SMARTCOOL™

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

For the three months ended June 30, 2015 and 2014
Expressed in Canadian Dollars

www.smartcool.net

Smartcool Systems Inc.
7155 Kingsway
PO Box 54523 Highgate PO
Burnaby, BC
V5E 4J6 Canada

TEL +1 604 669 1388
TOLL-FREE +1 888 669 1388
FAX +1 604 602 0674
EMAIL officeCanada@smartcool.net

SMARTCOOL™

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.
Condensed consolidated statements of financial position
(Expressed in Canadian dollars, unless otherwise stated)
(unaudited)

	June 30 2015	December 31 2014
	$	$
ASSETS		
Current assets		
Cash and cash equivalents	44,174	15,490
Available-for-sale Securities	36,473	-
Trade and other receivables	439,900	146,918
Inventory	58,930	15,286
Prepaid expenses and deposits	112,563	74,887
	692,040	252,581
Property and equipment	30,714	45,448
Intangible assets	2,046,764	2,227,666
Total assets	2,769,518	2,525,695
LIABILITIES		
Current liabilities		
Trade payables and accruals	672,117	899,735
Short-term loans	130,000	67,238
Current portion of obligations under acquistion contracts	206,373	192,623
Current portion of debentures	246,764	259,470
Current portion of deferred tenant inducement	-	6,744
	1,255,254	1,425,810
Obligations under acquisition contracts	174,715	193,596
Deferred tax liability	227,601	249,919
Total liabilities	1,657,570	1,869,325
SHAREHOLDERS' EQUITY		
Share capital	31,567,617	30,733,413
Shares pending issue	25,000	-
Reserve for equity settled share based transactions	6,451,272	5,994,511
Warrants pending issue	82,400	-
Accumulated other comprehensive income	(378,876)	(385,806)
	37,747,413	36,342,118
Deficit	(36,635,466)	(35,685,748)
	1,111,948	656,370
Total liabilities and shareholders' equity	2,769,518	2,525,695

Approved and authorized for issue by the Board of Directors on August 28, 2015

"George Burnes"	"Theodore Konyi"
George Burnes	Theodore Konyi

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.
Condensed consolidated statements of operations
(Expressed in Canadian dollars, unless otherwise stated)
(unaudited)

	Three months ended June 30		Six months ended June 30	
	2015 $	**2014** $	**2015** $	**2014** $
Revenue	181,855	192,415	371,521	406,890
Cost of sales	32,527	42,553	56,969	72,535
Gross profit	149,328	149,862	314,552	334,355
Operating Expenses				
General and administrative expenses	473,530	291,888	809,131	537,588
Stock-based compensation	97,427	26,486	136,711	67,592
Research and development	-	-	-	-
Amortization and depreciation	147,984	81,000	304,187	162,001
	718,941	399,374	1,250,029	767,181
Operating loss	(569,613)	(249,512)	(935,477)	(432,826)
Rental income	19,018	29,002	47,546	58,004
Finance expense	(32,404)	(17,148)	(55,917)	(37,152)
Foreign exchange gain (loss)	(22,714)	(7,471)	(23,731)	3,513
Inventory received from third party	-	-	-	25,378
Loss on debt settlement	-	-	(4,456)	-
	(36,100)	4,383	(36,558)	49,743
Income tax recovery	12,696	-	22,318	-
Net loss for the period	**(593,017)**	**(245,129)**	**(949,717)**	**(383,083)**
Loss from discontinued operations	**-**	**(284,040)**	**-**	**(426,155)**
Net loss	**(593,017)**	**(529,169)**	**(949,717)**	**(809,237)**
Net loss per share				
Basic	(0.01)	(0.01)	(0.01)	(0.01)
Diluted	(0.01)	(0.01)	(0.01)	(0.01)
Continuing operations	(0.01)	(0.00)	(0.01)	(0.00)
Weighted average number of common shares outstanding (basic and diluted)	**115,155,869**	**86,451,143**	**103,768,561**	**82,889,010**

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Condensed consolidated statements of comprehensive income

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

	Three months ended June 30		Six months ended June 30	
	2015	**2014**	**2015**	**2014**
	$	**$**	**$**	**$**
Net loss for the period	**(593,017)**	**(529,169)**	**(949,717)**	**(809,237)**
Other comprehensive income	11,610	17,445	6,930	68,487
Total comprehensive loss	**(581,407)**	**(511,724)**	**(942,787)**	**(740,750)**

SMARTCOOL™

Smartcool Systems Inc.
Condensed consolidated statements of cash flows

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

	Three months ended June 30 2015 $	Three months ended June 30 2014 $	Six months ended June 30 2015 $	Six months ended June 30 2014 $
Cash flows from operating activities				
Loss for the period	(593,017)	(529,169)	(949,717)	(809,237)
Items not affecting cash:				
Depreciation of property and equipment	7,502	12,257	15,885	26,498
Amortization of intangible assets	140,482	170,240	288,302	339,990
Gain on sale of property and equipment	-	(9,258)	-	(10,171)
Inventory acquired at no charge	-	-	-	(25,378)
Shares issued to settle trade payables	-	-	195,422	-
Note receivable executed for shares issued	75,000	-	75,000	-
Shares received to settle trade and other receivables	-	-	(40,526)	-
Stock-based compensation	97,427	26,486	136,711	67,592
Deferred tax liability	(12,696)	(23,435)	(22,318)	(21,428)
Deferred tenant inducement	(2,700)	(4,042)	(6,744)	(8,085)
Foreign exchange (gain) loss	14,834	14,227	30,483	(60,633)
Accrued interest on short-term loans	366	1,427	1,466	3,927
Accrued interest on debentures	4,720	4,178	17,607	18,672
Accretion of obligation under acquisition contract	8,900	12,089	18,426	25,692
	(259,182)	(325,000)	(240,002)	(452,561)
Changes in non-cash working capital items:				
Trade and other receivables	(153,187)	(41,650)	(292,982)	(71,084)
Inventory	13,099	31,264	(43,644)	70,500
Prepaid expenses and deposits	(102,677)	(25,038)	(37,676)	(27,218)
Trade payables and accruals	3,325	(24,737)	(227,618)	87,477
Net cash flows used in operating activities	(498,622)	(385,161)	(841,922)	(392,886)
Cash flows from investing activities				
Disposal of property and equipment	-	13,172	-	14,084
Purchase of property and equipment	-	-	-	(17,224)
Net cash used in investing activities	-	13,172	-	(3,140)
Cash flows from financing activities				
Shares and warrants issued for cash net of issue costs	484,566	479,424	825,418	479,425
Short-term loan	61,296	(70,000)	61,296	(70,000)
Decrease in debentures	(8,000)	(20,344)	(8,000)	(32,195)
Decrease in acquisition contract obligation	-	(41,269)	(19,091)	(55,148)
Increase in motor finance	-	(1,067)	-	15,804
Net cash (used in) provided by financing activities	537,862	346,744	859,623	337,886
Net decrease in cash and cash equivalents	39,240	(25,245)	17,701	(58,140)
Effects of exchange rates changes on cash	(549)	17,445	10,983	68,487
Cash and cash equivalents, beginning of period	5,483	46,182	15,490	28,036
Cash and cash equivalents, end of period	44,174	38,382	44,174	38,382

