# NEODYM TECHNOLOGIES INC.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

FOR PERIODS ENDED MAY 31, 2011 AND 2010

(Unaudited – Prepared by Management)

# NOTICE

## No auditor review of the Interim Financial Statements

The accompanying unaudited condensed consolidated interim financial statements of Neodym Technologies Inc. ("the Company"), for the three months ended May 31, 2011, have been prepared by management and have not been the subject of a review by the Company's external independent auditors.

**NEODYM TECHNOLOGIES INC.**
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION**
(Unaudited)

| | **May 31 2011** | February 28 2011 | March 1 2010 |
|---|---|---|---|
| | **$** | $ | $ |
| **ASSETS** | | | |
| **CURRENT** | | | |
| Cash and cash equivalents | **19,676** | 14,830 | 15,719 |
| Accounts receivable (Note 3) | **32,950** | 23,546 | 26,171 |
| Materials inventory | **17,123** | 15,373 | 21,812 |
| | **69,749** | 53,749 | 63,702 |
| **EQUIPMENT** (Note 4) | **1,317** | 1,407 | 1,221 |
| **INTANGIBLE ASSETS** (Note 5) | **11,312** | 11,499 | 14,105 |
| | **82,378** | 66,655 | 79,028 |
| **LIABILITIES** | | | |
| **CURRENT** | | | |
| Accounts payable and accrued liabilities (Note 6) | **58,888** | 56,456 | 56,681 |
| Related party payables (Note 9) | **954,425** | 930,966 | 804,460 |
| Sales prepayment | **62,890** | 63,221 | 68,330 |
| Loans payable (Note 7) | **20,252** | 23,000 | 24,003 |
| | **1,096,455** | 1,073,643 | 953,474 |
| **SHAREHOLDERS' DEFICIENCY** | | | |
| **SHARE CAPITAL** (Note 8) | **1,092,985** | 1,092,985 | 1,092,985 |
| **CONTRIBUTED SURPLUS** | **24,589** | 24,589 | 24,589 |
| **DEFICIT** | **(2,131,651)** | (2,124,562) | (1,992,020) |
| | **(1,014,077)** | (1,006,988) | (874,446) |
| | **82,378** | 66,655 | 79,028 |

**GOING CONCERN AND NATURE OF OPERATIONS** (Note 1)

**APPROVED ON BEHALF OF THE BOARD OF DIRECTORS:**

*Signed:* ***"Juraj Krajci"***
Director

*Signed:* ***"Stephen Pearce"***
Director

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

**NEODYM TECHNOLOGIES INC.**
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF OPERATIONS**
(Unaudited)

| | For The Three Months Ended May 31 2011 | May 31 2010 |
|---|---|---|
| | **$** | $ |
| **REVENUE** | | |
| Sales | **58,006** | 46,542 |
| Cost of sales | **(21,219)** | (16,103) |
| Gross Profit | **36,787** | 30,439 |
| **ADMINISTRATIVE EXPENSES** | | |
| Advertising and promotion | **532** | 487 |
| Amortization and depreciation | **1,940** | 690 |
| Audit | **850** | |
| Bank charges, interest and exchange | **1,299** | 1,442 |
| Customer service and application support | **5,300** | 10,358 |
| Management fees | **17,227** | 30,595 |
| Marketing | **5,357** | 7,473 |
| Office | **4,588** | 2,318 |
| Foreign exchange loss (gain) | **(14)** | 106 |
| Regulatory and stock transfer fees | **1,904** | 1,881 |
| Rent | **750** | 750 |
| Research and development | **3,352** | 3,301 |
| Telephone | **791** | 907 |
| Write off of accounts receivable | **-** | |
| | **43,876** | 60,308 |
| **LOSS FOR THE PERIOD** | **(7,089)** | (29,869) |
| **NET LOSS PER SHARE - BASIC AND DILUTED** | **(0.00)** | (0.00) |
| **WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING** | **10,151,920** | 10,151,920 |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

