

ZTEST Electronics Inc.
Unaudited Condensed Interim Consolidated Financial Statements
December 31, 2013
(Stated in Canadian Dollars)

Notice To Reader

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the unaudited condensed interim consolidated financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

These unaudited condensed interim consolidated financial statements were approved by the Board of Directors on February 25, 2014. They have not been reviewed by the Company's auditors.

The accompanying unaudited condensed interim consolidated financial statements have been prepared by and are the responsibility of management. These condensed interim consolidated financial statements are presented on the accrual basis of accounting and accordingly, a precise determination of many assets and liabilities is dependent upon future events. Where necessary, management has made informed judgments and estimates in accounting for these assets and liabilities and for transactions which were not complete at the end of the reporting period. Recognizing that the Company is responsible for both the integrity and objectivity of the financial statements, management is satisfied that these unaudited condensed interim consolidated financial statements have been fairly presented.

ZTEST Electronics Inc.**Unaudited Condensed Interim Consolidated Statements of Financial Position**

(Stated in Canadian Dollars)

December 31, 2013

	Dec. 31 2013	June 30 2013
Assets		
Current assets		
Cash and cash equivalents	\$ 122,083	\$ 120,614
Restricted cash	250,000	250,000
Accounts receivable	382,341	506,799
Inventories (note 3)	505,998	632,459
Prepaid expenses	3,647	7,944
	1,264,069	1,517,816
Lease deposit (note 7)	35,000	35,000
Equipment (note 4)	560,755	623,373
	\$ 1,859,824	\$ 2,176,189
Liabilities		
Current liabilities		
Customer deposits	\$ -	\$ 5,113
Accounts payable and accrued liabilities	393,162	565,524
Notes payable (note 5)	144,735	-
Dividends payable	263,337	263,337
Current portion of long-term debt (note 6)	87,249	406,051
Preferred shares (note 8)	473,855	473,855
	1,362,338	1,713,880
Long-term debt (note 6)	18,830	45,788
	1,381,168	1,759,668
Deficiency in assets		
Share capital (note 8)	22,343,053	22,330,215
Warrants (note 8)	76,677	76,677
Contributed surplus (note 8)	613,819	569,452
Deficit	(22,554,893)	(22,559,823)
	478,656	416,521
	\$ 1,859,824	\$ 2,176,189

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

Approved by the Board:

Signed: "John Perreault"

Director

Signed: "Wojciech Drzazga"

Director

ZTEST Electronics Inc.**Unaudited Condensed Interim Consolidated Statements of Changes in Equity**

(Stated in Canadian Dollars)

December 31, 2013

	Share Capital	Warrants	Contributed Surplus	Deficit	Total
Balance, June 30, 2012	22,065,037	81,564	485,451	(22,708,142)	(76,090)
Exchange of Class A shares for common shares	(91,049)	-	91,049	-	-
Stock-based compensation	-	-	20,578	-	20,578
Derecognition of dividends	-	-	4,864	-	4,864
Net income for the period	-	-	-	42,125	42,125
Balance, December 31, 2012	21,973,988	81,564	601,942	(22,666,017)	(8,523)
Private placement, net of costs	157,810	-	-	-	157,810
Allocated to warrants	(37,859)	37,859	-	-	-
Stock options exercised	126,030	-	(54,030)	-	72,000
Warrants exercised	110,246	(42,746)	-	-	67,500
Stock-based compensation	-	-	21,540	-	21,540
Net income for the period	-	-	-	106,194	106,194
Balance, June 30, 2013	22,330,215	76,677	569,452	(22,559,823)	416,521
Stock options exercised	12,838	-	(5,338)	-	7,500
Stock-based compensation	-	-	49,705	-	49,705
Net income for the period	-	-	-	4,930	4,930
Balance, December 31, 2013	\$ 22,343,053	\$ 76,677	\$ 613,819	\$ (22,554,893)	\$ 478,656

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

ZTEST Electronics Inc.**Unaudited Condensed Interim Consolidated Statements of Comprehensive Income**

(Stated in Canadian Dollars)

