SMARTCOOL™

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

For the three months ended September 30, 2016 and 2015
Expressed in Canadian Dollars

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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™

Smartcool Systems Inc.

Condensed consolidated statements of financial position

(Expressed in Canadian dollars, unless otherwise stated)

	September 30 2016	December 31 2015
	$	$
ASSETS		
Current assets		
Cash and cash equivalents	22,068	18,478
Available-for-sale securities (note 8)	20,263	12,158
Trade and other receivables (note 3)	314,785	507,718
Inventory (note 4)	144,326	61,211
Prepaid expenses and deposits	71,618	125,651
	573,060	725,216
Property and equipment	6,687	18,840
Intangible assets (note 5)	1,280,131	1,692,967
Total assets	1,859,878	2,437,023
LIABILITIES		
Current liabilities		
Trade payables and accruals	732,234	759,990
Short-term loans (note 6)	403,560	276,450
Current portion of obligations under acquistion contracts (note 7)	266,687	258,562
Current portion of debentures (note 9)	273,227	254,707
	1,675,708	1,549,708
Obligations under acquisition contracts (note 7)	99,107	155,967
Deferred tax liability (note 12)	164,121	202,209
Total liabilities	1,938,936	1,907,884
SHAREHOLDERS' EQUITY		
Share capital (note 10(a))	32,081,737	31,672,684
Shares pending issue	-	52,250
Reserve for equity settled share based transactions (note 10(b))	6,641,572	6,547,080
Accumulated other comprehensive income	(351,488)	(380,654)
	38,371,821	37,891,360
Deficit	(38,450,879)	(37,362,221)
	(79,058)	529,139
Total liabilities and shareholders' equity (deficiency)	1,859,878	2,437,023

Approved and authorized for issue by the Board of Directors on November 29, 2016

"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)

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
	$	$	$	$
Revenue	81,547	126,602	250,897	498,123
Cost of sales	13,829	35,172	64,050	92,142
Gross profit	67,718	91,430	186,847	405,981
Operating Expenses				
General and administrative expenses (note 17)	269,043	346,948	811,679	1,156,081
Share-based compensation (note 10(b))	5,702	64,406	36,983	201,117
Research and development	-	965	2,027	965
Amortization and depreciation (note 5)	142,060	145,763	426,253	449,950
	416,805	558,082	1,276,942	1,808,113
Operating loss	(349,087)	(466,652)	(1,090,095)	(1,402,132)
Rental income	-	-	-	47,546
Finance expense	(24,191)	(24,317)	(81,149)	(80,234)
Finance income	-	-	11	-
Foreign exchange gain (loss)	(12,598)	9,179	44,486	(14,553)
Loss on receivables settlement (note 8)	-	-	-	(4,456)
	(36,789)	(15,138)	(36,652)	(51,697)
Loss before income tax	(385,876)	(481,790)	(1,126,747)	(1,453,828)
Income tax recovery	12,696	12,645	38,088	34,963
Net loss for the period, net of tax	**(373,180)**	**(469,146)**	**(1,088,659)**	**(1,418,866)**
Net loss per share				
Basic	(0.00)	(0.00)	(0.01)	(0.01)
Diluted	(0.00)	(0.00)	(0.01)	(0.01)
Weighted average number of common shares outstanding (basic and diluted)	**135,848,172**	**119,427,737**	**128,882,336**	**105,075,829**

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.
Consolidated statements of comprehensive loss
(Expressed in Canadian dollars, unless otherwise stated)

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
	$	$	$	$
Net loss for the period	**(373,180)**	**(469,146)**	**(1,088,659)**	**(1,418,866)**
Other comprehensive loss	8,914	2,159	29,166	9,089
Total comprehensive loss	**(364,266)**	**(466,987)**	**(1,059,493)**	**(1,409,777)**

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.
Consolidated statements of cash flows
(Expressed in Canadian dollars, unless otherwise specified)