See accompanying notes to the consolidated financial statements

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

(unaudited)

	Share capital	Reserve for equity settled share based transactions	Accumulated other comrprehensive income	Deficit	Total Shareholders' Equity
	$	$	$	$	$
Balance at January 1, 2014	**30,309,075**	**5,847,515**	**(129,636)**	**(33,901,721)**	2,125,233
Net loss				(809,237)	(809,237)
Foreign currency translation adjustment			68,487		68,487
Total comprehensive loss for the period			68,487	(809,237)	(740,750)
Share issued for:					
Private placement	430,600				430,600
Warrants		55,900			55,900
Share issue costs	(6,262)	(814)			(7,076)
Stock based compensation		67,592			67,592
Balance at June 30, 2014	**30,733,413**	**5,970,193**	**(61,149)**	**(34,710,958)**	**1,931,500**
Net loss				(974,790)	(974,790)
Foreign currency translation adjustment			(324,657)		(324,657)
Total comprehensive loss for the period			(324,657)	(974,790)	(1,299,447)
Share issued for:					
Private placement					-
Warrants					-
Share issue costs					-
Stock based compensation		24,318			24,318
Balance at December 31, 2014	**30,733,413**	**5,994,511**	**(385,806)**	**(35,685,748)**	**656,370**
Net loss				(949,717)	(949,717)
Available-for-sale securities unrealized loss			(4,053)		(4,053)
Foreign currency translation adjustment			10,983		10,983
Total comprehensive loss for the period			6,930	(949,717)	(942,787)
Share issued for:					
Private placement	629,396				629,396
Debt settlement	231,522				231,522
Shares subscribed	25,000				25,000
Warrants		331,919			331,919
Warrants pending issue		82,400			82,400
Share issue costs	(26,713)	(11,869)			(38,582)
Stock based compensation		136,711			136,711
Balance at June 30, 2015	**31,592,617**	**6,533,672**	**(378,876)**	**(36,635,466)**	**1,111,948**

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Notes to the Consolidated Financial Statements
For the three months ended June 30, 2015
(expressed in Canadian dollars, except where otherwise indicated)

1. Nature of Operations and Going Concern

Smartcool Systems Inc. ("Smartcool" or the "Company"), which was incorporated on August 31, 2000 under the Canada Business Corporations Act as 378211 Canada Inc., changed its name to Citotech Systems Inc. on October 16, 2000, and changed its name again to Smartcool Systems Inc. on July 20, 2004.

In 2004, the Company incorporated a wholly owned subsidiary, Smartcool Systems (USA) Inc. ("Smartcool USA"), under the laws of Nevada. Smartcool International Inc. ("Smartcool International"), another wholly owned subsidiary, was incorporated in Barbados in June 2006. In April 2008, the Company completed the incorporation of its subsidiary, Smartcool Systems (EMEA) Ltd. ("Smartcool EMEA"), headquartered in Alton, England. In February 2011, Smartcool EMEA acquired all the outstanding shares of Smartcool Systems UK ("Smartcool UK"), also headquartered in Alton, England.

In response to an unexpected shift, which management believes is short-term in nature, in energy saving strategies of European customers, the Company has decided to redirect the region's focus from direct sales to distribution sales for the medium term. Smartcool EMEA and Smartcool UK were discontinued through voluntary liquidation in September 2014 and a new wholly owned subsidiary, Lenten Street Limited, was incorporated in Alton in October 2014 to assume the distribution rights previously granted to Smartcool UK and Smartcool EMEA. 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. V6L 1M6

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 quarter ended June 30, 2015, the Company had a net loss of $593,017 compared to $$529,169 ($245,129 from continuing operations and $284,040 from discontinued operations) for the same period of 2014.

The company had a deficit of $36,635,466 as at June 30, 2015 (December 31, 2014 - $35,685,748). As at June 30, 2015, the Company had negative working capital of $563,214 (December 31, 2014 - $1,173,229). This improvement in working capital was attributable to a shares-for-debt settlement completed in March and two private placements completed in January and May 2015. To ensure that the Company continues to be a going concern over the next twelve months, the Company has explored different ways to grow revenue and monitor costs, including the restructure of its sales network and the acquisition of a complementary technology from SmartACR. The Company is also planning on obtaining additional capital in the fall.

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 June 30, 2015 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, 2014.

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 17, and are presented in Canadian dollars except where otherwise indicated.

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, Lenten Street, Smartcool EMEA and Smartcool UK from February 28, 2011, the date of acquisition. 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.

Foreign Currency

The functional currency of Smartcool and Smartcool International has been determined to be the Canadian dollar. The functional currency of Smartcool USA is the United States dollar. The functional currency of Smartcool EMEA and Smartcool UK and Lenten Street is the British pound. The consolidated financial statements have been translated to the Canadian dollar in accordance with IAS 21, “The Effects of Changes in Foreign Exchanges Rates”.

The assets and liabilities of foreign operations are translated into Canadian dollars at the exchange rate at period end and statement of operations items are translated using the exchange rates at the date of the transactions. All resulting exchange differences are taken directly to a separate component of equity, foreign currency translation adjustment reserve. On disposal of a foreign operation, the deferred cumulative amount recognized in the foreign currency translation adjustment reserve relating to that particular foreign operation is recognized in foreign exchange gain or loss in the statement of operations.