December 31, 2013

	Three months ended		Six months ended	
	2013	2012	2013	2012
Product sales	\$ 945,951	\$ 1,113,223	\$ 2,080,201	\$ 2,185,879
Cost of product sales (note 3)	615,708	743,090	1,328,416	1,432,617
	330,243	370,133	751,785	753,262
Expenses				
Selling, general and administrative (note 13)	330,541	309,266	675,117	625,259
Stock-based compensation (note 8)	49,705	-	49,705	20,578
Interest expense - long term (note 9)	7,976	22,106	17,568	51,130
Interest expense - other	571	148	782	297
Loan guarantee fees	-	2,400	-	4,800
Depreciation of equipment	756	948	1,512	1,896
Foreign exchange (gain) loss	(5)	3,310	3,332	11,215
	389,544	338,178	748,016	715,175
(Loss) income before miscellaneous income and income taxes	(59,301)	31,955	3,769	38,087
Miscellaneous income	373	1,381	1,161	4,038
(Loss) income before provision for income taxes	(58,928)	33,336	4,930	42,125
Provision for income taxes	-	-	-	-
Comprehensive (loss) income for the period	\$ (58,928)	\$ 33,336	\$ 4,930	\$ 42,125
Comprehensive (loss) income per share				
Basic	\$ (0.01)	\$ 0.01	\$ 0.00	\$ 0.01
Fully diluted	\$ (0.01)	\$ 0.01	\$ 0.00	\$ 0.01
Weighted average shares outstanding				
Basic	10,648,696	7,161,942	10,639,729	7,121,944
Fully diluted	10,648,696	7,161,942	11,935,295	7,121,944

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

ZTEST Electronics Inc.

Unaudited Condensed Interim Consolidated Statements of Cash Flows

(Stated in Canadian Dollars)

December 31, 2013

	Three months ended		Six months ended	
	2013	2012	2013	2012
Cash flow from operating activities				
Net (loss) income for the period	\$ (58,928)	\$ 33,336	\$ 4,930	\$ 42,125
Items not involving cash				
Depreciation of equipment	31,309	38,444	62,618	75,889
Interest accretion	3,906	3,782	7,777	12,668
Share based payments	49,705	-	49,705	20,578
Debt forgiveness	-	(1,000)	-	(3,280)
Changes in non-cash working capital items:				
Accounts receivable	166,736	167,366	124,458	299,135
Inventories	72,839	57,346	126,461	51,367
Prepaid expenses and other assets	5,196	(7,830)	4,297	(11,604)
Customer deposits	(24,312)	49,848	(5,113)	105,352
Accounts payable and accrued liabilities	(112,361)	(124,179)	(172,362)	(213,161)
	134,090	217,113	202,771	380,069
Cash flow from investing activities				
Purchase of equipment	-	-	-	(1,690)
Cash flow from financing activities				
Proceeds of share issuance	-	-	7,500	-
Repayment of long-term debt	(100,370)	(81,308)	(208,802)	(172,133)
	(100,370)	(81,308)	(201,302)	(172,133)
Increase in cash and cash equivalents	33,720	135,805	1,469	206,246
Cash and cash equivalents, beginning of period	88,363	252,256	120,614	181,815
Cash and cash equivalents, end of period	\$ 122,083	\$ 388,061	\$ 122,083	\$ 388,061

Supplemental Disclosure of Cash Flow Information

During the period the Company had cash flows arising from interest and income taxes paid as follows:

Cash paid for interest	\$ 4,662	\$ 15,734	\$ 10,958	\$ 36,536
Cash paid for income taxes	\$ -	\$ -	\$ -	\$ -

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

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

1. Business of the Company

ZTEST Electronics Inc. ("the Company") amalgamated under the laws of Ontario and carries on business at 523 McNicoll Avenue, Toronto, Ontario designing, developing, and assembling printed circuit boards and other electronic equipment. The Company's shares trade on the Canadian Venture Exchange under the symbol "ZTE".

2. Significant Accounting Policies

Statement of compliance

The Company has prepared these unaudited condensed interim financial statements in accordance with IAS 34, *Interim Financial Reporting*, employing all of the same accounting policies and methods of computation, except as noted under changes in accounting policies, as disclosed in the annual financial statements as at June 30, 2013.

