ESTEC SYSTEMS CORP.

Consolidated Financial Statements
Quarters ended September 30, 2012 and 2011

NOTE: These condensed interim consolidated financial statements have been prepared by management and have **NOT** been reviewed by our external auditors

ESTEC SYSTEMS CORP.
Interim Consolidated Statements of Financial Position (Unaudited)
(Expressed in Canadian Dollars)
September 30, 2012

	Notes	September 30, 2012 ($)	June 30, 2012 ($)
ASSETS			
CURRENT			
Cash		180,902	-
Trade and other receivables	8	947,672	1,236,128
Prepaid expenses		46,346	73,808
Inventory	9	261,559	135,566
Deposit held in trust		-	-
		1,436,479	1,445,502
PROPERTY AND EQUIPMENT	10	223,296	219,892
INTANGIBLE ASSETS	11	154,215	159,689
GOODWILL	12	570,601	590,855
		948,112	970,436
TOTAL ASSETS		2,384,591	2,415,938
LIABILITIES AND EQUITY			
CURRENT			
Bank indebtedness	13	-	155,340
Trade and other payables	14	492,676	480,804
Customer deposits			59,685
Income tax payable	15	737	764
Current portion of callable debt	16	100,000	100,000
		593,413	796,593
Callable debt due after one year	16	1,266,667	1,291,667
		1,860,080	2,088,260
ADVANCES FROM RELATED PARTIES	18	489,677	489,677
TOTAL LIABILITIES		2,349,757	2,577,937
EQUITY			
Share capital	19	1,232,263	1,232,263
Contributed surplus	20	16,848	16,346
Accumulated other comprehensive income		30,343	35,683
Deficit		(1,244,620)	(1,446,291)
TOTAL EQUITY		34,834	(161,999)
TOTAL LIABILITIES AND EQUITY		2,384,591	2,415,938

Approved on behalf of the Board

_________________________ Director _________________________ Director

ESTEC SYSTEMS CORP.
Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income
(Unaudited)
(Expressed in Canadian Dollars)
September 30, 2012 and 2011

	Notes	Three months ended September 30, 2012 ($)	Three months ended September 30, 2011 ($)
CONTINUING OPERATIONS			
REVENUE		1,382,493	958,939
DIRECT EXPENSES		535,005	127,511
		847,488	831,428
EXPENSES			
Selling, general and administrative expenses (Schedule 1)		578,869	839,497
Interest on callable debt		15,690	-
Amortization		11,643	12,372
Loss on disposal of property and equipment		2,015	406
		608,217	852,275
		239,271	(20,847)
OTHER INCOME (EXPENSE)			
Transaction closing costs		-	(13,164)
Unrealized foreign exchange		(39,430)	14,933
Realized foreign exchange		3,696	-
INCOME BEFORE TAX		203,537	(19,078)
Income tax expense		1,865	18,047
NET (LOSS) INCOME		201,672	(37,125)
CHANGES IN COMPREHENSIVE INCOME			
Foreign currency translation (loss) / gain		(5,340)	24,672
COMPREHENSIVE INCOME (LOSS)		196,332	(12,453)
BASIC AND DILUTED INCOME PER SHARE	21	.02	(0)
WEIGHTED AVERAGE NUMBER OF SHARES		10,461,629	10,461,629

ESTEC SYSTEMS CORP.
Condensed Interim Consolidated Statements of Equity (Unaudited)
(Expressed in Canadian Dollars)
September 30, 2012 and 2011

	Share capital ($)	Contributed surplus ($)	Accumulated other comprehensive income ($)	Deficit ($)	Total ($)
As at June 30, 2011	1,232,263	15,844	18,767	(1,627,328)	(360,454)
Stock based compensation expense	-	502	-	-	502
Income and comprehensive income for the period	-	-	24,672	(37,125)	(12,453)
As at September 30, 2011	1,232,263	16,346	43,439	(1,664,453)	(372,405)
As at June 30, 2012	1,232,263	16,346	35,683	(1,446,291)	(161,999)
Stock based compensation expense	-	502			502
Loss and comprehensive income for the period	-	-	(5,340)	201,672	196,332
As at September 30, 2012	1,232,263	16,848	30,343	(1,244,619)	34,835

ESTEC SYSTEMS CORP.
Condensed Interim Consolidated Statements of Cash Flow (Unaudited)
(Expressed in Canadian Dollars)
September 30, 2012 and 2011

	Three months ended Sept 30, 2012	Three months ended Sept 30, 2011
	($)	($)
OPERATING ACTIVITIES		
Net (loss) income	201,672	(37,125)
Items not affecting cash:		
Amortization	11,643	12,372
Loss on disposal of property and equipment	2,015	406
Foreign exchange	(5,340)	24,672
Stock-based compensation	502	502
	210,492	827
Change in non-cash working capital	146,452	162,372
Cash flow from (used by) operating activities	356,944	163,199
INVESTING ACTIVITIES		
Purchase of property and equipment	(20,702)	(25,000)
Cash flow used by investing activities	(20,702)	(25,000)
FINANCING ACTIVITIES		
Advances (to) from related parties	-	(7,876)
Cash flow from financing activities	-	(7,876)
INCREASE (DECREASE) IN CASH	336,242	130,323
Bank indebtedness – Beginning of period	(155,340)	(143,154)
Cash – End of period	180,902	(12,831)

1. DESCRIPTION OF BUSINESS

ESTec Systems Corp. (the "Company") is the manager of two entirely owned companies: a forensic and design engineering company, Allan R. Nelson Engineering (1997) Inc., and an electronics manufacturing company, Encore Electronics Inc.