**NEODYM TECHNOLOGIES INC.**
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF SHARHOLDERS' EQUITY AND DEFICIT**
**FOR THE THREE MONTHS ENDED MAY 31, 2011 AND 2010**
(Unaudited)

| | SHARE CAPITAL | | | | CONTRIBUTED | | | |
|---|---|---|---|---|---|---|---|---|
| | NUMBER | | AMOUNT | | SURPLUS | DEFICIT | | TOTAL |
| Balance, February 29, 2010 | 12,151,920 | $ | 1,092,985 | $ | 24,589 | (1,993,884) | $ | (872,450) |
| Net loss for the year | - | | - | | - | (134,538) | | (134,538) |
| Balance, February 28, 2011 | 12,151,920 | $ | 1,092,985 | $ | 24,589 | (2,126,832) | $ | (1,006,988) |
| Net loss for the period | - | | - | | - | (7,089) | | (7,089) |
| **Balance, May 31, 2011** | **12,151,920** | **$** | **1,092,985** | **$** | **24,589** | **(2,134,429)** | **$** | **(1,014,077 )** |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

**NEODYM TECHNOLOGIES INC.**
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS**
(Unaudited)

| | For The Three Months Ended | |
|---|---|---|
| | **May 31 2011** | May 31 2010 |
| | **$** | $ |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Loss for the period | **(7,089)** | (29,869) |
| Adjust for items not requiring an outlay of cash: | | |
| Amortization | **1,940** | 690 |
| Foreign exchange loss (gain) | **(14)** | 106 |
| | **(5,163)** | (29,073) |
| Change in non cash working capital items: | | |
| Accrued Interest payable | **(2,748)** | 252 |
| Accounts receivable | **(9,721)** | 2,818 |
| Materials inventory | **(1,750)** | 67 |
| Accounts payable and accrued liabilities | **2,432** | 1,348 |
| | **(16,950)** | (24,588) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Product development | **(1,663)** | (1,647) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Related party payable | **23,459** | 22,026 |
| **INCREASE (DECREASE) IN CASH** | **4,846** | (4,209) |
| **CASH AND CASH EQUIVALENTS – Beginning of period** | **14,830** | 14,760 |
| **CASH AND CASH EQUIVALENTS – End of period** | **19,676** | 10,551 |

| | | |
|---|---|---|
| **SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION** | | |
| Interest paid | **3,000** | - |
| Income tax paid | **-** | - |

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

## 1. GOING CONCERN AND NATURE OF OPERATIONS

Neodym Technologies Inc. (the "Company") was incorporated under the laws of British Columbia, and its principal business activity is the development and sales of gas safety and loss control systems. The Company's registered office is located at 711 – 675 West Hastings Street, Vancouver BC, V6B 1N2

These consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 Interim Financial Reporting under International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board. These are the Company's first IFRS consolidated interim financial statements for a portion of the period covered by the Company's first IFRS annual financial statement for the year ending February 28, 2012. Subject to certain IFRS transitions elections disclosed in Note 13, the Company has consistently applied the same accounting policies in its opening IFRS balance sheet at March 1, 2010 and throughout all periods presented, as if the policies has always been if effect. Theses consolidated interim financial statements have been prepared in accordance with IAS 34. Interim Financial Reporting and do not contain all of the information required for full annual financial statements. The Company prepared its previous 2010 annual and interim financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") and these consolidated interim financial statements should be read in conjunction with the Company's 2010 annual financial statements considering the IFRS transition disclosures included in Note 13.

These consolidated financial statements have been prepared on the assumption that the Company is a going concern, meaning that it will continue in operation for the foreseeable future and will be able to realize assets and discharge liabilities in the normal course of operations. The Company reported net comprehensive losses for the periods ended May 31, 2011 and 2010 of $7,089 and $29,869 and had working capital deficiencies of $1,026,706 and $918,602 at these dates. These factors create doubt as to the ability of the Company to continue as a going concern. The Company is critically dependent on investor financing and increasing levels of sales in order to carry out its short term plans for development, production and marketing. The consolidated financial statements do not reflect adjustments to the carrying values of assets should the Company be unable to generate sufficient sales or otherwise raise additional funds to continue operations.