The notes to these unaudited condensed interim consolidated financial statements are intended to provide a description of events and transactions that are significant to an understanding to the changes in the Company's financial position and performance since June 30, 2013. Certain disclosures that appear in the annual financial statements have not been reproduced in these unaudited condensed interim consolidated financial statements and, in this regard only, these unaudited condensed interim financial statements do not conform in all respects to the requirements of IFRS for annual consolidated financial statements. Accordingly, these unaudited condensed interim consolidated financial statements should only be read in conjunction with the annual financial statements as at June 30, 2013.

These unaudited condensed interim consolidated financial statements were authorized for issuance by the Board of Directors of the Company on February 25, 2014.

Basis of presentation and going concern considerations

These unaudited condensed interim consolidated financial statements have been compiled by management on a historical cost basis using the accrual basis of accounting, except for cash flow information, and in accordance with IFRS applicable to a going concern. The Company's continuance as a going concern is dependent upon its ability to obtain adequate financing and its ability to generate positive cash flow from operations. If the going concern assumption were not appropriate for these condensed interim consolidated financial statements then adjustments would be necessary in the carrying values of assets and liabilities, the reported revenues and expenses, and the statement of financial position classifications used.

Basis of consolidation

These unaudited condensed interim consolidated financial statements include the accounts of the Company as well as the following subsidiaries' assets and liabilities and the revenues and expenses, arising subsequent to the date of acquisition:

Permatech Electronics Corporation (öPECö)	- 100% owned ⁽¹⁾
Northern Cross Minerals Inc.	- 66.7% owned (inactive)

⁽¹⁾ The Company has granted a creditor the right to acquire a 24% interest in PEC (*note 6*).

Changes in accounting policies

Each of the following was adopted July 1, 2013 without impact upon the amounts or disclosures presented in these unaudited condensed interim consolidated financial statements.

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.

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.

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

2. Significant Accounting Policies - continued

Significant accounting judgments and estimates

The preparation of these unaudited condensed interim consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. The significant estimates and judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied to the annual consolidated financial statements for the year ended June 30, 2013.

Impairment of non-financial assets

At the end of each reporting period, the Company reviews the carrying amounts of its non-financial assets with finite lives to determine whether there is any indication that those assets have suffered an impairment loss.

The Company has assessed the assets of all its operating entities and has determined that there is no impairment of its non-financial assets.

3. Inventories

The carrying value of inventory is comprised of:

	Dec. 31 2013	June 30 2013
Raw materials and supplies	\$ 492,006	\$ 592,668
Work in process	13,973	12,877
Finished goods	19	26,914
	\$ 505,998	\$ 632,459

Inventory utilization during the period was as follows:

	Dec. 31 2013	Dec. 31 2012
Raw materials and supplies used	\$ 828,620	\$ 955,329
Labour costs	356,441	363,511
Depreciation	61,106	74,993
Other costs	56,450	51,022
Net change in finished goods and work in process	25,799	(12,238)
Cost of product sales	\$ 1,328,416	\$ 1,432,617

4. Equipment

	Computer Equipment	Office Equipment	Manufacturing Equipment	Leasehold Improvements	Total
Cost:					
Balance, June 30, 2012	\$ 168,136	\$ 71,277	\$ 2,356,046	\$ 61,003	\$ 2,656,462
Additions	-	-	1,690	-	1,690
Balance, Dec. 31, 2012	168,136	71,277	2,357,736	61,003	2,658,152
Additions	1,016	-	11,317	-	12,333
Balance, June 30, 2013	169,152	\$ 71,277	\$ 2,369,053	\$ 61,003	\$ 2,670,485
Additions	-	-	-	-	-
Balance, Dec. 31, 2013	\$ 169,152	\$ 71,277	\$ 2,369,053	\$ 61,003	\$ 2,670,485

