2 were determined by discounting the future payments at 10%.

These obligations are being accreted to their face value over their term. The accretion charge for the period is recorded within finance expense in the statement of operations.

These obligations are to be repaid as follows:

- £130,000 ($215,332) in five instalments of £26,000 on December 15, 2014 and June 15, 2015, 2016, 2017 and 2018;
- £76,000 ($125,886) in five instalments of £19,000 on December 15, 2015, 2016, 2017 and 2018; and
- £25,000 ($41,411) in 2016.

£206,000 ($341,218) of this debt is secured by non-interest bearing promissory notes and £25,000 ($41,411) is unsecured. These balances may be repaid at any time or from time-to-time without notice, bonus or penalty. Because the Company failed to make payments for UK 1 as required, the Company is obligated to pay the creditor, at the discretion of the creditor, an amount equal to £1,300,000 minus any payments made. To date, the creditor has not requested payment of this amount.

At March 31, 2017, the carrying amount of these obligations under acquisition contracts was as follows:

	TECC 1	TECC 2	UK 1	UK 2	Total
Balance, January 1, 2015	**$188,053**	**$88,840**	**$63,249**	**$46,077**	**$386,219**
Payments	-	-	(19,091)	-	(19,091)
Debt settlement (note 9 b))	-	(24,510)	-	(11,590)	(36,100)
Accretion	21,161	11,373	-	3,800	36,334
Foreign exchange	25,051	10,036	6,860	5,220	47,167
Balance, December 31, 2015	234,265	85,739	51,018	43,507	414,529
Accretion	14,336	8,002	-	2,613	24,951
Foreign exchange	(44,881)	(16,525)	(9,608)	(8,317)	(79,331)
Balance, December 31, 2016	**$203,720**	**$77,216**	**$41,410**	**$37,803**	**$360,149**
Accretion	3,005	1,391		443	4,839
Foreign exchange	1,675	634	340	311	2,960
Balance, March 31, 2017	**$208,400**	**$79,241**	**$41,750**	**$38,557**	**$367,948**
Current portion	166,332	59,819	41,750	29,034	296,935
Long-term portion	**$42,068**	**$19,422**	**$-**	**$9,523**	**$71,013**

Principal	$217,100	$ 86,172	$ 41,750	$ 40,748	$ 385,770
Future accretion	(8,700)	(6,931)	(-)	(2,191)	(17,822)
Carrying amount	$ 208,400	$ 79,241	$41,750	$ 38,557	$367,948

8. Debentures

There were 71 debenture units outstanding at maturity on March 1, 2015. The Company was unable to redeem them or make interest payments as scheduled. The Company approached the debenture holders with an offer to extend the maturity date of the debentures to March 31, 2016, with the outstanding principal plus accrued interest becoming the new principal balance. Two debenture holders (representing 9 units) with an outstanding balance totaling $31,116 did not agree to extend the terms of their debentures. 12 debenture holders (representing 62 units) with an outstanding balance totaling $238,546 agreed to extend the terms of their debentures. Pursuant to the terms and conditions of the debenture extension agreement, the debentures are unsecured and interest on the principal balance outstanding shall accrue at the rate of 12% per annum and is payable monthly, commencing April 1, 2015. A principal pre-payment amount (not-defined) was due on September 30, 2015. This amount was not paid and the Company was in default at Mar 31, 2017 and December 31, 2016. On May 1, 2017, principal payment of $40,758 was made. The Company also issued 238,546 share purchase warrants to the debenture holders.

The terms and conditions of the refinanced debentures were not significantly different from the original terms and conditions and no gain or loss on debt extension was recognized. The refinanced principal balance of $238,546 was allocated between the fair values of the liability component ($216,231) and the equity component relating to the share purchase warrants ($22,315) using the residual method. The liability component is measured at amortized cost. The $22,315 was credited to the reserve for equity settled share-based transactions.