## 2. SIGNIFICANT ACCOUNTING POLICIES

### a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Accounting Standard ("IAS") 34 Interim Financial Reporting under International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board. These are the Company's first IFRS consolidated interim financial statements for a portion of the period covered by the Company's first IFRS annual financial statement for the year ending February 28, 2012. Subject to certain IFRS transitions elections disclosed in Note 13, the Company has consistently applied the same accounting policies in its opening IFRS balance sheet at March 1, 2010 and throughout all periods presented, as if the policies has always been if effect. Theses consolidated interim financial statements have been prepared in accordance with IAS 34. Interim Financial Reporting and do not contain all of the information required for full annual financial statements. The Company prepared its previous 2010 annual and interim financial statements in accordance with Canadian Generally Accepted Accounting Principles ("GAAP") and these consolidated interim financial statements should be read in conjunction with the Company's 2010 annual financial statements considering the IFRS transition disclosures included in Note 13.

These condensed consolidated interim financial statements were approved for issue by the Board of Directors on August 29, 2011.

### b) Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Neodym Systems Inc. All significant intercompany transactions and balances have been eliminated upon consolidation. The functional currency of the Company is the Canadian dollar.

2. **SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**c) Use of estimates**

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenditures during the reporting period. Significant areas requiring the use of management estimates relate to the determination of impairment of assets, and determination of fair value for stock based compensation and transactions. Due to the inherent uncertainty involved with making such estimates, actual results reported in future years could differ from these estimates.

**d) Financial instruments**

Financial assets and liabilities are recognized on the balance sheet when the Company becomes party to the contractual provisions of the instrument. The classification of financial instruments dictates how these assets and liabilities are measured subsequently in the Company's financial statements.

The Company designated its cash and cash equivalents as financial instruments at fair value through profit or loss (FVTPL), which are measured at fair value with any changes in fair value recognized in earnings for the period. Accounts receivables are classified as loans and receivables. Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, these financial assets are recorded at amortized cost using the effective interest method, except for short-term receivables when the recognition of interest would be immaterial. Accounts receivable are assessed for evidence of impairment at each reporting date, with any impairment recognized in earnings for the period. Accounts payable, accrued liabilities, due to related parties, sales prepayment and loans payable are classified as financial liabilities. Financial liabilities are initially recorded at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy establishes three levels to classify the inputs to valuation techniques used to measure fair value, by reference to the reliability of the inputs used to estimate the fair values, described as follows:

Level 1: Valuations based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: Valuations based on directly or indirectly observable inputs in active markets for similar assets or liabilities, other than Level 1 prices such as quoted interest or currency exchange rates; and

Level 3: Valuations based on significant inputs that are not derived from observable market data, such as discounted cash flow methodologies based on internal cash flow forecasts.

**e) Cash and cash equivalents**

For purposes of reporting cash flows, the Company considers cash and short-term investments to include amounts held in banks and highly liquid investments with remaining maturities at point of purchase of 90 days or less. The Company places its cash and cash investments with institutions of high-credit worthiness. As at May 31, 2011, there is $Nil (2010 - $Nil) included as cash equivalents.

2. **SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**e) Foreign currency translation**

Transactions in foreign currencies are translated at the exchange rate in effect at the date of the transaction. Foreign denominated monetary assets and liabilities are translated to their Canadian dollar equivalents using foreign exchange rates prevailing at the statement of financial position date. Non-monetary items are translated into Canadian dollars at the exchange rate in effect on the respective transaction dates. Revenues and expenses are translated at average rates for the period, except for amortization, which is translated on the same basis as the related asset. Exchange gains or losses arising on foreign currency translation are reflected in profit or loss for the period.