Allan R. Nelson Engineering Inc. (ARN) is made up of a group of highly educated engineers and technologists with different skills and backgrounds. ARN provides engineering services such as design engineering, failure analysis, inspection and certification of equipment, equipment appraisals, accident investigations, maintenance engineering, capital project commissioning, expert witness testimony and product development. This company also delivers engineering services to all major insurance companies throughout Canada and has a focus toward damage from petrochemicals, manufacturing and drilling accidents. ARN operates in many industries such as oil and gas, petrochemical, mining, construction, forestry, power and utilities, manufacturing and transportation industries.

Encore Electronics Inc. (Encore) is a manufacturing and design company whose products are used in a wide variety of engineering and technology industries. Such products include: signal conditioners, custom power supplies, computer controlled amplifiers and computer controlled signal conditioning instrumentation. Encore has its own product line and manufactures products specific to customer needs. Encore's products and services are used in many industries, some of which include: aircraft engines, automotive and turbine testing, product design, research and development, power generation and aerospace and electronics.

The Company was incorporated under the Business Corporations Act of Alberta and is traded on the TSX Venture Exchange. The address of its registered head office is #209, 17510 – 102 Avenue NW, Edmonton, Alberta, T5S 1K2, Canada.

2. BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE

The interim consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Accounting Standards ("IAS") 34, Interim Financial Reporting, as issued by the International Accounting Standards Board ("IASB"). They should be read in conjunction with the Company's consolidated financial statements and related notes included in the Company's Financial Information contained in its audited consolidated financial statements for the year ended June 30, 2012.

2. BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE *(continued)*

The consolidated financial statements have been prepared on a historical cost basis, except for certain financial assets and liabilities which are stated at fair value. The consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. Management has determined that the functional currency of Encore is the US dollar and that the presentation currency will be the Canadian dollar.

These consolidated financial statements include the accounts of the Company and its subsidiaries as follows:

- Allan R. Nelson Engineering (1997) Inc.
- Encore Electronics Inc.

All significant intercompany transactions and balances have been eliminated upon consolidation.

These consolidated interim financial statements of the Company for the three month period ended September 30, 2012 were authorized for issue by the Board of Directors in accordance with a resolution of the Company on **November 28, 2012**.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following are the significant accounting policies applied by the Company in preparing its consolidated financial statements:

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value, including liabilities for cash-settled share-based payment arrangements.

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. Subsidiaries are all entities over which the Company has control, where control is defined as the power to govern financial and operating policies. The Company has a shareholding of 100% of the voting rights in its subsidiaries. Subsidiaries are fully consolidated from the date control is transferred to the Company, and are no longer consolidated on the date control ceases.

Intercompany transactions, balances, income and expenses, and gains or losses on transactions are eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the accounting policies adopted by the Company.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial instruments

The Company classifies its financial assets and liabilities into one of the following categories, depending on the purpose for which the financial instrument was acquired. The Company's accounting policy for each category is as follows:
Financial assets and financial liabilities at fair value through profit or loss (FVTPL)

Financial assets and financial liabilities classified as FVTPL are acquired or incurred principally for the purpose of selling or repurchasing them in the near term. They are recognized at fair value based on market prices, with any resulting gains and losses reflected in profit and loss for the period in which they arise.

Held-to-maturity financial assets

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and a fixed maturity which an entity has the intention and ability to hold to maturity. They are measured at amortized cost using the effective interest rate method less any impairment loss. A gain or loss is recognized in profit and loss when the financial asset is derecognized or impaired, and through the amortization process. The Company did not have any held-to-maturity investments during the three month period ended September 30, 2012.

Loans and receivables

Loans and receivables are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They are initially recognized at fair value plus transaction costs that are directly attributable to their acquisition or issue and subsequently carried at amortized cost, using the effective interest rate method, less any impairment losses. Amortized cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognized in profit or loss when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables and other financial liabilities are measured at amortized cost, using the effective interest rate method less any impairment loss.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Available-for-sale financial investments

Non-derivative financial assets that do not meet the definition of loans and receivables or FVTPL are classified as available-for-sale and comprise principally the Company's strategic investments in entities not qualifying as subsidiaries or associates. Available-for-sale investments are carried at fair value with changes in fair value recognized in other comprehensive loss/income. Where there is a significant or prolonged decline in the fair value of an available-for-sale financial asset (which constitutes objective evidence of impairment), the full amount of the impairment, including any amount previously recognized in other comprehensive loss/income, is recognized in profit or loss. If there is no quoted market price in an active market and fair value cannot be readily determined, available-for-sale investments are carried at cost.

On sale or impairment, the cumulative amount recognized in other comprehensive loss/income is reclassified from accumulated other comprehensive loss/income to profit or loss.

Impairment of financial assets

At each reporting date the Company assesses whether there is any objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is deemed to be impaired, if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset and that event has an impact on the estimated future cash flows of the financial asset or group of financial assets.

The Company does not use any derivative or hedging instruments.

The Company did not have any available-for-sale financial investments during the three month period ended September 30, 2012.

