

ESTEC SYSTEMS CORP.

Consolidated Financial Statements
Quarters ended December 31, 2013 and 2012

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

ESTEC SYSTEMS CORP.

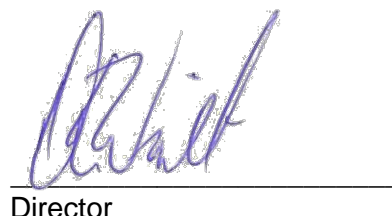
Interim Consolidated Statements of Financial Position (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013

		December 31, 2013	June 30, 2013
	Notes	(\$)	(\$)
ASSETS			
CURRENT			
Cash	3	177,270	394,034
Trade and other receivables	4	1,068,701	1,092,914
Inventory	5	223,922	265,252
Prepaid expenses		63,080	105,258
		<u>1,532,973</u>	<u>1,857,458</u>
PROPERTY AND EQUIPMENT	6	153,782	168,828
INTANGIBLE ASSETS	7	207,303	201,327
GOODWILL	8	617,261	610,413
		<u>978,346</u>	<u>980,568</u>
TOTAL ASSETS		<u>2,511,319</u>	<u>2,838,026</u>
LIABILITIES AND EQUITY			
CURRENT			
Bank indebtedness	3	185,000	195,000
Trade and other payables	10	486,736	613,397
Customer deposits		56,335	46,835
Income tax payable		9,179	12,549
Current portion of callable debt	11	100,000	100,000
		<u>837,250</u>	<u>967,781</u>
Callable debt due after one year	11	1,141,667	1,191,667
		<u>1,978,917</u>	<u>2,159,448</u>
ADVANCES FROM RELATED PARTIES	12	465,518	465,518
TOTAL LIABILITIES		<u>2,444,435</u>	<u>2,624,966</u>
EQUITY			
Share capital	13	1,232,263	1,232,263
Contributed surplus		17,350	16,848
Accumulated other comprehensive income		66,162	57,826
Deficit		(1,248,891)	(1,093,877)
TOTAL EQUITY		<u>66,884</u>	<u>213,060</u>
TOTAL LIABILITIES AND EQUITY		<u>2,511,319</u>	<u>2,838,026</u>

Approved on behalf of the Board


Director
Director

ESTEC SYSTEMS CORP.

Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013 and 2012

	Three months ended December 31, 2013	Three months ended December 31, 2012
	(\$)	(\$)
CONTINUING OPERATIONS		
REVENUE	1,330,547	1,352,841
DIRECT EXPENSES	641,507	675,035
	689,040	677,806
EXPENSES		
Selling, general and administrative expenses (Schedule 1)	745,213	674,842
Interest on callable debt	14,119	15,093
Amortization	7,994	12,804
Loss on disposal of property and equipment	-	1,118
	767,326	703,857
	(78,286)	(26,051)
OTHER INCOME (EXPENSE)		
Unrealized foreign exchange	36,414	58,705
Realized foreign exchange	(701)	(3,472)
INCOME BEFORE TAX	(42,573)	29,182
Income tax expense	(926)	3
NET INCOME (LOSS)	(43,499)	29,185
CHANGES IN COMPREHENSIVE INCOME		
Foreign currency translation (loss) / gain	16,313	2,764
COMPREHENSIVE INCOME (LOSS)	(27,186)	31,949
BASIC AND DILUTED INCOME PER SHARE	0.0	0.0
WEIGHTED AVERAGE NUMBER OF SHARES	10,461,629	10,461,629

ESTEC SYSTEMS CORP.

Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013 and 2012

	Six months ended December 31, 2013	Six months ended December 31, 2012
	(\$)	(\$)
CONTINUING OPERATIONS		
REVENUE	2,608,284	2,735,334
DIRECT EXPENSES	1,341,321	1,236,782
	1,266,963	1,498,552
EXPENSES		
Selling, general and administrative expenses (Schedule 1)	1,370,915	1,226,969
Interest on callable debt	28,676	30,783
Amortization	15,941	24,447
Loss on disposal of property and equipment	-	3,133
	1,415,532	1,285,332
	(148,569)	213,220
OTHER INCOME (EXPENSE)		
Unrealized foreign exchange	9,489	19,275
Realized foreign exchange	2,584	224
INCOME BEFORE TAX	(136,496)	232,719
Income tax expense	18,518	1,862
NET INCOME (LOSS)	(155,014)	230,857
CHANGES IN COMPREHENSIVE INCOME		
Foreign currency translation (loss) / gain	8,336	(2,576)
COMPREHENSIVE INCOME (LOSS)	(146,678)	228,281
BASIC AND DILUTED INCOME PER SHARE		
	(.02)	.02
WEIGHTED AVERAGE NUMBER OF SHARES	10,461,629	10,461,629

ESTEC SYSTEMS CORP.

Interim Consolidated Statements of Equity (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013 and 2012

	Share capital	Contributed surplus	Accumulated other comprehensive income	Deficit	Total
	(\$)	(\$)	(\$)	(\$)	(\$)
As at July 1, 2012	1,232,263	16,346	35,683	(1,446,291)	(161,999)
Stock based compensation expense	-	502	-	-	502
Income and comprehensive income for the period	-	-	(2,576)	230,857	228,281
As at December 31, 2012	1,232,263	16,848	33,107	(1,215,434)	66,784
As at July 1, 2013	1,232,263	16,848	57,826	(1,093,877)	213,060
Stock based compensation expense	-	502	-	-	502
Loss and comprehensive income for the period	-	-	8,336	(155,014)	(146,678)
As at December 31, 2013	1,232,263	17,350	66,162	(1,248,891)	66,884

ESTEC SYSTEMS CORP.

Condensed Interim Consolidated Statements of Cash Flow (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013 and 2012

	Three months ended December 31, 2013	Three months ended December 31, 2012
	(\$)	(\$)
OPERATING ACTIVITIES		
Net (loss) income	(43,499)	29,185
Items not affecting cash:		
Amortization	7,994	12,804
Loss on disposal of property and equipment	-	1,118
Stock based compensation	-	-
Cumulative foreign exchange	(11,016)	(2,644)
	(46,521)	40,463
Change in non-cash working capital	(77,100)	(66,428)
Cash flow from (used by) operating activities	(123,621)	(25,965)
INVESTING ACTIVITIES		
Purchase of property and equipment	-	(10,049)
Purchase of intangible assets	-	-
Cash flow used by investing activities	-	(10,049)
FINANCING ACTIVITIES		
Advances (to) from related parties	-	(51,855)
Repayment of callable debt	(25,000)	(25,000)
Cash flow from financing activities	(25,000)	(76,855)
INCREASE (DECREASE) IN CASH	(148,621)	(112,869)
Cash / bank indebtedness – beginning of period	140,891	180,902
Cash / bank indebtedness– end of period	(7,730)	68,033

ESTEC SYSTEMS CORP.

Condensed Interim Consolidated Statements of Cash Flow (Unaudited)

(Expressed in Canadian Dollars)

December 31, 2013 and 2012

	Six months ended December 31, 2013 (\$)	Six months ended December 31, 2012 (\$)
OPERATING ACTIVITIES		
Net (loss) income	(155,014)	230,857
Items not affecting cash:		
Amortization	15,941	24,447
Loss on disposal of property and equipment	-	3,133
Stock based compensation	502	502
Cumulative foreign exchange	(1,258)	17,016
	(139,829)	275,955
Change in non-cash working capital	(12,810)	80,024
Cash flow from (used by) operating activities	(152,639)	355,979
INVESTING ACTIVITIES		
Purchase of property and equipment	-	(30,751)
Purchase of intangible assets	(4,125)	-
Cash flow used by investing activities	(4,125)	(30,751)
FINANCING ACTIVITIES		
Advances (to) from related parties	-	(51,855)
Repayment of callable debt	(50,000)	(50,000)
Cash flow from financing activities	(50,000)	(101,855)
INCREASE (DECREASE) IN CASH	(206,764)	223,373
Cash / bank indebtedness – beginning of period	199,034	(155,340)
Cash / bank indebtedness– end of period	(7,730)	68,033
Cash flows supplementary information:		
Interest paid from operating activities	9,146	25,203
Interest paid from financing activities	31,956	34,293
Income taxes paid	20,245	-
Cash (bank indebtedness) consists of:		
Cash	177,270	316,758
Bank indebtedness	185,000	248,725
	(7,730)	68,033

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

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. ARN 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, 2013.