**f) Share capital**

i) Non-monetary consideration - Shares, agent's warrants, stock options and other equity instruments issued as purchase consideration in non-monetary transactions are recorded at fair value determined by management using the Black-Scholes option pricing model. The fair value of the shares issued is based on the trading price of those shares on the NEX on the date of the agreement to issue shares as determined by the Board of Directors.

ii) Stock based compensation - The Company measures the cost of the service received for all stock options made to consultants, employees and directors based on an estimate of fair value at the date of grant. The Company uses the Black-Scholes option pricing model to estimate the fair value of each stock option at the date of grant. Stock options which vest immediately are recorded at the date of grant. Stock options that vest over time are recorded over the vesting period using the straight line method. Stock options issued to outside consultants that vest over time are valued at the grant date and subsequently re-valued on each vesting date. Stock based compensation is recognized as expense or, if applicable, capitalized to mineral property costs with a corresponding increase in contributed surplus. On exercise of the stock option, consideration received and the estimated fair value previously recorded in contributed surplus is recorded as share capital.

iii) Share issuance costs - Costs directly identifiable with the raising of share capital financing are charged against share capital. Share issuance costs incurred in advance of share subscriptions are recorded as non-current deferred assets. Share issuance costs related to uncompleted share subscriptions are charged to operations.

**h) Equipment**

Equipment is stated at cost less accumulated depreciation and accumulated impairment losses. The cost of an item of equipment consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located. Depreciation is recorded at the following rates:

| | |
|---|---|
| Communication equipment | 20% |
| Computers | 30% |
| Machinery and equipment | 20% |

In the year of acquisition, depreciation is provided at one-half the normal rate. An item of equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in profit or loss.

2. **SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**i) Inventory**

Inventory is recorded at the lower of cost and net realizable value, and is comprised of materials required for the production of the Company's gas leak detection products.

An assessment is made of net realizable value from the inventory in each period. When inventories are sold, the carrying amount of those inventories is recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realizable value and all losses of inventories is recognized as part of the cost of goods and services expense in the period the write-down or loss occurs. When the circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in net realizable value because of changed economic circumstances, the amount of the write-down is reversed, limited to the amount of the original write-down, so that the new carrying amount is the lower of the cost and the revised net realizable value. The amount of any reversal of any write-down of inventories arising from an increase in net realizable value is recognized as a reduction in the amount of inventories recognized as part of the cost of goods and services expense in the period in which the reversal occurs.

**j) Intangible assets**

Intangible assets acquired separately - Patents are reported at cost less accumulated amortization and impairment losses. Patent costs represent amounts paid to third parties for the registration of patents. Amortization is charged on a straight line basis over a twenty year period. The estimated useful life and amortization method are reviewed each year end, with the effect of any changes in estimate being accounted for on a prospective basis.

Internally-generated intangible assets – Deferred Product Development Costs are recognized only if all of the following conditions are met: an asset is created that can be identified; it is probable that the asset created will generate future economic benefits; the development cost of the asset can be measured reliably; and the product from which the asset arises meets the IFRS criteria for technical and commercial feasibility. Internally-generated intangible assets are amortized on a straight-line basis over their useful lives. Costs meeting the capitalization criteria are recorded as Deferred Product Development Costs. Amortization is provided on a straight-line basis over the estimated three year commercial lives of the products. Where no internally generated intangible asset can be recognized, development expenditure is recognized as an expense in the period in which it is incurred. Capitalized expenses include the cost of material, direct labor, direct overhead and outsourcing costs.

**k) Revenue recognition**

Revenue from the sale of products is recognized upon shipment, which is when: ownership is transferred, the fee is fixed and determinable, the collection of resulting receivables is probable and any uncertainties with regard to customer acceptance are insignificant.

Revenue from the provision of engineering services is recognized upon project/service completion.

2. **SIGNIFICANT ACCOUNTING POLICIES** (Continued)

**l) Research and development**

An internally-generated intangible asset arising from product development is recognized only if all of the following conditions are met: an asset is created that can be identified; it is probable that the asset created will generate future economic benefits; the development cost of the asset can be measured reliably; and the product from which the asset arises meets the IFRS criteria for technical and commercial feasibility. Internally-generated intangible assets are amortized on a straight-line basis over their useful lives. Costs meeting the capitalization criteria are recorded as Deferred Product Development Costs. Amortization is provided on a straight-line basis over the estimated three year commercial lives of the products. Where no internally generated intangible asset can be recognized, development expenditure is recognized as an expense in the period in which it is incurred. Capitalized expenses include the cost of material, direct labor, direct overhead and outsourcing costs.