Financial liabilities

Financial liabilities are classified as other financial liabilities of FVTPL, based on the purpose for which the liability was incurred. The Company’s liabilities comprised bank indebtedness, trade and other payables, callable debt and advances to related parties, all of which are classified as other financial liabilities. These liabilities are initially recognized at fair value net of any transaction costs directly attributable to the issuance of the instrument and subsequently carried at amortized cost using the effective interest rate method. This ensures that nay interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the statement of financial position. Interest expense in this context includes initial transaction costs and premiums payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Trade and other payables represent liabilities for goods and services provided to the Company prior to the end of the year which are unpaid.

The Company classified its financial instruments as follows:

- Trade and other receivables are classified as loans and receivables;
- Bank indebtedness and callable debt are classified as FVTPL;
- Trade and other payables are classified as other financial liabilities;
- Advances from related parties are classified as other financial liabilities.

Revenue recognition

ARN: The Company derives revenue from both consulting and engineering contracts. The Company recognizes such revenue when services are provided, in the amount stated in the contract with the customer and when there is reasonable assurance that collection will occur. On the occasion that customers make deposits in advance, the revenue will not be recorded until the related service has been performed.

Encore: When products are sold, revenue is recognized when the title of ownership is passed to the customer and when there is reasonable assurance that collection will occur. This generally corresponds to the shipment of such goods.

Foreign currency translation

Transactions in foreign currencies are initially recorded by the Company's entities at the functional currency rates prevailing at the date of the transaction. Assets and liabilities, including non-monetary assets and liabilities, denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling at the reporting date.

All differences are taken to the income statement with the exception of all monetary items that form part of a net investment in a foreign operation. These are recognized in other comprehensive income until the disposal of the net investment, at which time they are reclassified to profit or loss. Tax charges and credits attributable to exchange differences on those monetary items are also recorded in other comprehensive income.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Foreign operations and goodwill

Management has determined that the functional currency of Encore Electronics Inc. is the US dollar. Since the functional currency is different from the presentation currency, which is the Canadian dollar, the results and financial position of foreign operations are translated into the presentation currency as follows:

- Assets and liabilities for each balance sheet presented are translated at the closing rate prevailing at the balance sheet date;

- Income and expenses for each income statement are translated at average exchange rates for the year, which approximates the exchange rates at the dates of the transactions; and

- All resulting exchange differences are taken to the foreign currency translation reserve within equity.

The goodwill which arose from the acquisition of Encore Electronics Inc. in fiscal 2011 is treated as an asset of the foreign operation and as such is translated at the closing rate.

Business combinations and goodwill

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the Company elects whether it measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

When the Company acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree. If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognized at fair value at the acquisition date. Subsequent changes in the fair value of the contingent consideration which is deemed to be an asset or liability will be recognized in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it will not be remeasured.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Subsequent settlement is accounted for within equity. In instances where the contingent consideration does not fall within the scope of IAS 39, it is measured in accordance with the appropriate IFRS. Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognized for non-controlling interest over the net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the subsidiary acquired, the difference is recognized in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

<u>Taxes</u>

Current income taxes

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 in the countries where the Company operates and generates taxable income.

Current income tax relating to items recognized directly in equity is recognized in equity and not in the income statement. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred income tax

Deferred tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the statement of financial position. Deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted at the end of the reporting periods and which are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Deferred tax liabilities

- are generally recognized for all taxable temporary differences, and

- are not recognized on temporary differences that arise from goodwill which is not deductible for tax purposes.

Deferred tax assets

- are recognized to the extend it is probably that taxable profits will be available against which the deductible temporary differences can be utilized; and

- Are reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are not recognized in respect of temporary differences that arise on initial recognition of assets and liabilities acquired other than in a business combination.

Sales tax

Revenues, expenses, assets and liabilities are recognized net of the amount of sales tax, except:

- Where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable

- Receivables and payables are stated with the amount of sales tax included

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

<u>Trade and other receivables</u>

Trade and other receivables are amounts due from customers, financial institutions and suppliers from providing services or sale of goods in the ordinary course of business. Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

payments (more than 30 days overdue) are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in the income statement within operating expenses.

When a trade and other receivable is uncollectible, it is written off against the allowance account for trade and other receivables. Subsequent recoveries of amounts previously written off are credited against operating expenses in the income statement.

Inventory

Inventory is measured at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. Inventory includes all costs to purchase, convert, and bring the inventories to their present location and condition.

- The Company's inventory of raw materials is recorded at the lower of cost and net realizable value

- Work-in-process and finished goods are valued at the lower of cost (including overhead) and net realizable value [less normal profit margin]. Cost is determined by the first-in, first-out method

- For manufactured inventories and work in progress, cost includes direct materials and where applicable, direct labour costs and overheads incurred in bringing the inventories to their present location and condition. Overheads are applied on the basis of normal operating capacity.

Any write-down or loss of inventory is recognized as an expense in the year it is incurred. Inventory write-downs are reversed when the net realizable value of inventories increases subsequent to the initial write-down. The amount of the reversal of a write-down of inventories is limited to the original amount of the write-down.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Property and equipment

Property and equipment is stated at cost or deemed cost less accumulated amortization. Property and equipment are amortized over their estimated useful lives on a declining-balance method at the following rates:

Equipment	20%
Computer software	30%
Office equipment	20%
Computer hardware	20%
Inspection equipment	20%

The Company regularly reviews its property and equipment to eliminate obsolete items. Amortization is calculated at half the normal rate in the year of acquisition.

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less accumulated amortization and accumulated impairment losses, if any. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is reflected in the income statement in the year in which the expenditure is incurred.