For foreign subsidiaries where the Canadian dollar is the functional currency, non-monetary assets and liabilities are translated to Canadian dollars using the exchange rate in effect at the original transaction date. Monetary balances are translated at rates of exchange at the period end date. The translation difference resulting from translating the foreign currencies to Canadian dollars is recorded as a component of foreign exchange gain or loss.

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^{TM} brand, ESM^{TM} intellectual property, distribution rights, distribution agreements, supplier agreements and customer relationship. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The ESM^{TM} 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. During the year ended December 31, 2013, management re-assessed the useful lives of the intangible assets as follows:

	2013	2012
ESM™ Intellectual property	13.5 years	10 years
North American distribution rights	10 years	10 years
TECC and United Kingdom distribution rights	9.5 - 12 years	5 - 9 years
Distribution agreements	13.5 - 15 years	10 - 15 years
Supplier agreements	13.5 years	10 years
Customer relationship	12 years	5 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.

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.

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.

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 amortizations) is greater than the current fair value, less any impairment previously recognized in profit or loss. The impairment amount is transferred from equity to the statement of operations. Reversals of available-for-sale financial assets are not recognized in profit.

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.

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.

Accounting Standards Issued but not yet Effective

At the date of authorization of these consolidated financial statements, the IASB and IFRIC have issued the following new and revised standards and amendments which are not yet effective:

- IFRS 9, "Financial Instruments". This standard is effective for annual periods beginning on or after January 1, 2018 and replaces IAS 39 and IFRIC 9 for classification and measurement of financial assets and financial liabilities.

- IFRS 15 – Revenue from Contracts with Customers. This standard is effective for annual periods ending on or before December 31, 2017 and is available for early adoption and replaces IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfer of Assets from Customers, and SIC 31Revenue – Barter Transactions Involving Advertising Services.

3. Trade Receivables

	June 30, 2015	**December 31, 2014**
[1]Trade receivables, net of allowances for doubtful accounts	$ 353,348	$138,258
Other receivables	86,552	8,660
	$ 439,900	**$146,918**

Allowance for doubtful accounts as at June 30, 2015 was $218,667 (December 31, 2014 - $235,955).

4. Inventory

	June 30, 2015	**December 31, 2014**
ESM™ ECO3™	$55,697	$11,744
Other products	3,233	3,542
	$58,930	**$15,286**

During the three months ended June 30, 2015, total inventories of $12,831 were recognized as costs of sales (June 30, 2014 - $49,715). During the six months ended June 30, 2015, total inventories of $33,626 were recognized as costs of sales (June 30, 2014 - $105,022).

5. Property and Equipment

The Company leased certain assets under finance lease agreements. These leases expired in April 2012 and August 2013.
As at June 30, 2015, the Company had no assets under capital lease (December 31, 2014 – $Nil).

6. Intangible Assets

Indefinite Lives

As at June 30, 2015, ESM™ brand (b) had a carrying value of $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, 2013	**$256,982**	**$124,100**	**$1,861,742**	**$113,651**	**$4,733,689**	**$1,078,091**	**$8,168,255**
Effect of change in foreign exchange rates	12,366	-	-	-	303,091	96,560	412,017
Balance at December 31, 2013	**269,348**	**124,100**	**1,861,742**	**113,651**	**5,036,780**	**1,174,651**	**8,580,272**
Effect of change in foreign exchange rates	17,370	-	-	-	115,438	36,718	169,526
Balance at December 31, 2014	**286,718**	**124,100**	**1,861,742**	**113,651**	**5,152,218**	**1,211,369**	**8,749,798**
Acquisition		75,000				32,400	107,400
Effect of change in foreign exchange rates	15,714						15,714
Balance at June 30, 2015	**$ 302,432**	**$199,100**	**$1,861,742**	**$113,651**	**$ 5,152,218**	**$1,243,769**	**$ 8,872,912**

Accumulated Amortization and Impairment							
	North American distribution rights	ESM™ intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1, 2013	**$256,982**	**$80,665**	**$968,519**	**$73,873**	**$2,369,912**	**$540,311**	**$4,290,262**
Amortization	-	6,205	113,288	5,685	396,996	76,494	598,668
Effect of change in foreign exchange rates	12,366	-	-		176,445	55,584	244,395
Balance at December 31, 2013	**269,348**	**86,870**	**1,081,807**	**79,558**	**2,943,353**	**672,389**	**5,133,325**
Amortization	-	6,204	141,907	5,685	405,477	77,835	637,108
Impairment	-	-	175,313	-	344,251	184,465	704,029
Effect of change in foreign exchange rates	17,370	-	-	-	65,654	20,746	103,770
Balance at December 31, 2014	**286,718**	**93,074**	**1,399,027**	**85,243**	**3,758,735**	**955,435**	**6,578,232**
Amortization		5,604	59,800	2,838	192,306	27,754	288,302
Effect of change in foreign exchange rates	15,714						15,714
Balance at June 30, 2015	**$ 302,432**	**$ 98,678**	**$ 1,458,827**	**$ 88,081**	**$ 3,951,041**	**$ 983,189**	**$ 6,882,248**

Carrying Value							
	North American distributio	ESM™ intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distributio	Customer relationship	Total
Balance at January 1, 2013	$	$43,435	$893,223	$39,778	$2,363,777	$537,780	$3,877,993
Balance at December 31, 2013	**$ -**	$37,230	$779,935	$34,093	$2,093,427	$502,262	$3,446,947
Balance at December 31, 2014	$ -	$ 31,026	$ 462,715	$ 28,408	$1,393,483	$ 255,934	$2,171,566
Balance at June 30, 2015	$ -	**$100,422**	**$ 402,915**	**$ 25,570**	**$1,201,177**	**$260,580**	**$1,990,664**

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.

As at June 30, 2015 and December 31, 2014, the cost of distribution agreements consisted of:

ESM™ Distribution agreements	$1,835,702
Other distribution rights	26,040
Total	**$1,861,742**

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 have 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") (see note 8).

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 have resulted in significant uncertainty in future cash generation of these assets, an impairment loss of $528,716 was recorded based on cash flow projections as at December 31, 2014 as follows.

