SMARTCOOL™ SYSTEMS INC

Management Discussion and Analysis

For the year ended December 31, 2008

The following Management Discussion and Analysis ("MD&A"), dated April 27th, 2009, provides information that management believes is relevant to an assessment and understanding of the company's consolidated results of operations and financial condition. This discussion should be read in conjunction with the audited consolidated financial statements and accompanying notes for the year ended December 31, 2008.

Forward Looking Statements

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

Business Overview

Smartcool Systems Inc. is a cleantech company that specializes in energy and cost reduction technologies for air conditioning and refrigeration systems. Smartcool's first product, the Energy Saving Module™ (ESM)™, has met with a great deal of success targeting industrial and commercial businesses around the world. The expansion of the product line with introduction of the new ECO^3™ in early 2009 has launched Smartcool into a new era of development and growth.

Smartcool Systems Inc. was established in 2004, and was initially the North American distributor for the ESM™ on behalf of Abbotly Technologies Pty Ltd of Australia. In 2006, Smartcool International Inc., a 100% wholly owned subsidiary of Smartcool Systems Inc., purchased the assets of Abbotly, including intellectual property of the ESM™, and became the sole distributor and manufacturer. With research and development moving to the Vancouver head office, Smartcool Systems was well positioned for further corporate and product development.

Smartcool International Inc. is the master distributor of Smartcool's product line and is located in Barbados. Following the acquisition, Smartcool International developed an international network of distributors using strategically located offices based in London, England, Sydney, Australia and Houston, Texas to build support and sales channels. . Smartcool Systems USA Inc. is the head distributor for the U.S., Canada (excluding B.C.) and the Caribbean. Smartcool Systems EMEA was formed in 2008 and is the master distributor for Europe, the Middle East, Africa and the Indian Sub-Continent. The Sydney office supports distributors through the Americas and the Asia–Pacific region. Across the four branches of the company, Smartcool employs 28 people, with the management team and a full office of 16 people in Vancouver. The following graphic illustrates the current structure of the Smartcool organization including third party distributors:

Market Opportunity

Achieving greater energy efficiency is a crucial step towards building more sustainable communities. The generation of electricity for use in buildings is the single largest producer of greenhouse gases in the world. There are two ways to reduce the emissions caused by electricity. The first would be to use more renewable energy sources like wind and solar power. The second is to reduce the amount of electricity currently being used around the world. Taking advantage of this 'fifth fuel' is achieving greater momentum every year and provides the most cost effective option for reducing emissions.

According to the International Energy Outlook 2006, world energy consumption is expected to increase by 71% from 2003 to 2030, most rapidly in the industrial sector. In the U.S. alone, space cooling and refrigeration accounts for 15% of total electricity consumption. At a rate of US$0.07/kWh in the commercial sector, air-conditioning and refrigeration accounts for US$26 billion in spending annually. Energy consistently ranks as the second or third largest operating expense for businesses with air-conditioning and refrigeration typically representing the largest electrical expense in the market verticals that Smartcool is targeting.

In countries with higher ambient temperatures, the usage in air conditioning will be significantly higher, coming much closer to 30%. There has been a great deal of development in the lighting field to reduce energy, however, in the area of air conditioning and refrigeration, most of the development has resulted in expensive and complex systems requiring highly skilled installers and programmers. The cost of these systems has prohibited the installation by most small to medium consumers and even larger businesses have been challenged to meet the expense.

With ever increasing energy demands and the rising cost of power, both Government and Industry are searching for ways to simultaneously reduce operating costs and decrease their environmental impact. Governments are implementing rebate programs for companies that institute energy saving measures. Companies are realizing the economic and social benefits of implementing aggressive environmentally conscious programs that reduce their energy costs. The new administration in the U.S has highlighted the energy crisis as a significant challenge they are fully prepared to address. The investment of over US$150 billion over the next 10 years to address the dependence on foreign oil, address the global climate crisis and create millions of new jobs is a clear indication of that commitment.

Smartcool is helping clients achieve greater energy efficiency, increase profits and promote environmental sustainability through the installation of the Energy Saving Module™ and ECO^{3}™.

Technology Overview

The Energy Saving Module™ and ECO^3™ are green technologies that reduce the electricity usage (kWh) and demand (KW) of air conditioning and refrigeration compressors through enhanced system performance. This provides substantial economic and environmental benefits for Smartcool's growing customer base. Smartcool's products are compatible with all types of control systems including the latest building automation systems and computer controlled refrigeration plants. Energy savings achieved by the ESM™ and ECO^3™ are quantifiable and the products can qualify for government and utility rebates. The technology has been validated by rigorous third party testing, government organizations and private business installations.

The Energy Saving Module™ (ESM™)

The Energy Saving Module™ is designed specifically to reduce the electricity consumption (kWh) and maximum demand (KW/KVA) of refrigeration and air conditioning compressors by improving their performance and maintaining temperature control. The ESM™ is designed to interface with all types and makes of air conditioning and refrigeration controllers from the simple thermostat single condensing systems to the most sophisticated computer based multiple compressor parallel systems.

The ESM™ is not a controller. It is a supplement to the existing system - designed to work with the existing air conditioning and refrigeration equipment along with current control methodology in order to reduce the energy consumption. When a call for cooling comes from the existing controls, the ESM™ takes over to determine when and for how long each compressor or unloader will run. Because the primary control is not replaced, the ESM™ can be put into bypass at any time and the system returns to operating exactly as it was prior to the installation. This is an important distinction for system repairs and/or troubleshooting.