The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortized over their useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the income statement in the expense category consistent with the function of the intangible assets.

Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the income statement when the asset is derecognized.

<u>Impairment</u>

Impairments are recorded when the recoverable amount of assets are less than their carrying amounts. The recoverable amount is the higher of an asset's fair value less cost to sell or its value in use. Impairment losses other than those relating to goodwill, are evaluated for potential reversals of impairment when events or changes in circumstances warrant such consideration.

a) Non-financial assets

The carrying values of non-financial assets with finite lives, such as property and equipment are assessed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows.

b) Intangible assets and goodwill

The carrying values of all intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Additionally, the carrying values of identifiable intangible assets with indefinite lives and goodwill are tested annually for impairment.

- Intangible assets with indefinite lives are subject to an annual impairment assessment. For purposes of impairment testing, the fair value of the intangible assets are determined using a combination of a discounted cash flow approach and earnings multiple approach.

- For the purpose of impairment testing, goodwill is allocated to cash-generating units ("CGU") based on the level at which management monitors it, which is not higher than an operating segment. Goodwill is allocated to those CGU's that are expected to benefit from the business combination in which the goodwill arose.

<u>Bank indebtedness and callable debt</u>

The Company's bank indebtedness and callable debt are classified as current liabilities because the lender has the right to demand repayment within one year.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Trade and other payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business. Trade payables are recognized initially at fair value and subsequently measured at amortized cost, and are classified as current liabilities if payment is due within one year or less.

Provisions

Provisions represent liabilities to the Company for which the amount or timing is uncertain. Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are not recognized for future operating losses. Provisions are measured at the present value of the expected expenditures to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in provision due to passage of time is recognized as interest expense.

Leases

Leases are classified as either operating or finance, based on the substance of the transaction at inception of the lease. Classification is re-assessed if the terms of the lease are changed.

a) Finance lease

Leases in which substantially all the risks and rewards of ownership are transferred to the Company are classified as finance leases. Assets meeting finance lease criteria are capitalized at the lower of the present value of the related lease payments or the fair value of the leased asset at the inception of the lease. Minimum lease payments are apportioned between the finance charge and the liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

b) Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments under an operating lease (net of any incentives received from the lessor) are recognized in the income statement on a straight-line basis over the period of the lease.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Comprehensive income

Comprehensive income consists of net earnings and other comprehensive income (OCI). OCI represents changes in shareholders' equity during a period arising from transactions and other events and circumstances from non-owner sources and includes unrealized gains and losses on financial assets classified as available for sale and changes in the fair value of the effective portion of cash flow hedging instruments.

Earnings per share

The income (loss) per share calculation is based on the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated using the treasury stock method to determine the dilutive effect from the exercise of stock options. This assumes that any proceeds received from in-the-money options would be used to buy back common shares at the average market price during the year. When the results of calculating diluted earnings per share are anti-dilutive, they are excluded from the dilutive calculation. Refer to Note 20 for the calculation of the earnings per share for the period ended September 30, 2012.

Statement of Cash Flow

The Company is using the indirect method in its presentation of the Statement of Cash Flow.

Share-based payment transactions

The Company has a Stock Purchase Option Plan under which options may be granted to directors, officers, key employees.

Management estimates the fair value of the stock options granted. The grant date fair value of awards granted to directors, officers and employees pursuant to the Stock Option Plan is recognized as an employee expense, with a corresponding increase in contributing surplus, over the period that the employee unconditionally become entitled to the awards (vesting period). The fair value is amortized over the vesting period when options do not vest immediately. Management estimates the fair value of the options issued each year, if applicable, using the Black-Scholes option pricing model.

When the options are exercised, the proceeds together with the amount recorded in contributed surplus are recorded in share capital.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Significant accounting judgments, estimates and assumptions

The preparation of the Company's consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

Judgments

In the process of applying the Company's accounting policies, management has made the following judgments, which have the most significant effect on the amounts recognized in the consolidated financial statements:

Estimates and assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below. The Company based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

Impairment of non-financial assets

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Company is not yet committed to or significant future investments that will enhance the asset's performance of the cash generating unit being tested. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash-inflows and the growth rate used for extrapolation purposes.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Share-based payment transactions

The Company measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires the determination of the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating fair value for share-based payment transactions are disclosed in Note 16.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations, changes in tax laws, and the amount and timing of future taxable income. Given the wide range of international business relationships and the long-term nature and complexity of existing contractual agreements, differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expense already recorded. The Company establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities of the respective counties in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority.

Such differences of interpretation may arise on a wide variety of issues depending on the conditions prevailing in the respective Company's domicile. As the Company assesses the probability for litigation and subsequent cash outflow with respect to taxes as remote, no contingent liability has been recognized.

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

Fair value of financial instruments

Where the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, their fair value is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible.

(Expressed in Canadian Dollars)

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments (Note 21).

Development costs

Development costs are capitalized in accordance with the accounting policy. Initial capitalization of costs is based on management's judgment that technological and economic feasibility is confirmed, usually when a product development project has reached a defined milestone according to an established project management model. In determining the amounts to be capitalized, management makes assumptions regarding the expected future cash generation of the project, discount rates to be applied and the expected period of benefits.

