MANAGEMENT'S DISCUSSION & ANALYSIS

For the Fiscal Year Ended May 31, 2015

Introduction

This Management Discussion and Analysis (MD&A) explains the material changes in Thermal Energy International Inc.'s ("Thermal Energy" or the "Company") financial position and results of operations for the fiscal year ended May 31, 2015 (or "FY 2015"), and compares the FY 2015 financial results to the previous year ended May 31, 2014 (or "FY 2014"). The consolidated financial statements and notes to the consolidated financial statements constitute an integral part of the discussion and should be read in conjunction with this MD&A. Unless otherwise indicated, all comparisons to the fourth quarter of FY 2015 are against the fourth quarter of FY 2014. Additional information relating to the Company is available on SEDAR at www.sedar.com.

Currency

All financial information in this report is stated in Canadian Dollars, which is both the presentation and functional currency of the Company. Approximately 55% of our operations, assets and liabilities are denominated in British Pound Sterling. As such, foreign currency fluctuations affect the reported values of individual lines on our statement of financial position and income statement. When the Canadian dollar strengthens, the reported values decrease and the opposite occurs when the Canadian dollar weakens.

Review and Approval by the Board of Directors

The Board of Directors, on recommendation of the Audit Committee, approved the content of this MD&A on September 16, 2015. Disclosure contained in this document is current to this date, unless otherwise stated.

Forward-Looking Statements

This MD&A may include statements that are forward-looking. These statements are not guarantees of future performance and are subject to risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. We discuss the principal risks of our business in Section 7 of this MD&A. We cannot provide any assurance that forecasted financial or operational performance will actually be achieved. If it is achieved, we cannot provide assurance that it will result in an increase in our share price. See Section 8 entitled "Forward-Looking Information".

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1. Our Business

1.1 Company Overview

Thermal Energy, established in 1991, is an innovative cleantech company and a global provider of proprietary and proven energy and water efficiency and emission reduction products and solutions to the industrial, commercial and institutional markets. The Company is headquartered in Ottawa, Canada, with offices in the U.K., Italy, U.S., China and sales worldwide.

Thermal Energy engages clients through a unique mix of process, energy, environmental and financial expertise to save our customers money and improve their bottom lines by reducing their fuel use and carbon emissions. The Company's award winning products have an excellent track record of longevity, proven reliability and performance and have been shown to provide: significant energy savings; improved water efficiency; reduced greenhouse gas emissions; lower maintenance costs; improved product quality; and increased production efficiency. Thermal Energy's products are effective in a wide range of industries and applications.

More information on Thermal Energy can be found at www.thermalenergy.com. **GEM™, FLU-ACE®, THERMALONOx™** and **DRY-REX™** are trademarks of Thermal Energy.

1.2 Core Businesses

The Company operates in the energy efficiency industry in North America, Europe, China and the rest of the world. The Company markets, sells, engineers, fabricates, constructs, installs and supports two technology lines – heat recovery solutions (**FLU-ACE**®) and condensate return system solutions (**GEM™** steam traps). The Company is also developing a third technology line - low temperature biomass drying systems (**DRY-REX™)**.

Before 2007, the Company concentrated mainly on the selling of heat recovery systems but had begun selling GEM™ product through a distribution agreement with Gardner Energy Management Limited, based in the U.K. In 2008, the Company acquired Gardner Energy Management Limited, which sells the GEM™ product throughout the world. As part of this transaction, the Company also acquired the 67% share of GEMchem Ltd, a UK-based water treatment company providing services within the UK only.

The acquisition of Gardner Energy Management Limited resulted in the Company having two primary operational bases, one in Ottawa, Canada covering North America and China, and the other in Bristol, United Kingdom, covering Europe and the rest of the world. Although the Ottawa base is deemed to be the center of excellence for the heat recovery side of the business, and Bristol the center of excellence for condensate return system solutions, continuous cross-training means that both bases have expertise across both major product lines.

Although the Company markets its products throughout the world, the majority of sales are from within North America and Europe, due to the proximity to the Company's bases. While this continues to be the key focus, the Company also continues to look for new distributors in regions deemed to have potential.

1.3 Strategy

The Company's mission is to be a best-in-class provider of return on investment-driven thermal energy efficiency technology and solutions to the industrial, institutional, and commercial sectors, helping our clients around the world improve their bottom line, move towards sustainable operations and reduce their environmental and carbon footprint. The Company's products and services are "best-in-class" with world-wide application in a broad range of sectors.

The Company has representation in 28 countries around the world but our current focus is on the key markets of North America, Europe and the Middle East. Despite significant growth over the last few years, Thermal Energy's penetration in these markets remains low and therefore the Company plans to continue growing our sales and distribution capabilities in these markets while at the same time begin to build our business in other energy-intensive markets around the world.

We have sold our proprietary and proven products to hundreds of companies and institutions, including approximately 50 large multinational companies in the pharmaceutical, food and beverage, pulp and paper, chemical and petrochemical sectors. So far the Company has only partially penetrated 100 of the more than 2,000 global sites of these multi-national companies. Thermal Energy has executed a corporate-wide global roll-out of our product with two of these multi-national companies and is currently working with additional companies with the goal of executing similar corporate roll-outs.

With a global sales and distribution network the Company also has the opportunity to introduce new synergistic products and services, and acquire complementary products and businesses that can be distributed through our existing network.

Finally, the Company is also developing a number of recurring revenue streams such as rental and shared savings programs as well as service and maintenance programs.

2. Performance Measures

The Company believes the following performance measures provide useful information to both management and investors to better understand the financial performance and financial position of the Company.

2.1 Adjusted Operating Cash Flow

Adjusted operating cash flow (defined as income (loss) for the period, plus items not involving cash but excluding any changes in working capital items, plus finance lease payments received) is a performance measure used to gauge the cash generating capability of the Company. The impact changes in working capital items has on cash balances is excluded from the calculation of operating cash flow because changes in working capital items are usually only temporary and can fluctuate significantly from period to period and therefore are not a good indicator of the Company's longer term cash generating capabilities.

It is important to note that cash flow is not the same as net income, which includes transactions that did not involve actual cash outflows and excludes some transactions that did involve actual cash inflows. The calculation of adjusted operating cash flow starts with net income as identified in the Consolidated Statements of Comprehensive Income and then adds or subtracts a number of items identified in the Statement of Cash Flows. Adjusted operating cash flow does not have a standardized meaning prescribed by International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies. The most directly comparable measure calculated in accordance with generally accepted accounting principles within the financial statements is net cash provided (used) in operating activities, as disclosed in the statement of cash flows.

2.2 EBITDAS

Management believes that EBITDAS (earnings before interest, taxation, depreciation, amortization, impairment of goodwill and other intangible assets, share-based compensation expense and net write down of lease) is a useful performance measure as it approximates cash generated from operations, before tax, capital expenditures and changes in working capital and excludes non-operating items. EBITDAS also assists comparison among companies as it eliminates the differences in earnings due to how a company is financed. EBITDAS does not have a standardized meaning prescribed by International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies. . The most directly comparable measure calculated in accordance with generally accepted accounting principles within the financial statements is income (loss) before income taxes, as disclosed in the statements of comprehensive income.