The ESM™ enables the compressor to maximize the rate of heat removal by optimizing the natural physical properties of the compressor operating cycle. This process, known as "Compressor Optimization" can reduce compressor running time by up to 30% with no affect on the temperature conditions.

The ECO^3™

In early 2009, Smartcool Systems Inc. launched its newest product: the ECO^3™. This unique retrofit device can be installed on any air conditioning or refrigeration unit with one or two compressors, and will save an average of 12% of the energy used by that system. The most significant feature of the new ECO^3™ is its ability to save energy on the cooling and heating cycles of compressor driven heat pumps, significantly increasing the opportunity for energy savings. With its IP64 enclosure rating, and its simple installation process, the ECO^3™ can be installed quickly (under 2 hours by an experienced technician) in virtually any location without additional and often costly protection from the elements. Once installed, the large display screen of the ECO^3™ allows for easy monitoring of the amount of energy it is saving for the customer.

Third Party Assessment

Smartcool's technology has undergone significant testing, resulting in a great deal of evidence of its energy saving capabilities. In addition to independent third party tests, over 26,000 units of the ESM™ and ECO^3™ have been installed worldwide.

The University of Miami, on behalf of Florida Power and Light (FPL), conducted extensive testing of the ESM™ installed over a twelve month period in 2006. The testing showed that the ESM™ reduced kWh usage of the entire air conditioning system by 8.9% – which provides a savings of 13.38% of the kWh usage by the compressors, an annual reduction of 43,660 kWh and a reduction in greenhouse gas emissions of 58,911 lbs.

Oak Ridge National Laboratory (ORNL), a division of the U.S. Department of Energy, conducted a two phase test of the ESM™ in 2004-2005. The first phase of the test involved the analysis of data collected from an installation on a refrigeration rack in a grocery store. Phase 1 results were sufficiently promising to merit and a second phase of testing in a controlled laboratory environment. The second phase evaluated the ability of the ESM™ to reduce the electrical consumption of a four compressor roof top unit in a controlled laboratory

environment. Test results showed an 11.87% reduction in kWh usage by the compressors in the system and a 2.2% demand (KW) reduction.

Previously, a test on a refrigeration system was conducted by the Los Angeles Department of Water and Power (LADWP). The ESM™ was installed on two compressors of the refrigeration system of Notrica's Market in Bellflower, California. The average daily kWh usage savings recorded during this test was between 20% and 24%. These reductions were achieved while maintaining the temperature performance of the system.

Applications for Smartcool's Technology

The ESM™ and ECO³™ have a large number of potential applications in a variety of different industries. Between the two products, Smartcool is able to offer a cost-effective energy efficiency solution for virtually any cooling systems, with the exception of blast chillers. In every Smartcool installation, the ESM™ and ECO³™ provide great economic, environmental and energy reducing benefits for the client's facility.

Air Conditioning Units

The ESM™ is compatible with any air conditioning system, while the ECO³™ is compatible with packaged units with one or two stages of control. Air conditioning in facilities such as commercial real estate, supermarkets, hotels, restaurants, schools, hospitals, data centers and telecommunications facilities can all benefit from the energy efficiency products supplied by Smartcool.

Refrigeration Units

The ECO³™ is compatible with any single compressor refrigeration system. The ESM™ is compatible with all refrigeration systems, including large multi-compressor racks. Process cooling, cold storage warehouses, hospitals, supermarkets, mini-marts or convenience stores, restaurants and many other businesses can save money on their refrigeration bills by installing the ESM™ or ECO³™.

Chillers

Most modern chillers are fitted with Micro-Processor Chiller Management Systems that usually allow a third party interface to modify the chiller capacity control. The Intelligent Interface Module allows the ESM™ to modify chiller capacity control using remote set point control, temperature reset, dual set point control or pulse width modulation.

The ability of the ESM™ to provide savings on a chiller is achieved by the ability of the IIM to interface with the primary controller causing the unit to shed load for a period of time to reduce the amount of energy the system is using. The ESM™ is able to provide this set point shift/load shifting through the full range of ambient conditions and not just at low ambient conditions.

Competitive Advantage

There are no direct competitors at this time, and those few products that are geared towards energy efficiency in the air conditioning and refrigeration market do not provide the same package of benefits as does the ESM™ or ECO^3™. Most other products aiming to save energy on air conditioning and refrigeration systems do not target the compressors, despite the compressors being responsible for most of the energy consumed by the system. Smartcool's products target the compressors specifically, and are miles ahead of the competition with thanks to a solid technical foundation and certain unique features.

The ECO^3™ has been developed using the experience gained through distribution of the ESM™, a product that has already met a high level of success with 26,000 units installed around the world. Case studies from ESM™ installations in all of Smartcool's targeted vertical markets show a large, satisfied customer base. As reported previously, Smartcool's ESM™ has also undergone significant independent third party testing, including field and laboratory tests by Oak Ridge National Laboratory (ORNL) on behalf of Wal-Mart, the University of Miami on behalf of Florida Power and Light (FPL) and Los Angeles Department of Water and Power (LADWP). All of the results from these tests have been positive and have verified the effectiveness of the technology.

Experience gained from the development and marketing of the ESM™ has allowed the ECO^{3}™ to be created and launched into the market with a solid and credible foundation. This gives potential customers additional confidence in the company and the technology, leading them to choose Smartcool over other alternatives.