4. TRADE AND OTHER RECEIVABLES

	September 30, 2012	June 30, 2012
	($)	($)
Trade receivables	952,082	1,240,538
Allowance for doubtful accounts	(4,410)	(4,410)
Balance, end of period	947,672	1,236,128

		Past due but not impaired			
	Total	< 30 days	30-60 days	60-90 days	> 90 days
	($)	($)	($)	($)	($)
September 30, 2012	952,082	625,040	50,051	164,903	112,088
June 30, 2012	1,240,538	706,973	149,396	278,759	105,410

(Expressed in Canadian Dollars)

5. INVENTORY

	September 30, 2012	June 30, 2012
	($)	($)
Raw Materials	27,790	24,223
Work in progress*	178,432	47,601
Finished goods	58,519	61,485
Change in foreign exchange rates	(3,182)	2,257
	261,559	135,566

*Work in progress contains $75,360 from Allan R. Nelson Engineering, all other amounts belong to Encore's inventory.

The Company measures inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the normal practice of business, less any estimated costs required to complete and make the sale. Inventory costs include all amounts required to purchase and transform an item to its final state and transfer to its final location. Inventory that is slow moving or obsolete will be put to an inventory valuation reserve. During the period, write-downs of inventories totaled $nil (June 30, 2012 - $nil) and there were no reversals of previous write-downs.

(Expressed in Canadian Dollars)

6. PROPERTY AND EQUIPMENT

	June 30, 2012 Cost	Additions	Disposals	Sept 30, 2012 Cost
	($)	($)	($)	($)
Equipment	133,731	-	-	133,731
Computer software	167,988	-	-	167,988
Computer hardware	64,200	2,686	2,287	64,599
Equipment	55,912	-	-	55,912
Office equipment	31,171	18,016	8,950	40,237
Inspection equipment	7,949	-	-	7,949
Change in foreign exchange	2,421	(4,668)	-	(2,247)
	463,372	16,034	11,237	468,169

	June 30, 2011 Accumulated amortization	Amortization expense	Disposals	Sept 30, 2012 Accumulated amortization
	($)	($)	($)	($)
Equipment	27,894	4,648	-	32,542
Computer software	116,207	3,911	-	120,118
Computer hardware	33,392	1,493	970	33,915
Equipment	36,933	949	-	37,882
Office equipment	21,508	622	8,252	13,878
Inspection equipment	7,041	45	-	7,086
Change in foreign exchange	505	(1,052)	-	(547)
	243,480	10,616	9,222	244,874

	Sept 30, 2012 Net book value	June 30, 2012 Net book value
	($)	($)
Equipment	101,189	105,837
Computer software	47,870	51,780
Computer hardware	30,684	30,808
Equipment	18,030	18,979
Office equipment	26,359	9,664
Inspection equipment	863	908
Change in foreign exchange	(1,699)	1,916
	223,296	219,892

(Expressed in Canadian Dollars)

7. INTANGIBLE ASSETS

	July 1, 2012 Balance	Addition	Amortization/ Write-off	Sept. 30, 2012 Total
	($)		($)	($)
Intellectual property	104,850	-	-	104,850
Customer list	30,000	-	-	30,000
ISO manual	22,000	-	-	22,000
Change in foreign exchange	2,839	(5,474)	-	(2,635)
At September 30, 2012	159,689	(5,474)	-	154,215

	July 1, 2011 Balance	Addition	Amortization/ Write-off	June 30, 2012 Total
	($)		($)	($)
Intellectual property	104,850	-	-	104,850
Customer list	30,000	-	-	30,000
ISO manual	22,000	-	-	22,000
Change in foreign exchange	(5,599)	8,438	-	2,839
At September 30, 2011	151,251	8,438	-	159,689

8. GOODWILL

	September 30,2012	June 30, 2012
Goodwill, beginning of year	$ 590,855	$ 559,632
Change in foreign exchange rate	(20,254)	31,223
	$ 570,601	$ 590,855

The goodwill arose from the acquisition of Encore Electronics Inc. in fiscal 2011. Any goodwill arising on the acquisition of a foreign operation is treated as an asset of the foreign operation. As a result, it is translated at the year-end rate.

9. IMPAIRMENT TESTING OF GOODWILL AND INTANGIBLE ASSETS

Goodwill acquired through business combinations has been allocated to one cash-generating unit, which is also an operating and reportable segment, with a net loss, for the year ended June 30, 2012, of $257,351 attributable to Encore. The Company performed its annual impairment test as at June 30, 2012. The Company considered the relationship between its market capitalization, and its book value among other factors, when reviewing for indicators of impairment.

The fair value of Encore has been determined based on cash flow projections from financial budgets approved by senior management covering a five-year period. The pre-tax discount rate applied to cash flow projection ranges between 14.30% and 16.70% and cash flow beyond five-year period are extrapolated using a 3% growth rate, which management believes is consistent with inflationary expectations. As a result of this analysis, management did not identify an impairment for goodwill and intangible assets.

Key Assumptions

The calculation of value in use for Encore is most sensitive to the following assumptions:

a. *Gross margin* – Gross margin are based on average values achieved in recent periods, which are reflected in the Company's budget. The Company believes gross margin will be relatively consistent in the future and accordingly, no changes have been reflected in cash flows over the projected periods.

b. *Discount rate* – Discount rate represent the current market assessment of the risks specific to each cash-generating unit, regarding the time value of money and individual risks of the underlying assets that have not been incorporated into the cash flow estimates. The discount rate calculation is based on the specific circumstances of the Company and its operating segments and is derived from the weighted average cost of capital ("WACC") of relevant market participants. The WACC takes into account both debt and equity.

c. *Growth rates estimates* – Rate are based on expectations by management considering the industry and locations in which the Company operates.

