

Condensed interim consolidated financial statements of

**Sustainable Energy  
Technologies Ltd.**

December 31, 2011

# Sustainable Energy Technologies Ltd.

December 31, 2011

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# Sustainable Energy Technologies Ltd.

## Condensed interim consolidated statements of financial position

(Unaudited)

	Note	December 31, 2011	September 30, 2011 (Note 24)	October 1, 2010 (Note 24)
		\$	\$	\$
<b>Assets</b>				
Current:				
Cash and cash equivalents		225,072	328,821	561,373
Accounts receivable and advances		981,129	1,093,381	978,192
Inventory	6	3,339,977	3,590,075	2,741,574
Prepaid expenses and deposits		75,432	212,401	601,645
		4,621,610	5,224,678	4,882,784
Non-current:				
Development costs	7	1,291,281	1,393,176	1,567,428
Capital assets	8	129,934	152,536	259,438
Other long term assets		75,152	150,303	243,783
		6,117,977	6,920,693	6,953,433
<b>Liabilities</b>				
Current:				
Accounts payable and accrued liabilities	16	1,156,201	1,641,421	2,206,264
Bank debt	17	1,121,690	1,346,662	-
Energy Northwest - current portion	9	271,366	266,268	217,826
		2,549,257	3,254,351	2,424,090
Non-current:				
Energy Northwest obligation	9	1,085,464	1,065,073	871,303
Preferred shares	12	6,468,607	5,582,607	5,242,677
		10,103,328	9,902,031	8,538,070
<b>Shareholders' equity (deficiency)</b>				
Share capital	10	34,272,067	34,258,068	30,393,463
Warrants	13	2,307,257	2,275,418	1,355,535
Equity component of preferred shares	12	3,611,283	3,184,383	2,812,455
Shared-based payment reserve	14	4,912,390	4,819,067	4,445,087
Foreign currency translation reserve		(215,587)	(171,906)	-
Deficit		(48,872,761)	(47,346,368)	(40,591,177)
		6,117,977	6,920,693	6,953,433

Going Concern (note 3) and Commitments (note 21)

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

On behalf of the Board:

\_\_\_\_\_ {signed}

Michael Carten, Director

\_\_\_\_\_ {signed}

Robert Penner, Director

# Sustainable Energy Technologies Ltd.

Condensed interim consolidated statements of loss and comprehensive loss

For the three months ended December 31,

(Unaudited)

	Note	2011	2010
		\$	(Note 24) \$
Sales		1,011,215	994,465
Cost of sales		774,589	872,512
Gross margin		236,626	121,953
Expenses			
General and administrative	19	513,728	940,105
Operations		281,170	469,319
Product research and development		221,821	630,621
Selling and marketing		211,972	155,345
		1,228,691	2,195,390
<b>Loss before undernoted items</b>		<b>(1,008,989)</b>	<b>(2,073,437)</b>
Financing costs		(544,388)	(511,245)
Interest and other		10,010	8,831
<b>Net loss</b>		<b>(1,526,393)</b>	<b>(2,575,851)</b>
Foreign currency adjustment to equity		(43,681)	54,599
<b>Total comprehensive loss</b>		<b>(1,570,074)</b>	<b>(2,521,252)</b>
<b>Loss per common share</b>			
Basic and diluted		(0.01)	(0.02)
<b>Weighted average number of common shares</b>			
Basic and diluted		200,269,944	166,078,413

*The accompanying notes are an integral part of these consolidated financial statements.*

# Sustainable Energy Technologies Ltd.

## Condensed interim consolidated statements of changes in equity

(Unaudited)

	Share capital	Share based payment reserve	Warrants	Equity component of preferred shares	Deficit	Foreign currency translation reserve	Total
	\$	\$	\$	\$	\$	\$	\$
<b>Balance, October 1, 2011</b>	34,258,068	4,819,067	2,275,418	3,184,383	(47,346,368)	(171,906)	(2,981,339)
Loss for the period					(1,526,393)		(1,526,393)
Other Comprehensive loss						(43,681)	(43,681)
Issue of share capital	13,999						13,999
Warrants issued			98,411				98,411
Warrants expired		66,572	(66,572)				-
Equity component of preferred shares				426,900			426,900
Share-based payments		26,751					26,751
<b>Balance, December 31, 2011</b>	<b>34,272,067</b>	<b>4,912,390</b>	<b>2,307,257</b>	<b>3,611,283</b>	<b>(48,872,761)</b>	<b>(215,587)</b>	<b>(3,985,351)</b>
<b>Balance, October 1, 2010</b> (note 24)	30,393,463	4,445,087	1,355,535	2,812,455	(40,591,177)	-	(1,584,637)
Loss for the period					(2,575,851)		(2,575,851)
Other Comprehensive loss						54,599	54,599
Issue of share capital	2,571,859						2,571,859
Transaction costs	(265,177)						(265,177)
Warrants issued			66,572				66,572
Equity component of preferred shares				251,270			251,270
Share-based payments		87,746					87,746
<b>Balance, December 31, 2010</b>	<b>32,700,145</b>	<b>4,532,833</b>	<b>1,422,107</b>	<b>3,063,725</b>	<b>(43,167,028)</b>	<b>54,599</b>	<b>(1,393,619)</b>

