



# EUROCONTROL TECHNICS GROUP INC.

## CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

As at and for the three and nine months ended September 30, 2014 and 2013

(In Canadian dollars)

(UNAUDITED)

## **EUROCONTROL TECHNICS GROUP INC.**

### **NOTICE OF NO AUDITOR REVIEW OF CONDENSED CONSOLIDATED 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 interim financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated 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 condensed consolidated interim 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.

# EUROCONTROL TECHNICS GROUP INC.

Condensed Consolidated Interim Statements of Financial Position (unaudited)  
(Expressed in Canadian dollars)

| As at,  | Notes  | September 30,<br>2014 | December 31,<br>2013 |
|---|--------|-----------------------|----------------------|
| <b>ASSETS</b>                                     |        |                       |                      |
| <b>Current assets</b>                             |        |                       |                      |
| Cash  |        | \$ 2,609,102          | \$ 2,185,662         |
| Amounts receivable                                | 7      | 631,891               | 583,698              |
| Inventories                                       | 8      | 608,823               | 545,360              |
| Prepaid expenses                                  |        | 19,447                | 28,340               |
| Total current assets                              |        | 3,869,263             | 3,343,060            |
| <b>Non-current assets</b>                         |        |                       |                      |
| Loan receivable                                   | 21     | -                     | 322,807              |
| Equipment   | 9      | 244,236               | 223,288              |
| Deferred development costs                        | 10     | 309,272               | 337,388              |
| Technology rights                                 | 11     | 2,380,385             | 2,654,718            |
| Intellectual property                             | 5      | 312,115               | 349,568              |
| <b>TOTAL ASSETS</b>                               |        | <b>\$ 7,115,271</b>   | <b>\$ 7,230,829</b>  |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>       |        |                       |                      |
| <b>Current liabilities</b>                        |        |                       |                      |
| Accounts payable and accrued liabilities          | 12, 18 | \$ 900,712            | \$ 835,987           |
| Shareholder loans                                 | 13     | 1,261,904             | 1,491,322            |
| Total current liabilities                         |        | 2,162,616             | 2,327,309            |
| <b>Non-current liabilities</b>                    |        |                       |                      |
| Loan  |        | 10,729                | 22,749               |
| Total liabilities                                 |        | 2,173,345             | 2,350,058            |
| <b>Shareholders' equity</b>                       |        |                       |                      |
| Issued capital                                    | 14     | 14,690,341            | 14,690,341           |
| Warrants reserve                                  | 15     | -                     | -                    |
| Share-based payment reserve                       | 16     | 395,856               | 395,856              |
| Accumulated other comprehensive income            |        | 145,174               | -                    |
| Deficit   |        | (10,289,445)          | (10,205,426)         |
| Total shareholders' equity                        |        | 4,941,926             | 4,880,771            |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b> |        | <b>\$ 7,115,271</b>   | <b>\$ 7,230,829</b>  |

Nature of operations and going concern (note 1)  
Commitments and contingencies (note 23)  
Events after the reporting period (note 24)

## APPROVED ON BEHALF OF THE BOARD:

Signed "W. BRUCE ROWLANDS" \_\_\_\_\_, Director

Signed "GADI GONEN" \_\_\_\_\_, Director

*The accompanying notes are an integral part of these condensed consolidated interim financial statements*

# EUROCONTROL TECHNICS GROUP INC.

## Condensed Consolidated Interim Statements of Operations and Comprehensive Loss (unaudited)

(Expressed in Canadian dollars)

|  |        | Three months ended<br>September 30, |              | Nine months ended<br>September 30, |              |
|--|--------|-------------------------------------|--------------|------------------------------------|--------------|
|  |        | 2014                                | 2013         | 2014                               | 2013         |
| <b>Revenue</b>   | 6      | \$ 1,612,337                        | \$ 1,530,889 | \$ 4,502,508                       | \$ 4,693,203 |
| Costs of sales   |        | (621,365)                           | (695,214)    | (1,885,727)                        | (1,982,834)  |
| Direct amortization  | 10, 11 | (113,301)                           | (261,710)    | (339,903)                          | (846,634)    |
| <b>Gross profit</b>  |        | 877,671                             | 573,965      | 2,276,878                          | 1,863,735    |
| <b>Expenses</b>  |        |                                     |              |                                    |              |
| Consulting and management  | 18     | 212,706                             | 161,697      | 671,589                            | 635,704      |
| Depreciation   | 9      | 14,265                              | 19,831       | 56,012                             | 47,408       |
| Administration   |        | 183,862                             | 221,769      | 582,495                            | 714,409      |
| Sales and marketing expenses   |        | 71,909                              | 147,803      | 296,422                            | 276,406      |
| Research and development   | 23 (b) | 408,605                             | 185,387      | 630,632                            | 537,065      |
| Public company costs   |        | 22,732                              | 21,852       | 111,582                            | 86,834       |
| Share-based expense  | 16     | -                                   | -            | -                                  | 151,000      |
| <b>Total expenses</b>  |        | 914,079                             | 758,340      | 2,348,732                          | 2,448,826    |
| <b>Loss before the undernoted</b>  |        | (36,408)                            | (184,375)    | (71,854)                           | (585,091)    |
| <b>Other income and expense</b>  |        |                                     |              |                                    |              |
| Finance (loss) income  |        | (175)                               | (918)        | (676)                              | (568)        |
| Foreign exchange (loss) gain   |        | 62,617                              | (69,591)     | 79,543                             | 70,894       |
| Finance expense  | 18     | (24,084)                            | (25,191)     | (74,752)                           | (72,384)     |
|  |        | 38,358                              | (95,700)     | 4,115                              | (2,058)      |
| Loss before income taxes   |        | 1,950                               | (280,075)    | (67,739)                           | (587,149)    |
| Income tax recovery (expense)  |        | (4,029)                             | (5,145)      | (16,280)                           | (13,923)     |
| <b>Net loss</b>  |        | (2,079)                             | (285,220)    | (84,019)                           | (601,072)    |
| <b>Loss per share</b>  |        |                                     |              |                                    |              |
| Basic  |        | \$ (0.00)                           | \$ (0.00)    | \$ (0.00)                          | \$ (0.01)    |
| Diluted  |        | \$ (0.00)                           | \$ (0.00)    | \$ (0.00)                          | \$ (0.01)    |
| <b>Weighted average common shares outstanding</b>  |        |                                     |              |                                    |              |
| Basic  |        | 89,160,738                          | 89,160,738   | 89,160,738                         | 89,160,738   |
| Diluted  |        | 89,160,738                          | 89,160,738   | 89,160,738                         | 89,168,738   |
| <b>Other comprehensive income (loss) - items that may subsequently reclassify into income (loss)</b> |        |                                     |              |                                    |              |
| Net loss   |        | (2,079)                             | (285,220)    | (84,019)                           | (601,072)    |
| Exchange gain on translation of foreign subsidiary   |        | 100,054                             | -            | 145,174                            | -            |
| <b>Net comprehensive income (loss)</b>   |        | 97,975                              | (285,220)    | 61,155                             | (601,072)    |