2.3 Order Backlog

Order backlog is a useful performance measure that Management uses as an indicator of the short term future revenue of our Company resulting from already recognized orders. However, there is no comparable IFRS financial measure for order backlog. The Company includes in "order backlog" any purchase orders that have been received by the Company but have not yet been reflected as revenue in the Company's published financial statements. It is important to note that once an order or partial order is recorded as revenue, the order backlog is reduced by the amount of the newly reported revenue. Order backlog does not have a standardized meaning prescribed by generally accepted accounting principles or International Financial Reporting Standards and therefore may not be comparable to similar measures presented by other companies.

3. Performance

3.1 Summary of Fourth Quarter Results

	Q4 2015	Q4 2014
	$	$
Revenue	**2,525,061**	4,717,007
Cost of Sales	**(1,331,240)**	(1,979,439)
Gross Profit	**1,193,821**	2,737,568
Administration, selling, marketing and business development expenses	**(1,508,900)**	(1,959,732)
Research and development expenses	**(7,996)**	(111,546)
Operating income (loss) before impairment	**(323,075)**	666,290
Impairment	**-**	-
Operating income (loss)	**(323,075)**	666,290
Finance Revenue	**6,574**	29,705
Income (loss) before income taxes	**(316,501)**	695,995
Income taxes (expense) recovery	**(21,141)**	1,403
Net income (loss) for the period	**(337,642)**	697,398
Exchange differences on translation of overseas operations	**(18,464)**	(49,356)
Total comprehensive income (loss) for the period	**(356,106)**	648,042

Revenues and Gross Profits

Revenues were $2,525,061 in the quarter ended May 31, 2015, representing a decrease of $2,191,946, or 46%, compared to $4,717,007 in the quarter ended May 31, 2014. Sales of heat recovery systems decreased by $1,926,278 (55.7%) from the same period in the previous year, while sales of GEM™ condensate return systems decreased by $265,668 (21.1%).

Revenues from sales of heat recovery systems in the current quarter included the substantial conversion at a site of a food manufacturer, as announced January 26, 2015, and one at a manufacturer of interior lining products, as announced January 5, 2015, plus the first half of a hospital conversion, as announced January 29, 2015, as well as the initial engineering stages of a project at a packaged food company, as announced December 1, 2014. This compared to the substantial completion of an installation at a major pulp and paper company as announced June 3, 2013, plus two hospital conversions and an equipment sale to a global diversified mining and materials company, as announced December 18, 2013, in the same quarter of the previous year.

GEM™ condensate return system sales for the final quarter of FY 2015 decreased from the same period of the previous year due mainly to lack of any significant projects. The final quarter of FY 2014 included the fulfilment of two orders received from a global diversified healthcare company, as announced February 18, 2014 and May 12, 2014, plus a further site conversion of a Fortune 500 food and beverage company, but there were no comparable orders in the current period, although there was an increase in the number of smaller orders across North America and the rest of the world.

The gross profit of $1,193,821 in the quarter ended May 31, 2015 represented a decrease of $1,543,747, or 56.4%, from the $2,737,568 achieved in the quarter ended May 31, 2014. This decrease was the result not only of lower revenues, but also decreased margins on heat recovery projects. The current period included two projects which were specifically costed to encourage customers to agree to trials with the aim of proving the technology and as a result ultimately receiving further orders for their other sites. Gross profit expressed as a percentage of sales was 47.3% in the final quarter of FY 2015 compared with 58.0% in the final quarter of FY 2014.

Expenses

Administration, selling, marketing and business development expenses in the quarter ended May 31, 2015 totaled $1,508,900 compared to $1,959,732 in the quarter ended May 31, 2014, a decrease of $450,832. This decrease was predominantly the result of reduced commissions attached to revenues, plus the lack of any staff incentive due to the current year losses, as well as increased foreign exchange gains resulting from the strengthening of the US dollar against the Canadian dollar.

Research and development costs of $7,996 in the final quarter of FY 2015 compared to $111,546 in the final quarter of FY 2014. The current year saw the virtual completion of work on the ISTP project, for which the Company had previously received an offer of government funding through ISTP Canada, as announced February 8, 2012. The funding agreement was signed by both parties on January 21, 2013. Also offsetting research and development costs in the fourth quarter of the current year was $33,876 in SR&ED funding.

Finance revenue in the fourth quarter of FY 2015 of $6,574 compared to $29,705 recognized in the fourth quarter of FY 2014. The interest rate implicit in the lease of 14.3% is applied against the reducing finance lease receivable balance, hence lower finance revenues as the term of the agreement progresses. The existing lease expired in April 2015. Although it was extended by a further two years on May 1, 2015, the interest earned in the final quarter was against a lesser balance than in the same period of the prior year.

Loss before income taxes for the quarter ended May 31, 2015 was $316,501 compared to income of $695,995 in the same quarter of the previous year. The loss in the final quarter of the current year was a direct result of the reduced revenues and hence reduced gross profit, which was not sufficient to cover the fixed costs of the company.

Income tax charge in the fourth quarter of FY 2015 was $21,141, compared to a recovery of $1,403 in the fourth quarter of FY 2014, as a result of profits in the quarter of subsidiaries.

Net loss for the fourth quarter of FY 2015 was $337,642 compared to net income of $697,398 in the same quarter of the previous year.

Comprehensive loss was $356,106 for the final quarter of FY 2015 compared to income of $648,042 for the final quarter of FY 2014. Both quarters saw a slight strengthening of the Canadian dollar against the UK pound sterling from the end of the February quarters, hence the worse comprehensive income or loss arising from the translation of assets recorded in sterling.

3.2 Review of Year End Results

	2015	2014
	$	$
Revenue	**6,800,192**	13,150,810
Cost of Sales	**(3,172,087)**	(6,177,190)
Gross Profit	**3,628,105**	6,973,620
Administration, selling, marketing and business development expenses	**(5,879,062)**	(6,186,962)
Research and development expenses	**(127,377)**	(211,917)
Operating income (loss)	**(2,378,334)**	574,741
Finance Revenue	**60,063**	133,678
Income (loss) before income taxes	**(2,318,271)**	708,419
Income taxes (expense) recovery	**163,454**	(74,396)
Net income (loss) for the period	**(2,154,817)**	634,023
Exchange differences on translation of overseas operations	**48,373**	344,244
Total comprehensive income (loss) for the period	**(2,106,444)**	978,267

Revenues and Gross Profits

Revenues were $6,800,192 in FY 2015 compared to $13,150,810 in FY 2014, a decrease of $6,350,618, or 48.3%. Sales of heat recovery systems decreased in the year by $5,038,361 (60.2%), while sales of GEM™ condensate return systems decreased by $1,312,257 (27.4%).

The $8,369,102 heat recovery systems revenues achieved in FY 2014 included revenues from projects at two sites of a major Fortune 500 food and beverage company, as announced September 16, 2013, plus the substantial completion of an installation at a major pulp and paper company as announced June 3, 2013, as well as revenue from projects at three major hospitals. Other than one further site conversion of the same major Fortune 500 food and beverage company, as announced August 27, 2014, plus the substantial completion of an installation at a site of another food producer, as announced January 26, 2015, and the first half of a hospital conversion, as announced January 29, 2015, there were no significant projects similar to those mentioned above in the current year.