	Impairment
Distribution rights - major customer	$344,251
Customer relationship	184,465
Total impairment	**$528,716**

d. *SmartACR Intellectual property and customer relationship*

In February 2015, the Company acquired $107,400 of intangible assets in relation to the transfer of a portion of SmartACR's business to the Company (see note 12). These intangible assets include SmartACR intellectual property and customer relationship.

The expected lives of these assets have been determined to be 10 years and 5 years, respectively.

		Expected life
SmartACR intellectual property	$75,000	10 years
Customer relationship	32,400	5 years
Total	**$107,400**	

7. Short-term Loans

On May 20, 2013, the Company obtained a short term loan of $125,000 from an investor. The loan had annual interest rate of 6% and matured in three months, on August 20, 2013. The loan's maturity date has been extended to December 31, 2013 and interest rate reset to 8%. This loan was paid off in May 2015.

On June 25, 2015, the Company obtained a short term loan of $200,000 from an investor. The loan has monthly interest rate of 1% and matures on October 31, 2015 with a 60 day extension. Any portion of principal that remains outstanding on December 31, 2015 can be converted to Smartcool common shares at a price of $0.06 per share, at the note holder's discretion. Principal of $130,000 less prepaid interest of $8,000 was advanced to the Company on June 25, 2015. The remaining balance of $70,000 will be advanced when the Company provides a 7 day notice.

Interest expense for the three months ended June 30, 2015 was $8,367 (June 30, 2014 - $1,427). Interest expense for the six months ended June 30, 2015 was $9,467 (June 30, 2014 - $3,927).As at June 30, 2015, the outstanding balance of short term loans was $130,000. (December 31, 2014 - $67,238).

8. Obligations Under Acquisition Contracts

TECC Services

In July 2008, the Company acquired the exclusive rights to distribute the ESMTM in the United Kingdom, Spain, Portugal, and the Middle East from T.E.C.C. 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. Upon closing, payment of $873,393 (£435,000) was made and 743,709 shares were issued. The remaining balance of $1,204,680 (£600,000) was due in scheduled instalments over four years with the last payment due on July 16, 2012. The obligation amount of $1,204,680 (£600,000) was originally non-interest bearing and was recorded at its present value using a discount rate of 16%. The purchase agreement was then amended in 2009 and again in 2012 to accrue interest at Royal Bank of Canada prime rate plus 4% and to adjust timing and amount of repayments.

As at December 10, 2013, the balance of $886,714 (£508,217), including accrued interest of $145,181 (£83,217), was outstanding. The Company was able to negotiate a debt reduction and the existing obligation was extinguished and replaced with two new obligations. These new obligations had principal amounts of $226,798 (£130,000) and $112,527 (£64,500), are non-interest bearing, unsecured, and were to be paid in annual installments over 5 years starting December 15, 2014.

The fair values of the new obligations were determined to be $155,182 (£88,950) and $73,317 (£42,025) based on discounting the future payments at 16%. The obligations under the acquisition contracts are being accreted to their face value over their term. The accretion charge for the period is recorded within interest expense.

This debt settlement resulted in a gain of $658,215 for the year ended December 31, 2013.

In March 2015, the Company issued 490,200 common shares at a deemed price of $0.05 per share to settle a portion of the obligations that was due on December 15, 2014 (£12,900).

As at June 30, 2015, the outstanding balance was $292,153 (£148,950).

Balance, January 1, 2013	**$776,611**
Accrued interest	45,968
Foreign exchange	64,135
Debt reduction	(658,215)
Balance, December 10, 2013	**228,499**
Accretion	2,154
Foreign exchange	2,372
Balance, December 31, 2013	**233,025**
Accretion	38,303
Foreign exchange	5,565
Balance, December 31, 2014	**276,893**
Debt settlement	(24,510)
Accretion	16,562
Foreign exchange	23,208
Balance, June 30, 2015	**292,153**
Current portion	**(148,734)**
Long-term portion	**$ 143,419**

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). Upon closing, $2,922,622 (£1,840,438) was settled in cash with the remaining balance of $1,582,200 (£1,000,000) due in four equal installments over the next 12 months. The Company was unable to make the first quarterly payment as scheduled.

As at December 10, 2013, the principal balance of $1,744,600 (£1,000,000) and accrued interest of $285,274 (£163,517) were outstanding. The Company was able to negotiate a debt reduction and the existing obligation was extinguished and replaced with two new obligations. These new obligations had principal amounts of $130,845 (£75,000), which is non-interest bearing, secured, and will be paid in installments over 6 months, and $53,210 (£30,500), which is non-interest bearing, unsecured, and will be paid in installments over 5 years. Fees of $2,291,510 (£1,300,000) were to be payable by the Company if it defaults on any of the prepayment terms with respect to the obligation with a principal amount of £75,000.

Their fair values were determined to be $126,048 (£72,250) and $40,230 (£23,060), respectively, based on discounting the future payments at 10%. The obligations under the acquisition contracts are being accreted to their face value over their term. The accretion charge for the period is recorded within interest expense.

This debt settlement resulted in a gain of $1,863,596 for the year ended December 31, 2013.

The terms of the obligation with principal amount of £75,000 was renegotiated again in December 2014.

Payment of $19,091(£10,000) was made in February 2015. In March 2015, the Company issued 231,800 common shares at a deemed price of $0.05 per share to settle a portion of the obligations that was due on December 15, 2014 (£6,100).

As at June 30, 2015, the outstanding balance was $88,935 (£45,368).