**m) Asset impairment**

On an annual basis, or when impairment indicators arise, the Company evaluates the future recoverability of its patent and deferred product development costs. Capitalized costs are written off to the extent that the accumulated costs exceed the undiscounted cash flows expected to be generated from those assets. When an asset is not recoverable, the impairment loss recognized is measured as the amount by which the carrying amount of the asset exceeds its fair value.

Where practicable, deferred product development costs are allocated to products or product groups on a specific identification basis. When costs are not specifically identified, costs are allocated on the basis of relative specifically identified costs.

**n) Income taxes**

Current income tax:
Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date.

Deferred income tax:
Deferred income tax is provided using the balance sheet method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority. Valuation allowances are provided where net deferred income tax assets are not more likely than not to be realized.

**o) Earnings per share**

Basic earnings per share are calculated by dividing net income (loss) by the weighted average number of shares issued and fully paid. The calculations of earnings per share on a diluted basis are calculated using the treasury stock method, which considers the potential exercise of outstanding financial instruments with equity purchase or conversion features.

## 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

### p) Future accounting pronouncements

The following accounting pronouncements are applicable to future reporting periods. The Company is currently evaluating the effects of adopting these standards:

IFRS 9 Financial instruments:

Effective for annual periods beginning on or after January 1, 2013, with earlier adoption permitted. As part of the project to replace IAS 39, Financial Instruments: Recognition and Measurement, this standard retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets. More specifically, the standard:

− establishes two primary measurement categories for financial assets: amortized cost and fair value;
− prescribes that classification depends on entity's business model and the contractual cash flow characteristics of the financial asset;
− eliminates the existing categories: held to maturity, available for sale, and loans and receivables.

Certain changes were also made regarding the fair value option for financial liabilities and accounting for certain derivatives linked to unquoted equity instruments.

## 3. ACCOUNTS RECEIVABLE

| | **May 31, 2011** | February 28, 2011 |
|---|---|---|
| Value added tax recoverable | **$ 10,108** | $ 12,606 |
| Deposit | **250** | 250 |
| Sales receivables | **22,592** | 10,690 |
| | **$ 32,950** | $ 23,546 |

## 4. EQUIPMENT

| | **Costs** | | | |
|---|---|---|---|---|
| | **Communication Equipment** | **Computers** | **Machinery and Equipment** | **Total** |
| Balance March 1, 2010 | **$ 557** | **$ 14,203** | **$ 572** | **$ 15,332** |
| Additions | **-** | **641** | **-** | **641** |
| Balance February 28, 2011 | **557** | **14,844** | **572** | **15,973** |
| Additions | **-** | **-** | **-** | **-** |
| Balance May 31, 2011 | **$ 557** | **$ 14,844** | **572** | **$ 15,973** |

## 4. EQUIPMENT

| | Accumulated Depreciation | | | |
|---|---|---|---|---|
| | **Communication Equipment** | **Computers** | **Machinery and Equipment** | **Total** |
| Balance March 1, 2010 | **$ 503** | **$ 13,065** | **$ 543** | **$ 14,111** |
| Depreciation | **11** | **438** | **6** | **455** |
| Balance February 28, 2011 | **514** | **13,503** | **549** | **14,566** |
| Depreciation | **2** | **87** | **1** | **90** |
| Balance May 31, 2011 | **$ 516** | **$ 13,590** | **550** | **$ 14,656** |

| | Net Carrying Amount | | | |
|---|---|---|---|---|
| | **Communication Equipment** | **Computers** | **Machinery and Equipment** | **Total** |
| Balance March 1, 2010 | **$ 54** | **$ 1,138** | **$ 29** | **$ 1,221** |
| Balance February 28, 2011 | **43** | **1,341** | **23** | **1,407** |
| Balance May 31, 2011 | **41** | **$ 1,254** | **22** | **1,317** |

