General

The following management's discussion and analysis ("MD&A") of the financial condition and results of operations of ZTEST Electronics Inc. ("ZTEST" or the "Company") constitutes management's review of the factors that affected the Company's consolidated financial and operating performance for the year ended June 30, 2013. The MD&A was prepared as of October 25, 2013 and was approved by the Board of Directors on October 25, 2013. It should be read in conjunction with the consolidated financial statements of the Company for the year ended June 30, 2013, including the notes thereto. Unless otherwise stated, all amounts discussed herein are denominated in Canadian dollars.

Additional information about the Company can be found at www.sedar.com.

The Company

The Company operates a single business segment involving the design, development, and assembly of printed circuit boards. The management of the Company is comprised of the following individuals:

Name	Position(s)
Wojciech Drzazga	Director and CEO
John Perreault (1)	Director and President
K. Michael Guerreiro (1) (2)	Director
Mike Hiscott (1) (2)	Director
Arn Schoch (3)	Director
Michael D. Kindy	VP Finance & CFO
William R. Johnstone	Secretary

(1) Denotes member of audit committee
(2) Denotes member of compensation committee
(3) Mr. Schoch, an independent Director, was appointed to the Board on March 11, 2013.

Corporate Performance

The 2013 fiscal year was another positive year for the Company with good profitability, strong cash flow, improved liquidity, and enhanced financial position.

Each of the four fiscal quarters of 2013 was profitable. In fact the Company has now been profitable in seven of the last eight fiscal quarters, including the last six consecutively. The Company had previously established the objective of becoming profitable on a consistent basis and although two fiscal years is not a sufficient basis to declare unequivocally that this has been achieved, recent results certainly suggest that it is well on its way.

2013 was an excellent year for cash flow. Cash flow from operations was positive for the eighth consecutive year and, at $457,838, 2013 was second only to 2010 in terms of being the best year yet. Positive cash flow from operations was identified in prior years as one of the most important factors relative to the Company's ability to maintain and grow its operations and to enhance its financial position and, after eight years, it would appear to be safe to say that a history of positive cash flow from operations has been established.

In 2013 the Company made more progress in addressing liquidity concerns by independently establishing a commercial line of credit to provide the ability to address any short-term financing requirements that may arise. Prior to the 2010 fiscal year the Company frequently borrowed from private lenders to support its working capital requirements. In May 2011, with a guarantee provided by a private lender, a commercial line of credit was established. In May 2013 the Company replaced the guarantee of the private lender with its own security. Although the Company, thus far, has only utilized this line of credit on a very limited basis its availability provides necessary financial flexibility and the elimination of the guarantee, and the associated guarantee fees, makes it available on a much more economical basis.

Corporate Performance - continued

The Company's financial position also continues to improve with 2013 marking the return to a positive net equity position. A number of factors contributed to this accomplishment but the most significant was a reduction of $657,275, or over 27% in total liabilities. This was made possible by utilizing cash generated from operations as well as cash received from a private placement financing, the exercise of stock options, and the exercise of share purchase warrants, to accelerate the reduction of long-term debt.

Management will continue striving to build upon the successes achieved in 2013, to manage and minimize business risks, and to maximize the value derived for its stakeholders. The following data, prepared in accordance with International Financial Reporting Standards, may provide some additional insights relative to the Company's operating performance and financial position:

	For the fiscal years ended:		
	June 13	June 12	June 11
Total Revenues	4,601,698	4,572,417	4,010,068
Net income (loss) income from operations	141,007	390,936	(178,066)
Per share	0.017	0.055	(0.031)
Net income (loss) for the year	148,319	392,778	(180,359)
Per share	0.018	0.056	(0.031)
Total assets	2,176,189	2,340,853	2,106,570
Total long-term financial liabilities	45,788	698,648	1,051,125
Total liabilities	1,759,668	2,416,943	2,575,438