In November 2016, the Company and 5 debenture holders (representing 35 units) with an outstanding balance totaling $159,785 entered into an amending agreement whereby the maturity date was extended to March 31, 2017 and a General Security Agreement over the assets of the Company was granted to these debtors.

During the three months ended March 31, 2017, accrued interest expense was $7,348 and interest payments were $28,854. The interest charge is recorded within finance expense in the statement of operations.

At Mar 31, 2017, the carrying amount of the debentures was as follows:

Maturity date	**March 1, 2015**	**March 31, 2016**	**March 31, 2017**	**Total**
Balance, January 1, 2015	**$259,470**	**$-**	**$-**	**$259,470**
Amended debentures	(238,546)	238,546	-	-
Fair value of share purchase warrants	-	(22,315)	-	(22,315)
Accrued interest	12,332	40,779	-	53,111
Interest payments	(699)	(18,860)	-	(19,559)
Principal payments	(16,000)	-	-	(16,000)
Balance, December 31, 2015	**$16,557**	**$238,150**	**$-**	**$254,707**
Amended debentures	-	(159,785)	159,785	-
Accrued interest	1,814	14,910	18,798	35,522
Interest payments	-	(917)	-	(917)
Principal payments	-	(8,738)	-	(8,738)
Balance, December 31, 2016	**$18,371**	**$83,620**	**$178,583**	**$280,574**
Accrued interest	454	2,194	4,700	7,348
Interest payments	(2,223)	-	(26,631)	(28,854)
Balance, March 31, 2017	**$16,602**	**$85,814**	**$156,652**	**$259,068**
Current portion	**$16,602**	**$85,814**	**$156,652**	**$259,068**
Long-term portion	$-	$-	$-	$-

Maturity date	March 1, 2015	March 31, 2016	March 31, 2017	Total
Principal	$15,117	$73,155	$156,652	$244,924
Accrued interest	1,485	12,659	-	14,144
Balance owing and carrying amount	$ 16,602	$ 85,814	$ 156,652	$259,068

9. Issued Capital and Equity Reserve

Authorized

Unlimited common shares without par value
100,000,000 Class A preferred shares
100,000,000 Class B preferred shares

a. *Issued common shares*

	Shares	Amount
Balance, January 1, 2015	**89,017,297**	**30,733,413**
Issued via private placements	28,450,000	736,196
Issued for debt settlement	4,630,440	231,522
Share issuance costs	-	(28,447)
Balance, December 31, 2015	**122,097,737**	**31,672,684**
Warrants exercised – pending in 2015	545,000	27,250
Issued – pending in 2015 (i)	500,000	25,000
Reclassification of fair value of exercised warrants	-	4,387
Issued via private placements (ii)(iii)(iv)(v)	18,200,000	383,017
Cancelled (vi)	(500,000)	(16,642)
Share issuance costs (ii)(iii)(ix)(v)	-	(13,834)
Balance, December 31, 2016	**140,842,737**	**$ 32,081,862**
Issued via private placements (xii)	20,000,000	255,400
Share issuance costs (xii)	-	(6,857)
Warrant amendment (xiii)	-	(399,215)
Balance, March 31, 2017	**160,842,737**	**$31,931,190**

i. On February 15, 2016, the Company issued 500,000 common shares at a deemed price of $0.05 per share to SmartACR pursuant to a license termination agreement (note 10).

ii. On May 5, 2016, the Company issued 6,600,000 Units at $0.025 per unit pursuant to the first tranche of a non-brokered private placement for gross proceeds of $165,000. Of this amount, $136,793 was allocated to share capital and $28,207 to share purchase warrants (note 9(c)(i)). Each Unit consists of one common share and one warrant. Cash issuance costs of $4,026 and agent warrant issuance costs of $800 for 128,000 agent warrants issued were allocated to common shares.

iii. On June 21, 2016, the Company issued 5,400,000 Units at $0.025 per unit pursuant to the second tranche of a non-brokered private placement for gross proceeds of $135,000. Of this amount, $111,922 was allocated to share capital and $23,078 to share purchase warrants (note 9(c)(ii)). Each Unit consists of one common share and one warrant. Cash issuance costs of $6,150 were allocated to common shares.