## 5. INTANGIBLE ASSETS

### a) Deferred Product Development Costs

Deferred product development costs represent wages, design fees, and material costs directly attributable to the development of the Company's gas leak sensing and detection equipment as follows:

| | **Costs** | **Amortization** | **Total** |
|---|---|---|---|
| Balance March 1, 2010 | **$ 900,519** | **$ 888,031** | **$ 12,488** |
| Additions | **10,332** | **12,736** | **(2,404)** |
| Balance February 28, 2011 | **910,851** | **900,767** | **10,084** |
| Additions | **1,663** | **1,799** | **(136)** |
| Balance May 31, 2011 | **$ 912,514** | **$ 902,566** | **$ 9,948** |

### b) Patent

| | **Costs** | **Amortization** | **Provision for impairment** | **Total** |
|---|---|---|---|---|
| Balance March 1, 2010 | **$ 20,037** | **$ 6,266** | **$ 12,154** | **$ 1,617** |
| Additions | **-** | **202** | **-** | **202** |
| Balance February 28, 2011 | **20,037** | **6,468** | **12,154** | **1,415** |
| Additions | **-** | **51** | **-** | **51** |
| Balance May 31, 2011 | **$ 20,037** | **$ 6,519** | **12,154** | **$ 1,364** |

5. **INTANGIBLE ASSETS** (continued)

The Company has registered a patent in the United States relating to its gas detection method and apparatus. The patent expires in 2019.

The patent is not used in any of the current products and there is doubt that the Company will be able to generate future economic benefits from this patent. Therefore, impairment of $12,154 has been provided.

6. **ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

| | **May 31, 2011** | February 28, 2011 |
|---|---|---|
| Trade payables | **$ 58,888** | $ 56,456 |

7. **LOANS PAYABLE**

| | **May 31, 2011** | February 28, 2011 |
|---|---|---|
| Repayable on demand, bearing interest at 5% per annum | **$ 10,000** | $ 10,000 |
| Repayable on demand, bearing interest at 5% per annum | **10,000** | 10,000 |
| Accrued interest | **252** | 3,000 |
| | **$ 20,252** | $ 23,000 |

**8. SHARE CAPITAL**

a) Authorized - Unlimited common shares without par value

b) Share purchase warrants - No share purchase warrants were outstanding as at May 31, 2011.

c) Share purchase option - No stock options were outstanding as at May 31, 2011.

d) Performance shares

2,000,000 common shares are restricted and can be released on the basis of cumulative cash flow with one share released for each $0.087 per share of cumulative cash flow generated before May 2011. The Company's shareholders have approved the change of release provisions on the escrow shares from a performance based formula to a time release formula. This change is subject to regulatory approval.

As at May 31, 2011, no performance shares had been released. Performance shares are excluded from the calculation of weighted average number of shares outstanding in determining basic and diluted loss per share.

## 9. RELATED PARTY TRANSACTIONS

a) Pursuant to a management agreement, the Company was charged $7,500 (2010: $7,500) for office, accounting and administrative support by a private company controlled by a former director. The contract is on a monthly basis and can be terminated by either party with 30 days notice. Pursuant to an employment services agreement, the Company was charged $16,398 (2010: $32,375) for management and product development services provided by a private company controlled by a director. The same company also charged $3,657 (2010: $2,757) for assembly and manufacturing services and $750 (2010: $750) for office rent. The Company was charged $9,000 (2010: $13,500) for marketing and product development services by a director.

b) Related party payables of $954,425 (2010: $823,170) are owed to companies which have certain current or former directors in common, of which $934,445 (2010: $803,843) relates to the agreements disclosed in Note 8(a). They are non-interest bearing and have no fixed terms of repayment.

Related party transactions are conducted in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the parties.

## 10. SEGMENTED INFORMATION

The Company operates in one business segment, which is the development, manufacture and sale of gas detection devices and systems. Substantially all of the Company’s identifiable assets are located in Canada.

## 11. ECONOMIC DEPENDENCE

The Company derives a sizable percent of its revenue from its largest customers. The cancellation of purchase orders from one or more of these customers may have a material adverse impact on the Company.