Certain features of the ECO^{3}™ also give it an advantage over potential competitors. It is the only product on the market that can save energy on the cooling and heating cycles of compressor driven heat pumps. These types of heat pumps are very common, particularly in areas where cooling may not be necessary year round such as in British Columbia. The ECO^{3}™ has exclusive access to this large market, as it provides the most effective energy efficiency device for customers with these types of units. The IP64 rating and simple installation cut down on additional costs for the customer, as extra protection and long labour hours are not necessary.

Highlights of 2008

Smartcool completes roll-outs to major clients in Australia and the UK

Smartcool successfully completes the first installation of an ESM™ on a centrifugal compressor

Smartcool signs distribution agreements for Germany and Barbados

University of Miami on behalf of Florida Power and Light releases positive results of year-long testing on the ESM™

Smartcool is approved for BC Clean Tech Tax Credit

Smartcool acquires the exclusive rights to distribute the ESM in the United Kingdom, Spain, Portugal, and the Middle East from T.E.C.C Services Ltd.

Offices developed further in Vancouver, London, Houston, and Sydney to provide optimal support to regional distributors

Sales are finalized with major clients such as the Radisson SAS in Dubai, Ayala Land in the Philippines, Barbados Dairy Industries, and Bezeq in Israel.

Already in the first quarter of 2009 Smartcool has signed two new distributors in Chile and South Africa, launched its new ECO^{3}™, and become an approved contractor through BC Hydro's Power Smart program.

Smartcool announces the successful installation in 25 Sainsbury grocery stores in the United Kingdom and becomes an approved product for Sainsbury's Re-Fit program

A Year in Review - 2008

Building on the success of 2007, Smartcool experienced an extremely positive year in 2008. Consolidating its position as an international cleantech company, Smartcool signed exclusive agreements with new independent distributors in Germany, Philippines, India and Barbados. The existing offices in Vancouver, Houston and Sydney continued to provide valuable support and expertise, particularly to distributors in the Americas and the Asia Pacific region.

Significantly, a new subsidiary was launched in mid-2008 to manage distribution throughout Europe, the Middle East, Africa and the Indian Sub-Continent. Smartcool Systems EMEA Ltd. established headquarters in London, UK and immediately began developing new sales channels and vertical markets within its expansive territory. Relationships with existing distributors were reinforced with support from a strong team in London, and new distributors completed training and initial projects in India, South Africa, and in Europe.

Smartcool's Energy Saving Module™ received further validation when the University of Miami released the results of its 12 month test, conducted on behalf of Florida Power and Light. This rigorous third party testing once again confirmed the ESM™ as a reliable, proven and unique energy efficiency device providing substantial benefits to clients. Earlier in the year the ESM™ was successfully installed on a centrifugal compressor for the first time, demonstrating its versatility and wide range of potential applications. The new Intelligent Interface Module, a highly specialized addition to the ESM™ allowed the product to interface successfully with the complex control system on the centrifugal. This was just one of the major technical advances that Smartcool made in 2008.

Throughout its experience in the energy efficiency market, Smartcool has perceived a need for a simple, packaged retrofit device targeting smaller air conditioning and refrigeration systems. While the ESM™ can certainly save energy on these systems, with its complex algorithms and more involved installation process, it is not the most economical option. In response to this observed need, Smartcool developed its newest product, the ECO^3™. Initial testing was conducted at various facilities in 2008 with the first demo models sold by the end of the year. The official launch of the ECO^3™ took place in February 2009, with the positive test results from 2008 providing an important foundation for the first round of sales. Already there is a great deal of interest in the ECO^3™ as new non-exclusive distributors sign on with Smartcool and initial purchase orders for the product have been received.

With continued innovation and expansion to new territories, Smartcool anticipates continued revenue growth in 2009 despite wider economic turmoil. The launch of the ECO^3™ along with new distribution agreements signed for South Africa and Chile, are just some of the successes achieved in the first quarter. Additionally, Smartcool has begun to build its business closer to home, gaining approval under the BC Clean Tech Tax Credit and inclusion as a BC Hydro contractor. Whether at home or abroad, Smartcool will continue to provide top quality energy efficiency products and services, establishing a strong base for growth and success in the future.

Financial Overview

The financial highlights for the year 2008 are as follows:

Revenue was $1,175,168, increased by $727,893 or 163%, compared to $447,275 for the prior year. Total assets were $8,281,026 compared to $9,313,309 for the year 2007. Net loss was $4,370,883 ($0.11 per share) for the year, compared to $4,323,282 ($0.13 per share) in prior year.

The Company had $2,252,857 in cash and cash equivalents and short-term investments of $25,608 at the end of the year, compared to $6,020,860 in cash and cash equivalent and short-term investments of $227,536 in the previous year.

Total liabilities at the end of year 2008 were $1,350,285which include the current portions of purchase obligations to TECC Services, capital leases and deferred tenant inducement totaling $725,818 and Long-term liabilities were $624,467, consisting of acquisition obligations ($540,669), balance of capital leases ($9,145) and deferred tenant inducement ($74,653).