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

# Sustainable Energy Technologies Ltd.

## Condensed interim consolidated statements of cash flows

For the three months ended December 31,

(Unaudited)

	Note	2011 \$	2010 (Note 24) \$
<b>Operating activities</b>			
Net loss		(1,526,393)	(2,575,851)
Amortization of capital assets and capitalized development costs		105,706	109,882
Share-based payments		26,751	87,746
Finance costs		544,338	511,246
Unrealized foreign exchange loss (gain)		(15,195)	90,697
		(864,793)	(1,776,281)
Net change in non-cash working capital	21	88,871	(815,831)
Cash flow used in operating activities		(775,922)	(2,592,112)
<b>Financing activities</b>			
Bank loan		(224,972)	-
Proceeds on issuance of LP units		-	2,550,000
Cost of issuing LP units		-	(231,534)
Proceeds from preferred shares		1,000,000	800,000
Cost of issuing preferred shares		(36,156)	(36,382)
Cash financing costs paid		(19,962)	(5,950)
Cash flow from financing activities		718,910	3,076,134
<b>Investing activities</b>			
Capital asset additions		(14,779)	(40,304)
Cash flow from investing activities		(14,779)	(40,304)
Foreign exchange on cash and cash equivalents held in foreign operations		(31,958)	20,284
Net change in cash and cash equivalents		(103,749)	464,002
Cash and cash equivalents, beginning of period		328,821	561,373
<b>Cash and cash equivalents, end of period</b>		<b>225,072</b>	<b>1,025,375</b>
<b>Cash and cash equivalents comprised of</b>			
Cash		225,072	590,345
Term deposits at weighted average interest rate of .003%		-	435,030

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

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 1. Description of the business

Sustainable Energy Technologies Ltd (“Sustainable Energy”, “Sustainable” or the “Company”) develops and manufactures advanced power inverters for the emerging alternative and renewable energy industry - solar photovoltaic (“PV”) systems, small wind turbines, fuel cells and all forms of energy storage. The Company is a publicly traded company headquartered at 609-14th St NW, Calgary, Alberta, Canada and its shares trade on the Toronto Stock Exchange Venture Exchange “TSX-V” under the symbol “STG”.

### 2. Basis of preparation

#### (a) Adoption of new and revised standards

In conjunction with the Company’s annual audited consolidated financial statements to be issued under International Financial Reporting Standards (“IFRS”) for the year ending September 30, 2012, these condensed interim consolidated financial statements (“consolidated financial statements”) present the Company’s initial financial statements of loss and comprehensive loss and financial position under IFRS as at and for the three months ended December 31, 2011, including 2010 comparative periods. As a result, they have been prepared in accordance with IFRS 1, “First-time Adoption of International Financial Reporting Standards” and with International Accounting Standard (“IAS”) 34, “Interim Financial Reporting”, as issued by the International Accounting Standards Board (“IASB”). These consolidated financial statements do not include all the necessary annual disclosures in accordance with IFRS. Previously, the Company prepared its interim and annual consolidated financial statements in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”).

The preparation of these consolidated financial statements resulted in selected changes to the Company’s accounting policies as compared to those disclosed in the Company’s annual audited consolidated financial statements for the year ended September 30, 2011, issued under Canadian GAAP. Consequently, these consolidated interim financial statements should be read in conjunction with the Canadian GAAP annual audited consolidated financial statements for the year ended September 30, 2011.

A summary of the Company’s significant accounting policies under IFRS, which have been retrospectively and consistently applied except where specific exemptions permitted an alternative treatment upon transition to IFRS in accordance with IFRS 1, is presented in note 3 and are based on IFRS issued and effective as of December 31, 2011. Any subsequent changes to IFRS that come in effect as at September 30, 2012 could result in restatement to these consolidated financial statements, including the transition adjustments recognized on the transition to IFRS.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in note 24.

#### (b) Basis of consolidation

The consolidated financial statements of Sustainable Energy Technologies Ltd. include the accounts of the Company and its subsidiaries: Sustainable Energy Systems Inc. (“SES”), Sustainable Energy Europa S.L. (“SEE”), STG Markets Limited Partnership (“STGLP”), Sustainable Energy Laboratories Ltd. (“SEL”), International Power Systems, Inc. (“IPS”), Mainpower Hellas (MPH) and Sustainable Energy France (SEF).

All intra-Company transactions, balances, revenue and expenses are eliminated in full on consolidation.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 2. Basis of preparation (continued)

#### (b) Basis of consolidation (continued)

Subsidiaries that are directly controlled by the parent company or indirectly controlled by other consolidated subsidiaries are fully consolidated. All intercompany balances, transactions and income are eliminated. The Company currently has no special purpose entities of which it retains control and accordingly the consolidated financial statements do not include the accounts of any such entities.