## 12. CAPITAL RISK MANAGEMENT

The Company's objective when managing capital is to maintain its ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders. The Company includes equity, comprised of issued capital stock, warrant capital, contributed surplus and deficit, in the definition of capital. The Company’s primary objective with respect to its capital management is to ensure that it has sufficient cash resources to further develop and market its gas leak detection products, and to maintain its ongoing operations. To secure the additional capital necessary to pursue these plans, the Company may attempt to raise additional funds through the issuance of equity and warrants or by securing strategic partners. The Company is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital risk management strategy during the current period.

## 13. FINANCIAL INSTRUMENTS

The Company has exposure to credit, foreign currency, market and liquidity risks from its use of financial instruments. This note provides information about the Company's exposure to each of these risks, and the Company's objectives, policies and processes for measuring and managing such risks. The board of directors has overall responsibility for the establishment and oversight of the Company's risk management framework

a) Fair values - The Company's financial instruments at February 28, 2011 consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, amounts due to related parties, sales prepayment and loans payable. Cash and cash equivalents are carried at fair value using a level 1 fair value measurement. The carrying value of accounts receivable, amounts due to related parties, accounts payable and accrued liabilities, sales prepayment and loans payable approximate their fair value because of their nature and respective maturity dates or durations.

b) Credit risk - The Company's largest customer accounts receivable balances represent a sizable percentage of total receivables.

c) Foreign currency risk - The Company's activities that result in exposure to fluctuations in foreign currency exchange rates consist of the sale of products to customers invoiced in foreign currencies and the purchase of services, materials, and property and equipment from suppliers invoiced in foreign currencies. The Company does not use derivative instruments to hedge its currency risk. A majority of the Company's accounts receivable are denominated in U.S. dollars.

d) Market risk - Market risk is the risk that changes in market conditions, such as input parts prices, interest rates, and foreign exchange rates, will affect the Company's cash flows or the value of its financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns. The Company does not utilize financial derivatives or other contracts to manage market risks.

e) Liquidity risk - Liquidity risk is the risk that the Company will encounter difficulty in paying obligations as they come due. The Company's financial liabilities consist of accounts payable, related party payables, sales prepayment and loans payable. Accounts payable consists of invoices payable to trade suppliers for capital and operating expenditures and for general corporate expenses. The Company processes invoices within a normal payment period. Loans payable are renegotiated to extend terms and conditions as required. Sales prepayment represents funds advanced as a deposit to secure a special order that has subsequently been cancelled. These funds will be used to defray the development and certification costs related to the project. Related party payables do not bear any interest and are provided on a non-secured basis. The Company prepares funds from operations and capital expenditure budgets, which are regularly monitored and updated.

## 14. FIRST TIME ADOPTION OF IFRS

a) Transition to IFRS

The Company has adopted IFRS effective March 1, 2011 with a transition date of March 1, 2010. Prior to the adoption of IFRS the Company prepared its financial statements in accordance with Canadian GAAP. The comparative information presented in these first consolidated interim financial statements for the three months ended May 31, 2010, year ended February 28, 2011 and the opening financial position as at March 1, 2010 (the "Transition Date") have been prepared in accordance with the accounting policies referenced in Note 2 and IFRS 1, First-Time Adoption of International Financial Reporting Standards ("IFRS 1").

b) Adoption of IFRS

- Equipment - All items had fair values that approximated their carrying values on March 1, 2010. The company completed impairment reviews and concluded that the assets were not impaired in accordance with IFRS and as a result, no transition adjustment was recorded.

- Business combinations – The Company elected under IFRS 1 to not to apply IFRS 3, Business Combinations retrospectively to any business combinations that may have occurred prior to its Transition Date and such business combinations have not been restated.

- Share based payments – The Company has not applied this retrospectively to fully vested equity settles grants.

- Cumulative translation differences – IFRS 1 permits cumulative translation differences at the date of transition to be deemed zero. The Company elected to deem cumulative translation differences to be zero on March 1, 2010 and as a result, a transition adjustment was recorded.