Balance, January 1, 2013	**$1,759,746**
Accrued interest	122,072
Foreign exchange	148,056
Debt reduction	(1,863,596)
Balance, December 10, 2013	**166,278**
Accretion	980
Foreign exchange	1,724
Balance, December 31, 2013	**168,982**
Payments	(73,219)
Accretion	8,454
Foreign exchange	5,109
Balance, December 31, 2014	**109,326**
Payments	(30,681)
Accretion	1,865
Foreign exchange	8,425
Balance, June 30, 2015	**88,935**
Current portion	(57,639)
Long-term portion	**$31,296**

At June 30, 2015, the carrying amount of these obligations was as follows:

TECC and Smartcool UK Modified Acquisition Obligations	TECC 1	TECC 2	UK 1	UK 2	Total
Balance December 10, 2013	**$155,182**	**$73,317**	**$126,048**	**$40,230**	**$394,777**
Accretion	1,463	691	743	237	3,134
Foreign exchange	1,611	761	1,307	417	4,096
Balance, December 31, 2013	**158,256**	**74,769**	**128,098**	**40,884**	**402,007**
Payments	-	-	(73,219)	-	(73,219)
Accretion	26,033	12,270	4,256	4,198	46,757
Foreign exchange	3,764	1,801	4,114	995	10,674
Balance, December 31, 2014	**188,053**	**88,840**	**63,249**	**46,077**	**386,219**
Payments		(24,510)	(19,091)	(11,590)	(55,191)
Accretion	10,985	5,577	-	1,865	18,427
Foreign exchange	16,302	6,906	4,877	3,548	31,633
Balance, June 30, 2015	215,340	76,813	49,035	39,900	381,088
Current portion	(133,594)	(15,140)	(49,035)	(8,604)	(206,373)
Long-term portion	**$ 81,746**	**$ 61,673**	**$-**	**$ 31,296**	**$ 174,715**

Pursuant to the negotiated extensions, these obligations are to be repaid as follows:

- £130,000 in five instalments of £26,000 on December 15, 2014 and June 15, 2015, 2016, 2017 and 2018;
- £95,000 in five instalments of £19,000 on December 15, 2014, 2015, 2016, 2017 and 2018; and
- £35,000 in a lump sum payment of £10,000 in January 2015 and monthly instalments of £4,000 until the debt has been repaid in full.

9. Debt Settlement

a) In February 2015, the Company received 810,520 common shares of ATI Airtest Technologies at a deemed price of $0.05 to settle outstanding trade receivables of US$15,975 and CDN$25,000. This settlement resulted in a loss of $4,456 which has been recognized in the statement of operations.

These shares have been classified as available-for-sale financial assets. As at June 30, 2015, the market value of these shares was $36,473. This change in fair value has been recorded in other comprehensive income.

b) In March 2015, the Company issued 4,630,440 common shares at a deemed price of $0.05 per share to settle outstanding debts of $231,522 with two consultants, four employees and two former directors of the Company.

	Amount	Number of shares
Consulting fees	$93,350	1,867,000
Salaries	100,000	2,000,000
Expenses	2,072	41,440
Acquisition obligations	36,100	722,000
Total	$231,522	4,630,440

10. Debentures

In 2010, the Company issued 122 debenture units at $5,000 per unit for aggregate proceeds of $610,000. Each unit comprised a debenture with a principal balance of $5,000 and 8,600 share purchase warrants. Finder's fees of $57,249 were paid to the brokers. The net proceeds of $552,751 were allocated between the fair values of the liability component ($544,650) and the equity component relating to the share purchase warrants ($8,101) using the residual method. The liability component was measured at amortized cost. The $8,101 was credited to the reserve for equity settled share-based transactions.

One whole warrant entitled the holder to purchase one common share at the price of $0.50 per share for a period of three years from the date of issuance. If the Company's shares trade at an average price of $0.80 per share for a period of 60 days, the Company, at its election, may force exercise or cancellation of the warrants.

The Company did not make quarterly principal payments under the terms of the debentures and in January 2013 approached all holders requesting an extension of up to two years. The debenture holders agreed to extend the debentures effective March 1, 2013 under the following terms:

Two additional interest payments ($300 per unit) as specified by the original terms were added to outstanding principal balance; and

Interest of 12% on the outstanding principal balance was to be paid quarterly commencing June 1, 2013.

The Company also agreed to issue 3,000 share purchase warrants for each unit and 351,000 new warrants were issued (note 11 (c)).

The terms of the debenture extension were significantly different from the original terms, resulting in a loss on debt extinguishment of $7,606. This loss was netted against the gain on debt settlement. The new principal balance of $345,090 was allocated between the fair values of the liability component ($292,397) and the equity component relating to the share purchase warrants ($52,693) using the residual method. The liability component was measured at amortized cost. The $52,693 was credited to the reserve for equity settled share-based transactions.

There were 71 units outstanding on maturity date March 1, 2015. The Company was unable to redeem them or make interest payments totaling $28,892 as scheduled.

Two debenture holders with total outstanding balance of $31,116 did not agree to extend the terms of their debentures but the Company was able to reach an agreement with 12 debenture holders to refinance the majority of these secured debentures. These secured debentures, which expired March 1, 2015 and which, in the aggregate, represent total debt of $238,546, have been replaced by new, unsecured debentures. The new debentures bear interest at 12% payable monthly, with 50% of the principal amount to be repaid on September 30, 2015 and the balance to be paid at maturity on March 31, 2016. In addition, the Company has issued 238,546 warrants (note 11 (3)) to the debenture holders. These non-transferable warrants will entitle the holder to purchase one common share of the Company for an exercise price of $0.06 until they expire on March 31, 2016. This refinancing was approved by the TSX Venture Exchange.

The terms of the new debentures were not significantly different from the original terms and no gain or loss on debt extinguishment was recognized. The new 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 was measured at amortized cost. The $23,133 was credited to the reserve for equity settled share-based transactions.

At June 30, 2015, the principal balance of the new debentures was $238,546 and the carrying amount was $225,665.

Maturity date	**March 31, 2016**
Balance at March 31, 2015	$216,231
Accrued interest	16,590
Interest payments	(7,156)
Balance at June 30, 2015	**$ 225,665**
Current portion	(225,665)
Balance	$-

During the three months ended June 30, 2015, accrued interest of $16,590 (June 30, 2014 - $12,534) was calculated by applying the weighted average effective interest rate of 26% to the liability component of the debentures.

At June 30, 2015, the principal balance of the debentures that matured on March 1, 2015 was $20,116 and the carrying amount was $21,099.