The accompanying notes are an integral part of these condensed consolidated interim financial statements

## EUROCONTROL TECHNICS GROUP INC.

Condensed Consolidated Interim Statements of Changes in Shareholders' Equity (unaudited)

(Expressed in Canadian dollars)

|  | Number of<br>Shares | Issued Capital<br>(Note 14) | Warrants<br>Reserve<br>(Note 15) | Share-based<br>Payment<br>Reserve<br>(Note 16) | Deficit        | Accumulated<br>Other<br>Comprehensive<br>Income | Total        |
|--|---------------------|-----------------------------|----------------------------------|--|----------------|---|--------------|
| Balance as at December 31, 2012                    | 89,160,738          | \$ 14,690,341               | \$ 866,379                       | \$ 296,736                                     | \$(10,681,464) | \$ -  | \$ 5,171,992 |
| Expiry of stock options                            | -                   | -                           | -                                | (35,960)                                       | 35,960         | -   | -            |
| Share-based expense                                | -                   | -                           | -                                | 151,000  | -              | -   | 151,000      |
| Loss for the period                                | -                   | -                           | -                                | -  | (601,072)      | -   | (601,072)    |
| Balance as at September 30, 2013                   | 89,160,738          | \$ 14,690,341               | \$ 866,379                       | \$ 411,776                                     | \$(11,246,576) | \$ -  | \$ 4,721,920 |
| Expiry of warrants                                 | -                   | -                           | (866,379)                        | -  | 866,379        | -   | -            |
| Expiry of stock options                            | -                   | -                           | -                                | (15,920)                                       | 15,920         | -   | -            |
| Income for the period                              | -                   | -                           | -                                | -  | 158,851        | -   | 158,851      |
| Balance as at December 31, 2013                    | 89,160,738          | \$ 14,690,341               | \$ -                             | \$ 395,856                                     | \$(10,205,426) | \$ -  | \$ 4,880,771 |
| Exchange gain on translation of foreign subsidiary | -                   | -                           | -                                | -  | -              | 145,174   | 145,174      |
| Loss for the period                                | -                   | -                           | -                                | -  | (84,019)       | -   | (84,019)     |
| Balance as at September 30, 2014                   | 89,160,738          | \$ 14,690,341               | \$ -                             | \$ 395,856                                     | \$(10,289,445) | \$ 145,174                                      | \$ 4,941,926 |

*The accompanying notes are an integral part of these condensed consolidated interim financial statements*

**EUROCONTROL TECHNICS GROUP INC.**  
**Condensed Consolidated Interim Statements of Cash Flows (unaudited)**  
**(Expressed in Canadian dollars)**

| <b>For the nine month periods ended September 30,</b> | <b>Notes</b> | <b>2014</b>         | <b>2013</b>         |
|---|--------------|---------------------|---------------------|
| <b>Cash provided by (used in):</b>                    |              |                     |                     |
| <b>Operating activities</b>                           |              |                     |                     |
| Loss for the period                                   |              | \$ (84,019)         | \$ (601,072)        |
| Items not involving cash:                             |              |                     |                     |
| Amortization of intellectual property                 |              | 37,453              | -                   |
| Amortization of equipment                             | 9            | 56,012              | 47,408              |
| Amortization of deferred development costs            | 10           | 28,116              | 153,519             |
| Amortization of technology right                      | 11           | 274,333             | 693,115             |
| Share-based expense                                   |              | -                   | 151,000             |
| Foreign exchange loss (gain)                          |              | (2,328)             | (87,395)            |
| Foreign exchange gain on shareholder loans            |              | (43,272)            | 81,654              |
| Accrued interest on shareholder loans                 |              | 74,752              | 72,384              |
| Working capital adjustments                           |              |                     |                     |
| Change in amounts receivable                          |              | (48,193)            | 419,526             |
| Change in inventories                                 |              | (63,463)            | 46,291              |
| Change in prepaid expenses                            |              | 8,893               | 59,258              |
| Change in accounts payables and accrued liabilities   |              | 64,725              | (356,957)           |
| <b>Cash flows from operating activities</b>           |              | <b>303,009</b>      | <b>678,731</b>      |
| <b>Investing activities</b>                           |              |                     |                     |
| Equipment expenditures                                |              | (50,166)            | (18,468)            |
| Loan repayments                                       |              | (12,020)            | -                   |
| Loan payments received                                |              | 322,807             | (11,041)            |
| <b>Cash flows from (used in) investing activities</b> |              | <b>260,621</b>      | <b>(29,509)</b>     |
| <b>Financing activities</b>                           |              |                     |                     |
| Repayment of shareholder loans                        |              | (260,898)           | (256,182)           |
| <b>Cash flows used in financing activities</b>        |              | <b>(260,898)</b>    | <b>(256,182)</b>    |
| <b>Effect of exchange rate changes on cash</b>        |              | <b>120,708</b>      | <b>79,568</b>       |
| <b>Increase (Decrease) in cash</b>                    |              | <b>423,440</b>      | <b>472,608</b>      |
| <b>Cash, beginning of the period</b>                  |              | <b>2,185,662</b>    | <b>1,582,030</b>    |
| <b>Cash, end of the period</b>                        |              | <b>\$ 2,609,102</b> | <b>\$ 2,054,638</b> |
| <b>Supplementary cash flow information</b>            |              |                     |                     |
| Interest paid   |              | \$ 74,752           | \$ 72,384           |

*The accompanying notes are an integral part of these condensed consolidated interim financial statements*

# **EUROCONTROL TECHNICS GROUP INC.**

## **Notes to the Condensed Consolidated Interim Financial Statements (unaudited)**

**(Expressed in Canadian dollars)**

**For the three and nine month periods ended September 30, 2014 and 2013**

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### **1. NATURE OF OPERATIONS AND GOING CONCERN**

Eurocontrol Technics Group Inc. (the "Company") is a publicly listed company incorporated in British Columbia and Continued in the Province of Ontario. The Company participates in the energy security and authentication, verification and certification markets globally.

The Company's shares are listed on the TSX Venture Exchange ("TSXV") under the symbol "EUO". The head office, principal and registered address and records office of the Company is located at 401 Bay Street, Suite 2828, Toronto, Ontario, M5H 2Y4.

Due to a history of annual operating losses, the Company's continuance as a going concern is dependent upon its ability to maintain profitable levels of operation. It is not possible to predict if the Company will maintain profitable levels of operations. Management of the Company expects that the Company's revenue from operations, together with its existing cash and other current assets, will be adequate to meet its short-term working capital requirements during the next 12 months.

These consolidated financial statements were approved and authorized for issuance by the Board of Directors of the Company on November 25, 2014.

### **2. BASIS OF PRESENTATION**

#### **Statement of compliance**

These condensed consolidated interim financial statements, including comparatives, have been prepared in accordance with International Accounting Standards ("IAS") 34 'Interim Financial Reporting' ("IAS 34") using accounting policies consistent with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

#### **Basis of measurement**

These condensed consolidated interim financial statements have been prepared on the basis of accounting policies and methods of computation consistent with those applied in the Company's December 31, 2013 annual financial statements.