Selected Annual Information

The following is selected information on Smartcool's financial performance for the past three years:

	December 31, 2006	December 31, 2007	December 31, 2008
Revenue	$325,166	$447,275	$1,175,168
Selling, General & Administrative	$1,276,450	$2,741,892	$4,414,683
Net loss	$(2,066,868)	$(4,323,281)	$(4,370,883)
Net loss – Per Share (Basic and Diluted)	$(0.11)	$(0.13)	$(0.11)
Total Assets	$4,726,602	$9,313,309	$8,281,026
Total Long Term Liabilities	$238,862	$111,004	$1,350,285
Cash Dividends	$0	$0	$0

Year 2008 saw a significant growth in the company's revenue. The addition of several channels to Smartcool's global distribution network and increased business volumes with existing distributors have resulted in 163% increase in sales bringing total revenue to $1,175,168. Smartcool's strategy of investing in corporate funded offices in specific regions have allowed for more marketing and technical support to existing sales channels resulting in the revenue growth seen in 2008. Gross revenue of $1,175,168 consists of distribution sales of $972,842 and direct sales of $202,326. Direct sales, generated primarily in the US, though increasing in 2008, did not meet management expectations due to the longer than expected sales cycle with larger, multi-location companies. One particular large international company during the fourth quarter has entered into a five year agreement with Smartcool for installation of the ESM™ and ECO³™ in multiple sites. As well, testing has continued with other such companies.

Selling, general and administrative ("S,G & A") expenses for the year was $4,414,683, increased by $1,672,791 or 61% from $2,741,892 for the prior year. This increase was a result of continued expansion, in the United States, Australia and the United Kingdom. A number of full-time employees were hired during the year to support continued growth. In addition to the new employees, Smartcool also engaged strategic consultants that have provided access to decision makers in both the private and public sectors.

Result of Operations

Revenue

Revenue for the year was $1,175,168 (2007 - $447,275) with $972,842 or 75% relating to distribution sales (2007 - $403,704) and $202,326 or 25% relating to retail sales (2007 - $43,571).

Gross profit

Total gross profit for the year 2008 was $747,278 or 64% of revenue compared to $189,579 or 42% for the previous year. The 2008 gross margin has increased as the company reduced its installation costs (2% of sales in 2008, compared to 10% in 2007) as the percentage of revenue for distributor sales increased versus direct sales. Royalties, as a percentage of sales, has decreased considerably from 17% in 2007 to 4% in 2008 due to increased sales outside of North America. Under the terms of the Abbotly USA acquisition contract (See notes to Financial Statements - Commitments 12 (d)), minimum royalties of US$40,000 are due Abbotly USA annually. As International sales improve and royalties remain at the minimum, as occurred in 2008, gross margin will improve. Also, 2007 royalties, including accruals from 2006, amounted to $77,078 compared to royalties of $42,574 for 2008.

Selling, general and administrative expenses

Selling, general and administrative expenses for the period were $4,414,683 compared to $2,741,892 of the previous year. The increase reflected increased higher wages and salaries ($2,146,261 compared to $738,320 in 2007), greater consulting and management ($815,792 compared to $599,777 in 2007), greater travel expenses ($475,840 compared to $384,408 in 2007), increased rent ($111,915 compared to $64,604 in 2007) and office expenses ($186,780 compared to $130,245 in 2007). Areas where reduction of expenses occurred were investor relations ($158,477 compared to $235,116) and professional fees ($156,609 compared to $198,526 in 2007).

Net loss

Net loss for the year 2008 was $4,370,883 compared to $4,323,281 in the prior year. The significant increase in revenue has been offset by increase in operating costs as US operations continued to expand and opening offices in both the UK and Australia to support the growth of sales channels internationally. The acquisition of TECC distribution rights, an important strategic move, also contributed to a greater loss due to the non-cash intangible asset amortization expense. The loss per share (basic and diluted) for the year was $0.11, compared to $0.13 for 2007. Loss per share is calculated based on the weighted average number of common shares outstanding throughout the year. The decrease in the loss per share was a result of increase in the weighted average common shares.

Amortization

Amortization expenses were $450,095 for the year 2008 compared to $302,937 for the prior year. Amortization on property and equipment was $121,738 (2007 - $82,050) and amortization of intangible assets was $328,357 (2007 - $220,887). The increase in intangible assets amortization was a result of the acquisition of distribution rights from TECC Services.

Stock-based compensation

Stock-based compensation costs decreased to $449,639 from $1,229,257 in 2007. This decrease was a primarily a result of a smaller number of stock options being granted in the period (385,000 options compared to 2,195,000). In addition, fair values of the options granted in the period were lower due to low stock market price. All of the cost in the period was related to management, general and administrative services (2007 - 1,190,364 was related to management, general and administrative services and $38,893 was related to technical consulting services).

Capital expenditure

Capital expenditures for the year 2008 were $126,367, compared to $182,022 in 2007. These expenditures were primarily for the acquisition of additional testing equipment needed at a couple of multiple site customers. In addition to the purchase of equipment, the company also invested a total of $106,561 in new product development which was capitalized and amortized starting September 1, 2008.

Intangible assets

Smartcool acquired the intellectual property of the ESM™ and its world-wide distribution rights in the year 2006. The acquisition was closed on June 30, 2006 at a price of AU$2,895,000. Total payments of AU$195,000 or CDN$185,133 were made in 2008 (AU$1,200,000 or CDN$1,082,840 were made in 2007 and AU$1,500,000 or CDN$1,310,090 were made in 2006). At December 31, 2008, no amount of the purchase price was owed. The acquired assets included four distribution contracts and several supplier agreements along with the intellectual property of the ESM™ and the ESM™ brand. Certain intangible assets were tested for impairment at year end with no impact on balance sheet..