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 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 six month period ended December 31, 2013 were authorized for issue by the Board of Directors in accordance with a resolution of the Company on the 28th of February, 2014.

3. CASH AND BANK INDEBTEDNESS

Cash and bank indebtedness are comprised of the following:

	December 31, 2013	June 30, 2013
	(\$)	(\$)
Cash in bank	251,379	462,245
Outstanding deposits	10,000	-
Outstanding cheques	(84,109)	(68,211)
Net cash	177,270	394,034
Bank indebtedness	(185,000)	(195,000)
Cash	(7,730)	199,034

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

3. CASH AND BANK INDEBTEDNESS *(continued)*

ARN and ESTec: The bank revolving demand facility #1, is authorized to a total of \$250,000 with interest payable at prime plus 1.50%. At December 31, 2013 \$185,000 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: Bank revolving US demand facility #2 is authorized to a total of \$300,000 USD with interest payable at prime plus 2.60%. At December 31, 2013 \$nil was outstanding on this credit facility. A general security agreement and limited guarantees from directors and related parties in the amounts of \$300,000 have been pledged as collateral for the credit facility.

4. TRADE AND OTHER RECEIVABLES

	December 31, 2013	June 30, 2013
	(\$)	(\$)
Trade receivables	1,073,361	1,108,323
Allowance for doubtful accounts	(4,660)	(15,409)
Balance, end of period	1,068,701	1,092,914

	Past due but not impaired				
	Total	< 30 days	30-60 days	60-90 days	> 90 days
	(\$)	(\$)	(\$)	(\$)	(\$)
December 31, 2013	1,073,361	440,151	295,507	198,223	139,480
June 30, 2013	1,108,323	615,658	118,182	90,900	283,583

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

5. INVENTORY

	December 31, 2013	June 30, 2013
	(\$)	(\$)
Raw Materials	82,900	111,711
Work in progress*	81,497	74,433
Finished goods	49,713	66,699
Change in foreign exchange rates	9,812	12,409
	223,922	265,252

*Work in progress contains \$59,833 with respect to Allan R. Nelson Engineering (June 30, 2013 - \$13,295), all other amounts relate 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, 2013 - \$nil) and there were no reversals of prior write-downs.

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

6. PROPERTY AND EQUIPMENT

	June 30, 2013			December 31, 2013
	Cost	Additions	Disposals	Cost
	(\$)	(\$)	(\$)	(\$)
Equipment	136,961	-	-	136,961
Computer hardware	67,547	-	-	67,547
Equipment	55,912	-	-	55,912
Office equipment	40,137	-	-	40,137
Inspection equipment	7,949	-	-	7,949
Change in foreign exchange	7,094	1,616	-	8,710
	315,600	1,616	-	317,216

	June 30, 2013			December 31, 2013
	Accumulated amortization	Amortization expense	Disposals	Accumulated amortization
	(\$)	(\$)	(\$)	(\$)
Equipment	47,726	8,093	-	55,819
Computer hardware	31,851	3,573	-	35,424
Equipment	40,729	1,519	-	42,248
Office equipment	16,765	2,326	-	19,091
Inspection equipment	7,223	73	-	7,296
Change in foreign exchange	2,478	1,078	-	3,556
	146,772	16,662	-	163,434

	December 31, 2013	June 30, 2013
	Net book value	Net book value
	(\$)	(\$)
Equipment	81,142	89,235
Computer hardware	32,123	35,696
Equipment	13,664	15,183
Office equipment	21,046	23,372
Inspection equipment	653	726
Change in foreign exchange	5,154	4,616
	153,782	168,828