#### (c) Statement of compliance

The consolidated financial statements have been prepared in accordance with IAS 34 and were approved and authorized for issuance by the Board of Directors (“the Board”) on March 29, 2012.

#### (d) Critical accounting estimates

The preparation of these consolidated financial statements requires management to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, sales and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, management bases its estimates on historical experience and other assumptions that it believes are reasonable in the circumstances. Actual results may differ from the estimates. There have been no changes made to the methodology to determine critical accounting estimates during the past two fiscal years. The following reflect the most significant estimates and assumptions used in the preparation of the Company's consolidated financial statements.

##### *i. Capital assets and development costs*

Capital assets and development costs are reviewed for impairment at least annually or when events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. To determine recoverability, management estimates the fair value less costs to sell of the asset or the asset's value in use using estimates. The value in use is determined by estimating the future cash flows projected to be generated by these assets. These cash flows are discounted using an estimated rate of return and compared to their respective carrying value. In performing this analysis, estimates and assumptions are made about factors such as current and future contracts with clients, margins, market conditions and the useful lives of assets. If estimates or assumptions change from those used in the current analysis, the Company may be required to recognize an impairment loss in future periods, which would decrease capital assets or development costs and increase reported expenses.

##### *ii. Valuation adjustments for inventory*

Valuation adjustments for inventory related assets are comprised of the impairments or recoveries recorded against inventories. The Company records valuation adjustments for inventory related assets by comparing the inventory cost to its net realizable value. This process requires the use of estimates and assumptions related to future market demand, costs and prices. Such assumptions are reviewed quarterly and have a significant impact on the valuation adjustments for inventory.

##### *iii. Share-based payment transactions*

Share-based payments comprise compensation expense related to the granting of stock options and warrants. The Company values stock option expense and warrants using a fair value-based method of accounting. The fair value of stock options and warrants is estimated at the grant or issue date using the Black-Scholes option pricing model (the “model”) or the fair value of services received in the case of warrants. The model requires the input of a number of assumptions, including expected dividend yield, expected stock price volatility, expected time until exercise, forfeiture rate, and risk-free interest rates.



# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 2. Basis of preparation (continued)

#### (d) Critical accounting estimates (continued)

##### iii. *Share-based payment transactions (continued)*

Certain assumptions such as expected stock price volatility, forfeiture rate and expected time until exercise are determined using management's best estimates and involve inherent uncertainties relating to market conditions, forfeitures and exercise which are outside of the control of the Company. Such assumptions are reviewed quarterly and have a significant impact on the estimates of fair value produced by the Black-Scholes option pricing model.

##### iv. *Recoverability of accounts receivable*

Accounts receivable includes amounts due from customers invoiced for the shipment of products or achievement of invoicing milestones. The Company, in the normal course of business, submits credit applications to the Export Development Corporation (EDC) for accounts receivable insurance approval. Clients who do not qualify for EDC credit are treated on a cash only basis.

##### v. *Preferred shares*

Preferred shares are comprised of a debt and equity component. The Company determines the fair values of the debt component at inception by using discounting the cash flows at the estimated market interest rate at that time. This method requires the input of a number of assumptions, including the estimated market rate of interest and the timing of any payment of dividends. These assumptions are determined using management's best estimates and involve inherent uncertainties are reviewed quarterly and have a significant impact on the estimates of fair value of the debt component of the preferred shares.

##### vi. *Fair value of financial instruments*

The Company is required to determine the fair value of its bank debt, Energy Northwest obligation and preferred shares. In determining the fair value of the Company's outstanding preferred shares, management uses internally developed models, which incorporate estimated market rates. In determining market rates, management adds a credit spread to quoted rates on Canadian government bonds with similar maturity dates to the Company's preferred shares. Estimates of market rates and the credit spread applicable could vary and result in a different disclosed fair value.

##### vii. *Income taxes*

The Company carries on business in several countries and as a result, is subject to income taxes in numerous jurisdictions. The determination of income tax is inherently complex and the Company is required to interpret continually changing regulations and make certain estimates and assumptions about future events. While income tax filings are subject to audits and reassessments, the Company believes it has adequately provided for all income tax obligations. However, changes in facts and circumstances as a result of income tax audits, reassessments, jurisprudence and any new legislation may result in an increase or decrease in the provision for income taxes.

##### viii. *Commitments, Contingencies and Guarantees*

By their nature, contingencies will only be resolved when one or more future events transpire. The assessment of contingencies inherently involves estimating the outcome of future events.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 2. Basis of preparation (continued)

#### (e) Critical accounting judgments

In applying the Company's accounting policies, management has made certain judgments that may have a significant effect on the amounts recognized in the financial statements. Such judgments include the determination of the functional currency.