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

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December 31, 2013

4. Equipment - continued

	Computer Equipment	Office Equipment	Manufacturing Equipment	Leasehold Improvements	Total
Accumulated Depreciation:					
Balance, June 30, 2012	\$ (161,343)	\$ (65,733)	\$ (1,604,138)	\$ (61,003)	\$ (1,892,217)
Depreciation	(1,060)	(554)	(75,275)	-	(76,889)
Balance, Dec. 31, 2012	(162,403)	(66,287)	(1,679,413)	(61,003)	(1,969,106)
Depreciation	(1,130)	(555)	(76,321)	-	(78,006)
Balance, June 30, 2013	(163,533)	(66,842)	(1,755,734)	(61,003)	(2,047,112)
Depreciation	(843)	(443)	(61,332)	-	(62,618)
Balance, Dec. 31, 2013	\$ (164,376)	\$ (67,285)	\$ (1,817,066)	\$ (61,003)	\$ (2,109,730)
Carrying Amounts:					
June 30, 2012	\$ 6,793	\$ 5,544	\$ 751,908	\$ -	\$ 764,245
December 31, 2012	\$ 5,733	\$ 4,990	\$ 678,323	\$ -	\$ 689,046
June 30, 2013	\$ 5,619	\$ 4,435	\$ 613,319	\$ -	\$ 623,373
December 31, 2013	\$ 4,776	\$ 3,992	\$ 551,987	\$ -	\$ 560,755

Specific manufacturing equipment is pledged as security (*notes 4 and 5*). The carrying amount of the pledged equipment at each date is as follows:

December 31, 2013	\$ 317,242
June 30, 2013	\$ 352,492
December 31, 2012	\$ 396,553
June 30, 2012	\$ 440,614

5. Note payable

	Dec. 31 2013	June 30 2013
Note, bearing interest at 7.0%, secured by specific equipment (<i>note 4</i>), matures October 2014. Monthly principal and interest payments of \$15,438 are required until September 2014 then a final payment of \$10,346 is due at maturity.	\$ 144,735	\$ -

This note arose upon settlement of a debenture payable (*note 6*)

6. Long-Term Debt

	Dec. 31 2013	June 30 2013
Non-interest bearing debenture has matured. ⁽¹⁾	\$ 39,600	\$ 39,600
Debenture, bearing interest at 10.5%, was secured by specific equipment (<i>note 4</i>) on a pro-rata basis with another debenture and matured September 2013. The holder of this debenture was issued 233,333 common shares of the Company.	-	99,580
Debenture, bearing interest at 7.0%, was secured by specific equipment (<i>note 4</i>) on a pro-rata basis with another debenture and matured December 2013. ⁽²⁾	-	228,962
Balance forward	\$ 39,600	\$ 368,142

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

6. Long-Term Debt - continued

	Dec. 31 2013	June 30 2013
Balance forward	\$ 39,600	\$ 368,142
Term loan bearing interest at the April 30 prime lending rate plus 8%, adjusted annually and currently at 11.00%, secured by a general security agreement covering the assets of PEC, matures April 2015. The loan has a face value of \$68,106. Blended monthly principal and interest payments of \$3,692 are required until April 2014, then \$4,920 until maturity. The creditor was granted an option to acquire a 24% interest in PEC for \$200,000 on or before May 1, 2015. ⁽³⁾	66,479	83,697
Total long-term debt	106,079	451,839
Less: Current portion	87,249	406,051
	<u>\$ 18,830</u>	<u>\$ 45,788</u>
The minimum annual future principal repayments are as follows:		
2014		\$ 87,249
2015		18,830
		<u>\$ 106,079</u>

(1) The debenture has matured but no means of settlement has been reached. It is classified as current.

(2) At maturity the balance of the debenture was settled through issuance of a note payable (note 5).

(3) Payable to a corporate shareholder that is controlled by the spouse of a Director of the Company (note 9).

7. Commitments

Bank operating loan

The Company has a \$250,000 line of credit with its financial institution from which nothing was drawn as at December 31, 2013 or June 30, 2013. The loan bears interest at the prime lending rate plus 0.5%, is due upon demand, is subject to renewal May 2014, and is secured by a \$250,000 term deposit and a general security agreement covering the assets of PEC. The term deposit bears interest at 1.25% and matured January 19, 2014 at which time the principal was reinvested at 1.25% until April 19, 2014.