(Expressed in Canadian Dollars)

10. BANK INDEBTEDNESS

Bank indebtedness is comprised of the following:

	Sept 30, 2012	June 30, 2011
	($)	($)
Cash in bank	499,325	205,949
Outstanding cheques	(72,623)	(106,764)
Net cash (deficit)	426,702	99,185
Bank operating line	(245,800)	(254,525)
Cash	180,902	(155,340)

ARN and ESTec: The bank revolving demand facility is authorized to a total of $250,000 with interest payable at prime plus 1.50%. At September 30, 2012 $nil was outstanding on this credit facility. A general security agreement and limited guarantees from directors and related parties in the amounts of $200,000 have been pledged as collateral for the bank operating line.

Encore: The bank revolving demand facility is authorized to a total of $500,000 USD with interest payable at prime less .50%. At September 30, 2012 $250,000 was outstanding on this credit facility. This line of credit is secured by a letter of credit provided by Export Development Canada.

11. TRADE AND OTHER PAYABLES

			Past due		
	Total	< 30 days	30-60 days	60-90 days	> 90 days
	($)	($)	($)	($)	($)
September 30, 2012	273,693	148,944	116,950	2,709	5,090
June 30, 2012	223,884	159,952	45,058	16,251	2,623

(Expressed in Canadian Dollars)

11. TRADE AND OTHER PAYABLES *(continued)*

	September 30, 2012	June 30, 2012
Trade payables	273,693	223,884
Other payables		
Accrued liabilities	61,513	62,143
Payroll payable	50,834	27,485
Vacation payable	79,174	129,456
GST payable	27,462	37,836
	492,676	480,804

Terms and conditions of the above financial liabilities:

- Trade payables are non-interest bearing and are normally settled on 60-day terms
- Other payables are non-interest bearing and have an average term of six months

12. CALLABLE DEBT

	September 30, 2012	June 30, 2012
Demand loan bearing interest at prime plus 1.50% per annum, repayable in monthly payments of $8,333 plus interest. The loan matures on May 3, 2026 and is secured with a general security agreement constituting a first ranking interest in all personal property, guarantees, and postponement of claims by related parties and directors.	1,366,667	1,391,667
Principal due in one year	(75,000)	100,000)
	1,291,667	1,291,667

Principal repayment terms are approximately:

Less than one year	75,000
Later than one year and not later than five years	500,000
Later than five years	791,667
	1,366,667

(Expressed in Canadian Dollars)

13. RELATED PARTIES

During the period, the Company had business transactions with corporations controlled by certain directors of the Company. These transactions, which were in the normal course of operations and measured at the exchange value agreed between the parties, are as follows:

	Sept 30, 2012	June 30, 2012
Advances from related parties:		
Advances from directors, non-interest bearing,unsecured	$ 166,911	$ 166,911
Advances from corporations controlled by directors, non-interest bearing, unsecured	322,766	322,766
	$ 489,677	$ 489,677
Companies controlled by certain directors:		
Rent expense	$ 40,050	$ 158,305

Advances from related parties have no fixed terms of repayment and the parties have waived their right to receive any repayment in the current year, therefore these amounts have been classified as long term.

14. SHARE CAPITAL

Authorized:
200,000,000 Common shares without par value

Issued and outstanding

	September 30, 2012		June 30, 2012	
	Shares	Stated Capital	Shares	Stated Capital
Balance – beginning of year				
Issued or repurchased	10,461,629	1,232,363	10,461,629	1,232,363
Shares outstanding at the end of period	10,461,629	1,232,363	10,461,629	1,232,363

(Expressed in Canadian Dollars)

15. LEASE COMMITMENTS

The Company has operating lease commitment relating to office space in the United States. The agreement requires the Company to make the following lease payments on a fiscal year basis:

Not later than one year	$61,920
Later than one year and not later than five years	$219,828
	$281,748

16. STOCK-BASED COMPENSATION PLAN

The Company has a stock option plan that provides for the issuance of stock options to employees, directors and officers. Stock options allow the holder to obtain one common share for each stock option exercised. Options granted to Directors vest immediately. Options granted to employees vest over a 4-year period, with 25% of options vesting on each anniversary of the date the options were granted. Outstanding stock options will expire over a period ending no later than July 24, 2014. The Company has reserved 1,046,162 shares in Treasury to meet share options outstanding, less options already issued.

The Company makes options available to all employees, directors, officers in tiered levels based on salary compensation and performance. As options expire or are exercised, new options are issued.

	September 30, 2012		June 30, 2012	
	Number	Weighted average exercise price	Number	Weighted average exercise price
Outstanding beginning of period	560,000	0.10	560,000	0.10
Expired	-	-	-	-
Outstanding at end of period	560,000	0.10	560,000	0.10

At the end of the period ended September 30, 2012 there were 560,000 options, with an exercise price of $0.10 and weighted average remaining contractual life of .99 years, outstanding.