iv. On September 19, 2016, the Company issued 5,400,000 Units at $0.025 per unit pursuant to the first tranche of a non-brokered private placement for gross proceeds of $135,000. Of this amount, $116,973 was allocated to share capital and $18,027 to share purchase warrants (note 9(c)(iii)). Each Unit consists of one common share and one warrant. Cash issuance costs of $2,489 were allocated to common shares.

v. On September 29, 2016, the Company issued 800,000 Units at $0.025 per unit pursuant to the second tranche of a non-brokered private placement for gross proceeds of $20,000. Of this amount, $17,329 was allocated to share capital and $2,671 to share purchase warrants (note 11(c)(iv)). Each Unit consists of one common share and one warrant. Cash issuance costs of $369 were allocated to common shares.

vi. On September 28, 2016, 500,000 shares were cancelled and returned to treasury because the outstanding proceeds of $25,000 had not been received. Of this amount, $16,642 was allocated to share capital and $8,358 to share purchase warrants.

vii. On March 15, 2017, the Company issued 20,000,000 Units at $0.02 per unit pursuant to a non-brokered private placement for gross proceeds of $400,000. Of this amount, $255,400 was allocated to share capital and $144,600 to share purchase warrants (note 9(c)(v)). Each Unit consists of one common share and one warrant. Cash issuance costs of $6,064 and agent warrant issuance costs of $794 for 248,000 agent warrants issued were allocated to common shares.

viii. On February 3, 2017, the Company amended the expiry dates and exercise prices of certain warrants. The fair value of these warrants increased by $399,215 as a result. Share purchase warrants increased accordingly and Share capital decreased by the same amount. See note 9(c)(vi).

b. ***Stock options***

Under the Company's stock option plan, the Company may grant stock options to employees, directors, officers and consultants. The maximum number of shares to be awarded under the plan is 23,885,547, as approved by the shareholders at the Company's 2015 Annual General Meeting. In 2010, the stock option plan was amended to extend the option term to a maximum period of ten years.

As at March 31, 2017, 11,470,000 options were outstanding. These options have vesting period of 5 years and a weighted average exercise price of $0.05. A summary of the Company's stock option activity for employees, directors, officers and consultants is as follows:

	Number of share options	Weighted average exercise price
Balance, January 1, 2015	**6,215,000**	**$0.07**
Granted	8,070,000	0.05
Forfeited and cancelled	(500,000)	0.05
Expired or exercised	(1,370,000)	0.10
Balance, December 31, 2015	**12,415,000**	**$0.05**
Granted	75,000	0.05
Expired or exercised	(545,000)	0.10
Balance, December 31, 2016	**11,945,000**	**$0.05**
Expired or exercised	(475,000)	0.10
Balance, March 31, 2017	**11,470,000**	**$0.05**

During the three months ended March 31, 2017, no options were granted.
Share-based payments for the three months was $184 (March 2016 - $18,785).

c. ***Share purchase warrants***

i. On May 5, 2016, the Company issued 6,600,000 Units at $0.025 per unit pursuant to the first tranche of a non-brokered private placement for gross proceeds of $165,000. Of this amount, $136,793 was allocated to share capital and $28,207 to share purchase warrants. Each Unit consists of one common share and one warrant. Cash issuance costs of $1,146 were allocated to share purchase warrants. The Company also issued 128,000 agent warrants valued at $800 pursuant to this private placement tranche.

ii. On June 21, 2016, the Company issued 5,400,000 Units at $0.025 per unit pursuant to the second tranche of a non-brokered private placement for gross proceeds of $135,000. Of this amount, $111,922 was allocated to share capital and $23,078 to share purchase warrants. Each Unit consists of one common share and one warrant. Cash issuance costs of $938 were allocated to share purchase warrants.