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

7. INTANGIBLE ASSETS

	July 1, 2013 Balance	Addition	Amortization/ Write-off	December 31, 2013 Total
	(\$)		(\$)	(\$)
Intellectual property	104,850	-	-	104,850
Customer list	30,000	-	-	30,000
Computer software	36,352	4,125	-	40,477
ISO manual	22,000	-	-	22,000
Change in foreign exchange	8,125	1,851	-	9,976
At December 31, 2013	201,327	5,976	-	207,303
	July 1, 2012 Balance	Addition	Amortization/ Write-off	June 30, 2013 Total
	(\$)		(\$)	(\$)
Intellectual property	104,850	-	-	104,850
Customer list	30,000	-	-	30,000
Computer software	51,865	-	15,513	36,352
ISO manual	22,000	-	-	22,000
Change in foreign exchange	2,839	5,286	-	8,125
At June 30, 2012	211,554	5,286	15,513	201,327

8. GOODWILL

	December 31, 2013	June 30, 2013
Goodwill, beginning of year	\$ 610,413	\$ 590,855
Change in foreign exchange rate	6,848	19,558
	<u>617,261</u>	<u>\$ 610,413</u>

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

8. GOODWILL (*continued*)

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 net earnings, for the year ended June 30, 2013, of \$397,688 attributable to Encore. The Company performed its annual impairment test as at June 30, 2013. 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 4.13% and 16.01% 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.

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

10. TRADE AND OTHER PAYABLES

	Total	< 30 days	Past due		
			30-60 days	60-90 days	> 90 days
	(\$)	(\$)	(\$)	(\$)	(\$)
December 31, 2013	320,051	196,917	25,475	43,502	54,157
June 30, 2013	298,349	224,624	40,482	7,878	25,365
			December 31, 2013	June 30, 2013	
Trade payables		\$	320,051	\$	298,349
Other payables					
Accrued liabilities			44,679		171,554
Payroll payable			34,281		41,090
Vacation payable			75,252		81,100
GST payable			12,473		21,304
		\$	486,736	\$	613,397

Terms and conditions of the above financial liabilities:

- Trade payables are non-interest bearing and are normally settled on 40-day terms
- Other payables are non-interest bearing and have an average term of six months

11. CALLABLE DEBT

	December 31, 2013	June 30, 2013
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.	1,241,667	1,291,667
Principal due in one year	(100,000)	(100,000)
	1,141,667	1,191,667

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
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Principal repayment terms are approximately:

Less than one year	50,000
Later than one year and not later than five years	400,000
Later than five years	791,667
	<u>1,241,667</u>

12. 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:

	December 31, 2013	June 30, 2013
	<u> </u>	<u> </u>
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	298,607	298,607
	<u>\$ 465,518</u>	<u>\$ 465,518</u>
Amounts within trade accounts payable:		
Due to directors	-	8,363
Due to corporations controlled by certain directors	46,054	47,250
	<u>46,054</u>	<u>47,250</u>
Companies controlled by certain directors:		
Rent expense (to a company controlled by certain directors)	\$ 94,390	\$ 161,447
Compensation paid to Executives of the Company	205,180	573,338
Compensation paid to independent directors of the Company	1,600	4,000
	<u>1,600</u>	<u>4,000</u>

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.

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

13. SHARE CAPITAL

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

Issued and outstanding

	December 31, 2013		June 30, 2013	
	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

14. LEASE COMMITMENTS

The Company has an 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	39,694
Later than one year and not later than 3 years	150,648
	190,342

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

15. 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 may be issued.

	December 31, 2013		June 30, 2013	
	Number	Weighted average exercise price	Number	Weighted average exercise price
Outstanding beginning of period	235,000	0.10	560,000	0.10
Expired	-	-	(325,000)	-
Outstanding at end of period	235,000	0.10	235,000	0.10

At the end of the period ended December 31, 2013 there were 235,000 options, with an exercise price of \$0.10 and weighted average remaining contractual life of .56 years, outstanding.