GEM™ condensate return systems sales in FY 2015 were $3,469,451 compared to $4,781,708 in FY 2014. FY 2014 saw the fulfilment of orders received from a major food and beverage manufacturer – our largest single GEM as of that date - as announced July 3, 2013; a global premium beer company, as announced February 10, 2014; a global diversified healthcare company, as announced February 18, 2014 and May 12, 2014; and a Fortune 500 food and beverage company, as announced September 13, 2013, as well as sales to three hospitals. Although in FY 2015, further sales were made to the Fortune 500 food and beverage company, as announced July 10, 2014, and additional orders were received from a leading performance materials and chemicals company, as announced October 15, 2014, there were no significant orders from hospitals and fewer significant orders overall.

The gross profit of $3,628,105 in FY 2015 represents a decrease of $3,345,515, or 48.0%, from the $6,973,620 achieved in FY 2014. The gross profit expressed as a percentage of sales were 53.4% in FY 2015 compared with 53.0% in FY 2014.

Expenses

Administration, selling, marketing and business development expenses in FY 2015 totaled $5,879,062, compared to $6,186,962 in FY 2014, a decrease of $307,900, or 5.0%. The lack of a staff incentive in the current year plus lower commissions on the reduced revenues were the main contributors to the decrease, as well as increased foreign exchange gains predominantly from the strengthening of the US dollar against the Canadian dollar. In addition, FY 2014 included recruitment costs relating to the additional sales and marketing staff employed during that year. These cost decreases were partially offset by the increased salaries relating to the strengthening of the sales force, sales training events and an increase in stock based compensation expense.

Research and development costs in FY 2015 totaled $127,377 compared to $211,917 in FY 2014. The ISTP project, which commenced in January 2013, as announced February 2012, continued throughout the current year, as well as various smaller projects developing complementary products to our existing portfolio. During the current year, the company recognized government funding of $124,019 towards the ISTP project as well recording SR&ED credits totaling $68,288, compared to $61,689 ISTP funding and a $56,875 SR&ED credit in the previous year.

Finance revenue in FY 2015 was $60,063, a decrease of $73,615 from the $133,678 received in FY2014. The current year saw the expiry of the existing lease, which was further extended in May 2015. The lower balance throughout FY 2015 resulted in lower finance revenue.

Loss before income taxes for the fiscal year ended May 31, 2015 was $2,318,271 compared to income of $708,419 for the fiscal year ended May 31, 2014. The $3,026,690 difference is the direct result of the decreased revenues in the year along with the increased staff costs. Between the second half of FY2014 and the first half of FY 2015, a total of five new regional sales managers were recruited. Due to the nature of our offerings and the lack of any prior presence in the regions covered by these new sales staff, FY 2015 was not expected to generate much return from this investment.

Income tax recovery in FY 2015 was $163,454, compared to a charge of $74,396 in the previous year. This change is the direct result of losses in the UK entity compared to profits in FY 2014.

Net loss for FY 2015 was $2,154,817, compared to net income in the year ended May 31, 2014 of $634,023.

Comprehensive loss was $2,106,444, compared to comprehensive income in the year ended May 31, 2014 of $978,267. The UK Pound Sterling further strengthened against the Canadian Dollar in FY 2015, albeit at a lower rate than the prior year, giving rise to an exchange gain on translation of overseas operations of $48,373 in FY 2015, compared to $344,244 in FY 2014.

Liquidity & Capital Resources

The working capital was $488,389 at May 31, 2015 compared to working capital of $2,770,280 at May 31, 2014 – a decrease of $2,281,891, with the Company's net cash position (Cash and cash equivalents less Bank loans) decreasing by $1,331,074 from $2,046,417 as at May 31, 2014 to $715,343 as at May 31, 2015.

The Company's working capital position over the last eight quarters can be summarized as follows:

	Aug 31, 2013 $	Nov 30, 2013 $	Feb 28, 2014 $	May 31, 2014 $	Aug 31, 2014 $	Nov 30, 2014 $	Feb 28, 2015 $	May 31, 2015 $
Current Assets	3,604,594	6,184,899	5,729,213	5,273,288	4,533,588	3,722,822	3,768,369	3,650,605
Current Liabilities	2,199,528	4,361,002	3,899,718	2,503,008	2,415,447	2,193,708	2,848,970	3,162,216
Working Capital	1,405,066	1,823,897	1,829,495	2,770,280	2,118,141	1,529,114	919,399	488,389

FY 2015 Changes

Current assets decreased in FY 2015 by $1,622,683 to $3,650,605, mostly due to a reduction in cash balances of $1,331,074, due to the loss experienced in the year, plus the expiry of the existing finance lease, the extension of which is at a lower value than the previous extension. Current liabilities meanwhile increased by $659,208 to $3,162,216, despite a decrease in accounts payable of $226,424. The increase was predominantly due to $932,823 additional deferred revenue relating to three heat recovery projects in progress at May 31, 2015.

As at May 31, 2015, $164,375 (8.3%) of the Company's trade receivables balance was over 90 days past due. Since that date, $163,000 has been received. None of the overdue balance is considered impaired as at May 31, 2015.

At May 31, 2015, the Company had operating lease commitments as shown below. The Company had no purchase obligations:

	Total $	Less than 1 year $	1-5 years $	More than 5 years $
Operating Leases	295,605	136,259	159,346	nil

Net cash used in operating activities in the year ended May 31, 2015 was $1,806,222. Net cash provided by investing activities of $687,412 comprised $724,014 finance lease principal payments received less $36,602 paid for additions to property, plant and equipment, mostly computer equipment and portable equipment for analysis of steam systems. A total of $195,366 was used in investing activities, for the repurchase of Class A common shares under the Normal Course Issuer Bid, as announced October 28, 2013 and October 30, 2014. After allowing negative $16,898 for the effect of exchange rate fluctuations on cash and cash equivalents, the net result of the above activities was a reduction in cash balance of $1,331,074.

Adjusted operating cash outflow (defined as net income or loss attributable to the owners of the parent, plus items not involving cash, after net tax and interest cash inflows or outflows, plus finance lease payments received) for the year ended May 31, 2015 was $1,404,427. After adjusting this for $322,219 of positive changes in non-cash working capital items and deducting $36,602 for the purchase of fixed assets, and $195,366 used for the repurchase of Class A common shares, and deducting $16,898 to allow for the effect of exchange rate fluctuations on cash and cash equivalents, the net cash outflow was $1,331,074, decreasing the net cash balance as at May 31, 2015 to $715,343 from $2,046,417 as at May 31, 2014.

In addition to its net cash balance of $715,343 as at May 31, 2015 the Company also had an estimated $140,000 of unused borrowing capacity under its bank loans. Order backlog as at May 31, 2015 was approximately $3.7 million compared to $1.8 million at the same time last year. As at September 16, 2015, the Company had $5.7 million in purchase orders that had not yet been reflected as revenue in the Company's published quarterly financial statements.