iii. On September 19, 2016, the Company issued 5,400,000 units at $0.025 per unit pursuant to the first tranche of a non-brokered private placement for gross proceeds of $135,000. Of this amount, $116,973 was allocated to share capital and $18,027 to share purchase warrants. Each Unit consists of one common share and one warrant. Cash issuance costs of $444 were allocated to share purchase warrants.

iv. On September 29, 2016, the Company issued 800,000 units at $0.025 per unit pursuant to the second tranche of a non-brokered private placement for gross proceeds of $20,000. Of this amount, $17,329 was allocated to share capital and $2,671 to share purchase warrants. Each Unit consists of one common share and one warrant.

v. On March 15, 2017, the Company issued 20,000,000 Units at $0.02 per unit pursuant to a non-brokered private placement for gross proceeds of $400,000. Of this amount, $255,400 was allocated to share capital and $144,600 to share purchase warrants. Each Unit consists of one common share and one warrant. Cash issuance costs of $3,411 and agent warrant issuance costs of $446 for 248,000 agent warrants issued were allocated to warrants.

vi. On February 3, 2017, the Company amended the expiry dates and exercise prices of certain warrants, as follows:

Warrants	Grant date	Original expiry date	Amended expiry date	Original exercise price	Amended exercise price
9,455,000	January 28, 2015	January 28, 2017	January 28, 2020	$0.05	No change
11,280,000	May 4, 2015	May 4, 2017	May 4, 2020	$0.10	$0.05
6,600,000	May 5, 2016	May 5, 2017	May 5, 2021	$0.05	No change
5,400,000	June 21, 2016	June 21, 2017	June 21, 2021	$0.05	No change
5,400,000	September 19, 2016	September 19, 2017	September 19, 2021	$0.05	No change
800,000	September 29, 2016	September 29, 2017	September 29, 2021	$0.05	No change

The fair value of the amended warrants increased by $399,215, as a result. Share purchase warrants increased and Share capital decreased by this amount.

As at March 31, 2017, there were 59,423,000 (December 31, 2016 – 43,175,000) outstanding warrants with a weighted average share price of $0.06 (December 31, 2016 - $0.07).

A summary of the Company's reserve for equity settled share-based transactions is as follows:

	Number of warrants	Weighted average share price
Balance, January 1, 2015	**5,216,000**	**$0.10**
Issued – private placements	28,450,000	0.09
Issued – agent warrants	112,000	0.10
Issued – debentures	238,546	0.06
Expired, exercised or cancelled	(5,216,000)	0.10
Balance, December 31, 2015	**28,800,546**	**$0.08**
Issued – private placements	18,200,000	0.05
Issued – agent warrants	128,000	0.05
Expired, exercised or cancelled	(3,953,546)	0.09
Balance, December 31, 2016	**43,175,000**	**$0.07**
Issued – private placements	20,000,000	0.05
Issued – agent warrants	248,000	0.05
Expired, exercised or cancelled	(4,000,000)	0.075
Balance, March 31, 2017	**59,423,000**	**$0.05**

Expiry date	Number of shares	Exercise price	Weighted average contractual life (years)
May 4, 2017*	112,000	$0.10	0.09
May 5, 2017*	128,000	$0.05	0.10
January 28, 2020	9,455,000	$0.05	2.83
March 15, 2020	20,248,000	$0.05	2.96
May 4, 2020	11,280,000	$0.05	3.09
May 5, 2021	6,600,000	$0.05	4.10
June 21, 2021	5,400,000	$0.05	4.23
September 19, 2021	5,400,000	$0.05	4.47
September 29, 2021	800,000	$0.05	4.50
Balance, March 31, 2017	**59,423,000**	**$0.05**	**3.35**

*Agent warrants.

10. Income Taxes

The Company's operations are conducted in a number of countries with complex tax legislation and regulations pertaining to the Company's activities. Any reassessment of the Company's tax filings by the tax authorities may result in material adjustments to net income or loss, tax assets and non-capital loss carry-forwards.