Operating leases

The Company leases its operating facility under a lease that is due to expire March 31, 2021. A lease deposit in the amount of \$35,000 has been paid and will be applied at the end of the lease. Minimum monthly rental payments ranging from \$7,470 to \$8,979 are required over the term of the lease as follows:

2014	\$ 89,635
2015	92,351
2016	99,594
2017	102,310
2018	105,026
Remaining	242,422
	<u>\$ 731,338</u>

8. Share Capital

(a) Authorized

Unlimited Common shares

Unlimited Non-voting, non-participating Class A special shares. All previously outstanding Class A special shares were exchanged for common shares and no additional shares may be issued.

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

8. Share Capital - continued

(a) Authorized - continued

Unlimited Preferred shares in one or more series. The following four series have been authorized to date:
Series A redeemable, voting shares were to be repurchased May 2004. ⁽¹⁾
Series B shares may no longer be issued and none remain outstanding.
Series C redeemable, voting shares were to be repurchased May 2007. ⁽¹⁾
Series D shares may no longer be issued and none remain outstanding.

⁽¹⁾ The right to vote at the meeting of common shareholders arises because the associated dividends are more than 12 months in arrears. Settlement of the repurchase price and the associated dividends payable has yet to be negotiated.

(b) Issued

	Dec. 31 2013	June 30 2013
Common shares	\$ 22,343,053	\$ 22,330,215

Common shares	Number of Shares	Amount
Balance June 30, 2012	7,062,488	\$ 21,965,037
Common shares issued in exchange for Class A shares ⁽¹⁾	91,208	8,951
Balance December 31, 2012	7,153,696	\$ 21,973,988
Private placement	2,200,000	119,951
Stock options exercised	720,000	126,030
Warrants exercised	500,000	110,246
Balance June 30, 2013	10,573,696	22,330,215
Stock options exercised	75,000	12,838
Balance December 31, 2013	10,648,696	\$ 22,343,053

⁽¹⁾ During the period ended September 30, 2012 the shareholders approved the issuance of 99,454 common shares in exchange for the 1,193,442 Class A Special Shares then outstanding. 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 8,246 common shares have been reserved and will be issued only in the event the remaining Class A shareholders identify themselves to the Company.

Preferred Shares:

	Dec. 31 2013	June 30 2013
Redemption value	\$ 665,402	\$ 665,402
Less: amount included in paid in capital	(191,647)	(191,647)
Amount included in current liabilities	\$ 473,855	\$ 473,855

(c) Details of warrants outstanding:

	Number of Warrants	Amount
Balance December 31, 2012 and June 30, 2012	1,400,000	\$ 81,564
Issued during the period	1,100,000	37,859
Exercised during the period	(500,000)	(42,746)
Balance December 31, 2013 and June 30, 2013	2,000,000	\$ 76,677

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

8. Share Capital - continued

(c) Details of warrants outstanding - continued:

	Number of Warrants	Exercise Price	Expiry Date
Issued Mar. 24, 2011	900,000	\$ 0.10	Mar. 24, 2016
Issued Feb. 4, 2013	1,100,000	\$ 0.10	Feb. 4, 2016

	Number of Warrants	Weighted Average Price per Warrant	Weighted Average Expiry Date
Beginning and end of period ⁽¹⁾	2,000,000	\$ 0.10	Feb. 26, 2016

⁽¹⁾ Subsequent to the end of financial reporting period the Company issued 400,000 warrants, to related parties, in connection with new equipment financing. Each warrant entitles the holders to acquire a common share of the Company for \$0.10 until October 31, 2017.