Maturity date	**March 1, 2015**
Balance at March 1, 2013	$214,629
Accrued interest	45,172
Interest payments	(22,722)
Principal payments	(19,981)
Balance at December 31, 2013	**$ 217,098**
Accrued interest	49,595
Interest payments	(7,223)
Balance at December 31, 2014	**$259,470**
Accrued interest	10,192
Balance at March 31, 2015	269,662
Replaced by new debentures	(238,546)
Remaining balance, March 31, 2015	31,116
Accrued interest	1,245
Interest payments	(262)
Principal payments	(11,000)
Balance at June 30, 2015	**$21,099**
Current portion	(21,099)
Balance	$-

11. 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, 2013	**64,287,297**	**$29,835,392**
Issued for cash via private placements (i)(ii)	15,000,000	500,000
Share issuance costs	-	(26,317)
Balance, December 31, 2013	**79,287,297**	**30,309,075**
Issued for cash via private placements (iii)	9,730,000	430,600
Share issuance costs	-	(6,262)
Balance, December 31, 2014	**89,017,297**	**$30,733,413**
Issued via private placements (iv)(v)	25,780,000	629,396
Issued for debt settlement (vi)	4,630,440	231,522
Share issuance costs	-	(26,714)
Balance, June 30, 2015	**119,427,737**	**$ 31,567,617**

i. On June 7, 2013, the Company completed a non-brokered private placement consisting of 10,000,000 common shares at a price of $0.025 per share for aggregate gross proceeds of $250,000. Cash issuance costs of $15,911 were allocated to common shares.

ii. On September 30, 2013, the Company completed a non-brokered private placement consisting of 5,000,000 common shares at a price of $0.05 per share for aggregate gross proceeds of $250,000. Cash issuance costs of $10,406 were allocated to common shares.

iii. On April 25, 2014, the Company issued 9,730,000 Units at $0.05 per unit pursuant to a non-brokered private placement for gross proceeds of $486,500. Of this amount, $430,600 was allocated to share capital and $55,900 to share purchase warrants (note 11 (c)(ii)). Each Unit consists of one common share and one-half warrant. Cash issuance costs of $6,262 were allocated to common shares.

iv. On January 28, 2015, the Company issued 14,000,000 Units at $0.025 per unit pursuant to a non-brokered private placement for gross proceeds of $350,000. Of this amount, $237,300 was allocated to share capital and $112,700 to share purchase warrants (note 11 (c)(iii)). Each Unit consists of one common share and one warrant. Cash issuance costs of $7,742 were allocated to common shares.

v. On May 4, 2015, the Company issued 11,780,000 Units at $0.05 per unit pursuant to a non-brokered private placement for gross proceeds of $589,000. Of this amount, $392,096 was allocated to share capital and $196,904 to share purchase warrants (note 11 (c)(iv)). Each Unit consists of one common share and one warrant. Cash issuance costs of $18,972 were allocated to common shares.

vi. On March 12, 2015, the Company issued 4,630,440 common shares at $0.05 per share to settle debt in the aggregate amount of $231,522.

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 12,161,745. In 2010, the stock option plan was amended to extend the option term to a maximum period of ten years.

As at June 30, 2015, 13,735,000 options were outstanding. These options have vesting periods of up to 5 years and weighted average exercise price of $0.06. 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, 2013	3,900,000	$0.28*
Granted	2,880,000	0.05
Forfeited and cancelled	(120,000)	0.53
Expired or exercised	(225,000)	0.08
Balance, December 31, 2013	6,435,000	$0.08
Granted	1,200,000	0.05
Forfeited and cancelled	(815,000)	0.11
Expired or exercised	(605,000)	0.10
Balance, December 31, 2014	**6,215,000**	**$0.07**
Granted	8,070,000	0.05
Expired or exercised	(550,000)	0.10
Balance, June 30, 2015	**13,735,000**	**$0.06**

* 0.13 after repricing

During the six months ended June 30, 2015, 5,370,000 (December 31, 2014 – Nil) options with weighted average fair value $0.03 were granted to directors, officers and employees. Out of these options, 1,970,000 had an exercise price ($0.05) lower than the stock price ($0.06) at the date of the grant. During the same period, 2,700,000 (December 31, 2014 - 1,200,000) options with weighted average fair value of $0.03 (December 31, 2015 - $0.035) were granted to consultants. Out of these options, 2,500,000 had an exercise price ($0.05) lower than the stock price ($0.06) at the date of the grant.

Share-based payments for the quarter ended June 30, 2015 was \$ 97,427 (June 30, 2014 - \$26,486), of which \$64,605 (June 30, 2014 - \$16,391) was related to directors, officers and employees and \$32,822 (June 30, 2014 - \$10,095) was related to consultants.

Share-based payments for the six months ended June 30, 2015 was \$136,711 (June 30, 2014 - \$67,592) of which \$102,917 (June 30, 2014 – \$36,762) was related to directors, officers and employees and \$33,794 (June 30, 2014 - \$30,830) was related to consultants.

c. *Share purchase warrants*

i. Pursuant to the terms of the March 1, 2013 debenture extension, the Company issued 351,000 share purchase warrants to debenture holders. Each warrant entitles the holder to purchase one common share at a price of \$0.15 until March 1, 2015. The fair value of these warrants was determined to be \$52,693, using the residual method (note 10).

ii. On April 25, 2014, the Company issued 9,730,000 Units at \$0.05 per unit pursuant to a non-brokered private placement for gross proceeds of \$486,500. Of this amount, \$430,600 was allocated to share capital and \$55,900 to share purchase warrants.

iii. On January 28, 2015, the Company issued 14,000,000 Units at \$0.025 per unit pursuant to a non-brokered private placement for gross proceeds of \$350,000. Of this amount, \$237,300 was allocated to share capital and \$112,700 to share purchase warrants. Cash issuance costs of \$2,157 were allocated to share purchase warrants.

iv. On May 4, 2015, the Company issued 11,780,000 Units at \$0.05 per unit pursuant to a non-brokered private placement for gross proceeds of \$589,000. Of this amount, \$392,096 was allocated to share capital and \$196,904 to share purchase warrants. Cash issuance costs of \$9,713 were allocated to share purchase warrants.

As at June 30, 2015, there were 26,130,546 (December 31, 2014 – 5,216,000) outstanding warrants with weighted average share price of \$0.08 (December 31, 2014 - \$0.10).