In assessing the ability to realize deferred tax assets, management considers whether it is probable that taxable profit will be available against which the deductible temporary difference can be utilized. As management believes there is uncertainty regarding the realization of these deferred tax assets, they have been classified as unrecognized tax assets as at December 31, 2016.

At December 31, 2016, the Company has unused non-capital losses of approximately $22,297,000 available to offset taxable income of future years. The non-capital losses will expire as follows:

	Canada	International	USA	UK	Total
Tax rate	**26%**	**2.5%**	**40%**	**20%**	
2016	$1,023,014	$-	$-	$-	1,023,014
2027	1,732,657	-	1,267,037	-	2,999,694
2028	1,127,657	-	2,188,026	-	3,315,683
2029	2,501,267	-	1,117,169	-	3,618,436
2030	910,879	-	1,102,960	-	2,013,839
2031	786,254	-	609,086	-	1,395,340
2032	400,145	-	236,380	-	636,525
2033	189,678	-	93,801	-	283,479
2034	3,775,936	1,518,362	-	-	5,294,298
2035	371,521	-	-	140,563	512,084
2036	877,113	101,452	43,612	182,506	1,204,683
	$13,696,121	**$1,619,814**	**$6,658,071**	**$323,069**	**$22,297,075**

Deferred Tax Liabilities

The Company recorded deferred tax liabilities of $1,078,565 as a result of the acquisition of Smartcool UK assets in February 2011. As at March 31, 2017, the deferred tax liability was $138,729 (December 31, 2016 - $151,425).

11. Segmented Information

The Company installs, distributes, markets and sells the ECO3 and ESM™ products and peripherals. Revenue from the ECO3 for the three months ended March 31, 2017 was $ 12,121 (March 31, 2016 - $20,646) and revenue for the ESM™ solution was $73,836 (March 31, 2016 - $121,851).

The Company operates in one segment. Revenue was derived from customers located in the following geographical regions:

	March 31, 2017		March 31, 2016	
	Amount	**%**	**Amount**	**%**
Americas	$ 12,487	15	$31,361	22
Europe, Middle East, Africa	73,470	85	111,136	78
Total revenue	**$ 85,957**	**100**	**$142,497**	**100**

Revenue per region was determined based on the location of the customer or their billing address.

12. Commitments

Consulting Agreements

In December 2014, the Company entered into a consulting agreement with Maxwell Mercantile Inc., an independent contractor, effective January 1, 2015. The contractor will provide management services to Smartcool in the role of Chief Executive Officer for a monthly fee of $15,000. He is entitled to receive an annual bonus equal to 5% of all sales revenue in excess of $1,500,000 per fiscal year or 10% of EBITDA (earnings before interest, taxes, depreciation and amortization) in excess of $300,000 per fiscal year, whichever is greater. The agreement has a twelve month-term with automatic renewals of additional twelve month terms unless either party gives 60 days written notice to the other of its intention not to renew. This agreement may be terminated by the Company upon payment of a termination fee of 12 times the monthly fee.

On April 1, 2015, the Company, through Smartcool USA, entered into a consulting agreement with Sand Dollar Management Inc., an independent contractor. The contractor is providing general management of the direct sale and installation of products to customer sites located in California, USA. The contractor will receive a monthly consulting fee equal to the lesser of 20% of gross revenues (as defined) and 40% of gross profits of the business unit (as defined). Pursuant to the agreement, the contractor was granted 2,000,000 stock options. These options vest in four equal instalments of 500,000 commencing on the date of grant and then six, 12 and 18 months thereafter. The agreement has a three-year term with automatic renewals of additional three-year terms unless either party gives 30 days written notice to the other of its intention not to renew. In the event that a change of control occurs and the Company terminates the agreement for any reason other than for cause, the Company must pay a lump sum termination fee equal to the amount of the consulting fee earned by the contractor during the 12 month period immediately preceding the date of termination