The following weighted average assumptions were used to calculate the fair value of the warrants issued during the period:

	Dec. 31 2013	June 30 2013
Dividend yield	None issued	Nil
Risk free interest rate (%)	None issued	1.17
Expected stock volatility (%)	None issued	107.56
Expected life (years)	None issued	3

(d) Details of options outstanding:

	Common Shares Under option	Number of Options Vested	Price/Option	Expiry Date
Granted Nov. 30, 2010	275,000 ⁽¹⁾	275,000	\$ 0.10	Nov. 30, 2015
Granted Sept. 14, 2012	130,000 ⁽¹⁾	130,000	\$ 0.10	Sept. 14, 2017
Granted March 11, 2013	200,000 ⁽¹⁾	200,000	\$ 0.15	Mar. 11, 2018
Granted December 31, 2013	600,000 ⁽¹⁾	600,000	\$ 0.10	Dec. 31, 2018

	Common Shares Under Option	Weighted Average Price/Option	Weighted Average Expiry Date
Beginning of period ⁽¹⁾	680,000	\$ 0.115	Jan. 20, 2017
Exercised during period ⁽¹⁾	(75,000)	0.100	Feb. 8, 2017
Issued during period ⁽¹⁾	600,000	\$ 0.100	Dec. 31, 2018
End of period ⁽¹⁾	1,205,000	\$ 0.108	Jan. 7, 2018

⁽¹⁾ Directors and/or Officers of the Company hold these options.

The following weighted average assumptions were used to calculate the fair value of the stock options granted during the period:

	Dec. 31 2013	June 30 2013
Dividend yield	Nil	Nil
Risk free interest rate (%)	1.93	1.34 to 1.40
Expected stock volatility (%)	119.90	106.53 to 107.26
Expected life (years)	5	5

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

(Stated in Canadian Dollars)

December 31, 2013

8. Share Capital - continued

(e) Share based payment transactions and contributed surplus

The Company has a stock option plan. The aggregate number of common shares reserved for issuance under this plan cannot exceed 20% of the aggregate number of common shares of the Company that are issued and outstanding. The Company has granted options for the purchase of common shares to employees, directors, officers and other service providers. The fair values of stock options granted have been determined using the Black-Scholes model and are added to contributed surplus as follows:

	Dec. 31 2013	June 30 2013
Contributed surplus, beginning of period	\$ 569,452	\$ 485,451
Dividends of PEC derecognized	-	4,864
Conversion of Class A shares to common shares	-	91,049
Stock based compensation	49,705	42,118
Stock options exercised	(5,338)	(54,030)
Contributed surplus, end of period	\$ 613,819	\$ 569,452

9. Related Party Transactions

In addition to key management personnel, the Company had transactions during the period and outstanding balances (*note 6*) at the end of the period with 1114377 Ontario Inc. (ō114377ō), a company controlled by the spouse of a Director of the Company.

All expenses and period end balances with related parties are at exchange amounts established and agreed to by the related parties. All transactions with related parties are in the normal course of operations and have been carried out on the same terms as those accorded to unrelated parties.

Description	Dec. 31 2013	Dec. 31 2012
Employee and consultant compensation ⁽¹⁾	\$ 164,392	\$ 162,763
Professional fees ⁽¹⁾	16,224	12,426
Interest expense ó long-term	4,933	6,492
Share issuance costs ⁽¹⁾	-	-
	\$ 185,549	\$ 181,681
Stock-based compensation ⁽¹⁾	\$ 49,705	\$ 20,578

⁽¹⁾ Transactions are with key management personnel. As at December 31, 2013 \$30,703 (June 30, 2013 - \$28,694) was payable to key management personnel and included in accounts payable and accrued liabilities.

10. Income Taxes

Unrecognized Deferred Tax Assets

Deferred income taxes are provided as a result of temporary differences that arise due to the differences between the income tax values and the carrying amount of assets and liabilities. Deferred income tax assets have not been recognized in respect of the following deductible temporary differences:

	Dec. 31 2013	June 30 2013
Share issuance costs	\$ 38,690	\$ 38,690
Intangible assets	43,280	43,280
Property, plant and equipment	300,258	237,640
Resource related expenditures	349,050	349,050
Scientific research and experimental development	1,050,618	1,050,618
Net capital loss carry forwards	2,280,030	2,280,030
Non-capital loss carry forwards	15,592,989	15,592,989

ZTEST Electronics Inc.