#### **Adoption of revised and new standards and interpretations**

The Company has adopted the following new standards, along with any consequential amendments, effective January 1, 2014. These changes were made in accordance with the applicable transitional provisions.

IAS 32, Financial Instruments, Presentation ("IAS 32") – In December 2011, effective for annual periods beginning on or after January 1, 2014, IAS 32 was amended to clarify the requirements for offsetting financial assets and liabilities. The amendments clarify that the right of offset must be available on the current date and cannot be contingent on a future date. The adoption of this standard did not result in any changes to the Company's disclosure of its financial instruments.

IAS 36 – Impairments of Assets ("IAS 36") was amended by the IASB in May 2013 to clarify the requirements to disclose the recoverable amounts of impaired assets and require additional disclosures about the measurement of impaired assets when the recoverable amount is based on fair value less costs of disposal, including the discount rate when a present value technique is used to measure the recoverable amount. The amendments to IAS 36 are effective for annual periods beginning on or after January 1, 2014. The adoption of this standard did not result in any changes to the Company's disclosure of its financial instruments.

## **EUROCONTROL TECHNICS GROUP INC.**

### **Notes to the Condensed Consolidated Interim Financial Statements (unaudited) (Expressed in Canadian dollars)**

**For the three and nine month periods ended September 30, 2014 and 2013**

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#### **2. BASIS OF PRESENTATION, (continued)**

IAS 39 – Financial Instruments: Recognition and Measurement (“IAS 39”) was amended by the IASB in June 2013 to clarify that novation of a hedging derivative to a clearing counterparty as a consequence of laws or regulations or the introduction of laws or regulations does not terminate hedge accounting. The amendments to IAS 39 are effective for annual periods beginning on or after January 1, 2014. The adoption of this standard did not result in any changes to the Company’s disclosure of its financial instruments.

IFRIC 21 – Levies (“IFRIC 21”) was issued in May 2013. IFRIC 21 provides guidance on the accounting for levies within the scope of IAS 37 – Provisions, Contingent Liabilities and Contingent Assets (“IAS 37”). IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (“obligating event”). IFRIC 21 clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. IFRIC 21 is effective for annual periods commencing on or after January 1, 2014. The adoption of this standard did not result in any changes to the Company’s disclosure of its financial instruments.

#### **New Accounting Policies not yet adopted:**

At the date of authorization of these financial statements, the IASB and IFRIC had issued the following new and revised Standards and Interpretations which are not yet effective for the relevant reporting periods and which the Company has not early adopted. The Company is currently assessing what impact the application of these standards or amendments will have on the interim condensed consolidated financial statements of the Company.

IFRS 9 – Financial Instruments (“IFRS 9”) was issued by the IASB in November 2009 with additions in October 2010 and May 2013 and will replace IAS 39 Financial Instruments: Recognition and Measurement (“IAS 39”). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9, except that an entity choosing to measure a financial liability at fair value will present the portion of any change in its fair value due to changes in the entity’s own credit risk in other comprehensive income, rather than within profit or loss. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. The Company has not yet determined the impact of the amendments on the Company’s financial statements.

IFRS 15 – Revenue from Contracts with Customers (“IFRS 15”). In May 2014, the IASB issued IFRS 15, Revenue from Contracts with Customers. IFRS 15 specifies how and when to recognize revenue as well as requires entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18, Revenue, IAS 11, Construction Contracts, and a number of revenue-related interpretations. Application of the standard is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions are leases, financial instruments and insurance contracts. IFRS 15 must be applied in an entity’s first annual IFRS financial statements for periods beginning on or after January 1, 2017. Application of the standard is mandatory and early adoption is permitted. The Company has not yet determined the impact of the amendments on the Company’s financial statements.



## EUROCONTROL TECHNICS GROUP INC.

Notes to the Condensed Consolidated Interim Financial Statements (unaudited)

(Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

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### 3. PRINCIPLES OF CONSOLIDATION

These consolidated financial statements for the three and nine month periods ended September 30, 2014 and 2013 include the financial position, results of operations and cash flows of the Company and its subsidiaries. The Company's subsidiaries are as follows:

| Name                                     | Country of incorporation | Economic interest | Basis of Accounting |
|--|--------------------------|-------------------|---------------------|
| Global Fluids International S.A. ("GFI") | Nevis                    | 100%              | Full consolidation  |
| Xenemetrix Ltd. ("Xenemetrix")           | Israel                   | 100%              | Full consolidation  |
| XwinSys Ltd. ("XwinSys")                 | Israel                   | 100%              | Full consolidation  |

#### *Subsidiaries*

Subsidiaries are entities over which the Company has control, whereby control is defined as the power to govern financial and operating policies of an entity so as to obtain benefit from its activities. Control is presumed to exist where the Company has a shareholding of more than one half of the voting rights in its subsidiaries. The effects of potential voting rights that are currently exercisable are considered when assessing whether control exists. Subsidiaries are fully consolidated from the date control is transferred to the Company, and are de-consolidated from the date at which control ceases.

#### *Business Combinations and Goodwill*

On the acquisition of a subsidiary that meets the definition of a business, the acquisition method of accounting is used to account for the acquisition as follows:

- cost is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange;
- directly attributable transaction costs are expensed rather than included in the acquisition purchase price;
- identifiable assets acquired and liabilities assumed are measured at their fair values as at the acquisition date except for non-current assets that are classified as held for sale in accordance with IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, which are recognized and measured at fair value less costs to sell;
- the excess of acquisition cost over the fair value of the identifiable net assets acquired is recorded as goodwill;
- if the acquisition cost is less than the fair value of the net assets acquired, the difference is recognized directly in the statement of operations;
- the interest of non-controlling shareholders in the acquiree is initially measured at the non-controlling shareholder's fair value; and
- the measurement of contingent consideration at fair value on the acquisition date is performed with subsequent changes in the fair value recorded through the statement of operations.

All material intercompany transactions between subsidiaries are eliminated in consolidation. After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is not amortized and is tested for impairment annually. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's cash generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. The level at which goodwill is allocated shall represent the lowest level within the entity at which the goodwill is monitored for internal purposes, but shall not be larger than an operating segment determined in accordance with IFRS 8 *Operating Segments*. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

# EUROCONTROL TECHNICS GROUP INC.

## Notes to the Condensed Consolidated Interim Financial Statements (unaudited) (Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

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### 4. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of consolidated financial statements in conformity with IFRS requires the Company's management to make judgments, estimates and assumptions about future events that affect the amounts reported in the consolidated financial statements and related notes to the financial statements. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results may differ from those estimates.