Smartcool 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") in the year July 2008. Consideration of £1,035,000GBP (CA$1,738,750) was payable in cash and £265,000GBP (CA$532,067) was payable in the form of common shares of the company. Upon closing, payment of £435,000GBP (CA$873,393) was made and 743,709 shares were issued. The share price was based on the average closing price of the company's shares on the TSX Exchange for 20 consecutive trading days, with the last of such trading days being the second day preceding the date of closing.

The remaining balance of £600,000GBP is due in scheduled instalments over four years with the last payment due on July 11, 2012. These instalments are non-interest bearing. At the acquisition date, the fair value of consideration was determined to be $2,270,800 based on discounting the future payments at a rate of 16%. Transaction costs of $28,300 were also incurred. As at December 31, 2008, £600,000GBP was still outstanding.

Impairment of Long-Lived Assets

Smartcool amortizes long-lived assets over the estimated useful life of the asset. Evaluation of all long-lived assets occurs periodically for impairment in accordance with Section 3062 and Section 3063 of the CICA Handbook. These sections require that long-lived assets be evaluated for impairment whenever events or changes in circumstances indicate that their carrying value may not be recoverable. Events or changes in circumstances include a significant adverse change in business climate that could affect their value. If such an event or change indicates that the carrying value of an asset may not be recoverable, or that our estimated amortization period was not appropriate, we would record an impairment charge against our long lived assets. The amount of impairment would be measured as the difference between the carrying value and the fair value of the impaired asset as calculated using a net realizable value methodology. An impairment charge would be recorded as an operating expense in the period of the impairment and as a reduction in the carrying value of that asset.

At December 31, 2008, given the current disruption and uncertainty in the global economy, the significant decrease in our stock price over the last fiscal quarter, and our revenue expectations not being met, we determined that the appropriate triggers had been reached for an impairment test on certain of our definite lived intangible assets. Our definite lived intangible assets are ESM™ intellectual property, ESM™ distribution contracts and ESM™ supplier contracts that we acquired from Abbotly USA, Abbotly Technologies Pty and TECC Services. These definite lived intangibles have net book values as at December 31, 2008 of approximately $93,000, $3,900,000 and $85,000, respectively.

As our revenue is primarily derived from the sales of ESM™ products, revenue associated with the above intangible assets is readily identifiable. Revenue from existing distribution channels is projected based on forecasts provided by the distributors themselves. Revenue expected from potential distribution channels is based on business development progress. Cost of goods sold projections are based on prices specified in supplier contracts and operating costs projections took into account cost reduction measures implemented recently. Our cash flow analysis extended over three to seven years, which are within the remaining amortization periods of the intangibles. These undiscounted cash flows supported the recoverability of our definite lived intangible assets.

Due to the above considerations, which are based on our best available information, we have not recorded any impairment on our long-lived assets in fiscal 2008. However, given the current state of the economy, we expect to continue to perform asset recoverability tests in future periods.

Summary of Quarterly Results

	Mar 2007 ($)	Jun 2007 ($)	Sep 2007 ($)	Dec 2007 ($)	Mar 2008 ($)	Jun 2008 ($)	Sep 2008 ($)	Dec 2008 ($)
Total Revenues	$11,781	$197,809	$54,107	$183,578	$422,663	$120,373	$204,793	$427,339
Income/(Loss)	(903,488)	(768,358)	(1,066,472)	(1,584,963)	(745,733)	(1,039,987)	(1,337,484)	($1,247,679)
Income/(Loss) Per Share – basic & diluted	(0.04)	(0.02)	(0.03)	(0.13)*	(0.02)	(0.03)	(0.03)	(0.11)*

*represents the loss per share (basic and diluted) for the fiscal years ended December 2007 and 2008

Revenue for the fourth quarter of 2008 was $427,339 compared to $183,578 for the same quarter of 2007, an increase of $243,761 or 133%. Contributing to the increase was a sale to a new distributor in Chile and existing distributors securing contracts with multi-site companies which required a purchase of equipment to support these installations. Certain distributors also placed orders for equipment under their minimum purchase obligations to ensure their continued exclusive rights in their territories.

Gross margin for the quarter was $283,383 and net loss was $1,247,679, compared to gross margin of $20,579 and net loss of $1,584,965 for the same period of the previous year. Gross margin increased by $262,804 or 13 times and net loss for the quarter decreased by $337,286 or 21%. The decrease in net loss was attributable to growth in revenue and foreign exchange gains on acquisition obligations and other payables. Loss per share for the period is $0.03 compared to $0.04 for the same period of the previous year.

Schedule of selling, general and administrative expenses

	12 months ending December 31, 2008	**12 months ending December 31, 2007**
Management and consulting fees	815,792	599,777
Salaries and benefits	2,146,261	738,320
Professional fees	156,609	198,526
Investor relations and media	216,724	323,035
Travel	475,840	384,408
Technical consulting	83,848	143,806
Rent, office and other expenses	519,609	354,020
Total selling, general & admin expenses	**4,414,683**	**2,741,892**
Stock-based compensation	449,639	1,229,257
Survey and testing cost	2,782	108,308
Research & Development	57,233	54,853
Amortization	450,095	302,937
Total operating expenses	**5,374,432**	**4,437,247**

The company's selling, general and administration expenses were $1,438,219 for the fourth quarter of 2008 compared to $851,881 for the same period in 2007.