Notes to Unaudited Condensed Interim Consolidated Financial Statements

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December 31, 2013

10. Income Taxes - continued

Share issue costs expire from 2014 to 2017. The non-capital loss carry forwards expire from 2027 to 2032. The net capital loss carry forwards may be carried forward indefinitely, but can only be used to reduce capital gains. The remaining deductible temporary differences may be carried forward indefinitely. Deferred tax assets have not been recognized in respect of these items because it is not probable that future taxable profit will be available against which the group can utilize the benefits therefrom.

11. Financial risk factors

The Company is exposed in varying degrees to a variety of financial instrument related risks:

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 period, one of the Company's customers accounted for more than 20% (27%) of total revenue (2012 none exceeding 20%). Amounts due from this customer accounted for 4% of the Company's accounts receivable at December 31, 2013 (June 30, 2013 - 24%). The loss of this customer or significant curtailment of purchases by this customer could have a material adverse effect 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 \$95,939 (June 2013 - \$196,064). This includes financial liabilities (a specific long-term debt instrument plus preferred shares and dividends payable) with an aggregate carrying amount of \$776,792 (June 2013 - \$776,792) which are past due and for which the timing of future cash flows are undetermined. The Company manages its liquidity risk through the management of its capital (*note 12*) 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 interest rate risk and currency risk. The interest rate risk arises from two long-term debt instruments for which interest rates are fixed annually based upon prevailing market rates. Currency risk relates 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. Credit risk is minimized through the reduction of debt when cash flow permits. Currency risk is closely monitored but not actively managed. During the period the Company incurred a loss on foreign exchange in the amount of \$3,332 (Dec. 2012 of \$11,215).

Sensitivity to market risks

If interest rates are 1% higher on the next subsequent interest adjustment date the monthly payments required on long-term debt over the next twelve months will increase by \$273 representing additional interest expense.

At December 31, 2013 the Company had US\$91,221 (2012 of US\$214,010) 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 \$4,851 in future cash inflow.

At December 31, 2013 the Company had US\$106,137 (2012 of US\$105,654) 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 \$5,611 in future cash outflow.

ZTEST Electronics Inc.

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(Stated in Canadian Dollars)

December 31, 2013

11. Financial risk factors - continued

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.

12. Capital disclosures

The Company's objective when managing capital is to ensure its ability to meet operating commitments as they become due and to provide return for shareholders. This is achieved by continuously monitoring actual and projected cash flows and making adjustments to capital as necessary. Except for the repayment terms associated with long-term debt instruments, there are no externally imposed capital requirements.

Management includes the following items in its definition of capital:

	Dec. 31 2013	June 30 2013
Long-term debt ⁽¹⁾	\$ 106,079	\$ 123,297
Share Capital	22,343,053	22,330,215
Warrants	76,677	76,677
Contributed surplus	613,819	569,452
Deficit	(22,554,893)	(22,559,823)
Net capital under management	\$ 584,735	\$ 539,818

⁽¹⁾ Excludes long-term debts that are both secured by specific equipment and due to unrelated parties.

13. Selling, general and administrative expenses

Selling, general and administrative expenses are comprised of the following amounts:

	Sept 30 2013	Sept 30 2012
Employee and consultant compensation (note 9)	\$ 450,752	\$ 399,144
Occupancy costs	132,728	132,918
Professional fees (note 9)	35,574	32,366
Shareholder services	13,171	21,338
Insurance	16,320	10,591
Other	26,572	28,902
	\$ 675,117	\$ 625,259

14. Subsequent events

Subsequent to the end of the financial reporting period the Company negotiated new financing in the aggregate amount of \$200,000 to fund the acquisition of new equipment. The new term loans are payable to related parties, are unsecured, bear interest at prime plus 6%, mature October 31, 2017, and may be repaid in advance at any time without bonus or penalty. Payments as to interest only are required until October 2014 after which the debts will be repaid in equal monthly payments blended as to interest and principal. As partial consideration for advancing the proceeds of these term loans the Company has issued 400,000 warrants to the lenders. Each warrant entitles the holder to acquire a common share of the Company for \$0.10 until October 31, 2017.