### 3. Going concern

The consolidated financial statements were prepared on a going concern basis. The going concern basis assumes that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

At December 31, 2011, the Company had not yet achieved profitable operations since its inception and accumulated a deficit of \$48,872,761 (2010 - \$43,167,028) and recognized a cash flow deficiency from operations at December 31, 2011 of \$775,922 (2010 - \$2,592,112). Whether and when the Company can attain profitability and positive cash flows is uncertain. Although the lack of profitable operations and cash flow deficiency may cast significant doubt on the Company's ability to continue as a going concern, the Company had a working capital surplus of \$2,072,353 at December 31, 2011 (2010 - \$3,752,724).

The ability to continue as a going concern is dependent on completing equity or debt financings or generating profitable operations in the future in order to meet liabilities as they come due and enable the Company to continue operations. The ability to continue as a going concern may be adversely impacted by any accelerating loss of customers and any falling sales per customer. To address its financing requirements, the Company will seek financing through the issuance of common shares, First Preferred Shares and Units of STG Markets Limited Partnership. The outcome of these matters cannot be predicted at this time.

These consolidated financial statements do not include any adjustments which could be significant to the amounts and classification of assets and liabilities that may be necessary should the Company be unable to obtain equity or debt financings or generating profitable operations in the future. Failure to continue as a going concern would require the restatement of assets, liabilities and shareholders' deficiency on a liquidation basis, which could differ materially from the going concern basis.

Management has also made significant estimates under the going concern assumption (see "critical accounting estimates"). These consolidated financial statements do not give effect to adjustments, if any, that may be necessary should the Company be unable to continue as a going concern.

### 4. Significant accounting policies

The significant accounting policies are set out below. All dollar amounts are expressed in Canadian dollars unless otherwise noted.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies

##### (a) Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument to another. Upon initial recognition all financial instruments, including derivatives, are recognized on the statement of financial position at fair value. Subsequent measurement is then based on financial instruments being classified into one of the following five categories: 1) loans and receivables, 2) assets held-to-maturity, 3) assets available-for-sale, 4) other financial liabilities, and 5) fair value through profit or loss. Financial instruments classified as fair value through profit or loss or available-for-sale items as a result of initially adopting this section are measured at fair value. Gains or losses on subsequent measurement of fair value through profit or loss are recognized in net income (loss), while gains and losses on subsequent measurement of available-for-sale items are recognized as an adjustment to other comprehensive income (loss).

At December 31, 2011, the Company's financial instruments include cash and cash equivalents, accounts receivable and advances, accounts payable and accrued liabilities, bank debt, Energy Northwest obligation and preferred shares. Cash and cash equivalents are measured at fair value consistent with the "fair value through profit or loss" classification. Net gains and losses arising from changes in fair value are recognized in net income upon derecognition or impairment. Accounts receivable and advances and other long term assets are measured at amortized cost consistent with the "loans and receivables" classification. Loans and receivables are subsequently measured at their amortized cost, using the effective interest method. Under this method, estimated future cash receipts are discounted over the asset's expected life, or other appropriate period, to its net carrying value. Accounts payable and accrued liabilities, bank loan, Energy Northwest obligation and preferred shares are measured at amortized cost using the effective interest method, consistent with the "other financial liabilities" classification. Equity instruments are recorded at the proceeds received with direct issue costs deducted.

Embedded derivatives are separated from the host contract and accounted for separately when all three of the following conditions are met: i) the economic characteristics and risks of the host contract and the embedded derivative are not closely related; ii) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and iii) the hybrid instrument is not measured at fair value with changes in fair value recognized in profit or loss. Changes in the fair value of the separated embedded derivative are recognized immediately in the statement of comprehensive income (loss).

The Company has an embedded derivative related to the Company's ability to redeem each series of preferred shares if certain conditions exist. The estimated value of this embedded derivative at December 31, 2011 is nil.

On initial recognition, the preferred shares were classified into debt and equity components at fair value. Subsequent to the initial recognition, the liability component is remeasured at amortized cost using the effective interest rate method. The equity component is not remeasured subsequent to initial recognition.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies (continued)

##### (a) Financial instruments (continued)

The effective interest method is a method of calculating the amortized cost of a financial asset/liability and of allocating interest income/expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash flows (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset/liability, or, where appropriate, a shorter period. Transaction costs are comprised primarily of legal, accounting, underwriters' fees and other costs directly attributable to the issuance of the financial instruments.

##### (b) Foreign currencies

###### *i. Foreign currency transactions*

The consolidated financial statements are prepared in Canadian dollars, which is the Company's functional currency. Transactions in foreign currencies are initially recorded at the functional currency spot rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency prevailing rate of exchange at the reporting date. Non-monetary items that are measured in terms of historical cost in foreign currency are translated using the prevailing exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

###### *ii. Foreign operations*

The assets and liabilities of foreign operations are translated to Canadian dollars at exchange rates at the reporting date. Foreign currency differences are recognized and presented in other comprehensive income (loss) and in the foreign currency translation reserve in equity.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign exchange gain and losses net of tax arising from those items are considered to form part of a net investment in a foreign operation and are recognized in other comprehensive income (loss) and presented in the translation reserve in equity.