- Estimates - An entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. The Company's IFRS estimates as of March 1, 2010 are consistent with its GAAP estimates for the same date.

- Financial instrument – The Company designated its cash and cash equivalents, short-term investments and marketable securities as FVTPL upon initial recognition in accordance with an investment strategy that management uses to evaluate performance on a fair value basis. This designation had no impact on the results and financial position of the Company as these financial assets were classified as held-for-trading under Canadian GAAP and recorded at fair value

c) Statements

In preparing the Company's IFRS Transition Date statements management noted that adjustments related to accumulated other comprehensive income were necessary to be made by the Company in its financial statements prepared in accordance with previous Canadian GAAP.

Other comprehensive income:

Under previous Canadian GAAP, the unrealized foreign exchange gains and losses were recognized as other comprehensive income and the balance was reported on the balance sheet as accumulated other comprehensive income until realized. Under IFRS, foreign exchange gains and losses resulting from dealing with currency other than the Company's functional currency are reported on the income statement.

14. **FIRST TIME ADOPTION OF IFRS** (continued)

c) Statements (continued)

Statements of Cash Flows

The IFRS transition adjustment noted above did not have a material impact on the cash flows statements.

Reconciliation statements follow:

| Condensed Consolidated Statements of Financial Position | March 1, 2010 | | | May 31, 2010 | | | February 28, 2011 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Canadian GAAP | Effect of Transition | IFRS | Canadian GAAP | Effect of Transition | IFRS | Canadian GAAP | Effect of Transition | IFRS |
| | $ | $ | $ | $ | $ | $ | $ | $ | $ |
| Total Assets | 77,702 | - | 77,702 | 71,044 | - | 71,044 | 66,655 | - | 66,655 |
| Total Liabilities | 950,152 | - | 950,152 | 973,363 | - | 973,363 | 1,073,643 | - | 1,073,643 |
| Shareholders' Equity | | | | | | | | | |
| Share Capital | 1,092,985 | - | 1,092,985 | 1,092,985 | - | 1,092,985 | 1,092,985 | - | 1,092,985 |
| Contributed Surplus | 24,589 | - | 24,589 | 24,589 | - | 24,589 | 24,589 | - | 24,589 |
| Accumulated Other Comprehensive (Loss) Income | 3,860 | (3,860) | - | 4,315 | (4,315) | - | 2,270 | (2,270) | - |
| Deficit | (1,993,884) | 3,860 | (1,990,024) | (2,024,208) | 4,315 | (2,119,893) | (2,126,832) | 2,270 | (2,124,562) |
| | (872,450) | | (872,350) | (902,319) | | (902,319) | (1,006,988) | | (1,006,988) |
| Total Liabilities and Shareholders' Equity | 77,702 | - | 77,702 | 71,044 | - | 71,044 | 66,655 | - | 66,655 |

14. **FIRST TIME ADOPTION OF IFRS** (continued)

c) Statements (continued)

| Condensed Consolidated Statements of Operations and Comprehensive Loss | Year Ended February 28, 2011 Canadian GAAP | Effect of Transition | Year Ended February 28, 2011 IFRS |
|---|---|---|---|
| | $ | $ | $ |
| Total Revenue | 121,321 | | 121,,321 |
| Total Expenses | (254,269) | (1,590) | (255,859) |
| Net Loss | (132,269) | | (134,538) |
| Other Comprehensive (Loss) | (1,590) | 1,590 | - |
| Comprehensive Loss | (134,538) | | (134,538) |

| Consolidated Statements of Interim Operations and Comprehensive Loss | Period Ended May 31, 2010 Canadian GAAP | Effect of Transition | Period Ended May 31, 2010 IFRS |
|---|---|---|---|
| | $ | $ | $ |
| Total Revenue | 30,439 | | 33,439 |
| Total Expenses | (60,763) | 455 | (60,308) |
| Net Loss | (30,324) | | (29,869) |
| Other Comprehensive (Loss) | 455 | (455) | - |
| Comprehensive Loss | (29,869) | | (29,869) |