The areas which require management to make significant judgments, estimates and assumptions in determining carrying values include, but are not limited to:

- **Assets' carrying values and impairment charges** - In the determination of carrying values and impairment charges, management looks at the higher of the recoverable amount or fair value less costs to sell in the case of assets and at objective evidence, significant or prolonged decline of fair value on financial assets indicating impairment. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period.
- **Impairment of technology rights, deferred development costs and intellectual property** - While assessing whether any indications of impairment exist for technology rights, deferred development costs and intellectual property, consideration is given to both external and internal sources of information. Information the Company considers include changes in the market, economic and legal environment in which the Company operates that are not within its control and affect the recoverable of such assets. Internal sources of information include the manner in which technology rights and deferred development assets are being used or are expected to be used and indications of expected economic performance of the assets. Estimates include but are not limited to estimates of the discounted future after-tax cash flows expected to be derived from the Company's technology rights, deferred development costs and intellectual property, costs to sell the assets and the appropriate discount rate.
- **Share-based payments** – The Company determines costs for share-based payments using market-based valuation techniques. The fair value of the market-based and performance-based non-vested share awards are determined at the date of grant using generally accepted valuation techniques. Assumptions are made and judgment used in applying valuation techniques. These assumptions and judgments include estimating the future volatility of the stock price, expected dividend yield, future employee turnover rates and future employee stock option exercise behaviors and corporate performance. Such judgments and assumptions are inherently uncertain. Changes in these assumptions affect the fair value estimates.
- **Income taxes** - The Company must make significant estimates in respect of the provision for income taxes and the composition of its deferred income tax assets and deferred income tax liabilities. The Company's operations are, in part, subject to foreign tax laws where interpretations, regulations and legislation are complex and continually changing. As a result, there are usually some tax matters in question which may, on resolution in the future, result in adjustments to the amount of deferred income tax assets and deferred income tax liabilities, and those adjustments may be material to the Company's financial position and results of operations.
- **Functional currency determination** - The functional currency for the Company and its subsidiaries is the currency of the primary economic environment in which the entity operates. Determination of functional currency is conducted through an analysis of the consideration factors identified in IAS 21 The Effects of Changes in Foreign Exchange Rates and may involve certain judgments to determine the primary economic environment. The Corporation reconsiders the functional currency of its entities if there is a change in events and conditions which determine the primary economic environment. Significant changes to those underlying factors could cause a change to the functional currency.
- **Contingencies** – refer to note 23.

## EUROCONTROL TECHNICS GROUP INC.

Notes to the Condensed Consolidated Interim Financial Statements (unaudited)  
(Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

### 5. INTELLECTUAL PROPERTY

The Company, through its wholly owned subsidiary XwinSys, holds intellectual property on image processing technology. The intellectual property is licensed until 2020. Intellectual property is being amortized over the estimated useful life on a straight-line basis of seven years.

#### Cost

|                                  |    |         |
|----------------------------------|----|---------|
| Balance as at December 31, 2012  | \$ | 349,568 |
| Additions                        |    | -       |
| Balance as at December 31, 2013  |    | 349,568 |
| Additions                        |    | -       |
| Balance as at September 30, 2014 | \$ | 349,568 |

#### Accumulated amortization

|                                  |    |        |
|----------------------------------|----|--------|
| Balance as at December 31, 2012  | \$ | -      |
| Amortization expense             |    | -      |
| Balance as at December 31, 2013  |    | -      |
| Amortization expense             |    | 37,453 |
| Balance as at September 30, 2014 | \$ | 37,453 |

#### Carrying amounts

|                                  |    |         |
|----------------------------------|----|---------|
| Balance as at December 31, 2013  | \$ | 349,568 |
| Balance as at September 30, 2014 | \$ | 312,115 |

### 6. OPERATING SEGMENTS

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity), whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

The Company conducts its business as a single operating segment.

#### *Geographical information*

The Company's revenue from external customers and information about its non-current assets by geographical location are detailed below.

|               | Revenue from<br>external customers   |              | Revenue from<br>external customers      |              |
|---------------|--------------------------------------|--------------|---|--------------|
|               | Three months ended September<br>2014 | 2013         | Nine months ended September 30,<br>2014 | 2013         |
| Africa        | \$ 1,200,806                         | \$ 1,068,147 | \$ 3,287,094                            | \$ 3,100,036 |
| North America | 149,665                              | 12,183       | 228,512                                 | 102,215      |
| Asia          | 144,050                              | 270,744      | 292,715                                 | 800,309      |
| Europe        | 109,683                              | 172,099      | 630,440                                 | 682,926      |
| South America | 8,133                                | 7,716        | 63,748                                  | 7,717        |
|               | \$ 1,612,337                         | \$ 1,530,889 | \$ 4,502,508                            | \$ 4,693,203 |

# EUROCONTROL TECHNICS GROUP INC.

## Notes to the Condensed Consolidated Interim Financial Statements (unaudited) (Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

### 6. OPERATING SEGMENTS, (continued)

GFI accounts for \$3,310,373 (2013 - \$3,479,171) of the revenue generated for the nine month period ended September 30, 2014, representing 74% (2013 – 74%) of overall revenue from the sale of its oil markers. Xenometrix accounts for \$1,192,135 (2013 - \$1,214,032) of the revenue generated for the nine month period ended September 30, 2014, representing 26% (2013 – 26%) of overall revenue. Xenometrix revenue is from sales of EDXRF systems.

|                            | As at September 30, 2014 |               |            |            |
|----------------------------|--------------------------|---------------|------------|------------|
|                            | South America            | North America | Asia       | Total      |
| Equipment                  | \$ -                     | \$ -          | \$ 244,236 | \$ 244,236 |
| Deferred development costs | 309,272                  | -             | -          | 309,272    |
| Technology rights          | 1,966,157                | -             | 414,228    | 2,380,385  |
| Intellectual property      | -                        | -             | 312,115    | 312,115    |

|                            | As at December 31, 2013 |               |            |            |
|----------------------------|-------------------------|---------------|------------|------------|
|                            | South America           | North America | Asia       | Total      |
| Equipment                  | \$ -                    | \$ -          | \$ 223,288 | \$ 223,288 |
| Deferred development costs | 337,388                 | -             | -          | 337,388    |
| Technology rights          | 2,144,899               | -             | 509,819    | 2,654,718  |
| Intellectual property      | -                       | -             | 349,568    | 349,568    |

### 7. AMOUNTS RECEIVABLE

| <b>As at,</b>     | September 30,<br>2014 | December 31,<br>2013 |
|-------------------|-----------------------|----------------------|
| Trade receivables | \$ 551,577            | \$ 580,272           |
| Tax receivables   | 52,342                | -                    |
| Other             | 27,972                | 3,426                |
|                   | <b>\$ 631,891</b>     | <b>\$ 583,698</b>    |

### 8. INVENTORIES

| <b>As at,</b>   | September 30,<br>2014 | December 31,<br>2013 |
|-----------------|-----------------------|----------------------|
| Materials       | \$ 213,834            | \$ 138,284           |
| Work in process | 102,172               | 44,001               |
| Finished goods  | 292,817               | 363,075              |
|                 | <b>\$ 608,823</b>     | <b>\$ 545,360</b>    |

Inventories are carried at the lower of cost and net realizable value. Materials, work in process, and finished goods are recorded at cost. For the three and nine month periods ended September 30, 2014 and 2013, the cost of inventories recognized as an expense and included in cost of sales was \$621,365 and \$1,885,727 respectively, (2013 - \$695,214 and \$1,982,834 respectively).