On disposal of a foreign operation, any cumulative exchange differences held in equity and arising after the date of transition to IFRS are transferred to the consolidated statement of comprehensive income (loss) as part of the profit or loss on sale.

##### (c) Inventory

Inventories are stated at the lower of cost or net realizable value. Inventory is valued on a weighted average cost basis. Net realizable value represents the estimated selling price for inventories less all estimated costs necessary to make the sale. The reversal of previous net realizable value write-downs is recorded when there is a subsequent increase in the value of inventory.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies (continued)

##### (d) Capital assets

Capital assets other than capitalized product development costs are stated in the consolidated statement of financial position at cost less accumulated amortization, impairment losses and government grants. Amortization is charged so as to write off the cost of assets, other than land, over their estimated useful lives, using the straight-line method. Amortization is charged once an asset is determined to be available for use. The estimated useful lives, residual values and amortization method are reviewed at each year end, with the effect of any changes in estimates accounted for on a prospective basis.

Assets held under finance leases are amortized over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

Amortization is charged over the estimated useful life of the asset at the following rates:

Furniture and equipment	5 years straight-line
Computer equipment	3 years straight-line
Computer software	1 year straight-line
Lab equipment	3 to 5 years straight-line
Dies and molds	1 year straight-line

The gain or loss arising on the disposal of capital assets is determined as the difference between the sales proceeds and the carrying amount of the asset, and is recognized in profit or loss.

##### (e) Research and development costs

Expenditures on research activities are recognized as an expense in the period in which they are incurred.

Internally-generated intangible assets arising from development (or from the development phase of an internal project) are recognized if, and only if, all of the following have been demonstrated:

- The technical feasibility of completing the intangible asset so that it will be available for use or sale;
- The intention to complete the intangible asset and use or sell it;
- The ability to use or sell the intangible asset;
- How the intangible asset will generate probable future economic benefits;
- The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and
- The ability to measure reliably the expenditures attributable to the intangible asset during its development.

The amount initially recognized for internally-generated intangible assets is the sum of the expenditures incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally-generated intangible asset can be recognized, development expenditures are charged to statement of comprehensive income (loss) in the period in which they are incurred.

Subsequent to initial recognition, internally-generated intangible assets are reported at cost less accumulated amortization and impairment losses.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies (continued)

##### (f) Impairment of capital assets and development costs

At each balance sheet date, the Company reviews the carrying amounts of its capital assets and development costs to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit ("CGU") to which the asset belongs. The recoverable amount is the higher of the fair value less costs to sell of the asset or the asset's value in use using estimates. The value in use is determined by estimating the future cash flows projected to be generated by these assets on a pre-tax basis. These cash flows are discounted at a rate reflecting the estimated time value of money and risk associated with the asset or CGU.

If the recoverable amount of an asset or CGU is estimated to be less than its carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset or CGU in prior years. A reversal of an impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

##### (g) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. All other borrowing costs are recognized in profit or loss in the period in which they are incurred.

##### (h) Government grants

Government grants are utilized to fund the various research and development technologies of the Company. Government grants are not recognized until there is reasonable assurance that the Company will comply with the conditions of the grant and that the grant will be received.

Government grants, including contingently repayable government grants, whose primary condition is that the Company should purchase, construct or otherwise acquire non-current assets are recorded as a deduction of the cost of the asset and transferred to profit or loss on a systematic and rational basis over the useful lives of the related assets. Other government grants, including contingently repayable government grants, are recognized as a reduction of the expense over the periods necessary to match them with the costs for which they are intended to compensate, on a systematic basis. Contingent government grant repayments will be shown as a government contribution repayment expense when incurred.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 4. Significant accounting policies (continued)

#### (i) Provisions and contingencies

##### *i. Provisions*

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

##### *ii. Contingencies*

When a contingency is substantiated by confirming events, can be reliably measured and will likely result in an economic outflow, a liability is recognized in the financial statements as the best estimate required to settle the obligation. A contingent liability is disclosed where the existence of an obligation will only be confirmed by a future event, or where the amount of a present obligation cannot be measured reliably or will likely not result in an economic outflow. Contingent assets are only disclosed when the inflow of economic benefits is probable. When the economic benefit becomes virtually certain, the asset is no longer contingent and is recognized in the financial statements.

#### (j) Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. Finance leases are capitalized at commencement of the lease term at the lower of the fair value of the leased asset or the present value of the minimum lease payments. Capitalized leased assets are amortized over the shorter of the estimated useful life of the assets and the lease term. Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognized immediately in profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the Company's general policy on borrowing costs. All other leases are classified as operating leases.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except when another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. The aggregate benefit of incentives is recognized as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

#### (k) Share-based payments

Share-based payments are comprised of stock option awards granted to employees, directors and others which are equity-settled share-based payments.