The Company's ability to realize its assets and discharge its liabilities depends on its ability to generate sufficient cash from operations or its ability to arrange debt or equity financing. No assurance can be given that any such additional funding will be available or that, if available, it can be obtained on terms favorable to the Company.

Management is of the opinion that sufficient working capital will be obtained from future cash flows by achieving profitable operations through continuing to manage expenditures, concentrating on restoring revenue to the level experienced in 2014 and growing revenues at growth rates experienced in the years ended May 31, 2010 through May 31, 2014. The Company cannot be certain that cash generated from its operations will be sufficient to satisfy its liquidity requirements and it may need to raise capital by obtaining financing.

A reconciliation of Net cash provided (used) in operating activities to adjusted operating cash flow is shown below:

	2013 $	2014 $	2015 $
Net cash provided (used) in operating activities	(763,924)	462,690	(1,806,222)
Changes in working capital	(1,332,548)	444,872	(322,219)
Finance lease principal payments received	712,213	441,562	724,014
Adjusted operating cash flow	(1,384,259)	1,349,124	(1,404,427)

Net Investment in Lease

The Company's net investment in lease includes the following:

	May 31, 2015 $	May 31, 2014 $
Total estimated minimum lease payments receivable	262,108	962,274
Less: unearned income	(34,024)	(57,235)
	228,084	905,039
Less: current portion	(111,524)	(765,509)
	116,560	139,530

Finance lease receivable relates to one arrangement. The estimated minimum lease payments receivable in this lease represent the estimated monthly energy outputs of the leased asset and are based on assumptions regarding the efficiency of the asset, the operations of the plant in which it is located and penalty payments resulting from temporary plant shut-downs. On December 31, 2012, the lease with Fortress Specialty Cellulose, as signed on June 29, 2010, expired. On November 27, 2012, an agreement was signed whereby the customer agreed to purchase the recovered energy for a further two years, after which the customer had the option to renew for an additional 24 months on substantially the same terms or purchase the asset from the Company.

On December 22, 2013, the site commenced a market downtime for a period of ten weeks, following the imposition of an interim duty in China on the import of Canadian dissolving pulp, further to which on April 11, 2014, an agreement was made to further extend the existing lease by five months to mid-May 2015.

On May 1, 2015, the customer signed a further extension for 24 months to May 1, 2017. Pursuant to this new extension, the customer has agreed to pay up to $12,000 per month over two years, at the end of which the customer has the option to purchase the asset from the Company.

As part of calculating the impact of the new lease extension, the existing net residual value of the equipment was re-assessed. The estimated value of any re-sale value or scrap value of the equipment less removal and re-sale costs was assessed as $nil and so a write-down of the $139,530 net residual value was taken. This write-down, combined with the write-down of the May 2015 expected payment under the terms of the previous lease, which was expected to expire in mid-May 2015, reduced the net revenue recognized on renewal of the lease to $69,791.

Until the expiry of the new lease on May 1, 2017, finance revenue will be recognized within the income statement at the interest rate implicit in the lease.

The estimated minimum lease payments receivable in this lease represent the estimated monthly energy outputs of the leased asset and are based on assumptions regarding the efficiency of the asset and the operations of the plant in which it is located.

Future estimated minimum lease payments receivable, and expected residual value of equipment at the end of the lease, under the sales-type lease are as follows:

	$
Less than one year	137,054
Between two and five years	125,054
Residual value of equipment	-
	262,108

Related Party Transactions

Options outstanding for Directors (excluding the CEO) as at May 31, 2015 were 1,500,000 of which 1,083,333 were exercisable. There were no warrants outstanding for Directors.

Options outstanding for Senior Management (including the CEO) as at May 31, 2015 were 11,159,470 of which 6,245,537 were exercisable. There were no warrants outstanding for Senior Management.

Directors and Senior Management Compensation

During the year ended May 31, 2015 compensation arrangements for directors was as follows:

$15,000 per annum per Director plus an additional $9,000 per annum payable to the Chairman of the Board, $6,000 per annum payable to the chairperson of the Audit Committee, $6,000 per annum payable to the chairperson of the Ethics, Governance and Compliance Committee and $1,000 payable for each in-person meeting.

During the year ended May 31, 2015, Directors fees paid were $90,041. Fees to the Chairperson of the Audit Committee were $6,000; fees to the Chairperson of the Ethics, Governance and Compliance Committee were $3,417, fees paid to the Chairman were $9,000; and a total of $22,000 was paid for in-person meetings.

Compensation paid to directors and officers during the year ended May 31, (inclusive of the amounts described above but excluding stock based compensation) was as follows:

	Salaries and fees		Incentives		Other short-term benefits		Total	
	2015 $	2014 $	**2015 $**	2014 $	**2015 $**	2014 $	**2015 $**	2014 $
Directors								
M. Williams	**25,000**	28,000	**-**	-	**-**	-	**25,000**	28,000
J. Kelly	**28,000**	31,000	**-**	-	**-**	-	**28,000**	31,000
D. Gibbs (resigned November 6, 2014)	**6,500**	19,000	**-**	-	**-**	-	**6,500**	19,000
W. Ollerhead	**19,000**	21,000	**-**	-	**-**	-	**19,000**	21,000
B. Linton	**21,417**	19,000	**-**	-	**-**	-	**21,417**	19,000
J. Schoenmakers	**19,000**	19,000	**-**	**-**	**-**	**-**	**19,000**	19,000
D. Spagnolo (appointed November 6, 2014)	**11,541**	-					**11,541**	-
Total	**130,458**	137,000	**-**	-	**-**	-	**130,458**	137,000
Senior Management								
W. Crossland	**240,000**	240,000	**-**	51,917	**3,783**	3,705	**243,783**	295,622
J. Flynn	**156,488**	142,661	**-**	28,285	**24,266**	26,439	**180,754**	197,385
R. Triebe	**153,699**	149,220	**-**	28,285	**7,426**	7,176	**161,125**	184,681
S. Mawby	**153,650**	140,075	**-**	28,285	**23,791**	26,005	**177,441**	194,365
M. Francoeur	**117,243**	111,395	**-**	28,285	**4,849**	4,289	**122,092**	143,969
I. Wales (appointed June 1, 2014)[1]	**66,450**	-	**-**	-	**10,649**	-	**77,099**	-
G. Bailey (left Jan 2014)	**-**	89,931	**-**	-	**-**	11,831	**-**	101,762
Total	**887,530**	873,282	**-**	165,057	**74,764**	79,445	**962,294**	1,117,784
Total Related Party Transactions	**1,017,988**	1,010,282	**-**	165,057	**74,764**	79,445	**1,092,752**	1,254,784

Other short-term benefits include cash payments for social security costs, employee benefits, and payments made into defined contribution pension plans of the Company's UK based subsidiaries.

(1) Isobel Wales was on maternity leave between November 10, 2014 and May 31, 2015

Normal Course Issuer Bid

On October 30, 2014, the Company announced its intent to continue its Normal Course Issuer Bid ("NCIB") for a further year. The NCIB was approved by the TSX Venture Exchange on November 3, 2014. During the 12-month period commencing November 3, 2014 and ending November 3, 2015, the Company may purchase on the TSX up to 13,018,133 common shares, representing approximately 8% of the then issued and outstanding common shares. The actual number of common shares purchased, if any, and the timing of such purchases will be determined by the Company by considering market conditions, share prices, its cash position, and other factors.