**EUROCONTROL TECHNICS GROUP INC.**Notes to the Condensed Consolidated Interim Financial Statements (unaudited)  
(Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

**9. EQUIPMENT**

|                                  |    | <b>Office furniture,<br/>computers and<br/>equipment</b> | <b>Vehicles</b> | <b>Total</b> |
|----------------------------------|----|--|-----------------|--------------|
| <b>Cost</b>                      |    |  |                 |              |
| Balance as at December 31, 2012  | \$ | 231,682  | 64,291          | 295,973      |
| Additions                        |    | 115,225  | -               | 115,225      |
| Disposals                        |    | (28,350)   | -               | (28,350)     |
| Balance as at December 31, 2013  |    | 318,557  | 64,291          | 382,848      |
| Additions                        |    | 50,166   | -               | 50,166       |
| Disposals                        |    | -  | -               | -            |
| Foreign exchange                 |    | 38,227   | 7,715           | 45,942       |
| Balance as at September 30, 2014 | \$ | 406,950  | 72,006          | 478,956      |
| <b>Accumulated depreciation</b>  |    |  |                 |              |
| Balance as at December 31, 2012  | \$ | 85,459   | \$ 21,500       | \$ 106,959   |
| Depreciation                     |    | 46,464   | 13,725          | 60,189       |
| Disposals                        |    | (7,588)  | -               | (7,588)      |
| Balance as at December 31, 2013  |    | 124,335  | \$ 35,225       | \$ 159,560   |
| Depreciation                     |    | 45,744   | 10,268          | 56,012       |
| Disposals                        |    | -  | -               | -            |
| Foreign exchange                 |    | 14,920   | 4,227           | 19,147       |
| Balance as at September 30, 2014 | \$ | 185,000  | \$ 49,720       | \$ 234,720   |
| <b>Carrying amounts</b>          |    |  |                 |              |
| Balance as at December 31, 2013  | \$ | 194,222  | \$ 29,066       | \$ 223,288   |
| Balance as at September 30, 2014 | \$ | 221,950  | \$ 22,286       | \$ 244,236   |

**EUROCONTROL TECHNICS GROUP INC.****Notes to the Condensed Consolidated Interim Financial Statements (unaudited)  
(Expressed in Canadian dollars)****For the three and nine month periods ended September 30, 2014 and 2013****10. DEFERRED DEVELOPMENT COSTS**

During the three month period ended March 31, 2014, the estimate of the useful life of the fuel marker and detectors was reassessed and the useful life was estimated to be ending in fiscal 2022.

|                                  | <u>Marker</u> | <u>Equipment</u> | <u>Total</u> |
|----------------------------------|---------------|------------------|--------------|
| <b>Cost</b>                      |               |                  |              |
| Balance as at December 31, 2012  | \$ 920,137    | \$ 651,922       | \$ 1,572,059 |
| Additions                        | -             | -                | -            |
| Balance as at December 31, 2013  | 920,137       | 651,922          | 1,572,059    |
| Additions                        | -             | -                | -            |
| Balance as at September 30, 2014 | \$ 920,137    | \$ 651,922       | \$ 1,572,059 |
| <b>Accumulated amortization</b>  |               |                  |              |
| Balance as at December 31, 2012  | \$ 460,065    | 590,416          | 1,050,481    |
| Amortization expense             | 122,684       | 61,506           | 184,190      |
| Balance as at December 31, 2013  | 582,749       | 651,922          | 1,234,671    |
| Amortization expense             | 28,116        | -                | 28,116       |
| Balance as at September 30, 2014 | \$ 610,865    | \$ 651,922       | \$ 1,262,787 |
| <b>Carrying amounts</b>          |               |                  |              |
| Balance as at December 31, 2012  | \$ 337,388    | \$ -             | \$ 337,388   |
| Balance as at September 30, 2014 | \$ 309,272    | \$ -             | \$ 309,272   |

**11. TECHNOLOGY RIGHTS**

The Company, through its wholly owned subsidiaries GFI and Xenemetrix, holds a licence to produce and sell fuel markers, detectors and XRF systems. The fuel markers and detectors are licensed under a 20 year licence agreement from the holder of the patents. The XRF systems are licensed until February 2018. Technology rights assets relating to markers and detectors and XRF Systems are being amortized over their estimated useful lives on a straight-line basis of 10 years (ending in fiscal 2016) and seven years (ending in fiscal 2018), respectively. During the three month period ended March 31, 2014, the estimate of the useful life of the fuel marker and detectors was reassessed and the useful life was estimated to be ending in fiscal 2022.

|                                  | <u>Markers and<br/>Detectors</u> | <u>XRF Systems</u> | <u>Total</u> |
|----------------------------------|----------------------------------|--------------------|--------------|
| <b>Cost</b>                      |                                  |                    |              |
| Balance as at December 31, 2012  | \$ 7,844,267                     | \$ 892,184         | \$ 8,736,451 |
| Additions                        | -                                | -                  | -            |
| Balance as at December 31, 2013  | 7,844,267                        | 892,184            | 8,736,451    |
| Additions                        | -                                | -                  | -            |
| Balance as at September 30, 2014 | \$ 7,844,267                     | \$ 892,184         | \$ 8,736,451 |
| <b>Accumulated amortization</b>  |                                  |                    |              |
| Balance as at December 31, 2012  | \$ 4,902,673                     | 254,910            | 5,157,583    |
| Amortization expense             | 796,695                          | 127,455            | 924,150      |
| Balance as at December 31, 2013  | 5,699,368                        | 382,365            | 6,081,733    |
| Amortization expense             | 178,742                          | 95,591             | 274,333      |
| Balance as at September 30, 2014 | \$ 5,878,110                     | \$ 477,956         | \$ 6,356,066 |
| <b>Carrying amounts</b>          |                                  |                    |              |
| Balance as at December 31, 2013  | \$ 2,144,899                     | \$ 509,819         | \$ 2,654,718 |
| Balance as at September 30, 2014 | \$ 1,966,157                     | \$ 414,228         | \$ 2,380,385 |

**EUROCONTROL TECHNICS GROUP INC.****Notes to the Condensed Consolidated Interim Financial Statements (unaudited)**  
**(Expressed in Canadian dollars)****For the three and nine month periods ended September 30, 2014 and 2013****12. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

| <b>As at,</b>       | September 30,<br>2014 | December 31,<br>2013 |
|---------------------|-----------------------|----------------------|
| Accounts payable    | \$ 491,339            | \$ 289,945           |
| Accrued liabilities | 409,373               | 546,042              |
|                     | <b>\$ 900,712</b>     | <b>\$ 835,987</b>    |