Liquidity and Capital Resources

Since incorporation, the company has financed its operations through the issuance of equity. A number of private placements along with the issuance of shares upon exercise of warrants and stock options have provided the company with working capital to date. During 2008, the company issued 3,329,250 common shares upon the exercise of the same number of warrants for cash proceeds of $1,603,105. An additional 35,000 common shares were issued upon the exercise of stock options, producing cash proceeds of $10,050. As at December 31, 2008, the company had $2,252,857 in cash and cash equivalents and $25,608 in short-term investments.

Working capital at the end of the year was $3,057,577 compared to working capital of $6,390,392 for the same period of 2007.

The company consumed cash resources of $3,768,003 during 2008, compared to net cash generation of $5,320,041 in 2007. In the period, the issuance of common shares upon exercise of warrants and stock options provided cash inflow of $1,613,656 while total cash resources of $1,086,836 were used to settle acquisition obligations and $791,656 to acquire additional inventory. The average monthly burn for 2008 was $354,000 compared to $237,000 for the previous year. The 49% increase in cash burn was primarily a result of the fast expansion of operations in the U.S and opening offices in London and Sydney.

Management believes cash generated from sales along with existing cash resources will enable the company to continue its operations, meet its acquisition obligations, and complete marketing strategies for the next twelve months. Management also expects that the effect of commercial, utility and government incentives, targeting energy efficiency and greenhouse gas reduction, will assist the Company in generating greater revenue opportunities.

Though in prior years the company was able to raise capital to finance its operations, the company's ultimate success and the recoverability of its intangible assets will depend on the company's ability to successfully execute its business plan which includes the existence of a market for its products, achieving profitable operations, meeting its business acquisition obligations, and the continued support of the company's shareholders and employees.

Due to the current economic crisis, the company might not be able to raise additional capital to expand its operations in the coming year. As a proactive action, the company has done a comprehensive review of its business development programs, operations and cash flow projections and taken certain cost reduction measures to ensure that it will have sufficient working capital to carry out its core business plan and meet its financial obligations in the next twelve to fifteen months.

Commitments

The company is committed to a number of financial obligations under premise lease, equipment lease and acquisition contracts. As at December 31, 2008, the company's commitments and obligations were as follows:

		Payment Due by Period		
Contractual Obligations	**Total**	Within 1 year	2-3 years	4-5 years
Premise lease	388,665	75,825	132,165	180,675
Capital lease	26,643	17,499	9,145	-
Acquisition obligations	809,109	268,440	310,035	230,634
Total contractual obligations	1,224,417	361,764	451,345	411,309

a) Premise lease

On June 1, 2005, the company entered into an agreement to lease office facilities for 10 years.

In February 2008, the company entered into a new lease agreement to lease office facilities in Texas for 37 months commencing February 1, 2008 and expiring February 28, 2011, for monthly rent payments of $1,800US per month, up to February 28, 2009 and monthly payments of $1,908US thereafter.

The future minimum commitments for the company's office premises are:

	$
2009	75,825
2010	77,220
2011	54,945
2012	51,300
2013 and thereafter	129,375
	388,665

For the year ended December 31, 2008, the company's rent expense including certain operating expenses and property taxes was $133,836 (2007 - $100,008) and its sublease revenue was $23,676 (2007 - $35,408).

b) Letter of credit

Upon the signing of the lease contract in June 2005, the company was required to secure its obligations with a letter of credit of $100,000. The letter of credit is reduced by $25,000 every year. As at December 31, 2008, the company had open letters of credit totaling $25,000 (December 31, 2007 - $50,000).

c) Equipment lease

In July 2005, the company signed contractual lease agreements for equipment as follows:

- Telecommunication equipment for 40 months at $8,400 per annum
- Office equipment for 36 months at $14,800 per annum

These contracts expired in July 2008.

In the year 2007, the company entered into two contractual lease agreements to finance the purchases of computer equipment. Both leases expire in June 2010 and have an implied annual interest rate of 16.17%. Interest paid in the year ended December 31, 2008 related to obligations under capital lease was $5,711 (2007 - $3,048).

The following is a schedule of future minimum lease payments under these capital leases together with the balance of the obligations.

Capital lease payments

	$
2009	20,634
2010	9,610
	30,244
Amount representing interest at 16.17%	(3,601)
Balance of the obligations	26,643
Less current portion	(17,499)
	9,144

In July 2008, Smartcool USA entered into an office equipment lease agreement. Under this agreement, the company is required to make 24 monthly payments of $369 starting August 2008.

d) Abbotly USA

Under the terms of the North American distribution rights acquisition (note 6(a) – December 31, 2008 financial statements) , the Smartcool Systems USA is required to pay a 20% royalty on products identified in the Assignment and Assumption agreement dated March 27, 2006 and purchased from Abbotly Pty (now Smartcool International) for North American sales. The initial term of the agreement was to expire on March 3, 2008. Smartcool USA under its rights in the Assignment and Assumption agreement has renewed the licensing agreement for another five year term. The company has purchased all of the remaining inventory from Abbotly USA as required under this agreement and is now required to pay a minimum of US$40,000 per year in royalty. For the three and nine months ended September 30, 2008, the company recorded royalties of US$12,112 and US$27,888. Payment of US$40,000 was made in July 2008. As at December 31, 2008, royalties of US$1,344 were payable to Abbotly USA (Year 2007 – US$76,840).