	For the three month periods ended:				
	June 13	Mar. 13	Dec. 12	Sept. 12	June 12
Total Revenues	1,288,374	1,127,445	1,113,223	1,072,656	1,289,855
Net income (loss) from operations	81,609	21,311	31,955	6,132	42,073
Per share - basic	0.008	0.003	0.004	0.004	0.006
Net income (loss) for the period	83,815	22,379	33,336	8,789	44,015
Per share - basic	0.008	0.003	0.005	0.004	0.006
Total assets	2,176,189	2,228,452	2,133,002	2,252,523	2,340,853
Total long-term financial liabilities	45,788	57,496	66,478	602,565	698,648
Total liabilities	1,759,668	2,036,126	2,141,525	2,299,246	2,416,943

	For the three month periods ended:				
	Mar. 12	Dec. 11	Sept. 11	June 11	Mar. 11
Total Revenues	1,483,588	839,112	959,862	957,817	820,976
Net income (loss) from operations	279,280	(17,116)	86,699	(100,165)	(117,154)
Per share - basic	0.040	(0.002)	0.012	(0.014)	(0.022)
Net income (loss) for the period	279,280	(17,216)	86,699	(98,320)	(117,154)
Per share - basic	0.040	(0.002)	0.012	(0.014)	(0.022)
Total assets	2,652,994	2,122,488	2,033,096	2,106,570	2,299,219
Total long-term financial liabilities	785,338	902,553	962,334	1,051,125	1,173,917
Total liabilities	2,773,099	2,521,873	2,415,265	2,575,438	2,712,514

There were no cash dividends paid or accrued during any of the periods noted above.

Results of Operations

The Company has reported income from operations of $141,007 and net income of $148,319 for the 2013 fiscal year and 2013 was the first fiscal year for which each of the four quarters were profitable., and the income for the final quarter of 2013 exceeding that of the final quarter of 2012, the annual results lag behind 2012 levels. This is primarily due to the anomalous results realized in the 3rd quarter of 2012. There are many factors that contribute to the Company's operating results and the highlights are discussed below.

Results of Operations - continued

Revenues for the 2013 fiscal year were $4,601,698 making this the sixth time in the past seven years that annual revenues have risen. The revenue increase over 2012 levels was a very modest $29,281 but the total still represents the highest annual revenue figure the Company has ever reported. Revenues for the fourth quarters of the 2013 and 2012 fiscal years were almost identical with 2012 being $1,481 higher. It is expected that revenues will remain reasonably consistent in the immediate future.

Although revenues remained consistent the gross margin was $45,738 higher in the final quarter of 2013 but declined by $126,220 overall in comparison to 2012 levels. The unusually strong margins realized in Q3 2012 skew the comparison of the annual figures but it remains that margins will fluctuate from period to period based upon the timing of and nature of product deliveries.

The different elements of cost of product sales, and the changes realized, are as follows:

Years ended	June 13	June 12	Change
Raw materials and supplies consumed	$ 2,044,591	$ 1,764,787	$ 279,804
Labour costs incurred	753,901	776,883	(22,982)
Depreciation	151,033	173,201	(22,168)
Other costs	125,700	140,020	(14,320)
Net change in finished goods and work in process	(33,878)	30,955	(64,833)
Total cost of product sales	$ 3,041,347	$ 2,885,846	$ 155,501

Three month periods ended	June 13	June 12	Change
Raw materials and supplies consumed	$ 579,970	$ 589,256	$ (9,286)
Labour costs incurred	201,323	187,907	13,416
Depreciation	37,977	43,760	(5,783)
Other costs	39,037	49,048	(10,011)
Net change in finished goods and work in process	(14,992)	20,563	(35,555)
Total cost of product sales	$ 843,315	$ 890,534	$ (47,219)

The cost of raw materials and supplies consumed rose almost 16% in 2013 following a 47% increase in 2012 over 2011 levels. The Company actively promotes turnkey assembly, which incorporates the procurement of components and supplies, as a cost-effective option for its customers. These increases reflect the current customers’ general concurrence. The final quarter of 2013 shows a minor contradiction to this trend as costs declined by 1.5% in comparison to the final quarter of 2012. This is the second consecutive quarter for which these costs have declined. This is believed to be reflective of a reduction in the growth rate for turnkey services but is not considered to be indicative of any shift in customer preferences. In Q3 2012 the Company experienced a significant surge in demand for turnkey services and no similar surge arose in 2013 as would be required in order for costs to not decline. The Company will continue to promote its turnkey service and, while it anticipates that demand will remain strong, the growth rate is expected to ease considerably.