**13. SHAREHOLDER LOANS**

|                             | September 30,<br>2014 | December 31,<br>2013 |
|-----------------------------|-----------------------|----------------------|
| <b>Euro loan</b>            |                       |                      |
| Principal € 500,000         | \$ 706,040            | \$ 731,420           |
| Interest € 424,622          | 599,600               | 556,708              |
|                             | 1,305,640             | 1,288,128            |
| Repayments                  | (43,736)              | -                    |
| Total outstanding Euro loan | 1,261,904             | 1,288,128            |
| <b>US dollar loan</b>       |                       |                      |
| Principal \$ 850,000        | 952,000               | 904,060              |
| Interest \$ 378,395         | 423,802               | 400,559              |
|                             | \$ 1,375,802          | \$ 1,304,619         |
| Repayments                  | (1,375,802)           | (1,101,425)          |
| Total outstanding US loan   | -                     | 203,194              |
| Total                       | \$ 1,261,904          | \$ 1,491,322         |

The total payable includes the principal amount of €500,000 (\$706,040) (December 31, 2013 - €500,000 (\$731,420)) and accrued interest of €424,622 (\$599,600) (December 31, 2013 - €380,567 (\$556,708)) loaned by the shareholders of GFI. These loans payable bear an annual interest rate of 7.2%. A director of the Company is among recipients of such loans.

As at September 30, 2014, the Company repaid €30,973 (\$43,736), (December 31, 2013 - €nil (\$nil)) resulting in an outstanding balance of €893,649 (\$1,261,904).

The remainder of the shareholder loans balance relates to the principal amount of US\$850,000 (\$952,000) (December 31, 2013 - US\$850,000 (\$904,060)) and accrued interest of US\$378,395 (\$423,802) (December 31, 2013 - US\$376,607 (\$400,559)) in loans payable to the shareholders of GFI. The US dollar shareholder loans will be repaid through 25% of the income generated by contracts of GFI. This portion of the loans payable bears an annual interest rate of 5.0%.

As at September 30, 2014, the Company repaid US\$1,228,395 (\$1,375,802), (December 31, 2013 - US\$1,035,563 (\$1,101,425)) resulting in an outstanding balance of \$nil (\$nil).

**EUROCONTROL TECHNICS GROUP INC.**

Notes to the Condensed Consolidated Interim Financial Statements (unaudited)  
(Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

**14. ISSUED CAPITAL**

**Authorized:** Unlimited common shares without par value

|                          | September 30,<br>2014 | December 31,<br>2013 |
|--------------------------|-----------------------|----------------------|
| Issued capital           | \$ 14,690,341         | \$ 14,260,341        |
| Fully paid common shares | 89,160,738            | 89,160,738           |

**Commons shares issued:**

|  | Number of<br>Shares | Value of shares |
|--|---------------------|-----------------|
| Balance as at December 31, 2013 and 2012 | 89,160,738          | \$ 14,260,341   |
| Balance as at September 30, 2014         | 89,160,738          | \$ 14,260,341   |

As at September 30, 2014 and December 31, 2013 and 2012, the Company had the following commitment to issue shares:

|   | Number of<br>Shares | Value of shares |
|---|---------------------|-----------------|
| Shares to be issued – warrants exercised  | 1,000,000           | \$ 260,000      |
| Shares to be issued – warrant valuation   | -                   | 170,000         |
| Balance as at December 31, 2012,<br>December 31, 2013 and<br>September 30, 2014 | 1,000,000           | \$ 430,000      |

**15. WARRANTS RESERVE**

The following table summarizes information about warrants:

|  | Number of<br>Warrants | Value      |
|--|-----------------------|------------|
| Balance as at December 31, 2012                        | 15,154,665            | \$ 866,379 |
| Warants expired  | (15,154,665)          | (866,379)  |
| Balance as at December 31, 2013 and September 30, 2014 | -                     | \$ -       |

There were no warrants outstanding as of September 30, 2014 and December 31, 2013 and 2012.



**EUROCONTROL TECHNICS GROUP INC.**  
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**16. SHARE-BASED PAYMENT RESERVE**

*Stock option plan*

The Board of Directors of the Company adopted a stock option plan (the "Plan") whereby the aggregate number of common shares reserved for issuance under the Plan, including common shares reserved for issuance under any other share compensation arrangement granted or made available by the Company from time to time, may not exceed 10% of the Company's issued and outstanding common shares. The Plan is administered by the Board of Directors and grants made pursuant to the Plan must at all times comply with the policies of the TSXV and the Plan.

The terms of any options granted under the Plan are fixed by the Board of Directors and may not exceed a term of five years. The exercise price of the options granted under the Plan is set at the last closing price of the Company's common shares before the date of grant.

Each employee share option converts into one common share of the Company on exercise. No amounts are paid or payable by the recipient on receipt of the option. The options carry neither rights to dividends nor voting rights. Options may be exercised at any time from the date of vesting to the date of their expiry.

The following table summarizes information about share-based payment reserve:

|  |    |           |
|--|----|-----------|
| Balance as at December 31, 2011                        | \$ | 640,100   |
| Expiry of stock options                                |    | (343,364) |
| Balance as at December 31, 2012                        | \$ | 296,736   |
| Share based payments                                   |    | 151,000   |
| Expiry of stock options                                |    | (51,880)  |
| Balance as at December 31, 2013 and September 30, 2014 | \$ | 395,856   |

The following share-based payment arrangements were in existence as at September 30, 2014:

| Number of options outstanding | Number of exercisable options | Grant date        | Expiry date       | Exercise price | Fair value at grant date |
|-------------------------------|-------------------------------|-------------------|-------------------|----------------|--------------------------|
| 1,700,000                     | 1,700,000                     | February 23, 2011 | February 23, 2016 | \$ 0.16        | 244,856                  |
| 5,112,500                     | 5,112,500                     | March 11, 2013    | March 11, 2018    | \$ 0.10        | 151,000                  |
| 6,812,500                     | 6,812,500                     |                   |                   |                | \$ 395,856               |

The share options outstanding as at September 30, 2014 had a weighted exercise price of \$0.11 (December 31, 2013: \$0.11) and a weighted average remaining contractual life of 2.9 years (December 31, 2013: 3.7 years).

All options vested on their date of issue and expire within five years of their issue, or 30 days after the resignation of the director, officer, employee or consultant.

**EUROCONTROL TECHNICS GROUP INC.**  
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**16. SHARE-BASED PAYMENT RESERVE (continued)**

*Fair value of share options granted in the nine month period ended September 30, 2014*

During the nine month period ended September 30, 2014, no share options were granted.

*Fair value of share options granted in the year ended December 31, 2013*

On March 11, 2013, 5,112,500 share options were granted to directors, officers and consultants of the Company to acquire the Company's shares at an exercise price of \$0.10 until March 11, 2018. These share options had an estimated fair value of \$151,000 at grant date.