In the year ended May 31, 2015 the Company purchased 2,012,000 common shares for a total purchase price of $195,366.

Segmented Information

In the years ended May 31, 2015 and May 31, 2014, the Company operated in the energy efficiency industry in North America, Europe, China and the rest of the world. The Company markets, sells, engineers, fabricates, constructs, installs and supports two technology lines – heat recovery solutions and condensate return system solutions. The Company is also developing a third technology line - low temperature biomass drying systems. Assets are located in Canada, Europe and China.

Management reporting comprises analysis of revenue and gross profit by product segment within two distinct geographical areas. All other items of revenue and expenses are considered on a geographical and/or global basis in making strategic decisions regarding the Company's future. The Company has two operational bases ("reporting units"), one in Canada covering North America and China, and the other in Bristol, United Kingdom, covering Europe and the rest of the world. These areas are determined by proximity of the region to the reporting unit, plus the location of the contracts in existence with agents and distributors in the respective areas and the historical relationships with those agents and distributors. Corporate costs that cannot easily be attributed to either of the two reporting units are included in reconciling items. The chief operating decision maker focuses on revenues and costs by geographical segments, but manages assets and liabilities on a global basis.

Segment information for the year ended May 31, 2015 and the comparative period are detailed in the table below.

	North America and China		Europe and Rest of World		Reconciling Items		Total	
	2015 $	2014 $	**2015 $**	2014 $	**2015 $**	2014 $	**2015 $**	2014 $
Total revenue from external customers	**3,084,773**	6,487,172	**3,715,419**	6,663,638	–	–	**6,800,192**	13,150,810
Cost of sales	**(1,906,068)**	(3,595,556)	**(1,266,019)**	(2,581,634)	–	–	**(3,172,087)**	(6,177,190)
Gross profit	**1,178,705**	2,891,616	**2,449,400**	4,082,004	–	–	**3,628,105**	6,973,620
Amortization of intangible assets	–	–	–	(8,303)	–	–	–	(8,303)
Other expenses	**(2,187,433)**	(2,336,212)	**(2,730,051)**	(2,861,207)	**(1,088,955)**	(1,193,157)	**(6,006,439)**	(6,390,576)
Finance revenue	**60,063**	133,678	–	–	–	–	**60,063**	133,678
Income (loss) before taxation	**(948,665)**	689,082	**(280,651)**	1,212,494	**(1,088,955)**	(1,193,157)	**(2,318,271)**	708,419
Tax (expense) recovery	**(7,223)**	(8,662)	**123,364**	(90,672)	**47,313**	24,938	**163,454**	(74,396)
Profit (loss) after taxation	**(955,888)**	680,420	**(157,287)**	1,121,822	**(1,041,642)**	(1,168,219)	**(2,154,817)**	634,023
Attributable to:								
Owners of the parent	**(948,484)**	685,743	**(161,259)**	1,109,472	**(1,041,642)**	(1,168,219)	**(2,151,385)**	626,996
Non-controlling interest	**(7,404)**	(5,323)	**3,972**	12,350	–	–	**(3,432)**	7,027

Reconciling items comprise the following:

	2015 $	2014 $
Corporate administration costs	**739,006**	874,646
Stock-based compensation	**229,298**	120,824
Professional fees	**138,091**	137,465
Depreciation of property, plant and equipment	**36,077**	38,401
Bank charges and interest	**39,390**	44,921
Foreign exchange differences	**(92,907)**	(23,100)
Total	**1,088,955**	1,193,157

Corporate administration costs include directors' fees, all costs relating to both the CEO and CFO, directors and officers insurance, corporate legal costs, public relations costs, professional fees relating to group tax planning and corporate filing costs as well as the Annual General Meeting.

During the year ended May 31, 2015, the Company had one customer in North America and China that accounted for 14.4% of total revenue for the year.

During the year ended May 31, 2014, the Company had one customer in North America and China that accounted for 25.7% and one customer in Europe and Rest of World that accounted for 9.9% of total revenue for the year.

Further geographical analysis:

	Sales for the year ended May 31,		Property, plant and equipment as at May 31,		Goodwill and intangibles assets as at May 31,		Finance lease receivable (non-current) as at May 31,	
	2015	2014	**2015**	2014	**2015**	2014	**2015**	2014
	$	$	**$**	$	**$**	$	**$**	$
Canada	**459,545**	3,480,287	**46,260**	48,964	–	–	**116,560**	139,530
U.S.A.	**2,618,679**	2,985,040	–	–	–	–	–	–
U.K.	**2,662,359**	5,731,390	**16,103**	13,626	**2,049,617**	1,959,270	–	–
Italy	**286,038**	336,648	–	–	–	–	–	–
Netherlands	**107,405**	109,127	–	–	–	–	–	–
Ireland	**54,838**	105,925	–	–	–	–	–	–
Germany	**197,956**	67,761	–	–	–	–	–	–
Rest of Europe	**36,636**	13,695	–	–	–	–	–	–
India	**113,959**	203,583	–	–	–	–	–	–
Kenya	**115,320**	70,258	–	–	–	–	–	–
China	**6,549**	21,846	–	–	–	–	–	–
Rest of world	**140,908**	25,250	–	–	–	–	–	–
Total	**6,800,192**	13,150,810	**62,363**	62,590	**2,049,617**	1,959,270	**116,560**	139,530

Material Segmentation Variances

Revenue

North America and China: revenue for the year ended May 31, 2015 was $3,084,773 compared to $6,487,173 for FY 2014. Heat recovery revenue decreased by $2,895,374. FY 2014 included revenue from projects at two sites of a major Fortune 500 food and beverage company, as announced September 16, 2013, plus the substantial completion of an installation at a major pulp and paper company as announced June 3, 2013. Although FY 2015 included one further site conversion of the same major Fortune 500 food and beverage company, as announced August 27, 2014, plus the substantial completion of an installation at a site of another food producer, as announced January 26, 2015, there was no replacement for the pulp and paper company project of the previous year. Revenue from sales of GEM™ products meanwhile decreased by $507,026, again due to a lower number of larger orders. Towards the latter part of the year, negotiations were in progress with two multi-site organizations for contracts for the supply of steam traps, however these were not completed in time to have any effect on FY 2015 revenues.