	Three months ended September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
	$	$	$	$
Cash flows from operating activities				
Net loss for the period	(373,180)	(469,146)	(1,088,659)	(1,418,866)
Items not affecting cash:				
Depreciation of property and equipment	4,448	5,281	13,417	21,166
Amortization of intangible assets	137,612	140,482	412,836	428,784
Shares issued to settle trade payables	-	-	-	195,422
Note receivable executed for shares issued	-	-	-	75,000
Shares received to settle trade and other receivables	-	-	-	(40,526)
Share-based compensation	5,702	64,406	36,983	201,117
Deferred tax liability	(12,696)	(12,696)	(38,088)	(35,014)
Deferred tenant inducement	-	-	-	(6,744)
Foreign exchange (gain) loss	(3,743)	11,360	(68,917)	42,764
Accrued interest on short-term loans	11,161	-	31,200	-
Accrued interest on debentures	7,567	5,473	28,177	23,080
Accretion of obligation under acquisition contract	5,464	9,377	19,773	27,803
	(217,665)	(245,463)	(653,278)	(486,013)
Changes in non-cash working capital items:				
Trade and other receivables	48,889	1,344	167,933	(291,638)
Inventory	9,059	2,635	(83,115)	(41,009)
Prepaid expenses and deposits	583	(7,005)	54,033	(44,681)
Trade payables and accruals	(25,398)	60,349	(27,756)	(167,269)
Net cash flows used in operating activities	(184,532)	(188,140)	(542,183)	(1,030,610)
Cash flows from investing activities				
Purchase of property and equipment	(1,312)	-	(1,312)	-
Net cash used in investing activities	(1,312)	-	(1,312)	-
Cash flows from financing activities				
Shares and warrants issued for cash net of issue costs	151,572	-	439,312	825,418
Short-term loan	46,368	173,533	96,368	234,829
Decrease in debentures	(9,656)	(5,000)	(9,656)	(13,000)
Decrease in acquisition contract obligation	-	-	-	(19,091)
Net cash (used in) provided by financing activities	188,284	168,533	526,024	1,028,156
Net decrease in cash and cash equivalents	2,439	(19,607)	(17,472)	(2,454)
Effects of exchange rates changes on cash	4,861	13,767	21,061	25,299
Cash and cash equivalents, beginning of period	14,767	44,174	18,478	15,490
Cash and cash equivalents, end of period	22,068	38,334	22,068	38,334

See accompanying notes to the consolidated financial statements

SMARTCOOL™

Smartcool Systems Inc.

Consolidated statements of shareholders' equity (deficiency)

(Expressed in Canadian dollars, unless otherwise stated)

	Share capital	Reserve for equity settled share based transactions	Accumulated other comprehensive income	Deficit	Total Shareholders' Equity (Deficiency)
	$	$	$	$	$
Balance at January 1, 2015	**30,733,413**	**5,994,511**	**(385,806)**	**(35,685,748)**	**656,370**
Net loss				(1,418,866)	(1,418,866)
Available-for-sale securities unrealized loss			(16,210)		(16,210)
Foreign currency translation adjustment			25,299		25,299
Total comprehensive loss for the period			9,089	(1,418,866)	(1,409,777)
Share issued for:					
Private placement	662,896				662,896
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		201,117			201,117
Balance at September 30, 2015	**31,626,117**	**6,598,078**	**(376,717)**	**(37,104,615)**	**742,863**
Net loss				(257,606)	(257,606)
Available-for-sale securities unrealized loss			(12,158)		(12,158)
Foreign currency translation adjustment			8,221		8,221
Total comprehensive loss for the period			(3,937)	(257,606)	(261,544)
Share issued for:					
Private placement	73,300				73,300
Shares subscribed	27,250				27,250
Warrants		(55,700)			(55,700)
Share issue costs	(1,734)	(434)			(2,168)
Share-based compensation		5,136			5,136
Balance at December 31, 2015	**31,724,933**	**6,547,080**	**(380,654)**	**(37,362,221)**	**529,139**
Net loss				(1,088,659)	(1,088,659)
Available-for-sale securities unrealized loss			8,105		8,105
Foreign currency translation adjustment			21,061		21,061
Total comprehensive loss for the period			29,166	(1,088,659)	(1,059,492)
Share issued for:					
Private placements	366,375				366,375
Warrant exercise	4,387	(4,387)			-
Warrants		64,424			64,424
Warrants pending issue					-
Share issue costs	(13,959)	(2,529)			(16,488)
Share-based compensation		36,983			36,983
Balance at September 30, 2016	**32,081,737**	**6,641,572**	**(351,488)**	**(38,450,879)**	**(79,058)**

See accompanying notes to the consolidated financial statements

Smartcool Systems Inc.
Notes to the Consolidated Financial Statements
For the three months ended September 30, 2016
(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 ESMTM and ECO3TM to end customers and to distributors worldwide.