These equity-settled share-based payments are measured at the fair value of the equity instruments and are recognized as an employee expense with the offsetting credit as an increase to the share-based payment reserve.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies (continued)

##### (k) Share-based payments (continued)

The fair value is measured at the grant date using the Black-Scholes options pricing model based on terms and conditions upon which the options were granted. Each tranche is recognized on a graded vesting basis over the period during which the options vest. At each balance sheet date, the Company revises its estimate of the number of equity instruments expected to vest as a result of the effect of non market based vesting conditions. The impact of the revision of the original estimates, if any, is recognized in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the share-based payment reserve.

Upon exercise of the share purchase option, the Company issues new shares. The associated fair value amount is reclassified from the share-based payment reserve to share capital. The proceeds received net of any directly attributable transaction costs are credited to share capital when the options are exercised.

##### (l) Revenue recognition

Revenue from product sales is generally recognized on shipment to the customer and when reasonable assurance exists regarding the measurement and collection of the consideration received. There may be instances where customers will request that the Company "bill and hold" their shipments until such time as the customers are prepared to receive the shipment. In these cases, revenue is recognized when the customer is invoiced for the goods which have been packaged and made ready for shipment, the risk of ownership is with the customer, and the terms and when reasonable assurance exists regarding the measurement and collection of the consideration received.

Engineering fee revenue is recognized when the service is performed. Licensing fee revenue is recognized when the Company has fulfilled all its obligations under the terms of the operative licensing agreement. In all cases no revenue would be recognized in circumstances where collection is not reasonably assured.

##### (m) Income taxes

Income taxes are recognized in the statement of comprehensive income (loss), except where they relate to items recognized in other comprehensive income (loss) or directly in equity, in which case the related taxes are recognized in other comprehensive income (loss) or equity. Taxes on income in interim periods are recorded using the tax rate that would be applicable to expected annual income. Annual taxes are recorded using the tax rate that has been enacted or substantively enacted by the balance sheet date.

Deferred tax assets and liabilities are recognized based on unused tax losses and tax credits and the difference between the tax and accounting values of assets and liabilities and are calculated using enacted or substantively enacted tax rates for the periods in which the unused tax losses and tax credits and differences are expected to reverse. The effect of tax rate changes is recognized in earnings or equity, as the case may be, in the period of substantive enactment.

Deferred tax assets are recognized only to the extent that it is probable that future taxable profits will be available against which the assets can be utilized.



# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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#### 4. Significant accounting policies (continued)

##### (m) Income taxes

Deferred tax liabilities are recognized for taxable temporary differences arising on investments in subsidiaries, joint ventures and associates. However, the Company does not recognize such deferred tax liabilities where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

The Company is subject to assessments by various taxation authorities that may interpret tax legislation differently. The final amount of taxes to be paid depends on a number of factors including the outcomes of audits, appeals, or negotiated settlements. The Company accounts for such differences based on its best estimate of the probable outcome of these matters.

##### (n) Loss per share

The Company computes basic loss per share using net income attributable to Sustainable shareholders divided by the weighted-average number of common shares outstanding. The company does not compute diluted earnings per share as this calculation would be anti-dilutive.

#### 5. Future accounting pronouncements

The Company has reviewed new and revised accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on the Company:

##### *IFRS 9 "Financial Instruments - Classification and Measurement"*

As of January 1, 2013, the Company will be required to adopt IFRS 9, "Financial Instruments", which is the result of the first phase of the IASB's project to replace IAS 39, "Financial Instruments: Recognition and Measurement". The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. The adoption of this standard is not expected to have a material impact on Sustainable's consolidated financial statements.

##### *IFRS 10 "Consolidated Financial Statements"*

On May 12, 2011, IFRS 10 - "Consolidated Financial Statements" was released and will be effective January 1, 2013 for the Company. The Company is currently evaluating the impact the adoption of this pronouncement will have on the consolidated financial statements.

##### *IFRS 13 "Fair Value Measurement"*

On May 12, 2011, IFRS 13 - "Fair Value Measurement" was released and will be effective January 1, 2013 for the Company. The Company is currently evaluating the impact the adoption of this pronouncement will have on the consolidated financial statements.

The following existing standards have been amended:

##### *IAS 1 "Presentation of Financial Statements"*

This amendment provides guidance on the presentation of items contained in other comprehensive income (OCI) and their classification within OCI. This is required to be applied beginning on or after July 1, 2012 with earlier adoption permitted.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 5. Future accounting pronouncements (continued)

#### IAS 12 "Income taxes"

This amendment removes subjectivity in determining on which basis an entity measures the deferred tax relating to an asset. The amendment introduces a presumption that an entity will assess whether the carrying value of an asset will be recovered through the sale of the asset. The amendment to IAS 12 is effective for reporting periods beginning on or after January 1, 2012.

Management is assessing the impact of these new standards and amendments but they are not expected to have a material impact on the Company's consolidated financial statements.