Europe and the rest of the world: revenue for the year ended May 31, 2015 was $3,715,419 compared to $6,663,637 for the previous year. Heat recovery revenue decreased by $2,142,989 in FY 2015, which saw no hospital conversions compared to three installations in FY 2014. Revenue from sales of GEM™ products meanwhile decreased by $805,229 from FY 2014, which included our largest GEM order to date from a major food and beverage manufacturer, as announced July 3, 2013 as well as three hospital conversions. In contrast, other than revenues generated from repeat business from a leading chemicals company, FY 2015 revenues saw no major projects, including hospital conversions, although it did see an increase in smaller projects throughout the region. The past year has seen changes to energy management within many hospitals in the UK in particular, with many health trusts enlisting energy management companies, either in the assessment of projects or in the overall management of energy efficiency within the trust. Although this is not expected to affect the success of our proposals, it has meant a delay in the turnaround of existing proposals, which have to effectively be re-presented to a new set of buyers, which negatively affected revenues from this customer base in FY 2015

Segment Income (loss) Before Tax

North America and China: Gross profit decreased by $1,712,911 in FY 2015 from the previous year. As a percentage of revenue, gross profit was 38.2% in FY 2015, lower than the 44.6% achieved in FY 2014. This decrease was due to FY 2015 including two projects which were specifically costed to encourage customers to agree to trials with the aim of proving the technology and as a result ultimately receiving further orders for their other sites. Other expenses in the region decreased by $148,779 (6.4%), representing a drop in commissions payable and profit related incentive, partially offset by increased sales staff costs. With finance revenue decreasing by $73,615 as the existing lease reached its expiry, the resulting segment loss before tax of $948,665 represented a fall of $1,637,747 from the previous year.

Europe and the rest of the world: gross profit decreased in the year ended May 31, 2015 from the previous year by $1,632,604, as a result of the decreased revenues, although gross profit as a percentage of revenue increased from 61.3% to 65.9% due to product split. A decrease in other expenses of $139,459 (4.9%) was again the result of a drop in commissions payable and profit related incentive, partly offset by increased sales staff costs. The resulting pre-tax loss of $280,651 compared to income of $1,212,494 for the prior year, a drop of $1,493,145.

Other expenses within Reconciling items, which incorporates all costs not specifically attributable to either regional operational center, decreased in FY 2015 from the prior year by $104,202. An increase in stock based compensation expense was more than offset by the lack of profit related incentive or professional fees relating to tax planning advice expensed in FY 2014.

Selected Annual Information

The following table shows selected consolidated financial data for the three most recently completed financial years.

Financial information for the years ending May 31, 2013, 2014 and 2015

	2013 $	2014 $	2015 $
Revenue	8,210,234	13,150,810	6,800,192
Gross Profit	4,977,452	6,973,620	3,628,105
Gross Profit Percentage	60.6%	53.0%	53.4%
EBITDAS(1)	(435,049)	879,244	(2,048,552)
Total net income (loss) attributable to owners of the parent	(2,825,023)	626,996	(2,151,385)
Net profit (loss) per share – basic and diluted	(0.017)	0.004	(0.013)
Total assets	6,032,496	7,445,964	5,896,865
Total long term financial liabilities	0	0	0
Cash dividends declared per share	0.00	0.00	0.00
Adjusted operating cash flow(2)	(1,384,259)	1,349,123	(1,404,427)

(1) EBITDAS represents earnings before interest, taxation, depreciation, amortization, impairment of goodwill and other intangible assets, share-based compensation expense and net write down of lease.
(2) Adjusted operating cash flow represents net income (loss) plus items not involving cash, plus lease payments received.

A reconciliation of Net income (loss) to EBITDAS is shown below:

	2013 $	2014 $	2015 $
Total net income (loss) attributable to owners of the parent	(2,825,023)	626,996	(2,151,385)
Total net income (loss) attributable to non-controlling interest	(23,799)	7,027	(3,432)
Interest paid	3,982	4,750	4,473
Interest received	(54)	(1,453)	(129)
Taxation	(192,050)	74,396	(163,454)
Depreciation	45,623	38,401	36,077
Amortization	98,295	8,303	-
Impairment of goodwill and intangible assets	2,305,000	-	-
Share based compensation	152,977	120,824	229,298
Net investment in finance lease	-	-	-
EBITDAS	(435,049)	879,244	(2,048,552)

FY 2015 saw a 48% drop in revenue, with a corresponding 48% decrease in gross profit to $3,628,105. Sales to hospitals fell drastically in the current year, with no entire heat recovery conversions or GEM™

installations being recorded. In the UK, a number of expected projects have been delayed due to the increased use of third parties to review and often manage energy reduction programs on behalf of the estates departments. This was a major contributory factor in the drop in both heat recovery and GEM sales, and consequently gross profit, in FY 2015. Despite lower commissions payable and no staff incentive due in the current year, other expenses were just 5% less than in FY 2014 due to increased costs relating to the extra sales and marketing staff added towards the end of FY 2014. Total assets fell in FY 2015 by $1,549,099, predominantly as a result of the decreased cash balance due to the performance in the year. The decrease in finance lease receivable was partially offset by increases in trade receivables and deferred tax assets.

In FY 2014, despite revenues just falling short of the previous record set in the year ended May 31, 2012, gross profit was $1,325,249 greater than in FY 2012 due in part to greater GEM revenues and in part to improved margins on heat recovery projects, which were also better than in FY 2013. FY 2014 saw six substantially complete installations of heat recovery systems compared to four in FY 2013. Although GEM sales to hospitals remained consistent from last year, the company enjoyed increases across all regions, partly due to orders received from a major food and beverage manufacturer, as announced July 3, 2013; a global premium beer company, as announced February 10, 2014; a global diversified healthcare company, as announced February 18, 2014 and May 12, 2014; and a Fortune 500 food and beverage company, as announced September 13, 2013, and partly due to the strengthening of the North American sales force as well as increased sales from agents and distributors within the rest of the world. Other expenses increased mainly due to additional commissions on the increased revenues, plus recruitment costs and travel expenses of additional sales and marketing staff, as well as staff incentive, for which there was no cost last year due to the losses made. Total assets increased during the year by $1,413,468, mainly resulting from increases in cash and trade receivables which were pushed up by GEM despatches at the end of FY 2014.

In FY 2013, revenues fell by $4,942,453 from the previous year, mainly due to the Fibrek project and the St. George NHS project which, combined, provided $7,797,215 in FY 2012. That said, the year saw three major hospitals ordering heat recovery systems, matching the number of sites in the previous year, plus the extension of the Greenpower Purchase Agreement contributed $1,561,998 towards revenue, with very little associated cost. Although revenue fell by $4,942,453, gross profit only decreased by $670,919 due to the profit recognized with respect to the Greenpower Purchase Agreement extension. This meant an improvement on gross profit as a percentage of revenues from 42.9% in FY 2012 to 60.6% in FY 2013. Other expenses increased mainly as a result of increased staff numbers plus the impairment charges relating to goodwill and other intangible assets. Total assets decreased by $3,941,659 during FY 2013, due mainly to cash received from outstanding Fibrek invoices as at May 31, 2012 being used to settle outstanding liabilities relating to Fibrek, as well as tax liabilities relating to FY 2012 and other accrued payments, plus the reduction in goodwill and other intangible assets relating to the impairment charges recorded in the year.