Labour costs have been declining in recent periods and the annual results for 2013 are consistent with this trend. However, a decline of less than 3% for the year, and the fact that Q4 costs are higher than the previous year, strongly suggest that this trend is certainly slowing and possibly at an end. The Company operates with a lean labour model and the Q4 results are evidence that short term fluctuations in demand will impact upon periodic results.

Results of Operations - continued

Depreciation costs are calculated as a percentage of the carrying value of equipment. The 2009 fiscal year was the most recent year for which equipment additions exceeded the annual depreciation charges so the carrying value of equipment has been on the decline. Management does not foresee the requirement for any significant equipment acquisitions in the near future so it is expected that depreciation charges will continue to decline.

Other costs include repairs and maintenance, stencils and tooling, packaging, and freight costs net of amounts recovered. Each of these costs is incurred on an as-needed basis without any specific correlation with revenues which can lead to fluctuations from one period to the next. Each of these costs is constantly monitored and is within management expectations so they will not be further elaborated upon.

Selling, general and administrative expenses for the periods ended June 30 were as follows:

Years ended	June 13	June 12	Change
Employee and consultant compensation	$ 832,729	$ 752,170	$ 80,559
Occupancy costs	258,703	260,807	(2,104)
Professional fees	66,024	43,864	22,160
Regulatory fees	30,677	17,817	12,860
Bad debts	-	8,047	(8,047)
Other costs	70,908	61,097	9,811
Total selling, general and administrative	$ 1,259,041	$ 1,143,802	$ 115,239

Three month periods ended	June 13	June 12	Change
Employee and consultant compensation	$ 250,731	$ 224,920	$ 25,811
Occupancy costs	64,327	67,009	(2,682)
Professional fees	11,425	7,923	3,502
Regulatory fees	993	1,774	(781)
Bad debts	-	-	-
Other costs	15,770	14,879	891
Total selling, general and administrative	$ 343,246	$ 316,505	$ 26,741

Compensation costs rose by 10.7% for the year, including an 11.5% increase in the final quarter. Costs have been trending higher since the end of a work-share program in April 2012. The increase includes higher compensation rates, increased consultancy costs, and higher director fees.

Occupancy costs consist primarily of rent and utility charges for the Company's operating facility. Base rental costs increased approximately 4% January 1, 2013 however this increase has been more than offset by lower utility costs.

Professional fees are comprised of the cost of legal services as well as the cost of the annual financial statement audit and similar expenses. Audit and similar expenses have increased by approximately $9,000 for the 2013 fiscal year reflecting the combination of higher costs in the 2013 fiscal year plus the effects of having corrected excess accruals in the 2012 fiscal year. Legal costs are approximately $13,000 higher for the 2013 fiscal year with this increase attributable to governance and stock related matters. Legal costs for 2013 exclude $6,000 in fees which were accounted for as stock issuance costs because they related specifically to the private placement transaction that was completed during the year.

Results of Operations - continued

Regulatory fees include all public disclosure, stock exchange and transfer agent fees incurred. The cost increase in 2013 arose prior to the final quarter and included the cost of issuing more news releases than in past years and the holding of a shareholders' meeting in September 2012. There were also additional filing fees incurred relative to the appointment of a new director and the issuance of stock options.

The remaining elements of SG&A are individually insignificant and, in aggregate, represent less than 5% of total SG&A for the periods presented. These expenses are continuously monitored by management and do not warrant detailed investigation or elaboration.