Transactions with Related Parties

Consulting fees of $259,185 were charged by directors of the company during the year (2007 - $62,200). Consulting and management fees of $90,997 were charged by three companies with common directors and officers during the year (2007 - $24,000). The company rents its office in the United Kingdom from a company with a common director. During the year ended December 31, 2008, rent expense was $21,539 (2007 –$nil). These transactions were recorded at their exchange amounts. At December 31, 2008, £8,328GBP (CDN$14,904) was owed to these related parties.

The company subleases its Vancouver office and other facilities to a company with a common director. During the year ended December 31, 2008, sublease income was $23,676 (2007 - $35,408). At December 31, 2008, $2,441 was owed from this related party (December 31, 2007 - $0).

Total purchases of £108,101GBP were made by a company with a common director during the year 2008. As at December 31, 2008, £71,147GBP was owed from this related party.

Outstanding Share Data

The authorized share capital of the company is an unlimited number of common shares without par value. As at December 31, 2008 the company had 41,182,646 common shares outstanding. The following table provided the weighted average number of common shares outstanding for the three months and the year ended December 31, 2008 and 2007.

	2008	2007
Three month weighted average	41,182,646	36,862,116
Annual weighted average	39,404,989	32,869,858

The increase in average number of common shares outstanding was a result of the issuance of 3,329,250 common shares upon the exercise of warrants, 35,000 common shares upon the exercise of options and 743,709 common shares upon the acquisition of TECC distribution rights.

As at April 24, 2009, the outstanding shares are 41,182,646 and fully diluted are 48,663,646.

Warrants and Stock options

As at December 31, 2008, there were 2,500,000 share purchase warrants and 4,981,000 stock options outstanding which collectively could result in the issuance of 7,481,000 common shares if these warrants and stock options are exercised. The outstanding options have weighted average exercise price of $0.67.

As at December 31, 2008 there were 4,396,000 exercisable options with a weighted exercise price of $0.65.

During the year 2008, 385,000 stock options were granted to consultants, employees, directors and officers of the company. Subsequent to the year end, 1,895,000 stock options were re-priced.

Subsequent Events

On January 6, 2009 Smartcool became a registered contractor in BC Hydro's "Power Smart Alliance". Power Smart has created many programs that accommodate residential, commercial and industrial customers. It is through these programs that Smartcool Systems will gain widespread exposure. BC Hydro provides its client base with in-depth information and financial incentives to help customers to reduce energy consumption and, in so doing, reduce costs and greenhouse gas emissions.

On February 25, 2009, Smartcool announced the worldwide launch of the ECO^{3TM}, an easily installed controller that provides fast return on investment (ROI) for businesses and homeowners seeking energy efficiency and cost savings from their air conditioning and refrigeration systems.

On March 3, 2009, Smartcool Systems announced that the company intended to reduce the exercise price of 1,895,000 incentive stock options - with exercises ranging from $0.90 per common share to $1.40 per common share – to an exercise price of $0.30 per common share. The re-pricing of the stock options is subject to the TSX Venture Exchange approval as well as, in the case of insiders of the company, the approval of disinterested shareholders. The company intended to seek such disinterested shareholders' approval for the amendment to insiders' options at its next annual general meeting currently scheduled to take place during the summer of 2009. There will be no change to the expiry dates of the options.

Critical Accounting Policies

Intangible assets

Intangible assets are recorded at cost and include the ESM^{TM} brand, ESM^{TM} intellectual property, distribution agreements and supplier agreements. The ESM^{TM} brand has been determined to have an indefinite life and is not amortized. The remaining intangible assets are amortized on a straight-line basis over their useful lives as follows:

ESM^{TM} Intellectual property	10 years
North American distribution rights	10 years
European distribution rights	9 years
Distribution agreements	10 - 15 years
Supplier agreements	10 years

Impairment of long-lived assets

Long-lived assets including property and equipment and intangible assets with a finite life are tested for impairment whenever events or changes in circumstances indicate that carrying value of an asset or asset group may not be recoverable. An impairment loss would be recognized when the carrying amount of an asset exceeds the estimated undiscounted future cash flow expected to result from the use of the asset and its eventual disposition. The amount of the impairment loss to be recorded is calculated by the excess of the asset's carrying value over the fair value. Fair value is generally determined using a discounted cash flow analysis.

Intangible assets with an indefinite life are reviewed 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 estimated fair value.

Revenue recognition

Revenue from the sale and installation of the ESM^{TM} in North America is recognized when the ESM^{TM} has been installed, title has transferred, collectability is reasonably assured and the fee is fixed and determinable. Revenue from the international distribution of the ESM^{TM} is recognized when the equipment has been shipped and title has transferred, collectability is reasonably assured and the fee is fixed and determinable. Provisions

are established for estimated warranty costs at the time revenue is recognized. The company records deferred revenue when cash deposits are received in advance of al of these revenue recognition criteria being met.

Research and development costs

Research costs are expensed as incurred. Development costs are expensed as incurred unless they meet specific criteria under Canadian GAAP for deferral and amortization, which relate primarily to technical, market and financial feasibility.

Stock-based compensation and other stock-based payments

The company applies fair value accounting to the grant of stock options to employees, consultants and others. The value of these options is determined using the Black Scholes pricing model and the resulting value is charged to operations over the vesting period. For options granted to non-employees, the fair value is measured when performance is complete, a performance commitment is made or the options are fully vested and non forfeitable, whichever is the earliest, and the expense is recognized over the period in which the goods or services from the non-employees are received. A corresponding increase in contributed surplus is recorded when stock options are expensed. When stock options are exercised, capital stock is credited by the sum of the consideration paid and the related portion previously recorded in contributed surplus.