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, 2013	**9,115,865**	**$0.43**
Granted	351,000	0.15
Expired, exercised or cancelled	(8,615,865)	0.44
Balance, December 31, 2013	**851,000**	**$0.24**
Granted	4,865,000	0.10
Expired, exercised or cancelled	(500,000)	0.30
Balance, December 31, 2014	**5,216,000**	**$0.10**
Granted	26,130,546	0.08
Expired, exercised or cancelled	(5,216,000)	0.10
Balance, June 30, 2015	**26,130,546**	**$0.08**

Expiry date	Number of shares	Exercise price	Weighted average contractual life (years)
March 31, 2016	238,546	0.06	0.75
January 28, 2017	14,000,000	0.06	1.58
May 4, 2017	11,892,000	0.10	1.84
Balance, June 30, 2015	**26,130,546**	**$0.08**	**1.69**

d. ***Shares pending issue***
Pursuant to a license termination agreement effective February 28, 2015 (note 12), 500,000 common shares at a deemed price of $0.05 per share will be issued to SmartACR.

e. ***Warrants pending issue***
Pursuant to an independent contractor agreement (note 12), 2,000,000 share purchase warrants will be issued to the owner of SmartACR.

12. SmartACR Absorption

On February 28, 2015, the Company executed a Termination Agreement ("TA") to terminate the license agreement with a licencee ("SmartACR") and to provide for the transition of a portion of

SmartACR's business to the Company. On March 1, 2015, the Company executed an Independent Contractor Agreement ("ICA") with the principal owner of SmartACR. The main reason for the business absorption was to acquire a technology designed by SmartACR, which enhances the application of Smartcool's ESM logarithm. Also, SmartACR has developed customer relationships with several major restaurant chains in North America.

Pursuant to the terms of the TA, the Company will issue an aggregate of 500,000 common shares of the Company at a deemed price of $0.05 per share and issue warrants to purchase 2,000,000 common shares of the Company at an exercise price of $0.05 per share for a period expiring on the earlier of (i) the third anniversary of the date of the termination agreement or (ii) the expiration or earlier termination of the ICA.
Pursuant to the terms of the ICA, the contractor will provide consulting services by acting as the VP Sales and Marketing, North America for a fee of $USD10,000 per month for the initial term from March 1, 2015 to February 29, 2016, and any renewal terms. The Company will grant the contractor options to purchase 500,000 common shares of the Company at an exercise price of $0.05 which shall vest in four equal instalments. After the end of the initial term and, if applicable, up to two consecutive renewal terms, the contractor shall be eligible to receive an annual performance bonus in an amount equal to 33% of the profit (as defined) during the immediately preceding 12 month period. The aggregate amount of all performance bonuses shall not exceed $400,000.

The fair value of the shares has been determined to be $25,000 (note 11(d)) and the fair value of the warrants $82,400 (note 11(e)). The allocation of the purchase price is based on management's estimates and certain assumptions with respect to the fair value increment associated with the assets acquired.

The purchase price allocation is summarized as follows:

	CAD
Common shares	$25,000
Fair value of warrants	82,400
	$107,400
Allocation of the purchase price	
Intellectual property	$75,000
Customer relationships	32,400
	$107,400

13. 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. During the three and six months ended June 30, 2015, these liabilities were reduced by $12,696 and $22,318, respectively (June 30, 2014 – Discontinued Operations $21,428 and $38,759) upon the recognition of amortization costs of these assets.

As at June 30, 2015, deferred tax liability was $227,601.

Balance, January 1, 2013	**$477,277**
Amortization of intangible assets	(67,890)
Effect of foreign exchange rate	36,367
Balance, December 31, 2013	**445,754**
Amortization of intangible assets	(73,909)
Impairment of intangible assets	(137,466)
Effect of foreign exchange rate	15,540
Balance, December 31, 2014	**249,919**
Amortization of intangible assets	(22,318)
Balance, June 30, 2015	**$ 227,601**

14. Segmented Information

The Company installs, distributes, markets and sells the ECO3 and ESM™ products and peripherals. Revenue from the ECO3 for the three and six months ended June 30, 2015 was $88,361 and $240,354, respectively. Revenue for the ESM™ solution for the three and six months ended June 30, 2015 was $93,494 and $131,167, respectively.
The Company operates in one segment. Revenue was derived from customers located in the following geographical regions:

Continuing Operations	**Three months ended June 30 2015**		**Three months ended June 30 2014**	
	Amount	**%**	**Amount**	**%**
Americas	$ 134,716	74	$ 63,886	33
Europe, Middle East, Africa	47,139	26	-	-
Australia	-	-	128,529	67
Total revenue	**$181,855**	**100**	**$ 192,415**	**100**

Continuing Operations	**Six months ended June 30 2015**		**Six months ended June 30 2014**	
	Amount	**%**	**Amount**	**%**
Americas	$ 262,891	71	$ 147,493	36
Europe, Middle East, Africa	108,630	29	-	-
Australia	-	-	259,397	64
Total revenue	**$371,521**	**100**	**$406,890**	**100**

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

15. Commitments

Premise Lease
The Company entered into a lease agreement to lease office facilities in Vancouver. This lease expired in May 2015.

Consulting Agreements
In December 2014, the Company entered into a consulting agreement with Maxwell Mercantile Inc. and Theodore Konyi, 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.

Debenture
The Company has a commitment to make principal repayments and interest payments related to debentures issued (note 10).

16. 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 Mercantle	Management services
Brad Nightingale Consulting	Consulting services
Global Telematic Solutions	Consulting services
384518 BC Ltd.	Consulting services
Windstone Financial Corp.	Consulting services
Richards Buell Sutton LLP	Legal services
Accupro Trademark Services LLP	Trademark 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.

	Three months ended June 30		**Six months ended June 30**	
	2015	2014	2015	2014
Management fees	$45,000	$-	$90,000	$-
Consulting fees	$ 79,508	$10,500	$ 100,162	$21,000
Legal fees	1,171	4,019	4,964	4,743
	$ 125,679	**$14,519**	**$ 195,126**	**$25,743**

Due to/from Related Parties

Included in trade and other receivables is $5,000 due from the President as at June 30, 2015 (December 31, 2014 - $5,000) related to an advance for travel expenses. The amount is unsecured, non-interest bearing and has no fixed terms of repayment.