13. Related Party Transactions

Trading Transactions

The Company's related parties consist of companies owned by executive officers and directors and key management as follows:

	Nature of Transaction
Maxwell Mercantile	Management services
Brad Nightingale Consulting	Consulting services
Global Telematic Solutions	Administration services

The Company incurred the following expenses in connection with the companies owned by key management and directors. These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

	Note	March 31, 2017	March 31, 2016
Consulting fees	(i)	$45,000	$56,529
Administration services	(ii)	3,986	-
		$48,986	**$56,529**

i. During the three months ended March 31, 2017, consulting fees of $45,000 were charged by a company with common directors (March 31, 2016 - $56,529).

ii. During the three months ended March 31, 2017, administration fees of $3,986 were charged by a company with common directors (March 31, 2016 - $Nil).

Due to/from Related Parties

Included in trade and other receivables is $5,000 due from the former President as at March 31, 2017 (December 31, 2016 - $5,000) related to an advance for travel expenses. The amount is unsecured, non-interest bearing and has no fixed terms of repayment (note 3).

Included in trade payables and accruals is $326,592 due to related parties as at March 31, 2017 (December 31, 2016 - $428,333) as follows:

	March 31, 2017	December 31, 2016
Chief Executive Officer	$34,742	$80,585
President	85,977	97,880
Chief Financial Officer	51,417	63,167
Executive VP	59,805	77,352
VP of Operations	76,000	83,838
Other related parties	18,651	25,511
Total	**$326,592**	**$428,333**

The amounts due to related parties are unsecured, non-interest bearing and have no fixed terms of repayment.

14. Financial Instruments

Financial Instruments

The Company has classified its financial instruments as follows:

	March 31, 2017	December 31, 2016
Financial assets		
FVTPL , measured at fair value:		
Cash and cash equivalents	$ 31,119	$3,317
Available-for-sale, measured at fair value:		
Securities	12,316	8,210
Loans and receivables, measured at amortized cost:		
Trade and other receivables	176,959	201,232
	$ 220,394	**$212,759**
Other financial liabilities, measured at amortized cost		
Trade payables and accruals	$699,796	$ 837,349
Loans and advances	455,463	485,191
Acquisition obligations and debentures	627,016	640,723
	$ 1,782,275	**$ 1,963,263**

Interest and accretion charged on loans, obligations under acquisition contracts and debentures are recognized in finance expense in the statement of operations.

Unrealized gain or loss on investment in securities is recognized in other comprehensive income.

Financial instruments recorded at fair value are measured using a three-level fair value hierarchy:

- Level 1: fair value is determined by reference to quoted prices in active markets for identical assets and liabilities.

- Level 2: fair value is determined based on inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly.

- Level 3: fair value is determined based on inputs that are unobservable and significant to the overall fair value measurement.

The carrying values of cash and cash equivalents, trade and other receivables, trade payables and accruals, loans and advances, obligations under acquisition contracts and debentures approximate fair value because of the short-term nature of these instruments.

Financial Risk Management

The Company is exposed to certain financial risks, including credit risk, liquidity risk, market risk and foreign currency risk.

a. *Credit risk*

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations and arises principally from the Company's cash and cash equivalents and trade and other receivables. The Company limits its exposure to credit loss by placing its cash and cash equivalents and short-term investments with high credit quality financial institutions. To mitigate credit risk with respect to trade receivables the Company subjects all major customer accounts to its credit evaluation process.

As at March 31, 2017, the Company had $176,959 (December 31, 2016 - $201,232) in trade and other receivables which were subject to credit risk (note 3).

b. *Liquidity risk*

The Company's consolidated financial statements have been prepared on a going concern basis, which assumes the realization of assets and the settlement of liabilities in the normal course of business. Liquidity risk results from the Company's inability to meet its financial obligations when they become due. As part of the risk management process, the Board approves the Company's annual operating and capital budgets as well as any material transactions outside the ordinary course of business. To ensure that the Company has sufficient liquidity to meet its current obligations in the next 12 months, measures have been taken to increase cash resources (note 1).