Quarterly financial information (unaudited)
For the eight quarters ended May 31, 2015

Quarter ended	31-May-15 $	28-Feb-15 $	30-Nov-14 $	31-Aug-14 $
Revenue	2,525,061	1,440,985	1,662,805	1,171,341
Gross Profit	1,193,821	711,906	1,019,426	702,952
Gross Profit Percentage	47.3%	49.4%	61.3%	60.0%
EBITDAS(1)	(256,642)	(647,245)	(486,557)	(658,108)
Total net income (loss)	(337,642)	(657,592)	(491,164)	(668,419)
Income (loss) per share, basic and diluted	(0.002)	(0.004)	(0.003)	(0.004)

Quarter ended	31-May-14 $	28-Feb-14 $	30-Nov-13 $	31-Aug-13 $
Revenue	4,717,007	2,897,535	4,014,145	1,522,123
Gross Profit	2,737,568	1,391,171	1,874,869	970,012
Gross Profit Percentage	58.0%	48.3%	46.7%	63.7%
EBITDAS(1)	709,637	144,664	311,366	(286,423)
Total net income (loss)	654,740	57,304	238,079	(323,127)
Income (loss) per share, basic and diluted	0.004	0.000	0.001	(0.002)

(1) EBITDAS represents earnings before interest, taxation, depreciation, amortization, share-based compensation expense and net write down of lease.

4. Business Outlook

- In June 2012, the Company received an order for approximately $562,000 from a publicly owned hospital for a heat recovery solution. This order was partially completed in FY 2013 and the customer is currently deciding on changes it may wish to be made before the project is continued. It is not yet known when this project may be completed.

- On December 1, 2014 the Company announced that it had received a purchase order valued at approximately $415,000 from a packaged foods company for the installation of a heat recovery system at one of its facilities. The order is expected to be fulfilled and revenue earned over the next six months. As at May 31, 2015, the project was one third complete.

- On January 5, 2015 the Company announced that it had received a purchase order valued at approximately $260,000 from a leading regional manufacturer of interior lining products for the construction industry for the installation of a heat recovery system at one of its facilities. The order is expected to be fulfilled and revenue earned over the next six months. As at May 31, 2015, the project was 70% complete.

- On January 29, 2015 the Company announced that it had received a purchase order for a 35% deposit toward a project valued at approximately $825,000 from a major hospital for the installation of a heat recovery system. Orders were subsequently received for the remaining 65% of the project, which is expected to be fulfilled and revenue earned over the next six months. As at May 31, 2015, the project was approximately 57% complete.

- On March 4, 2015 the Company announced that it had received a purchase order valued at approximately $656,000 from a leading dairy supplier for the installation of a heat recovery system at its facilities. The order is expected to be fulfilled and revenue earned over the next six months. As at May 31, 2015, the project was in early engineering stages and no revenue had yet been recognized.

- On April 29, 2015 the Company announced that it had received a purchase order valued at approximately $750,000 from a world leading food and beverage company for the installation of a heat recovery system at one of its sites. This represents the fifth heat recovery system order from this customer, which has also installed GEM™ traps at nine of its sites. The order is expected to be fulfilled and revenue earned over the next six months. As at May 31, 2015, the project was in the early stages and only 4% complete.

- On July 15, 2015 the Company announced that it had received a purchase order valued at approximately $335,000 from a district heating cooperative for the supply of heat recovery equipment. This is only the second time that we have sold our heat recovery equipment on its own, without installation. The order is expected to be fulfilled and revenue earned over the next six months.

- On July 27, 2015 the Company announced that it had received a purchase order valued at approximately $128,000 from a world-leading food and beverage company for the supply of GEM™ traps. The order represents the second GEM order for this particular site, which is one of nine that have been partially converted to GEM™ traps.

- On August 17, 2015 the Company announced that it had received a purchase order valued at approximately $520,000 from a world-leading diversified healthcare company for the supply of GEM™ traps. The order represents the third GEM order for this company, and is the largest GEM™ order received to date.

- The Company's order backlog as at May 31, 2015 was approximately $3.7 million. As at September 16, 2015, the Company had an order backlog of approximately $5.7 million, of which approximately $0.5 million is related to long term contracts and is not expected to be reflected in revenue within the next 12 months.

5. Summary of Outstanding Shares and Dilutive Instruments

The Company currently has the following shares and dilutive instruments outstanding:

Shares

159,264,616 class A common shares.

Options

Number of Options outstanding	Number of Options Exercisable	Exercise Price Per Share $	Expiry Date
2,250,000	**2,250,000**	**0.10**	**10-May-2016**
250,000	**250,000**	**0.10**	**12-Jul-2016**
4,340,000	**4,340,000**	**0.10**	**01-Dec-2016**
4,820,000	**3,213,334**	**0.10**	**22-Nov-2017**
3,411,000	**1,137,000**	**0.05**	**18-Nov-2018**
3,721,360	**1,240,453**	**0.10**	**28-May-2019**
250,000	**-**	**0.09**	**01-Dec-2019**
4,648,360	**-**	**0.08**	**29-May-2020**
23,690,720	**12,430,787**		

6. Critical Accounting Estimates and Changes in Accounting Standards

Critical Accounting Estimates

The preparation of financial statements in accordance with IFRS necessitates the use of management estimates, assumptions and judgment that affect reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities at the date of the financial statements. Although management reviews its estimates on an ongoing basis, actual results may differ from these estimates as confirming events occur. The following components of the financial statements depend most heavily on such management estimates, assumptions and judgment, any changes in which may have a material impact on the Company's financial condition or results of operations. For more information about certain assumptions and risks that may affect these estimates, assumptions and judgments, please see the "Forward Looking Information" section of this MD&A.

Valuation of goodwill and intangible assets and asset impairment

Goodwill and intangible assets are tested annually for impairment, or earlier if circumstances indicate an impairment.

An impairment loss is recognized for the amount by which an asset's or cash-generating unit's carrying amount exceeds its recoverable amount. To determine the recoverable amount, management estimates expected future cash flows from each asset or cash-generating unit and determines a suitable interest rate in order to calculate the present value of those cash flows. In the process of measuring expected future cash flows management makes assumptions about future operating results. These assumptions relate to future events and circumstances. The actual results may vary, and may cause significant adjustments to the Company's assets within the next financial year.

In most cases, determining the applicable discount rate involves estimating the appropriate adjustment to market risk and the appropriate adjustment to asset-specific risk factors.

Future production outputs relating to the finance lease

When a new finance lease or amendment is signed, in determining minimum lease payments receivable, management makes estimates regarding monthly energy outputs of the leased asset based on assumptions regarding the efficiency of the asset, the operations of the plant in which it is located, penalty payments resulting from temporary plant shut-downs and residual value of the equipment. These assumptions relate to future events and circumstances.

Assumptions used in the Black-Scholes fair value calculations

The estimation of share-based payment expense requires the selection of an appropriate valuation model and consideration as to the inputs necessary for the valuation model chosen. In calculating the share-based payment expense, key estimates such as the rate of forfeiture of options granted, the expected life of the option, the volatility of the Company's stock price and the risk free interest rate are used.

Revenue Recognition relating to contracts for heat recovery solutions

The stage of completion of any heat recovery solutions contract is assessed by management by taking into consideration all information available at the reporting date. In this process, management exercises significant estimate about milestones, actual work performed and the estimated costs to complete work.

Deferred tax assets

Deferred tax assets are recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable income will be available against which they can be utilized. These estimates are reviewed at every reporting date. 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 the reversal of existing differences, future taxable income and future tax planning strategies.