The share options were priced using the Black-Scholes option-pricing model as at the date of the grant assuming a five year term to maturity with an expected volatility based on historical prices of the Company, an expected dividend yield, and a risk free interest rate, as noted in the table below. Where relevant, the expected life used in the model has been adjusted based on management's best estimate for the effects of non-transferability, exercise restrictions, and behavioral considerations.

|                         | <b>Number of Options Granted</b> |         |
|-------------------------|----------------------------------|---------|
|                         | 5,112,500                        |         |
| Grant date share price  | \$                               | 0.04    |
| Exercise price          | \$                               | 0.10    |
| Expected volatility     |                                  | 123%    |
| Expected option life    |                                  | 5 years |
| Expected dividend yield |                                  | 0%      |
| Risk-free interest rate |                                  | 1.39%   |

*Movements in shares options during the period/year:*

The following reconciles the share options outstanding during the nine month period ended September 30, 2014 and years ended December 31, 2013 and 2012:

|  | Number of options | Weighted<br>average<br>exercise price |
|--|-------------------|---------------------------------------|
| Balance as at December 31, 2011                        | 4,110,000         | \$ 0.19                               |
| Expired  | (2,060,000)       | \$ 0.20                               |
| Balance as at December 31, 2012                        | 2,050,000         | \$ 0.18                               |
| Granted  | 5,112,500         | \$ 0.10                               |
| Expired  | (350,000)         | \$ 0.28                               |
| Balance as at December 31, 2013 and September 30, 2014 | 6,812,500         | \$ 0.11                               |

## EUROCONTROL TECHNICS GROUP INC.

### Notes to the Condensed Consolidated Interim Financial Statements (unaudited)

(Expressed in Canadian dollars)

For the three and nine month periods ended September 30, 2014 and 2013

#### 17. FINANCIAL INSTRUMENTS

Financial assets and financial liabilities as at September 30, 2014 and December 31, 2013 were as follows:

|  | Loans and<br>receivables | Other financial<br>liabilities | Total        |
|--|--------------------------|--------------------------------|--------------|
| <b>As at September 30, 2014</b>          |                          |                                |              |
| Cash                                     | \$ 2,609,102             | -                              | \$ 2,609,102 |
| Amounts receivable                       | 551,577                  | -                              | 551,577      |
| Loans receivable                         | -                        | -                              | -            |
| Accounts payable and accrued liabilities | -                        | 900,712                        | 900,712      |
| Shareholder loans                        | -                        | 1,261,904                      | 1,261,904    |
| Loans                                    | -                        | 10,729                         | 10,729       |

|  | Loans and<br>receivables | Other financial<br>liabilities | Total        |
|--|--------------------------|--------------------------------|--------------|
| <b>As at December 31, 2013</b>           |                          |                                |              |
| Cash                                     | \$ 2,185,662             | -                              | \$ 2,185,662 |
| Amounts receivable                       | 580,272                  | -                              | 580,272      |
| Loans receivable                         | 322,807                  | -                              | 322,807      |
| Accounts payable and accrued liabilities | -                        | 835,987                        | 835,987      |
| Shareholder loans                        | -                        | 1,491,322                      | 1,491,322    |
| Loans                                    | -                        | 22,749                         | 22,749       |

As at September 30, 2014, there are no significant concentrations of credit risk for loans as the Company currently transacts with highly rated counterparties. The carrying amount reflected above represents the Company's maximum exposure to credit risk for such loans and receivables. As at September 30, 2014 and December 31, 2013, the Company did not hold financial instruments recorded at fair value that would require classification within the fair value hierarchy.

The carrying value of cash, amounts receivable, loan receivable, accounts payable, accrued liabilities and loans classified as long term approximate fair value because of the limited terms of these instruments. It is not possible to determine if the shareholder loans are at fair value as there is no comparable market value for such loans.

#### 18. RELATED PARTY DISCLOSURES

The Company entered into the following transactions in the ordinary course of business with related parties:

- For the nine month period ended September 30, 2014 \$74,752 (2013 - \$72,384) in interest was charged on the shareholder loans as described in note 13.

**EUROCONTROL TECHNICS GROUP INC.**  
**Notes to the Condensed Consolidated Interim Financial Statements (unaudited)**  
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**18. RELATED PARTY DISCLOSURES (continued)**

*Compensation of key management personnel of the Company*

The remuneration of directors and other members of key management personnel during the three and nine month periods ended September 30, 2014 and 2013 were as follows:

|                                      | Three months<br>ended September 30, |            | Nine months<br>ended September 30, |            |
|--------------------------------------|-------------------------------------|------------|------------------------------------|------------|
|                                      | 2014                                | 2013       | 2014                               | 2013       |
| Short-term compensation and benefits | \$ 170,100                          | \$ 145,250 | \$ 621,500                         | \$ 438,750 |
| Share-based payments                 | -                                   | -          | -                                  | 126,000    |
|                                      | \$ 170,100                          | \$ 145,250 | \$ 621,500                         | \$ 564,750 |

As at September 30, 2014, an amount of \$74,685 (December 31, 2013 - \$101,762) due to members of key management personnel, was included in accounts payable and accrued liabilities. This amount is unsecured, non-interest bearing and without fixed terms of repayment.

In accordance with IAS 24, key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company directly or indirectly, including any directors (executive and non-executive) of the Company.

The remuneration of directors and key executives is determined by the compensation committee.

See also note 23.

**19. CAPITAL MANAGEMENT**

The Company manages and adjusts its capital structure based on available funds in order to support its operations. The capital of the Company consists of common shares and options. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The Company has entered into commercial operations and has begun to generate cash flows to support the ongoing and longer term strategy of the Company. However, the Company may continue to rely on capital markets to support continued growth.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. There were no changes in the Company's approach to capital management in the nine month period ended September 30, 2014. The Company and its subsidiaries are not subject to externally imposed capital requirements.

**20. FINANCIAL RISK FACTORS**

The Company's risk exposure and the impact on the Company's financial instruments are summarized below. There have been no changes in the risks, objectives, policies and procedures from the previous period.

***Credit risk:***

The Company's credit risk is primarily attributable to cash, amounts receivable and loan receivable. Financial instruments included in amounts receivable consist primarily of receivables due from customers. The Company currently transacts with highly rated counterparties for the sale of its marking systems. Management believes that the credit risk concentration with respect to these financial instruments is minimal.

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**20. FINANCIAL RISK FACTORS (continued)**

***Liquidity risk:***

Liquidity risk is the risk that the Company will not have sufficient cash resources to meet its financial obligations as they come due. The Company's liquidity and operating results may be adversely affected if the Company's access to the capital market is hindered, whether as a result of a downturn in stock market conditions generally or related to matters specific to the Company. The Company generates cash flow primarily from its financing activities. As at September 30, 2014, the Company had a cash balance of \$2,609,102 (December 31, 2013 - \$2,185,662) to settle current liabilities of \$2,162,616 (December 31, 2013 - \$2,327,309). This amount includes \$1,261,904 (December 31, 2013 - \$1,491,322) in shareholder loans (note 13).