ESTEC SYSTEMS CORP.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
Period Ended December 31, 2013 and 2012

16. SEGMENTED INFORMATION

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

	December 31, 2013		
	Engineering	Electronics	Total
Revenue	967,106	1,641,178	2,608,284
Direct expenses	(335,769)	(1,005,552)	(1,341,321)
Expenses	(714,726)	(656,189)	(1,370,915)
Amortization	(7,491)	(8,450)	(15,941)
Interest expense	(28,676)	-	(28,676)
Income (loss) from operations	(119,556)	(29,013)	(148,359)
Other income (expenses)	12,073	-	12,073
Income (loss) before income taxes	(107,483)	(29,013)	(136,496)
Income tax expense	-	(18,518)	(18,518)
Net income (loss)	(107,483)	(47,531)	(155,014)
Identifiable assets	715,128	1,796,191	2,511,319
Identifiable liabilities	1,137,210	1,307,225	2,444,435
	June 30, 2013		
	Engineering	Electronics	Total
Revenue	2,397,536	3,178,949	5,576,485
Direct expenses	(922,493)	(1,231,660)	(2,154,153)
Expenses	(1,474,510)	(1,458,652)	(2,933,162)
Amortization	(14,450)	(19,982)	(34,432)
Valuation allowance for intangible assets	(15,653)	-	(15,653)
Interest expense	(75,781)	(33,147)	(108,928)
Loss on disposal of property and equipment	(5,350)	(242)	(5,592)
Income (loss) from operations	(110,701)	435,266	324,565
Other income (expenses)	65,213	(24,105)	41,108
Income (loss) before income taxes	(45,488)	411,161	365,673
Income taxes	-	(13,259)	(13,259)
Net income (loss)	(45,488)	397,902	352,414
Identifiable assets	875,598	1,962,428	2,838,026
Identifiable liabilities	1,624,971	999,995	2,624,966

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17. 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% (2012 – 25.00%) in Canada and 36.84% in the US to the income for the year as follows:

	December 31, 2013	June 30, 2013
	(\$)	(\$)
<u>Income (loss) before income tax</u>	<u>(136,496)</u>	<u>365,674</u>
Income tax expense at the combined basic federal and provincial tax rate:	18,518	91,419
Non-deductible expense	-	(12,071)
Non-capital loss carried forward	-	15,650
<u>Non-capital losses applied in current year</u>	<u>-</u>	<u>(81,739)</u>
<u>Effective tax expense</u>	<u>18,518</u>	<u>13,259</u>

18. 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.

<i>Allan R. Nelson Engineering (1997) Inc./ ESTec Systems Corp.</i>	December 31, 2013	June 30, 2013
	(\$)	(\$)
Employer contributions expensed during the current period	28,063	54,093
<u><i>Encore Electronics Inc.</i></u>	<u>December 31, 2013</u>	<u>June 30, 2013</u>
	(\$)	(\$)
Employer contributions expensed during the current period	10,960	25,969

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19. 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:

	Three months ended December 31, 2013	Three months ended December 31, 2012
Net income (loss)	\$ (43,499)	\$ 29,185
Weighted average number of common shares outstanding during the period	10,461,629	10,461,629
Basic earnings (loss) per share	0.0	0.0
Common shares and stock options	10,696,629	10,696,629
Diluted earnings (loss) per share	0.0	0.0

	Six months ended December 31, 2013	Six months ended December 31, 2012
Net income (loss)	\$ (155,014)	\$ 230,857
Weighted average number of common shares outstanding during the period	10,461,629	10,461,629
Basic earnings (loss) per share	(0.02)	0.02
Common shares and stock options	10,696,629	10,696,629
Diluted earnings (loss) per share	(0.02)	0.02

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20. FINANCIAL INSTRUMENTS

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

	December 2013		June 30, 2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Loans and Receivables				
Cash	177,270	177,270	394,034	394,034
Trade and other receivables	1,068,701	1,068,701	1,092,914	1,092,914
Financial Liabilities				
Bank indebtedness	185,000	185,000	195,000	195,000
Trade and other payables	486,736	486,736	613,397	613,397
Advances from related parties	465,518	465,518	465,518	465,518
Callable debt	1,241,667	1,241,667	1,291,667	1,291,667

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 cash (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.

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20. 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 31.56% in trade and other receivables from its largest customer as at December 31, 2013.

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.