The ESMTM 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 ESMTM uses microprocessor technology and software algorithms.

Introduced in early 2009, the ECO3TM 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 ESMTM for these smaller systems.

During the quarter ended September 30, 2016, the Company had a net loss of $373,180 compared to $469,146 for the same quarter of 2015.

The company had a deficit of $38,450,879 as at September 30, 2016 (December 31, 2015 - $37,362,221). As at September 30, 2016, the Company had negative working capital of $1,102,648 (December 31, 2015 - $824,492). This reduction of working capital was attributable

to operating loss. To ensure that the Company continues to be a going concern over the next twelve months, the Company has raised additional capital by way of private placements in 2016. Significant growth in revenue as a result of the licensing of Connected Holdings is expected.

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 September 30, 2016 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, 2015.

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

Significant Judgments

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

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

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

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

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

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.

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 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 where the Canadian dollar is not the functional currency 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 recorded as a foreign currency translation adjustment, which is a component of accumulated other comprehensive income. On disposal of a foreign operation, the deferred cumulative amount included in accumulated other comprehensive income 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 recognized in foreign exchange gain or loss in the statement of operations.

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 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.

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 September 30, 2016 and December 31, 2015.

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 September 30, 2015 and December 31, 2015.

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.

The Company holds common shares of ATI Airtest Technologies Inc., a venture company traded on the TSX Venture exchange. The market value of these shares was $20,263 as of September 30, 2016 (note 8)

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, short-term loans, 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

A number of standards and amendments were issued effective for accounting periods beginning on or after January 1, 2016. Many of these updates are not applicable to the Company. As of January 1, 2016, the Company adopted the following IFRS standards and amendments:

- IAS 16 and IAS 38 (Amendments) – Method of Depreciation and Amortization
  The amendments to IAS 16 state that revenue-based methods of depreciation cannot be used for property, plant and equipment. The amendments to IAS 38 introduce a rebuttable presumption that the use of revenue-based amortization methods for intangible assets is inappropriate. This presumption could be overcome only when revenue and consumption of the economic benefits of the intangible asset are highly correlated or when the intangible asset is expressed as a measure of revenue.
- Annual Improvements to IFRS (2012-2014) Cycle.
  These amendments were made to clarify the following:
  . Changes in method for disposal under IFRS 5 Non-current Assets Held for Sale and Discontinued Operations;

. 'Continuing involvement" for servicing contracts and offsetting disclosures in condensed interim financial statements under IFRS 7 Financial Instruments: Disclosures;
. Discount rate in a regional market sharing the same currency under IAS 19 Employee Benefits;
. Disclosure of information 'elsewhere in the interim financial report' under IAS 34 Interim Financial Reporting

The adoption of the above standards did not have a significant impact on the Company's consolidated financial statements.

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.

- IFRS 16 – Leases
  This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments.
  This standard is effective for annual periods beginning on or after January 1, 2019.

3. Trade Receivables

	September 30, 2016	December 31, 2015
[1]Trade receivables, net of allowances for doubtful accounts	$304,040	$378,100
Other receivables	10,745	129,618
	$314,785	**$507,718**

Other receivables includes $5,000 (December 31, 2015 - $5,000) from the President of the Company relating to an advance for travel expenses (note15).

There was no allowance for doubtful accounts as at September 30, 2016 (December 31, 2015 - $Nil).

4. Inventory

	September 30, 2016	December 31, 2015
ESM™ ECO3™	$141,167	$ 57,573
Other products	3,159	3,638
	$144,326	**$61,211**

During the quarter ended September 30, 2016, total inventories of $12,346 were recognized as costs of sales (September 30, 2015 - $3,180).