The Company's debt load and the associated costs of financing continue to decline. They are comprised of interest on long-term debt, other interest expense, and loan guarantee fees as follows:

Years ended	June 13	June 12	Change
Interest expense – long term (cash based)	$ 65,559	$ 100,558	$ (34,999)
Interest expense – long term (accretion)	20,593	20,182	411
Interest expense – other	596	624	(28)
Loan guarantee fees	8,800	9,600	(800)
Total financing expenses	$ 95,548	$ 130,964	$ (35,416)

Three month periods ended	June 13	June 12	Change
Interest expense – long term (cash based)	$ 10,917	$ 22,123	$ (11,206)
Interest expense – long term (accretion)	4,037	4,620	(583)
Interest expense – other	149	162	(13)
Loan guarantee fees	1,600	2,400	(800)
Total financing expenses	$ 16,703	$ 29,305	$ (12,602)

Interest expense – long term consists of the interest amounts being paid (cash based) in accordance with the face value of long term debt instruments plus accretion of the difference between those face values and their carrying amounts. During the 2013 fiscal year the Company repaid $552,326 in long-term debt leading to a significant decline in cash based interest payments. The 2013 debt repayments included $233,500 in pre-payments against long-term debts that are subject to accretion. Accretion charges generally decline as the associated debt balances decline however incremental accretion charges arise at the time of pre-payment. The incremental charges arising from the 2013 pre-payments caused accretion expense to be marginally higher in the 2013 fiscal year than it was for 2012. The incremental charges associated with a $73,500 pre-payment made in the fourth quarter served to make the fourth quarter costs more comparable than they would otherwise have been. Total long term debt was reduced by over 54% in 2013 and almost 90% of the long-term debt remaining at June 30, 2013 is scheduled to be repaid during the 2014 fiscal year. Accordingly, the associated interest payments and interest accretion will be lower in future periods.

From May 2011 to May 2013 the Company incurred a fee of $800 per month in order to have an individual provide a guarantee for its $250,000 bank line of credit. In May 2013 the Company posted its own guarantee, in the form of a $250,000 term deposit. This meant the guarantee from this individual was no longer required and allowed the monthly fee to stop.

Liquidity

As at June 30, 2013 the Company reported a working capital deficiency of $196,064 representing a decline of $19,377 for the year and an improvement of $283,429 in the final quarter. The deficiency includes $776,792 in current liabilities that have been outstanding since June 2007, are not secured, bear no interest or other charges, and for which there are no immediate plans for settlement. Management does not consider the working capital deficiency to be a significant source of business risk and will continue to focus on maximizing cash flows from operations as opposed to managing this deficiency.

The Company utilizes long term debt as a means of financing new equipment acquisitions and of settling other obligations whenever suitable terms can be negotiated. The Company's short-term financing requirements, if any, are expected to be met through the bank operating line.

In addition to satisfying the cost of operations the Company must also address the payment or other settlement of the following amounts as at June 30, 2013:

	Due by June 2014	Due by June 2016	Due by June 2018	Due after June 2018	Total Due
Long-term debt [1, 2]	374,837	46,805	-	-	421,642
Operating leases	88,729	186,965	204,620	294,935	775,249
Actively serviced obligations	463,566	233,770	204,620	294,935	1,196,891
Repurchase of preferred shares [3, 4]	$ 665,501	$ -	$ -	$ -	$ 665,501
Settlement of dividends payable [5]	263,337	-	-	-	263,337
Debenture [6]	39,600	-	-	-	39,600
Past-due obligations	968,438	-	-	-	964,438
All obligations	$ 1,432,004	$ 233,770	$ 204,620	$ 294,935	$ 2,165,329

(1) Amount excludes a debenture which was past due.
(2) Long-term debt includes three obligations for which their carrying value is lower than their face values. The financial statements as at June 30, 2013 report these obligations based upon their carrying values while the figures reported above represent the non-discounted cash payments to be made.
(3) The repurchase price includes $473,855 reported as a current liability plus $191,646 in paid up capital that is reported as an element of share capital.
(4) Obligation came due May 2004 as to $160,000 and May 2007 as to $505,501. No settlement terms have been established.
(5) Obligation arose at various dates up to May 2007. No settlement terms have been established.
(6) Obligation matured December 2005. No settlement terms have been established.