All of the Company's financial liabilities other than shareholder loans have contractual maturities of less than 365 days and are subject to normal trade terms. The Company cannot ensure there is sufficient capital in order to meet short term business requirements, after taking into account cash flows from operations and the Company's holding cash. The Company is currently seeking sources of funding to meet short term liabilities, and short term cash requirements. The terms of the shareholder loans are described in note 13.

***Market risk:***

(a) Interest rate risk

The Company carries shareholder loans with interest and repayment terms as described in note 13. Management believes that interest rate risk is remote as the Company currently does not carry interest-bearing debt at floating rates.

(b) Foreign currency risk

The functional and reporting currency of the Company and its subsidiaries is the Canadian dollar. The Company undertakes transactions denominated in foreign currencies, including US dollars and Euros, and as such is exposed to price risk due to fluctuations in foreign exchange rates against the Canadian dollar. The Company does not use derivative instruments to reduce exposure to foreign exchange risk.

The exposure of the Company's financial assets and liabilities to foreign currency risk as at September 30, 2014 is as follows:

|  | <b>CDN<br/>Dollar</b> | <b>US<br/>Dollar</b> | <b>Euro</b>         | <b>Total<br/>(in CDN dollars)</b> |
|--|-----------------------|----------------------|---------------------|-----------------------------------|
| <b>Financial assets</b>                  |                       |                      |                     |                                   |
| Cash                                     | \$ 34,499             | \$ 2,574,603         | \$ -                | \$ 2,609,102                      |
| Amounts receivable                       | -                     | 631,891              | -                   | 631,891                           |
| Loan receivable                          | -                     | -                    | -                   | -                                 |
|  | <b>\$ 34,499</b>      | <b>\$ 3,206,494</b>  | <b>\$ -</b>         | <b>\$ 3,240,993</b>               |
| <b>Financial liabilities</b>             |                       |                      |                     |                                   |
| Accounts payable and accrued liabilities | \$ 51,283             | \$ 849,429           | \$ -                | \$ 900,712                        |
| Shareholder loans                        | -                     | -                    | 1,261,904           | 1,261,904                         |
| Loan                                     | -                     | 10,729               | -                   | 10,729                            |
|  | <b>\$ 51,283</b>      | <b>\$ 860,158</b>    | <b>\$ 1,261,904</b> | <b>\$ 2,173,345</b>               |

A 10% change in foreign exchange rates between the Canadian dollar and these foreign currencies over the next year would affect net loss by approximately \$465,000 (2013 - \$56,000) based on the foreign currency balances at September 30, 2014.

## **EUROCONTROL TECHNICS GROUP INC.**

**Notes to the Condensed Consolidated Interim Financial Statements (unaudited)**  
**(Expressed in Canadian dollars)**

**For the three and nine month periods ended September 30, 2014 and 2013**

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### **20. FINANCIAL RISK FACTORS (continued)**

#### **(c) Price risk**

The Company is engaged in the development and implementation of marking systems for various types of oil. As a result, the Company is exposed to price risk with respect to commodity prices, specifically oil. The Company closely monitors commodity prices to determine the appropriate course of action to be taken by the Company. The Company's future operations will be significantly affected by changes in the market prices for oil. Oil prices fluctuate on a daily basis and are affected by numerous factors beyond the Company's control. The supply and demand for oil, the level of interest rates, the rate of inflation, investment decisions by large holders of oil, and stability of exchange rates can all cause significant fluctuations in oil prices. Such external economic factors are in turn influenced by changes in international investment patterns, and monetary systems and political developments.

### **21. LOAN RECEIVABLE**

On September 20, 2012, the Company, through its wholly owned subsidiary Global Fluids International S.A., loaned US\$200,000 and paid for various expenses amounting to US\$114,094 on behalf of GFI U Ltd., a non-related company, pursuant to a five year contract extension with the Ministry of Energy and Mineral Development, Government of the Republic of Uganda for the continued deployment of the Company's Petromark™ technology in that country. The loan carries an interest rate of 10% and is without fixed terms of repayment. As at September 30, 2014, the loan was fully repaid and the balance of principal and interest outstanding amounts to \$nil (December 31, 2013 – \$322,807).

### **22. COMPARATIVE FIGURES**

The Company revised the classification of certain of its expenses to cost of sales and direct amortization. This classification includes: amortization of technology rights, general and administration expenses and R&D related expenses. In 2013, amortization of technology rights had been categorized as depreciation expense. This change in classification resulted in a reduction of expenses of \$1,692,388, an increase of cost of sales of \$999,273 and an increase in direct amortization of \$693,115. This reclassification was made in order to more accurately disclose the gross profit of the Company.

### **23. COMMITMENT AND CONTINGENCIES**

- a) In January 2012, a lawsuit for approximately US\$100,000 was filed against the Company by a supplier for services it alleges were received by the Company but not paid for. In the opinion of management, this lawsuit has no merit and the ultimate disposition of this lawsuit will not have a material adverse effect on the Company's consolidated financial condition, results of operations or future cash flows. As a result, this amount has not been reflected in these consolidated financial statements.
- (b) Royalty-bearing grants from the Government of Israel for funding approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the costs incurred and included as a deduction of research and development costs. Research and development grants amounted to approximately \$250,000 during the nine month period ended September 30, 2014. Royalty-bearing grants are repayable upon successful commencement of sales at a rate of 4% of sales up until the balance of the grants is repaid in full. As of September 30, 2014, the balance of the grants received to date to be repaid is approximately \$438,000.

## **EUROCONTROL TECHNICS GROUP INC.**

**Notes to the Condensed Consolidated Interim Financial Statements (unaudited)  
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### **24. EVENTS AFTER THE REPORTING PERIOD**

On November 3, 2014, the Company entered into a Letter of Intent (“LOI”) with Austin Automation and Instrumentation, Inc. (“Austin AI”), a private company located in Austin, Texas, to acquire the assets of Austin AI which will be combined with Eurocontrol’s wholly-owned subsidiary Xenemetrix (“Xenemetrix”).

Austin AI has been a distributor for Xenemetrix technology in the US and Asia since 2012. Both Xenemetrix and Austin AI have strong franchises in Energy Dispersive X-Ray Fluorescence (“ED-XRF”) technology and they represent a synergistic fit of technology and culture. The combination of Austin AI’s ED-XRF business with Xenemetrix’s existing business will produce broader distribution of both company’s products and access to new vertical markets through technological innovation.

The LOI is non-binding and outlines the Company’s intention to purchase the assets (excluding real estate) of Austin AI in exchange for 7,500,000 common shares of Eurocontrol and 2,500,000 common share purchase warrants which will vest based on certain sales performance criteria relating to several large contract opportunities, including a prospective contract valued at US\$40 million with a global consumer packaged goods company for installation of over 400 ED-XRF custom spectrometers over multiple years in a worldwide initiative. Austin AI has forecast US\$2 million in revenue for 2015 (not including sales from the potential US\$40 million contract described above).

Eurocontrol and Austin AI will work towards finalizing a definitive agreement by December 31, 2014, the expiry date of the LOI.