### 6. Inventory

The total carrying amount and classification of inventory was as follows:

	December 31, 2011	September 30, 2011	October 1, 2010
	\$	\$	\$
Finished goods	716,443	736,784	1,688,067
Component	2,514,771	2,744,528	927,162
Other	108,763	108,763	126,345
	<b>3,339,977</b>	<b>3,590,075</b>	<b>2,741,574</b>

As at December 31, 2011, \$3,339,977(2010 - \$3,590,375) of inventory was carried at cost and \$Nil was carried at net realizable value. The valuation write-down of inventory related assets recorded in the period ended December 31, 2011 totals \$Nil (2010 - \$Nil).

### 7. Development costs

Carrying value	December 31, 2011	September 30, 2011	October 1, 2010
	\$	\$	\$
Development of wind turbine technology	1	1	1
Development of power electronics intellectual property	1,291,279	1,393,174	1,567,426
Development of power electronics platform	1	1	1
Total	<b>1,291,281</b>	<b>1,393,176</b>	<b>1,567,428</b>

# Sustainable Energy Technologies Ltd.

Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

## 7. Development costs (continued)

Cost	Development of wind turbine technology	Development of power electronics intellectual property	Development of power electronics platform	Total
	\$	\$	\$	\$
Balance September 30, 2011	1,885,875	3,700,089	1,523,750	7,109,714
Additions	-	-	-	-
Disposals	-	-	-	-
Foreign currency translation	-	(32,693)	-	(32,693)
<b>Balance December 31, 2011</b>	<b>1,885,875</b>	<b>3,667,396</b>	<b>1,523,750</b>	<b>7,077,021</b>

Accumulated amortization and impairment	Development of wind turbine technology	Development of power electronics intellectual property	Development of power electronics platform	Total
	\$	\$	\$	\$
Balance September 30, 2011	1,885,874	2,306,915	1,523,749	5,716,538
Amortization	-	69,200	-	69,200
Foreign currency translation	-	-	-	-
<b>Balance December 31, 2011</b>	<b>1,885,874</b>	<b>2,376,115</b>	<b>1,523,749</b>	<b>5,785,738</b>

The cost of the development of the Company's power electronics intellectual property is being amortized straight line over the life of the relevant patents, which is estimated to be 16 years. At December 31, 2011, the patents had a remaining useful life of 6.75 years. Depreciation of the intangible asset is included in the statement of loss under the line item product research and development.

## 8. Capital assets

	December 31, 2011	September 30, 2011	October 1, 2010
	\$	\$	\$
Carrying value			
Computer equipment and software	24,163	30,866	99,121
Lab equipment	61,151	74,005	80,173
Furniture and equipment	35,240	40,568	66,014
Dies and molds	9,380	7,097	14,130
<b>Total</b>	<b>129,934</b>	<b>152,536</b>	<b>259,438</b>

# Sustainable Energy Technologies Ltd.

Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

## 8. Capital assets (continued)

<b>Cost</b>	<b>Computer equipment and software</b>	<b>Lab equipment</b>	<b>Furniture and equipment</b>	<b>Dies and models</b>	<b>Total</b>
	<b>\$</b>	<b>\$</b>		<b>\$</b>	<b>\$</b>
<b>Balance September 30, 2011</b>	483,306	578,871	160,914	43,156	1,266,247
Additions	7,590	2,112	-	5,077	14,779
Disposals	-	-	-	-	-
Foreign currency translation	-	-	(875)	-	(875)
<b>Balance December 31, 2011</b>	<b>490,896</b>	<b>580,983</b>	<b>160,039</b>	<b>48,233</b>	<b>1,280,151</b>

<b>Accumulated amortization and impairment</b>	<b>Computer equipment and software</b>	<b>Lab equipment</b>	<b>Furniture and equipment</b>	<b>Dies and models</b>	<b>Total</b>
	<b>\$</b>	<b>\$</b>		<b>\$</b>	<b>\$</b>
<b>Balance September 30, 2011</b>	452,440	504,865	120,346	36,060	1,113,711
Amortization	14,293	14,967	4,453	2,793	36,506
Foreign currency translation	-	-	-	-	-
<b>Balance December 31, 2011</b>	<b>466,733</b>	<b>519,832</b>	<b>124,799</b>	<b>38,853</b>	<b>1,150,217</b>

<b>Cost</b>	<b>Computer equipment and software</b>	<b>Lab equipment</b>	<b>Furniture and equipment</b>	<b>Dies and models</b>	<b>Total</b>
	<b>\$</b>	<b>\$</b>		<b>\$</b>	<b>\$</b>
Balance October 1, 2010	452,472	532,476	168,798	35,368	1,189,113
Additions	30,834	46,395	299	7,789	85,316
Disposals	-	-	(8,367)	-	(8,367)
Foreign currency translation	-	-	185	-	185
Balance September 30, 2011	483,306	578,871	160,915	43,157	1,266,248

<b>Accumulated amortization and impairment</b>	<b>Computer equipment and software</b>	<b>Lab equipment</b>	<b>Furniture and equipment</b>	<b>Dies and models</b>	<b>Total</b>
	<b>\$</b>	<b>\$</b>		<b>\$</b>	<b>\$</b>
Balance October 1, 2010	353,351	452,303	102,784	21,238	929,676
Amortization	99,090	52,562	17,562	14,822	184,036
Balance September 30, 2011	452,440	504,865	120,346	36,060	1,113,712