5. Intangible Assets

Indefinite Lives

As at September 30, 2016, 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

Definite Lives	Cost						
	North American distribution	Intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1,	**$269,348**	**$124,100**	**$1,861,742**	**$113,651**	**$5,036,780**	**$1,174,651**	**$8,580,272**
Effect of change in foreign exchange rates	17,370	-	-	-	115,438	36,718	169,526
Balance at December 31, 2014	**286,718**	**124,100**	**1,861,742**	**113,651**	**5,152,218**	**1,211,369**	**8,749,798**
Acquisition		25,000					25,000
Effect of change in foreign exchange rates	40,302						40,302
Balance at December 31, 2015	**327,020**	**149,100**	**1,861,742**	**113,651**	**5,152,218**	**1,211,369**	**8,815,100**
Effect of change in foreign exchange rates	(13,014)						(13,014)
Balance at September 30, 2016	**$ 314,006**	**$149,100**	**$1,861,742**	**$113,651**	**$5,152,218**	**$1,211,369**	**8,802,086**

Accumulated Depreciation and Impairment							
	North American distribution rights	ESM™ intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distribution rights	Customer relationship	Total
Balance at January 1, 2014	**$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	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		8,291	119,706	5,680	374,834	51,188	559,699
Effect of change in foreign	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		6,531	89,859	4,263	273,792	38,391	412,836
Effect of change in foreign	(13,014)						(13,014)
Balance at September 30, 2016	**$314,006**	**$107,896**	**$1,608,592**	**$95,186**	**$4,407,361**	**$1,045,014**	**$7,578,055**

Carrying Value							
	North American distributio	ESM™ intellectual property	Distribution agreements	Supplier agreements	EMEA & UK distributio	Customer relationship	Total
Balance at December 31, 2014	$ -	$ 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 September 30, 2016	$ -	**$41,204**	**$253,150**	**$18,466**	**$744,857**	**$166,355**	**$1,224,031**

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

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

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

b. *Distribution Rights from TECC Services*

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

c. *Intangible Assets from Smartcool UK*

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

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

d. *SmartACR Intellectual Property and Customer Relationship*

In February 2015, the Company acquired $25,000 of intangible assets in relation to the termination of a license agreement (note 11). These intangible assets include intellectual property ($25,000) and a customer relationship ($Nil).

6. Short-term Loan

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 was subsequently extended to December 31, 2013 and the interest rate reset to 8%. This loan was paid off in May 2015.

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.

On February 3, 2016, another loan of $50,000 was obtained. The loan had a monthly interest of 2% and matured on March 5, 2016. Management has requested an extension of the term.

On September 27, 2016, the Company received another short-term loan of $46,368 (US$35,000). The loan has monthly interest of 1% and matures on November 27, 2016. Any unpaid balance beyond maturity date bears monthly interest rate of 2%.

As at September 30, 2016, the outstanding balance of short term loans was $403,560. (December 31, 2015 - $276,450). Interest expense for the quarter ended September 30, 2016 was $11,161 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 7). 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 ($223,925) in five instalments of £26,000 on December 15, 2014 and June 15, 2015, 2016, 2017 and 2018;
- £76,000 ($130,910) in five instalments of £19,000 on December 15, 2015, 2016, 2017

and 2018; and
- £25,000 ($43,063) 2016.

£206,000 ($354,835) of this debt is secured by non-interest bearing promissory notes and £25,000 ($43,063) 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 September 30, 2016, 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 January 1, 2014	**$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			(19,091)		(19,091)
Debt settlement		(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	11,593	6,166	-	2,015	19,774
Foreign exchange	(38,754)	(14,227)	(8,345)	(7,183)	(68,509)
Balance, September 30, 2016	**207,104**	**77,678**	**42,673**	**38,339**	**365,794**
Current portion	(167,284)	(37,882)	(42,673)	(18,848)	(266,687)
Long-term portion	**$39,820**	**$39,795**	**$-**	**$19,492**	**$99,107**

Principal	$221,897	$88,076	$42,673	$41,648	$394,294
Future accretion	(14,793)	(10,398)	(-)	(3,309)	(28,500)
Carrying amount	$207,104	$77,678	$42,673	$38,339	$365,794

8. Receivables/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. At September 30, 2016, the market value of these shares was $20,263.

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

9. 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 and the remaining balance of the principal was due on maturity date, March 31, 2016. These amounts were not paid and the Company was in default as at September 30, 2016. The Company also issued 238,546 share purchase warrants to the debenture holders (note 10(c)(iii)). This refinancing was approved by the TSX Venture Exchange.

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.