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20. FINANCIAL INSTRUMENTS *(continued)*

At December 31, 2013 the Company's exposure to foreign currency risk are as follows:

Reporting Rate (\$US - \$CAD)	December 31, 2013	June 30, 2013
	1.0636	1.052
Cash and cash equivalents	205,253	382,460
Trade and other receivables	500,895	396,917
Trade and other payables	185,168	314,622

For each 1% change in rate, based on the monetary assets and liabilities held at December 31, 2013, the Company's net earnings would be impacted by approximately \$5,210 (June 2013 - \$4,648).

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 December 31, 2013. A change of 0.25% in the Canadian prime rate would result in an increase or decrease in the interest expense by approximately \$3,567 (June 2013 - \$3,716) 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
2014	185,000	486,736	50,000	721,736
2015	-	-	100,000	100,000
2016	-	-	100,000	100,000
2017	-	-	100,000	100,000
2018	-	-	100,000	100,000
Thereafter	-	-	791,667	791,667

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.

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21. 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, ensure adequate liquidity and financial flexibility, and satisfy internally determined capital guidelines based on risk management.

Capital is comprised of the Company's share capital, bank indebtedness and callable debt. As at December 31, 2013, the Company's share capital was \$1,232,263 (December 31, 2012 - \$1,232,263), bank indebtedness was \$185,000 (December 31, 2012 - \$248,725) and callable debt was \$1,241,667 (December 31, 2012 - \$1,341,667).

The Company is subject to an external capital requirement on its revolving demand facilities of debt service coverage of not less than 1.25:1 on a consolidated basis. At December 31, 2013 the Company is in compliance with this requirement.

22. CHANGES IN NON-CASH WORKING CAPITAL

	December 2013	June 2013
Trade and other receivables	\$ 24,213	\$ 143,214
Inventory	41,330	(129,686)
Prepaid Expenses	42,178	(31,450)
Trade and other payables	(126,661)	132,592
Income taxes	(3,370)	11,785
Customer deposits	9,500	(12,846)
	<u>\$ (12,810)</u>	<u>\$ 113,609</u>

23. ECONOMIC DEPENDENCE

The Company's subsidiary, Encore Electronics Inc., sells approximately 67% 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.

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24. STANDARDS ISSUED BUT NOT YET EFFECTIVE

Standards issued but not yet effective up to the date of issuance of the Company's financial statements are listed below. This listing is of standards and interpretations issued, which the Company reasonably expects to be applicable at a future date. The Company intends to adopt those standards when they become effective.

a) IAS 32 Financial Instruments: Presentation and IFRS 7 Financial Instrument and Disclosure

IAS 32 and IFRS 7 were amended to implement new disclosure requirements of the International Accounting Standard Board's ("IASB") publication on *Offsetting Financial Assets and Financial Liabilities*. The amendments to the standard are effective for annual periods beginning on or after January 1, 2013. The Company is in 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.

b) IFRS 9 Financial Instruments: Classification and Measurement

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.

c) IFRS 13 Fair Value Measurement

IFRS 13 establishes the definition of fair value and sets out a single IFRS framework for measuring fair value and the required disclosures in one comprehensive source. The standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. The Company intends to adopt IFRS 13 prospectively in its financial statements for its fiscal period beginning on July 1, 2013. The extent of the impact of adoption of IFRS 13 has not yet been determined.

d) 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, 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.

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25. 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)**

		Six months ended December 31, 2013 (\$)	Six months ended December 31, 2012 (\$)
EXPENSES			
Employee costs		1,024,937	925,514
Lease rentals on operating lease		94,390	80,038
Consulting and professional fees		58,327	52,922
Supplies and maintenance		36,706	22,949
Insurance		36,602	33,261
Repairs and maintenance		30,025	22,281
Advertising		30,560	23,402
Travel		15,742	13,814
Telephone and fax		13,741	20,243
Interest and bank charges		12,427	28,713
Public company compliance		10,950	12,458
Dues, memberships & business taxes		6,503	12,877
Training		4,225	2,016
Courier & Freight		1,028	969
Stock based compensation	15	502	502
Bad debts		(5,750)	-
		<u>1,370,915</u>	<u>1,251,959</u>