Changes in Accounting Standards

The Company has adopted the following new or amended accounting standards.

Amendments to IAS 32, "Financial Instruments: Presentation"

In December 2011, the IASB issued amendments to IAS 32, which clarifies the existing requirements for offsetting financial assets and financial liabilities. These amendments are effective for annual periods beginning on or after January 1, 2014, which was June 1, 2014 for the Company. The Company adopted the amendments on June 1, 2014. The adoption of the amendments to IAS 32 does not have a material impact on the consolidated financial statements.

IFRIC 21, “Levies”

In May 2013, the IASB issued IFRIC 21, Levies, which provides guidance on accounting for levies in accordance with the requirements of IAS 37, Provisions, Contingent Liabilities and Contingent Assets. The interpretation defines a levy as an outflow from an entity imposed by a government in accordance with legislation. It also notes that levies do not arise from executor contracts or other contractual arrangements. The interpretation also confirms that an entity recognizes a liability for a levy only when the triggering event specified in the legislation occurs. This IFRIC is effective for annual periods beginning on or after January 1, 2014, which was June 1, 2014 for the Company. The Company adopted the IFRIC 21 on June 1, 2014. The adoption does not have a material impact on the consolidated financial statements.

At the date of approval of the accompanying consolidated financial statements, certain new standards, amendments and interpretations to existing standards have been published but are not yet effective, and have not been adopted early by the Company. These standards will be adopted at the effective date.

Management anticipates that all of the pronouncements will be adopted in the Company’s accounting policy for the first period beginning after the effective date of the pronouncement. Information on new standards, amendments and interpretations that are expected to be relevant to the Company’s consolidated financial statements is provided below. Certain other new standards and interpretations have been issued, but are not expected to have an impact on the Company’s consolidated financial statements.

IFRS 9, “Financial Instruments”

In July 2014, the IASB issued the final version of IFRS 9, bringing together the classification and measurement, impairment and hedge accounting phases of the project to replace IAS 39, “Financial Instruments: Recognition and Measurement. IFRS 9 is applied retrospectively for annual years beginning on or after January 1, 2018. Early application is permitted. The Company does not intend to adopt this standard early and is currently evaluating the impact of adopting this standard on the consolidated financial statements.

IFRS 15, “Revenue from Contracts with Customers”

In May 2014, the IASB issued IFRS 15, “Revenue from Contracts with Customers”, which provides a single, principles-based five-step model for revenue recognition to be applied to all customer contracts, and requires enhanced disclosures. This standard is effective January 1, 2017 and allows early adoption. The Company does not intend to adopt this standard early and is currently evaluating the impact of adopting this standard on the consolidated financial statements.

7. Risk Factors and Risk Management

Management is confident about our long-term prospects, but does recognize that the company is exposed to a number of risks in the normal course of business that could negatively impact the financial condition of the Company.

Operational risks of the company include the ability to continue to secure and implement sales contracts for its GEM™ and FLU-ACE® technology solutions.

Financial risks and uncertainties of the Company include:

- The Company’s history of operating losses and uncertainty of future profitability;
- The ability to grow sales through the establishment of new cooperative partnerships and strategic alliances;
- The ability to grow sales through the licensing of the corporation’s technologies;
- The ability to secure and maintain the required outside working capital financing;
- The ability to achieve profitable operations through increased sales,
- Reliance on third party collaborations and license arrangements;
- Reliance on proprietary technology;
- Competition in the energy conservation and environmental compliance solutions;

- Product liability claims and insurance;
- Reliance on key personnel;
- The ongoing litigation with its former President & CEO;
- The ability to control costs and achieve a positive gross margin on projects; and,
- The effect of a continuing prolonged recession in Canada, USA and Europe to the financial markets in securing project financing and in particular to industrial and commercial customers in committing capital to projects.

Management's addressing of the risks:

FY 2012 saw the Company's first ever net profit, which was the result of increased revenues and strict cost control. FY 2013, however, produced an operating loss of $844,328, resulting from diminished revenues and increasing costs. Despite further cost increases as management continue to build the sales force, FY 2014 produced the company's best ever post-tax income of $634,023 as well as an increase in cash balance of $742,022, but this was again followed by a net loss of $2,154,817, accompanied by a cash decrease of $1,331,074 in FY 2015.

The Company actively protects its proprietary technology through registered trademarks and confidentiality agreements.

The Company maintains adequate forms of general liability insurance including product liability and errors and omission coverage.

Management believes that competition against its core technology of GEM®, FLU-ACE® and DRY-REX™ is limited at this time and believes that the market place is sufficiently large enough to mitigate the risk of stronger competition in the future.

Management continues to focus on strengthening relationships with key customers, as well as securing new relationships with multi-site organizations, which is anticipated to provide repeat business into the foreseeable future. Management continually monitors costs and cash flow to ensure that the Company has sufficient funds for operations while providing for future growth.

8. Forward-Looking Information

This MD&A contains certain "forward-looking statements." All statements, other than statements of historical fact, that address activities, events or developments that the Company believes, expects or anticipates will or may occur in the future (including, without limitation, statements regarding financial and business prospects and financial outlook) are forward looking statements. These forward-looking statements reflect the current expectations or beliefs of Management, based on information currently available to the Company. Forward-looking statements are subject to a number of risks, uncertainties and assumptions that may cause the actual results of the Company to differ materially from those discussed in the forward-looking statements and, even if such actual results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on the Company. Factors that could cause actual results or events to differ materially from current expectations include, among other things, changes in general economic and market conditions, changes to regulations affecting the Company's activities, and uncertainties relating to the availability and costs of financing needed in the future. Any forward-looking statement speaks only as at the date on which it is made and, except as may be required by applicable securities laws, the Company disclaims any intent or obligation to update any forward-looking statement, whether as a result of new information, future events or results or otherwise. Although Management believes that the assumptions inherent in the forward-looking statements are reasonable, forward-looking statements are not guarantees of future performance and, accordingly, undue reliance should not be put on such statements due to the inherent uncertainty therein.

9. Management's Responsibility for Financial Reporting

In compliance with the Canadian Securities Administrators' National Instrument 52-109 ("NI 52-109"), the Company has filed with applicable Canadian securities regulatory authorities, certificates signed by its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") that, among other things, report on the design and effectiveness of disclosure controls and procedures and the design of internal controls over financial reporting.

Under the supervision of the CEO and CFO, the Company maintains systems of internal accounting and administrative controls to provide reasonable assurance that the financial information is relevant, reliable and accurate and that transactions are authorized, assets are safeguarded and proper records are maintained. Internal controls over financial reporting, no matter how well designed, have inherent limitations and may not prevent or detect all misstatements. There were no changes to the Company's internal control over financial reporting during the year ended May 31, 2015 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The Board of Directors is responsible for ensuring that management fulfills its responsibility principally through its Audit Committee.

Thermal Energy's auditors, KPMG LLP, conducted an independent audit of the consolidated financial statements for the year ended May 31, 2015, performing such tests and other procedures as they consider necessary to express an audit opinion. The external auditors have full and unrestricted access to the Audit Committee to discuss their audit and related findings.