During the three months ended September 30, 2016, interest of $7,566, calculated at annual rate of 12%, was accrued. Interest charge is recorded within finance expense in the statement of operations.

At September 30, 2016, the carrying amount of the debentures was as follows:

Maturity date	March 1, 2014	March 1, 2015	March 1, 2016	Total
Balance, January 1, 2014	$31,985	$217,098	$-	$249,083
Accrued interest	1,343	49,595	-	50,938
Interest payments	(1,133)	(7,223)	-	(8,356)
Principal payments	(32,195)	-	-	(32,195)
Balance, December 31, 2014	**-**	**259,470**	**-**	**259,470**
New debentures issued	-	(238,546)	238,546	-
Fair value of share purchase	-	-	(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**
Interest payments			(918)	(918)
Principal payments			(8,738)	(8,738)
Accrued interest	-	1,361	26,815	28,176
Balance, September 30, 2016		17,918	255,309	273,227
Current portion		(17,918)	(255,309)	(273,227)
Long-term portion	$-	$-	$-	$-

Principal	$-	$15,117	$229,807	$244,924
Accrued interest	-	2,801	25,502	28,303
Balance owing	-	$17,918	$255,309	$273,227
Carrying amount	$-	$17,918	$255,309	$273,227

10. 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, 2014	**79,287,297**	**$30,309,075**
Issued for cash via private placements	9,730,000	430,600
Share issuance costs	-	(6,262)
Balance, December 31, 2014	**89,017,297**	**30,733,413**
Issued via private placements (ii)(iii)(iv)	28,450,000	736,196
Issued for debt settlement (v)	4,630,440	231,522
Share issuance costs	-	(28,447)
Balance, December 31, 2015	**122,097,737**	**31,672,684**
Issued – Pending in 2015 (vii)	500,000	25,000
Warrant exercise – Pending in 2015 (vi)	545,000	31,637
Issued via private placements (viii) (ix)	17,700,000	366,375
Share issuance costs	**-**	(13,959)
Balance, September 30, 2016	**140,842,737**	**$ 32,081,737**

i. 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 10(c)(ii)). Each Unit consists of one common share and one-half warrant. Cash issuance costs of $6,242 were allocated to common shares.

ii. 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 10(c)(iii)). Each Unit consists of one common share and one warrant. Cash issuance costs of $7,742 were allocated to common shares.

iii. 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 10(c)(iv)). Each Unit consists of one common share and one warrant. Cash issuance costs of $18,972 were allocated to common shares.

iv. On December 17, 2015, the Company issued 2,670,000 Units at $0.05 per unit pursuant to a non-brokered private placement for gross proceeds of $133,500. Of this amount, $106,800 was allocated to share capital and $26,700 to share purchase warrants (note 10 (c) (v)). Each Unit consists of one common share and one warrant. Cash issuance costs of $1,733 were allocated to common shares.

v. 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 (note 8 b)).

vi. In December 2015, 545,000 warrants were exercised at the price of $0.05 per warrant for total consideration of $27,250. The same number of shares was issued on January 11, 2016.

vii. 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 11).

viii. In April 2016 the Company announced a non-brokered private placement of up to 8,000,000 units at a price of $0.025 per unit, for gross proceeds of $200,000. Each unit consists of one common share and one non-transferable share purchase warrant. Each warrant entitles the holder to purchase one additional share for a period of 12 months from the closing date at an exercise price of $0.05. The maximum amount of gross proceeds was later increased to $300,000. On May 5, 2016, the first tranche of the private placement was closed and 6,660,000 units were issued for gross proceeds of $165,000. The second tranche was closed on June 21, 2016 and 5,400,000 units were issued for gross proceeds of $135,000, bringing total proceeds to $300,000. Of this amount, $248,715 was allocated to share capital and $51,285 to share purchase warrants.
Cash issuance costs of $10,176 were allocated to common shares.

ix. In July 2016 the Company announced a non-brokered private placement of up to 8,000,000 units at a price of $0.025 per unit, for gross proceeds of $200,000. Each unit consists of one common share and one non-transferable share purchase warrant. Each warrant entitles the holder to purchase one additional share for a period of 12 months from the closing date at an exercise price of $0.05. On September 19, 2016, the first tranche of the private placement was closed and 5,400,000 units were issued for gross proceeds of $135,000. The second tranche was closed on September 29, 2016 and 800,000 units were issued for gross proceeds of $20,000, bringing total proceeds to $155,000. Of this amount, $134,302 was allocated to share capital and $20,698 to share purchase warrants.
Cash issuance costs of $2,983 were allocated to common shares.