(Expressed in Canadian Dollars)

17. SEGMENTED INFORMATION

The Company operates in two distinct business segments. Segmented information is as follows:

	September 30, 2012		
	Engineering	Electronics	Total
Revenue	650,453	732,040	1,382,493
Direct expenses	168,817	366,188	535,005
Expenses	314,364	280,195	594,559
Amortization	7,019	4,624	11,643
Loss on disposal of property and equipment	2,015	-	2,015
Income (loss) from operations	158,238	81,033	239,271
Other income (expenses)	(35,734)	-	(35,734)
Income (loss) before income taxes	122,504	81,033	203,537
Income tax expense	-	1,865	1,865
Net income (loss)	122,504	79,168	201,672
Identifiable assets	902,126	1,478,098	2,380,224

	June 30, 2012		
	Engineering	Electronics	Total
Revenue	2,722,196	2,391,052	5,113,248
Direct expenses	816,915	1,198,470	2,015,385
Expenses	1,771,078	1,010,523	2,781,601
Amortization	31,060	25,852	56,912
Loss on disposal of property and equipment	1,720	-	1,720
Income (loss) from operations	101,423	156,207	257,630
Other income (expenses)	336,965	(412,815)	(75,850)
Income (loss) before income taxes	438,388	(256,608)	181,780
Income taxes	-	(743)	(743)
Net income (loss)	438,388	(257,351)	181,037
Identifiable assets	815,243	1,601,412	2,416,655

(Expressed in Canadian Dollars)

18. INCOME TAX

The income tax provision recorded differs from the amount which would be obtained by applying the statutory income tax rate of 25.00% (2011 – 27.25%) to the income for the year as follows:

	September 30, 2012	June 30, 2012
	($)	($)
Income before income tax	203,537	181,780
Income tax expense at the combined basic federal and provincial tax rate:	50,884	45,445
Non-deductible expense	-	(5,637)
Non-capital loss carried forward	-	57,874
Non-capital losses applied in current year	(49,019)	(97,682)
	1,865	-
Current	1,865	-
Deferred	-	-
Income taxes	1,865	-

(Expressed in Canadian Dollars)

19. PENSION PLAN

The pension plans are defined contribution (money purchase) plans, funded wholly by contributions. Pensions cost relates to current employee services and are charged to operation on a current basis.

Allan R. Nelson Engineering (1997) Inc./ ESTec Systems Corp.	September 30, 2012	June 30, 2012
	($)	($)
Employer contributions expensed during the current period	12,913	39,036
Estimated value of plan	215,602	195,848
Number of participants	17	16

Encore Electronics Inc.	September 30, 2012	June 30, 2012
	($)	($)
Employer contributions expensed during the current period	7,706	34,709
Estimated value of plan	266,590	247,253
Number of participants	22	22

Encore Electronics previously had a profit sharing plan. During the year ended June 30, 2012 they started a 401k pension plan and rolled the assets from the profit sharing into the pension plan.

(Expressed in Canadian Dollars)

20. EARNINGS PER SHARE

Basic earnings per share amounts are calculated by dividing net profit (loss) for the year attributable to common shareholders by the weighted average number of common shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit (loss) attributable to common shareholders by the weighted average number of common shares outstanding during the year plus the weighted average number of common shares that would be issued on conversion of all the dilutive potential common shares into common shares.

The following reflects the income and share data used in the basic and diluted earnings per share computations:

	September 30, 2012	June 30, 2012
Net income (loss)	$ 201,672	$ 181,037
Weighted average number of common shares outstanding during the period	10,461,629	10,461,629
Basic earnings per share	0.02	0.02
Common shares and stock options	11,021,629	10,461,629
Diluted earnings per share	0.02	0.02

(Expressed in Canadian Dollars)

21. FINANCIAL INSTRUMENTS

The Company's financial instruments consist of bank indebtedness, trade and other receivables, trade and other payables, callable debt, and advances from related parties.

	Sept. 2012		June 30, 2012	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value
Loans and Receivables				
Cash	**180,902**	**180,902**	-	-
Trade and other receivables	**947,672**	**947,672**	1,236,128	1,231,615
Financial Liabilities				
Bank indebtedness	**-**	**-**	155,340	155,340
Trade and other payables	**492,676**	**492,676**	480,804	480,804
Callable debt	**1,366,667**	**1,366,667**	1,391,667	1,391,667

Fair value

The advances from related parties are financial liabilities of the Company. The fair value of these amounts are less than the carrying value, as the amounts are non-interest bearing. As the amounts have no terms of repayment, the fair value cannot be calculated with any degree of certainty.

The fair value of callable debt is determined using the present value of future cash flows under current financing agreements, based on interest rates that are consistent with the current rates offered to the Company for debt with similar terms.

The fair value of bank indebtedness is measured under level 1 of the fair value hierarchy. The three levels of the fair value hierarchy are described as follows:

Level 1: Values based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability

Level 3: Value based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

21. FINANCIAL INSTRUMENTS *(continued)*

Risk Management Policy

The Company is exposed to market risk, credit risk, interest risk, liquidity risk and currency risk.

The Company's senior management oversees the management of these risks. The Board of Directors reviews and approves policies for managing each of these risks which are summarized below.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk can be heightened from exposure to a single customer or to several customers that have similar qualities and characteristics. The Company continuously evaluates the financial condition and credit worthiness of all customers and potential customers in order to lessen such risk. In the event that losses do occur, all impairments are recognized in the income statement in finance costs. The Company is subject to credit risk, having 16% in trade and other receivables from its largest customer as at September 30, 2012.

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market prices comprise four types of risk: interest rate risk, currency risk, commodity price risk and other price risk.