Capital Resources

The Company has access to a $250,000 revolving line of credit from its financial institution. The loan, which was not been drawn upon at June 30, 2013 or June 30, 2012, bears interest at the prime lending rate plus 0.5%, is due upon demand, matures May 13, 2014, and is secured by a general security agreement covering the assets of Permatech Electronics Corporation. Up to May 2013 the line of credit was also secured by the personal guarantee of an individual not related to the Company. This individual received a guarantee fee of $800 per month and 500,000 share purchase warrants which were exercised May 2013. This personal guarantee was replaced in May 2013 by Permatech posting security in the form of a $250,000 term deposit which must remain pledged until the next renewal date of May 2014.

The Company completed a private placement financing on February 4, 2013 which resulted in the issuance of 2,200,000 units at $0.08 per unit for gross proceeds of $176,000. Each unit was comprised of 1 common share and ½ share purchase warrant with the shares restricted from trading until June 5, 2013. Each full warrant entitles the holder to acquire one additional common share for $0.10 until February 4, 2016. The Company paid a cash finders' fee of $10,560 and incurred other costs of $7,630 in respect of this offering.

During the year 720,000 stock options and 500,000 share purchase warrants were exercised for aggregate proceeds of $139,500.

Related Party Transactions

The Company has an outstanding loan payable to 1114377 Ontario Inc., a company which is controlled by the spouse of Mr. W. Drzazga, the CEO and a Director of the Company. At its inception the loan provided the Company with cash for working capital purposes. The interest rate charged on the loan is consistent with the rates that were being charged to the Company by non-related parties for similar debts as at the date the loan originated.

The Company compensates its key management personnel for services rendered. These include salaries and benefits paid to the CEO and the President, consulting fees paid to the CFO, legal fees paid to a legal firm in which the Corporate Secretary is a partner, Directors' fees, and share-based payments. The Compensation rates are agreed to by the key management personnel and are predicated upon prevailing market rates.

The following balances are due to related parties as at June 30 of each year:

	2013	2012
Loan payable to 1114377 Ontario Inc. at prime +8% (1)	85,935	111,845
Consulting fees payable (2)	23,603	50,681
Legal fees payable (2)	1,991	1,570

(1) This is the face value of this obligation. It is reported in the consolidated financial statements at a discounted value. As additional compensation for having advanced these funds the creditor was granted an option that gives it the right to acquire a 24% interest in Permatech Electronics Corporation for $200,000 on or before May 1, 2015.
(2) Reported in the consolidated financial statements as an element of accounts payable and accrued liabilities.

The following expenses have arisen as a result of transactions involving the related parties defined above:

	2013	2012
Salaries and benefits (1)	$ 257,715	$ 246,125
Consulting fees (1)	32,348	60,264
Directors' fees (1)	29,850	11,300
Legal fees (2)	26,034	13,239
Interest expense – long term	12,309	14,433
Share issuance costs (3)	6,000	-
Cash based expenditures	$ 364,256	$ 345,361
Share-based payments	$ 42,118	$ -

(1) Reported in the consolidated financial statements as an element of employee and consultant compensation.
(2) Reported in the consolidated financial statements as an element of professional fees.
(3) Fees charged by legal firm in which the Corporate Secretary is a partner.

The following stock options have been issued to Directors and/or Officers of the Company and were outstanding as at June 30, 2013:

Description	Expiry Date	Number of Common shares
Stock options @ $0.10 per share (1, 3)	Nov. 2015	300,000
Stock options @ $0.10 per share (2)	Sept. 2017	180,000
Stock options @ $0.15 per share	Mar. 2018	200,000

(1) 600,000 options were exercised during the year leaving the above noted balance outstanding.
(2) 120,000 options were exercised during the year leaving the above noted balance outstanding.
(3) 75,000 options were exercised subsequent to June 30, 2013.