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

As at September 30, 2016, 12,220,000 options were outstanding. These options have vesting periods of up to 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, 2014	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
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	50,000	0.05
Expired or exercised	(245,000)	0.10
Balance, September 30, 2016	**12,220,000**	**$0.05**

During the nine months ended September 30, 2016, 50,000 (2015 - 5,370,000) options with fair value $0.02 were granted to an employee. None of these options had an exercise price ($0.05) lower than the stock price.
Share-based payments for the three months ended September 30, 2016 was $5,702 (September 30, 2015 - $64,406).

c. ***Share purchase warrants***

i) 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.

ii) 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.

iii) On March 31, 2015, the Company issued 238,546 share purchase warrants at $0.06 per warrant pursuant to debenture extension agreement. The fair value of these warrants was determined to be $22,315.

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

$9,712 were allocated to share purchase warrants

v) On December 17, 2015, the Company issued 2,670,000 Units at $0.05 per unit pursuant to a non-brokered private placement for gross proceeds of $133,500. Of this amount, $106,800 was allocated to share capital and $26,700 to share purchase warrants. Each Unit consists of one common share and one warrant. Cash issuance costs of $434 were allocated to share purchase warrants.

vi) On May 5, 2016, the Company issued 6,660,000 units at $0.025 per unit in the first tranche of a non-brokered private placement for gross proceeds of $165,000. On June 21, 2016, the Company issued 5,400,000 units in the second tranche for gross proceeds of $135,000. Each unit consists of one common share and one non-transferable share purchase warrant. Each warrant entitles the holder to purchase one additional share for a period of 12 months from the closing date at an exercise price of $0.05. Out of total gross proceeds of $300,000, $51,285 was allocated to share purchase warrants. Cash issuance costs of $2,084 were allocated to share purchase warrants. The company also issued 128,000 warrants to agents for finders' fee. The fair value of these warrants was determined to be $800.

vii) On September 19, 2016, the Company issued 5,400,000 units at $0.025 per unit in the first tranche of a non-brokered private placement for gross proceeds of $135,000. On September 29, 2016, the Company issued 800,000 units in the second tranche for gross proceeds of $20,000. Each unit consists of one common share and one non-transferable share purchase warrant. Each warrant entitles the holder to purchase one additional share for a period of 12 months from the closing date at an exercise price of $0.05. Out of total gross proceeds of $155,000, $20,698 was allocated to share purchase warrants. Cash issuance costs of $446 were allocated to share purchase warrants.

As at September 30, 2016, there were 45,845,000 (December 31, 2015 – 28,800,546) outstanding warrants with a weighted average share price of $0.07 (December 31, 2015 - $0.08).

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, 2014	**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	28,800,546	0.08
Expired, exercised or cancelled	(5,216,000)	0.10
Balance, December 31, 2015	**28,800,546**	**$0.08**
Granted	18,328,000	0.05
Expired, exercised or cancelled	(1,283,546)	0.07
Balance, September 30, 2016	**45,845,000**	**0.07**

Expiry date	Number of shares	Exercise price	Weighted average contractual life (years)
December 17, 2016	2,670,000	0.10	0.21
January 28, 2017	13,455,000	0.06*	0.33
May 4, 2017	11,892,000	0.10	0.59
May 5, 2017	6,728,000	0.05	0.60
June 21, 2017	5,400,000	0.05	0.73
September 19, 2017	5,400,000	0.05	0.97
September 29, 2017	800,000	0.05	1.00
Balance, September 30, 2016	**48,845,000**	**$0.07**	**0.56**

*$0.05 if exercised in the first year, $0.75 if exercised in the second year

11. License Agreement Termination

On February 28, 2015, the Company executed a Termination Agreement ("TA") with a licensee ("SmartACR "). The purpose of the TA was to terminate a license agreement dated November 29, 2013 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. 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 (notes 11 d) and 22) and was to issue 2,000,000 share purchase warrants. Pursuant to the terms of the ICA, the contractor was to 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. On April 22, 2015, the Company granted 500,000 options to the contractor. On November 15, 2015, the Company terminated the ICA. Pursuant to the terms of the TA, the share purchase warrants expired on the date of termination of the ICA. Pursuant to the Company’s stock option plan and the stock option agreement between the Company and the contractor, the 500,000 stock options were forfeited on November 15, 2015.