Included in trade payables and accruals is $252,254 due to related parties as at June 30, 2015 (December 31, 2014 - $434,324) as follows:

	June 30, 2015	**December 31, 2014**
Chief Executive Officer	$ 7,754	$-
President of the Company	78,031	112,879
Chief Financial Officer	41,667	75,632
Executive VP	8,826	37,046
VP of Operations	55,000	90,297
Other related parties	103,105	118,470
Total	**$ 294,383**	**$434,324**

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

17. Financial Instruments

Financial Instruments

The Company has classified its financial instruments as follows:

	June 30, 2015	December 31, 2014
Financial assets		
FVTPL , measured at fair value:		
Cash and cash equivalents	$44,174	$15,490
Available-for-sale, measured at fair value:		
Securities	36,473	-
Loans and accounts receivable, recorded at amortized		
Trade and other receivables	433,348	143,258
	$ 513,995	**$ 158,748**
Other financial liabilities, recorded at amortized cost		
Trade payables	$ 624,842	$ 826,630
Short-term loan	130,000	67,238
Acquisition obligations and debentures	627,852	645,689
	$ 1,382,694	**$ 1,539,557**

Interest income from FVTPL and interest expense from short-term loan, acquisition obligations, debentures and other financial liabilities are recognized in finance income and expense.

Unrealized 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 value of cash and cash equivalents, trade and other receivables, obligations under acquisition contracts, debentures and trade payables approximates the 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, and market 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 receivable. 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.

The Company has $ 353.348 (December 31, 2014 - $138,258) in trade receivables which are subject to credit risk.

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	$ 624,842	$ 624,842	$-
Short-term loan	130,000	130,000	-
Debentures	246,764	246,764	-
Obligations under acquisition	271,156	206,373	64,783
Total	**$ 1,272,762**	**$ 1,207,979**	**$ 64,783**

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 June 30, 2015, the Company's monetary assets and liabilities denominated in foreign currencies are as follows:

	USD	AUD	GBP
Assets			
Cash and cash equivalents	$18,281	$-	£-
Trade and other receivables	266,919	-	-
Total	**$285,200**	**$-**	**£-**
Liabilities			
Trade payables and accruals	$144,905	$2,622	£37,032
Acquisition obligations, current	-	-	105,217
Total	**$144,905**	**$2,622**	**£142,249**

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	($28,520)	$-	£-
Monetary liabilities	14,490	262	14,225
Net gain (loss)	**($14,030)**	**$262**	**£14,225**

Gain (loss) on $0.10 decrease in CAD	**USD**	**AUD**	**GBP**
Monetary assets	$28,520	$-	£-
Monetary liabilities	(14,490)	(262)	(14,225)
Net gain (loss)	**$14,030**	**(262)**	**(£14,225)**

e. ***Interest rate risk***

The Company is not exposed to this risk. TECC and Smartcool obligations under acquisition contracts have been modified and are no longer bearing interest based on Royal Bank of Canada prime rate.

18. General and Administrative Expenses

	Three months ended June 30, 2015	Three months ended June 30, 2014
Advertising and promotion	$9,541	$4,729
Bad debts	-	-
Consulting & management fees	220,278	95,597
Filing and transfer fees	32,579	3,892
Insurance	1,962	2,345
Interest	134	(86)
Investor relations	5,208	15,393
Product certification	1,501	2,617
Professional fees	24,310	6,305
Office and supplies	17,931	10,128
Rent	8,799	19,116
Salaries and benefits	117,437	120,412
Telephone	4,247	3,497
Travelling	29,604	7,943
Total selling, general & admin expenses	**473,530**	**291,888**
Share-based compensation	97,427	26,486
Amortization & depreciation	147,984	81,000
Total operating expenses	**$718,941**	**$399,374**

	Six months ended June 30, 2015	Six months ended June 30, 2014
Advertising and promotion	$9,875	$6,714
Bad debts	(15,894)	-
Consulting & management fees	327,342	167,591
Filing and transfer fees	39,527	10,298
Insurance	4,901	6,337
Interest	251	22
Investor relations	20,342	15,393
Product certification	3,042	2,617
Professional fees	49,981	9,643
Office and supplies	25,507	18,703
Rent	33,155	43,397
Salaries and benefits	245,519	234,448
Telephone	7,676	7,364
Travelling	57,905	15,061
Total selling, general & admin expenses	809,130	537,588
Share-based compensation	136,711	67,592
Amortization & depreciation	304,187	162,001
Total operating expenses	**$1,250,029**	**$767,181**

19. 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 June 30, 2015, the principal amount of debenture component was $258,662 (December 31, 2014 - $240,769) and shareholders' equity was $1,111,948 (December 31, 2014 - $656,370). The increase in shareholders' equity was attributable to January and May 2015 capital financing.

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;
- 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.

20. Discontinued Operations

In September 2014, as revenue from the Europe, Middle East region had significantly declined and there were no immediate sales anticipated, to reduce operating losses the Company decided to discontinue Smartcool EMEA and Smartcool UK's existing operations and shift the region's business focus from direct sales to distribution sales. These regional operations have been classified and accounted for as discontinued operations. The distribution rights in Europe, Middle East and Africa and customer relationship intangible assets reverted back to the Company as specified in the distribution agreement. The Company also assumed the obligations under acquisition contracts as it was a guarantor under the acquisition agreements.

An impairment loss of $607,260 was recognized based on a fair value less costs-to-sell assessment, which compared the carrying values of the liquidated assets and liabilities as of September 27, 2014 to their estimated realizable values.

Assets with liquidation value of $6,817 were acquired for $10,123 and liabilities of $32,834 were assumed by the Company in October 2014.

Loss from discontinued operations consists of the following:

	Three months ended June 30, 2015	**Three months ended June 30, 2014**
Revenue	$-	$ 7,129
Cost of sales adjustment	-	4,285
Gross profit	-	11,414
Operating expenses	-	(313,409)
Finance expense	-	(9,284)
Foreign exchange gain	-	(1,448)
Gain on sale of equipment	-	9,258
Income tax recovery	-	19,429
Loss from discontinued operations	**$-**	**($284,040)**

	Six months ended June 30, 2015	Six months ended June 30, 2014
Revenue	$-	$ 286,849
Cost of sales	-	(35,958)
Gross profit	-	250,891
Operating expenses	-	(703,657)
Finance expense	-	(19,877)
Foreign exchange gain	-	(2,442)
Gain on sale of equipment	-	10,171
Income tax recovery	-	38,759
Loss from discontinued operations	**$-**	**($426,155)**