Internal Controls over Financial Reporting and Disclosure Controls and Procedures

The Chief Executive Officer and Chief Financial Officer make no representation relating to the establishment and maintenance of the company's disclosure controls and procedures and internal controls over financial reporting.

Changes in Accounting Policies

Inventories

Effective January 1, 2008 the company prospectively adopted Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3031. This section prescribes the accounting treatment for inventories and provides guidance on the determination of costs and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

As a result of the adoption of this policy, the company has changed its inventory costing method from specific cost to weighted average cost and adjusted cost of inventory as at January 1, 2008 from $351,267 to $341,814. Retained earnings balance as at January 1, 2008 has been adjusted to $17,641,281 from $17,631,828.

Financial Instruments – Disclosure and Presentation

Effective January 1, 2008 the company adopted CICA Handbook Section 3862, Financial Instruments – Disclosure, and Section 3863, Financial Instruments – Presentation. Section 3862 requires disclosure of the significance financial instruments have on an entity's financial position and performance, the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. Section 3863, establishes standards for presentation of financial instruments and non-financial derivatives.

Section 3862 and section 3863 relate to disclosure and presentation only and did not have any impact on the company's financial results.

Capital Disclosure

Effective January 1, 2008 the company adopted Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1535, Capital Disclosure. Section 1535 requires the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and if it has not complied, the consequences of such non compliance.

The adoption of this standard did not have a material impact on the company's financial statements.

Assessing going concern

The Accounting Standards Board amended the CICA Handbook Section 1400, General Standards of Financial Statement Presentation, to include requirements for management to assess and disclose an entity's ability to continue as a going concern. Effective January 1, 2008, the company adopted this new standard. Management's assessment of the company's cash flow and revenue expectations throughout the year has lead to the conclusion that the adoption had no impact on the company's financial statements.

Future Accounting Standards

Goodwill and intangibles

In January 2008, the CICA issued Section 3064 "Goodwill and Intangible Assets" which replaces Section 3062 "Goodwill and Other Intangible Assets" and Section 3450 "Research and Development Costs". This section establishes standards for recognition, measurement, presentation and disclosure of goodwill and intangible assets by profit-oriented enterprises subsequent to their initial measurement.

The company will adopt this new requirement effective January 1, 2009 and is currently considering the impact this will have on its financial statements.

International Financial Reporting Standards

In February 2008, the Canadian Accounting Standards Board confirmed that International Financial Reporting Standards ("IFRS") will replace Canadian GAAP for publicly accountable profit-oriented enterprises for interim and annual financial statements effective January 1, 2011.

The company will therefore required to report using IFRS commencing with its unaudited interim financial statements for the three months ended March 31, 2011, which must include the interim results for the three months ended March 31, 2010**.** The company is currently reviewing the standards to determine the potential impact on its consolidated statements. The controller has been appointed to lead the conversion project and to communicate the impact of the new standards to the board and staff members. An analysis has been performed to identify differences between the company's current accounting policies and IFRS. Presently, the company is evaluating these differences and assessing the need for technology information system updates.

Risk Factors

The business of the company is subject to a number of risks and uncertainties associated with its business for the marketing and distribution of the ESM™.

Lack of Marketing Network

At the current time the company has continued to develop new marketing networks throughout the world. A primary objective of the company's business plan includes the identification and securing new networks however there can be no assurances of the amount of revenue that will be generated from these efforts. To mitigate the risk to a certain extent, the company when granting exclusive marketing rights for a territory will require a new distributor to agree to purchase a minimum amount of inventory in each year of the agreement to retain exclusivity. This provides the company with revenue from these territories.

Reliance on Key Personnel

The company is dependent on certain key members of its management team, and in particular Mr. George Burnes, President, to complete the market development of the ESM™. If any of these individuals are unavailable for any reason, the ability of the company to implement its business plan in the short term would be materially and adversely affected. To mitigate the risk to a certain extent, key personnel in the companies' subsidiaries have been added to complete new marketing initiatives in developing markets.

Concentration on a single product

Presently, as the company is placing its sole focus on the distribution of the ESM™, and ECO^{3}™, any unfavorable change in the quality of the product or the introduction of similar products by competitors in the market would affect the company's competitive advantage to a great extent. To mitigate the risk to a certain extent, the company expanded the application of it's technology and made available the ECO3 which allows for sales initiatives in new vertical markets and new distribution channels previously not available.

Currency risk

Presently the company's major business dealings are transacted in foreign currencies. Direct sales are in the United States currency as well as the majority of sales to distributors are also in US currency. Any devaluation in these currencies would affect the company's future revenues. Also, a significant portion of the company's expenses are in Canadian and Australian currencies. As long as the majority of revenue remains in US currency, appreciation in the value of Canadian and Australia currencies relative to the US dollar would worsen that affect on net operating results. To mitigate this risk to certain extent, recently the company has had most of its new purchases and sales contracts denominated in US dollars.

Competition Risk

Although the ESM™ and ECO^{3}™ are unique products and the company is not aware of any direct competitors, there is a possibility that new technologies will be developed that allow direct competition as energy saving activities gain more and more public support. These potential competitors may have greater resources and networking and the company may not be able to successfully compete with them. This direct competition may adversely affect the company's operating results and even its ability to sustain the business.