The value attributed to the shares was allocated as follows:

Intellectual property	$25,000
Customer relationships	-
	$25,000

12. Deferred Tax Liabilities

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, 2015.

At December 31, 2015, the Company has unused non-capital losses of approximately $21,068,000 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	$-	$ 177,029	$-	1,200,043
2027	1,732,657	-	1,314,970	-	3,047,627
2028	1,127,657	-	2,255,328	-	3,382,985
2029	2,501,267	-	1,151,532	-	3,652,799
2030	910,879	-	1,136,885	-	2,047,764
2031	786,254	-	627,821	-	1,414,075
2032	400,145	-	243,650	-	643,795
2033	189,678	-	96,686	-	286,364
2034	3,775,936	2,091,346	(70,493)	47,274	5,844,063
2035	133,704	(572,984)	(137,731)	125,901	(451,110)
	$ 12,581,191	**$ 1,518,362**	**$ 6,795,677**	**$ 173,175**	**$ 21,068,405**

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 months ended September 30, 2016, these liabilities were reduced by $12,696 upon the recognition of amortization costs of these assets.

As at September 30, 2016, deferred tax liability was $164,121 (December 31, 2015 - $202,209).

13. Segmented Information

The Company installs, distributes, markets and sells the ECO3 and ESM™ products and peripherals. Revenue from the ECO3 for the three and nine months ended September 30, 2016 was $7,623 (September 30, 2015 - $16,838) and $53,684 (September 30, 2015 - $257,192), respectively. Revenue for the ESM™ solution for the three and nine months ended September 30, 2016 was $73,924 (September 30, 2015 - $109,764) and $197,213 (September 30-2015 - $240,931), respectively.

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

	Three months ended September 30 2016		Three months ended September 30 2015	
	Amount	%	Amount	%
Americas	$12,271	15	$75,722	60
Europe, Middle East, Africa	69,276	85	50,880	40
Total revenue	**$81,547**	**100**	**$126,602**	**100**

	Nine months ended September 30 2016		Nine months ended September 30 2015	
	Amount	%	Amount	%
Americas	$69,773	28	$330,506	66
Europe, Middle East, Africa	181,124	72	167,617	34
Total revenue	**$250,897**	**100**	**$498,123**	**100**

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

14. Commitments

Premise Lease

The Company's lease agreement to lease office facilities in Vancouver expired in May 2015. The Company entered into a rental agreement to rent an office in Palm Springs for USD 2,900 per month. The agreement commenced on November 1, 2015 and expired on April 30, 2016.

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.

In April 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.

15. 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	Consulting services
384518 BC Ltd.	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 September 30		Nine months ended September 30	
	2016	**2015**	**2016**	**2015**
Management fees	$45,000	$45,000	$135,000	$135,000
Consulting fees	10,320	12,191	32,772	112,353
Legal fees	-	-	4,062	4,964
	$55,320	**$57,191**	**$171,834**	**$252,317**

i. During the three and nine months ended September 30, 2016, management fees of $45,000 (September 30, 2015 - $45,000) and $135,000 (September 30, 2015 - $135,000), respectively, were charged by a company with a common director.

ii. During the three and nine months ended September 30, 2016, consulting fees of $10,320 (September 30, 2015 - $12,191) and $37,772 (September 30, 2015 - $112,353), respectively, were charged by two companies with common director and officer.

iii. The Company uses the services of a law firm of which a former director is a partner. During the nine months ended September 30, 2016, fees in the amount of $4,062 (September 30, 2015 - $4,964) were charged to the Company for trademark services provided.

Due to/from Related Parties

Included in trade and other receivables is $5,000 due from the President as at September 30, 2016 (December 31, 2015 - $5,000) related to an advance for travel expenses. The amount is unsecured, non-interest bearing and has no fixed terms of repayment.