Convertible Instruments and Other Securities

The Company has the following securities issued and outstanding:

Share capital	Quantity	Amount
Common shares, June 30, 2012 and June 30, 2011	7,062,488	$ 21,773,391
Paid in capital of preferred shares		191,646
Class A special shares, June 30, 2012 and June 30, 2011	1,193,442	100,000
Share capital, June 30, 2012 and June 30, 2011		22,065,037
Private placement	2,200,000	176,000
Less: issuance costs		(18,190)
Less: value attributed to warrants		(37,859)
Stock options exercised	720,000	72,000
Plus: value previously attributed to options		54,030
Stock options exercised	500,000	67,500
Plus: value previously attributed to warrants		42,746
Class A special shares exchanged for common shares	(1,193,442)	(100,000)
Common shares issued for Class A special shares [1]	91,208	8,951
Share capital, June 30, 2013 and at the date of this document	10,573,696	22,330,215
Stock options exercised subsequent to June 30, 2013	75,000	13,225
Share capital, as at the date of this document	10,648,696	$ 22,343,440

[1] During the year the shareholders approved the issuance of 99,454 common shares in exchange for the 1,193,442 Class A Special Shares then outstanding. The issuance was recorded at fair value at the approval date and the difference between the carrying value of the Class A shares and the fair value of the 99,454 common shares was allocated to contributed surplus. 91,208 common shares have been issued to date, representing the entitlement of the Class A shareholders the Company was able to identify. The remaining common shares will be issued only in the event the remaining Class A shareholders identify themselves to the Company.

Preferred shares	Quantity	Amount
Series A preferred shares	166,667	$ 160,000
Series C preferred shares	288,858	505,501
Balance at June 30, 2013 and June 30, 2012		665,501
Less: amount accounted for as paid in capital		(191,646)
Liability element of preferred shares		$ 473,855

In addition to the shares issued and outstanding the Company has issued share purchase warrants and stock options as incentives to various parties. The following list itemizes the common shares that have been reserved to satisfy the conversions and exercise of warrants and options along with the expiry date associated therewith.

Shares reserved	Expiry Date	Number of Common shares
Common shares to be issued for Class A shares		8,246
Stock options @ $0.10 per share	Nov. 2015	300,000
Warrants @ $0.10 per share	Feb. 2016	1,100,000
Warrants @ $0.10 per share	Mar. 2016	900,000
Stock options @ $0.10 per share	Sept. 2017	180,000
Stock options @ $0.15 per share	Mar. 2018	200,000
Shares reserved, June 30, 2013		2,688,246
Stock options @ $0.10 per share, exercised	Nov. 2015	(75,000)
Shares reserved, as at the date of this document		2,613,246

Convertible Instruments and Other Securities - continued

Fully diluted position

Shares issued, June 30, 2013	10,573,696
Shares reserved, June 30, 2013	2,688,246
Fully diluted position, June 30, 2013 and at the date of this document	13,261,942

Note that the fully diluted position does not change as a result of the options exercised subsequent to June 30, 2013 as there is an equivalent increase in the number of shares issued and decrease in the number of shares reserved.

Additional disclosures relative to stock options are as follows:

	Common Shares Under Option	Weighted Average Price/Option	Weighted Average Expiry Date
Balance, June 30, 2012	900,000	$0.100	Nov. 30, 2015
Issued during the year	500,000	$0.120	Nov. 24, 2017
Exercised during the year	(720,000)	$0.100	Mar. 18, 2016
Balance, June 30, 2013	680,000	$0.110	Jan. 20, 2017
Exercised during the year	(75,000)	$0.100	Nov. 30, 2015
Balance, as at the date of this document	605,000	$0.117	Mar. 13, 2017

All stock options have vested and are held by Directors and Officers of the Company. The Company has no ability to cause these options to be exercised.

Additional disclosures relative to share purchase warrants are as follows:

	Number of Warrants	Weighted Average Price/Warrant	Weighted Average Expiry Date
Balance, June 30, 2012	1,400,000	$0.113	Mar. 18, 2015
Issued during the year	1,100,000	$0.100	Feb. 4, 2016
Exercised during the year	(500,000)	$0.135	May 13, 2013
Balance, June 30, 2013 and at the date of this document	2,000,000	$0.100	Feb. 26, 2016

Changes in Accounting Policy

The accounting policies followed by the Company are established in accordance with International Financial Reporting Standards (IFRS) and once policies are established they will not, as a matter of policy, be revised unless IFRS changes. The significant accounting polices utilized are disclosed in note 2 to the annual financial statements.