The Company does not currently have any significant direct exposure to commodity price risk or other price risk. Management believes the risk faced by the Company with regard to market risk is an acceptable risk faced in the ordinary course of business.

General economic conditions globally, including the relative strength of the Canadian dollar may adversely affect the value of the Company's business and the value of its financial instruments.

Currency risk

Currency risk is the risk to the Company's earnings that arise from fluctuations of foreign exchange rates and the degree of volatility of these rates. The Company is exposed to foreign currency exchange risk on bank indebtedness, trade and other receivables and trade and other payables held in US dollars. The Company does not use derivative instruments to reduce its exposure to foreign currency risk.

(Expressed in Canadian Dollars)

21. FINANCIAL INSTRUMENTS *(continued)*

At September 30, 2012 the Company's exposure to foreign currency risk are as follows:

	September 30, 2012	June 30, 2012
Reporting Rate ($US - $CAD)	**.9832**	1.018
	$US	
Cash and cash equivalents	**370,789**	84,712
Trade and other receivables	**352,732**	589,696
Trade and other payables	**225,523**	209,662

For each % change in rate, based on the monetary assets and liabilities held at year end, the Company's net earnings would be impacted by approximately $9,331 (June 2012 - $4,732).

Interest rate risk

Interest rate risk is an issue, whereby financial instrument values can be unfavorably affected by fluctuations in interest rates. The Company does not enter into derivative financing contracts. The Company is exposed to such risk because of its floating interest rate operating line and floating interest rate callable debt. Such fluctuations did not materially affect the Company's operating results as at September 30, 2012. A change of 0.25% in the Canadian prime rate would result an increase or decrease in the interest expense by approximately $3,750 per year.

Liquidity risk

Liquidity risk is the risk that the Company may not have cash to meet its financial liabilities as they come due. The Company has sufficient credit facilities to meet its current and long term financial needs.

	Bank Indebtedness	Accounts Payable	Callable Debt	Total
	$	$	$	$
2013	(180,902)	492,672	75,000	386,770
2014	-	-	100,000	100,000
2015	-	-	100,000	100,000
2016	-	-	100,000	100,000
2017	-	-	100,000	100,000
Thereafter	-	-	891,667	891,667

The Company's liquidity requirements are met through the cash generated from operations. Management monitors and manages its liquidity risk through regular review of its financial liabilities against the constraints of its available financial assets.

(Expressed in Canadian Dollars)

22. CAPITAL DISCLOSURE

The Company's objectives in managing capital are:

1. to safeguard its ability to operate as a going concern;
2. to maintain a strong financial position; and
3. to maintain a low cost of debt.

Protecting the ability to pay current and future liabilities includes maintain a prudent base of capital, ensuring adequate liquidity and financial flexibility and satisfying internally determined capital guidelines based on risk management.

Capital is comprised of the Company's share capital, bank indebtedness and callable debt. As at September 30, 2012, the Company's share capital was $1,232,263 (September 30, 2011 - $1,232,263), bank indebtedness was $(180,902) (September 30, 2011 - $12,831) and callable debt was $1,366,667 (September 30, 2011 - $1,466,667).

The Company is not subject to any external capital requirements.

23. CHANGES IN NON-CASH WORKING CAPITAL

		Sept. 2012		June 2012
Trade and other receivables	**$**	**288,456**		(489,245)
Inventory		**(125,993)**		21,226
Prepaid Expenses		**31,829**		(20,729)
Deposits held in trust		**-**		192,860
Trade and other payables		**11,872**		166,888
Income taxes		**(27)**		41
Customer deposits		**(59,685)**		59,685
	$	**146,452**	$	(69,274)

24. ECONOMIC DEPENDENCE

The Company's subsidiary, Encore Electronics Inc., sells approximately 43% of its products to one customer. Should this customer substantially change its dealings with Encore, management is of the opinion that continued viable operations for Encore would be doubtful.

25. STANDARDS ISSUED BUT NOT YET EFFECTIVE

IFRS 9 as issued reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard is effective for annual periods beginning on or after January 1, 2013. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The completion of this project is expected over the course of 2011. The adoption of the first phase of IFRS 9 is not expected to have a material effect on the classification and measurement of the Company's financial assets and liabilities. The Company will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture.

Other standards

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in Other Entities, IAS 27 Separate Financial Statements, IFRS 13 Fair Value Measurement, and amended IAS 28 Investments in Associates and Joint Ventures. Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

26. COMPARATIVE FIGURES

Some of the comparative figures have been reclassified to conform to the current year's presentation.

ESTEC SYSTEMS CORP.

Schedule 1 - Selling, General and Administrative Expenses

(Unaudited)

(Expressed in Canadian Dollars)

	Notes	Three months ended September 30, 2012	Three months ended September 30, 2011
		($)	($)
EXPENSES			
Employee costs		421,188	678,281
Lease rentals on operating lease		40,050	38,976
Repairs and maintenance		16,051	28,502
Supplies and maintenance		13,953	21,389
Interest and bank charges		12,995	21,128
Public company compliance		710	11,347
Telephone and fax		11,528	9,651
Insurance		16,508	9,020
Advertising		9,520	8,779
Property tax		2,387	7,922
Training		701	5,138
Postage		-	4,306
Subscriptions		340	1,097
Corporate tax expense		-	726
Stock based compensation	20	502	502
Product development		-	49
Bad debts		-	-
Travel		92	(772)
Consulting and professional fees		32,344	(6,544)
		578,869	839,497