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Included in trade payables and accruals is $372,821 due to related parties as at September 30, 2016 (December 31, 2015 - $313,103) as follows:

	September 30, 2016	**December 31, 2015**
Chief Executive Officer	$ 33,043	$ 28,553
President of the Company	100,939	98,753
Chief Financial Officer	59,667	49,191
Executive VP	45,233	17,346
VP of Operations	76,000	64,372
Other related parties	57,939	$ 54,888
Total	**$372,821**	**$313,103**

The amounts due to related parties are unsecured, non-interest bearing and have no fixed terms of repayment.
In March 2015, the Company issued 4,065,440 common shares at a deemed price of $0.05 per share to settle outstanding debts of $203,272 (note 8(b)).

Financial Instruments

Financial Instruments

The Company has classified its financial instruments as follows:

	September 30, 2016	December 31, 2015
Financial assets		
FVTPL , measured at fair value:		
Cash and cash equivalents	$22,068	$18,478
Available-for-sale, measured at fair value:		
Securities	20,263	12,158
Loans and accounts receivable, recorded at amortized cost:		
Trade and other receivables	309,039	496,626
	$351,370	**$527,262**
Other financial liabilities, recorded at amortized cost		
Trade payables	$ 683,882	$ 738,762
Short-term loan	403,560	276,450
Acquisition obligations and debentures	639,021	669,236
	$1,726,462	**$1,684,448**

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.

As at September 30, 2016, the Company has $309,039 (December 31, 2015 - $496,626) in trade and other 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 and accruals	$683,882	$ 683,882	$-
Short-term loans	403,560	403,560	-
Debentures	273,227	273,227	-
Obligations under acquisition contracts	334,208	266,687	67,521
Total	**$1,694,877**	**$1,627,356**	**$67,521**

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 September 30, 2016, the Company's monetary assets and liabilities denominated in foreign currencies are as follows:

	USD	AUD	GBP
Assets			
Cash and cash equivalents	$1,182	$-	£-
Trade and other receivables	231,654	-	-
Total	**$232,836**	**$-**	**£-**
Liabilities			
Trade payables and accruals	$130,057	$11,155	£55,693
Acquisition obligations, current	-	-	156,241
Total	**$130,057**	**$11,155**	**£211,934**

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	($23,284)	$-	£-
Monetary liabilities	13,006	1,115	21,193
Net gain (loss)	**($10,278)**	**$1,115**	**£21,193**

Gain (loss) on $0.10 decrease in CAD	USD	AUD	GBP
Monetary assets	$23,284	$-	£-
Monetary liabilities	(13,006)	(1,115)	(21,193)
Net gain (loss)	**$10,278**	**($1,115)**	**(£21,193)**

16. General and Administrative Expenses

	Three months ended September 30, 2016	Three months ended September 30, 2015
Advertising and promotion	$830	$290
Consulting & management fees	80,873	154,180
Filing and transfer fees	(377)	1,929
Insurance	5,477	9,361
Interest	55	21
Investor relations	1,495	5,124
Product certification	534	1,551
Professional fees	8,354	8,521
Office and supplies	5,625	6,861
Rent	2,105	5,618
Salaries and benefits	143,755	121,864
Telephone	4,710	4,497
Travelling	15,608	27,131
Total general & administrative expenses	**$269,043**	**$346,948**

	Nine months ended September 30, 2016	Nine months ended September 30, 2015
Advertising and promotion	$1,242	$10,165
Bad debts (recoveries)	-	(15,894)
Consulting and management fees	243,325	481,523
Filing and transfer fees	25,755	41,456
Insurance	10,695	14,263
Interest	4,314	272
Investor relations	7,325	25,467
Product certification	3,231	4,594
Professional fees	18,985	58,502
Office and supplies	21,627	32,370
Rent	21,465	38,772
Salaries and benefits	387,167	367,382
Telephone	13,187	12,172
Travelling	46,731	85,036
Total general and administrative expenses	**$811,679**	**$1,156,081**

17. 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 September 30, 2016, the principal amount of debenture component plus interest payable was $273,227 (December 31, 2015 - $260,097) and shareholders' deficiency was $79,058 (December 31, 2015 – Shareholders' Equity $529,139). The decrease in shareholders' equity was attributable to 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;
- 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, the Company is raising additional capital and expects significant growth in revenue as a result of the licensing of Connected Holdings.

The Company is not subject to any external capital restrictions.