Accounting Standards Effective For Future Periods

IFRS 9, *Financial Instruments: Classification and Measurement*, issued in December 2009, effective for annual periods beginning on or after January 1, 2015, with early adoption permitted, introduces new requirements for the classification and measurement of financial instruments. Management anticipates that this standard will be adopted in the Company's financial statements for the year beginning July 1, 2015 and has not yet considered the potential impact of its adoption.

IFRS 10 and 13 were issued in May 2011 and are effective for annual periods beginning January 1, 2013. These will be adopted in the Company's consolidated financial statements for the year beginning July 1, 2013 and are not expected to have any impact upon the amounts or disclosures presented herein.

> IFRS 10, *Consolidated Financial Statements,* replaces the consolidation guidance in IAS 27, *Consolidated and Separate Financial Statements,* and SIC-12, *Consolidation — Special Purpose Entities,* by introducing a single consolidation model for all entities based on control, irrespective of the nature of the investee.

Accounting Standards Effective For Future Periods - continued

IFRS 13, *Fair Value Measurement,* replaces the guidance on fair value measurement in existing IFRS accounting literature with a single standard. It defines and provides guidance on determining fair value and requires disclosures about fair value measurements, but does not change the requirements regarding which items are measured or disclosed at fair value.

IAS 28, *Investments in Associates and Joint Ventures*, amended in 2011, effective for annual periods beginning on or after January 1, 2013 prescribes the accounting for investments in associates and establishes the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This will be adopted in the Company's consolidated financial statements for the year beginning July 1, 2013 and is not expected to have any impact upon the amounts or disclosures presented herein.

Financial Instruments

The Company's financial instruments are comprised of the following:

Financial assets:	*Classification*
Cash and cash equivalents	Fair value through profit and loss
Restricted cash	Loans and receivables
Accounts receivable	Loans and receivables
Financial liabilities:	*Classification*
Customer deposits	Other financial liabilities
Accounts payable and accrued liabilities	Other financial liabilities
Dividends payable	Other financial liabilities
Preferred shares	Other financial liabilities
Long-term debt	Other financial liabilities

Fair value through profit and loss:
Financial assets are designated as fair value through profit and loss if they were acquired principally for the purpose of selling in the short term. Fair value through profit and loss assets are recognized and carried at their fair value.

Loans and receivables:
Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Other financial liabilities:
Other financial liabilities are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial instrument and of allocating interest and any transaction costs over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial instrument to the net carrying amount on initial recognition. Other financial liabilities are de-recognized when the obligations are discharged, cancelled or expired.

Impairment of financial assets:
Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the assets have been negatively impacted.

Financial instruments - continued

Evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

The carrying amount of financial assets is reduced by any impairment loss directly for all financial assets with the exception of accounts receivable, where the carrying amount is reduced through the use of an allowance account. When an account receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income for the period.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through income for the period to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Financial instruments recorded at fair value:
Financial instruments recorded at fair value on the consolidated statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

As of June 30, 2013 and 2012 cash and cash equivalents and restricted cash are measured at fair value and are classified within Level 1 of the fair value hierarchy.

Financial instruments recorded at amortized cost:
Financial instruments recorded at amortized cost on the consolidated statement of financial position are amortized using the market rates of interest prevailing at the inception of the financial instrument applied to expected future cash flows. The amortized cost is recomputed in the event that the underlying terms, and therefore the expected future cash flows, of the financial instrument are altered with any change in the amortized cost being charged to income of the period. Dividends payable and preferred shares are each carried at historical cost as the future cash flows cannot be reasonably estimated.

Risk Factors

Events seemingly unrelated to the Company, or to its industry, may adversely affect its finances or operations in ways that are hard to predict or defend against. For example, credit contraction in financial markets may hamper the Company's ability to access credit when needed or rapid changes in foreign exchange rates may adversely affect its financial results. Finally, a reduction in credit, combined with reduced economic activity, may adversely affect businesses and industries that constitute a significant portion of the Company's customer base. As a result, these customers may need to reduce their purchases, or the Company may experience greater difficulty in collecting amounts due from them. Any of these events, or others caused by uncertainty in world financial markets, may have a material adverse effect on the Company's business, operating results, and financial condition.