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	$ 699,796	$ 699,796	$-
Loans and advances	455,463	455,463	-
Obligations under acquisition contracts	367,948	296,935	71,013
Debentures	259,068	259,068	-
Total	**$1,782,275**	**$ 1,711,262**	**$ 71,013**

c. *Market risk*

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the Company's income or valuation of its financial instruments.

d. *Foreign currency risk*

The Company is exposed to fluctuations in foreign currency as most of its international distribution transactions are settled in U.S. dollars, Australian dollars, Canadian dollars and British pounds. The Company's net income or loss and cash flow will therefore be affected by fluctuations in foreign exchange rates. None of these risks has been mitigated through the use of foreign currency forward contracts.

As at March 31, 2017, the Company's monetary assets and liabilities denominated in foreign currencies are as follows:

	USD	AUD	GBP
Assets			
Cash and cash equivalents	$3,639	$-	£-
Trade and other receivables	103,700	-	-
Total	**$107,339**	**$-**	**£-**
Liabilities			
Trade payables and accruals	$119,297	$2,622	£61,693
Acquisition obligations	-	-	177,805
Total	**$119,297**	**$2,622**	**£239,498**

The following table demonstrates the effect of exchange rate movement on net income or loss due to gains and losses on the revaluation of monetary assets and liabilities denominated in foreign currencies:

Gain (loss) on $0.10 increase in CAD	**USD**	**AUD**	**GBP**
Monetary assets	($10,734)	$-	£-
Monetary liabilities	11,930	262	23,950
Net gain (loss)	**$1,196**	**$262**	**£23,950**
Gain (loss) on $0.10 decrease in CAD	**USD**	**AUD**	**GBP**
Monetary assets	$10,734	$-	£-
Monetary liabilities	(11,930)	(262)	(23,950)
Net gain (loss)	**($1,196)**	**($262)**	**(£23,950)**

15. General and Administrative Expenses

	Three months ended March 31. 2017	Three months ended March 31, 2016
Advertising and promotion	$939	$20
Consulting and management fees	78,223	83,529
Filing and transfer fees	9,208	8,970
Insurance	2,028	1,892
Interest	-307	1,655
Investor relations	500	4,580
Product certification	-	2,164
Professional fees	12,813	2,358
Office and supplies	7,071	6,221
Rent	2,469	14,031
Salaries and benefits	128,237	124,250
Telephone	2,169	5,035
Travelling	22,295	14,176
Total general and administrative expenses	**$265,646**	**$268,880**

16. Capital Management

The Company's capital structure includes debentures and shareholders' equity consisting of share capital, reserve for equity settled share-based transactions and deficit. As at March 31, 2017, the principal amount of the debenture component plus interest payable was $259,068 (December 31, 2016 - $280,574) and shareholders' deficiency was $595,087 (December 31, 2016 – $625,196). The reduction in shareholders' deficiency was attributable to capital financing in March 31, 201, offset by operating loss.

The Company's objectives when managing capital are:

- to effectively finance its operations and growth by meeting its operating and capital expenditure budgets;
- to maintain financial flexibility in order to meet financial obligations, including obligations under acquisition contracts;
- to ensure its ability to carry out its strategic plans and take advantage of acquisition opportunities; and

- to provide an appropriate investment return to its shareholders and maintain investor, creditor and market confidence.

To ensure that the Company continues to be a going concern with adequate working capital in the next 12 months steps have been taken to monitor expenses, grow revenue and arrange for additional capital financing.

The Company is not subject to any external capital restrictions.

17. Subsequent Events

On April 26, 2017, Smartcool announced a non-brokered private placement offering of up to 12,000,000 units at a price of $0.025 per unit, for maximum gross proceeds of $300,000. Each Unit consists of one common share and one warrant exercisable at $0.05 per warrant share for five years after closing.

The offering is subject to the Exchange's approval.