Risk Factors - continued

In addition to the foregoing, the Company is exposed to credit risk, concentration of credit risk, liquidity risk, and currency risk. The Company's primary risk management objective is to protect earnings and cash flow and, ultimately, shareholder value. Risk management strategies, as discussed below, are designed and implemented to ensure that the Company's risks and the related exposure are consistent with its business objectives and risk tolerance. There have been no changes to the risk management strategies during the current year.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company's primary exposure to credit risk is in its accounts receivable. In an effort to mitigate this risk, management actively manages and monitors its receivables and obtains pre-payments where warranted. Bad debt experience has not been significant and it has been determined that no allowance is required as all amounts outstanding are considered collectible**.**

Concentration of credit risk

Concentration of credit risk arises when a significant portion of the financial assets subject to credit risk arise from a single or limited number of sources. During the current year, one of the Company's customers accounted for more than 20% (36%) of total revenue (2012 –21%). Amounts due from this customer accounted for 24% of the Company's accounts receivable at June 30, 2013 (2012 - 22%). The loss of this customer or significant curtailment of purchases by such customer could have a material adverse affect on the Company's results of operations and financial condition. The Company monitors the relationship with this customer closely and ensures that every customer is subject to the same risk management criteria.

Liquidity risk

Liquidity risk arises through the excess of financial obligations over available financial assets due at any point in time. The Company has reported a working capital deficiency of $196,064 (2012 - $176,687). This includes financial liabilities (a specific long-term debt instrument plus preferred shares and dividends payable) with an aggregate carrying amount of $776,792 (2012 - $781,656) which are past due and for which the timing and amount of future cash flows are undetermined. The Company manages its liquidity risk through the management of its capital which incorporates the continuous monitoring of actual and projected cash flows to ensure that it has sufficient liquidity to meet its operating commitments without incurring unacceptable losses or risking damage to the Company's reputation.

Market risks

The Company is exposed to currency risk related to accounts receivable and accounts payable denominated in US dollars and the potential for future cash flows to fluctuate because of changes in foreign exchange rates. Currency risk is closely monitored but not actively managed. The Company has reported a foreign exchange loss of $18,775 (2012 – $16,138)).

Sensitivity to market risks

At June 30, 2013 the Company had US$131,220 (2012 –US$217,295) included in accounts receivable. A 5% increase in the value of the Canadian dollar relative to the US dollar would result in a reduction of $6,935 in future cash inflow.

At June 30, 2013 the Company had US$186,818 (2012 – US$151,702) included in accounts payable. A 5% decrease in the value of the Canadian dollar relative to the US dollar would result in an increase of $9,874 in future cash outflow.

The existence of both accounts receivable and accounts payable denominated in US$ do not serve as a hedge with respect to currency risk.

Based upon observations of recent market trends management believes that each of these outcomes is possible but most likely exceed the Company's immediate market risk exposures.

Forward-looking Information

Certain statements in this MD&A may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company and its subsidiary, or the industry in which they operate, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this report, the words "estimate", "believe", "anticipate", "intend", "expect", "plan", "may", "should", "will", the negative thereof or other variations thereon or comparable terminology are intended to identify forward-looking statements. Such forward-looking statements reflect the current expectations of the management of the Company with respect to future events based on currently available information and are subject to risks and uncertainties that could cause actual results, performance or achievements to differ materially from those expressed or implied by those forward-looking statements, such as reduced funding, long sales cycles, currency and interest rate fluctuations, increased competition and general economic and market factors and including the risk factors summarized below under the heading "Risk Factors". New risk factors may arise from time to time and it is not possible for management of the Company to predict all of those risk factors or the extent to which any factor or combination of factors may cause actual results, performance or achievements of the Company to be materially different from those expressed or implied in such forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. Although the forward-looking statements contained in this MD&A are based upon what management believes to be reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward-looking statements. The forward-looking statements contained in this MD&A speak only as of the date hereof. The Company does not undertake or assume any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, except as required by law.