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 9. Energy Northwest obligation

	December 31, 2011	September 30, 2011
	\$	\$
Obligation to Energy Northwest (\$1,334,150 US (2010 - \$1,111,791 US))	1,356,830	1,331,341
Less: current portion of Energy Northwest obligation	271,366	266,268
	<u>1,085,464</u>	<u>1,065,073</u>

During fiscal 2001, Energy Northwest (formerly "Washington Public Power Supply System") made contributions of US\$132,490 to Sustainable Energy Laboratories Ltd. ("SEL") towards the development of SEL's step wave power conversion technology. Under its agreement with SEL, Energy Northwest is entitled to compensation for such contribution in an amount equal to 10% of SEL's gross monthly sales: provided, however, that the compensation payable in any year is not to be less than US\$7,000 and not more than 20% of Energy Northwest's total investment to include applicable interest. Under the agreement, interest is to be applied to Energy Northwest's contribution at an annual (APR) rate of 20% of the remaining balance due. Compensation payments are to be completed by January 1, 2016. The obligation is unsecured.

The current portion of the long term obligation to Energy Northwest is dependent on forecast product sales, subject to the above noted annual minimum and maximum payments. Due to the emerging nature of the Company's business, it is not possible to accurately forecast future product sales, and the Company has elected to treat the maximum amount payable to Energy Northwest (\$271,366) as current.

The obligation represents the Company's estimate of a fixed obligation payable in respect of contributions made by Energy Northwest for the early development of the Company's technology. The obligation is non-recourse to the Company and represents the best estimate of the amount that could be repayable by SEL. The Company is in negotiations with Energy Northwest to restructure the terms and conditions of the obligation and therefore any gains/losses arising from the restructuring will be accounted for in the condensed consolidated statement of loss and comprehensive loss at the time the negotiations are finalized.

Because of the complex nature and the history of the Energy Northwest obligation, the Company believes that it is not possible to reliably measure the fair value of the Energy Northwest obligation. In particular, (i) payments under the obligation are dependent on the sales revenues of the Company over the remaining term of the instrument; and (ii) it is not clear that any balance of the compensation payable to Energy Northwest and unpaid interest remaining unpaid at January 1, 2016 can be pre-determined.

Under a scenario where the maximum amount payable per year is made and the unpaid balance including interest at the end of the term is paid, the fair value of the Energy Northwest obligation based on interest rates that would be available for the Company for similar obligations is estimated at \$890,000. The impact of reducing (increasing) the interest rate by 1% would increase (decrease) the fair value of the Energy Northwest obligation under this scenario by approximately \$10,000 \$(20,000), assuming all other variables are constant.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 9. Energy Northwest obligation (continued)

Under a scenario where the minimum amount payable per year is made and the unpaid balance including interest at the end of the term is paid, the fair value of the Energy Northwest obligation based on interest rates that would be available for the Company for similar obligations is estimated at \$500,000. The impact of reducing (increasing) the interest rate by 1% would increase (decrease) the fair value of the Energy Northwest obligation under this scenario by approximately \$20,000 \$(20,000), assuming all other variables are constant.

### 10. Share capital

The equity account balances at December 31, 2011, September 30, 2011 and October 1, 2010 include only those of the Sustainable parent entity. Sustainable Energy Systems Inc. ("SES"), Sustainable Energy Europa S.L. ("SEE"), STG Markets Limited Partnership ("STGLP"), Sustainable Energy Laboratories Ltd. ("SEL"), CWT Power Inc. (Washington) ("CWT US") and International Power Systems, Inc. ("IPS") account balances eliminate upon consolidation of these financial statements.

*Authorized*, unlimited number

The authorized capital of Sustainable consists of an unlimited number of common shares without nominal or par value, and an unlimited number of preferred shares, issuable in series, without nominal or par value.

Unlimited number of common shares without par value

Unlimited number of First Preferred Shares Series 7

Unlimited number of First Preferred Shares Series 8

Unlimited number of First Preferred Shares Series 9

Unlimited number of First Preferred Shares Series 10

Unlimited number of First Preferred Shares Series 11

Unlimited number of First Preferred Shares Series 12

Issued

Common shares	Number of shares	Amount \$
Balance, October 1, 2010	165,938,924	30,393,463
Issuance of common shares	16,192,857	2,267,000
Cost of issuance	-	(813,883)
Issuance of LP units	16,999,830	2,550,000
Cost of issuance	-	(265,177)
Conversion of preferred shares	1,102,337	126,665
Exercised warrants	-	-
<b>Balance, September 30, 2011</b>	<b>200,233,948</b>	<b>34,258,068</b>
Conversion of preferred shares	137,986	13,999
<b>Balance, December 31, 2011</b>	<b>200,371,934</b>	<b>34,272,067</b>

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 11. Share-based payments

The Company has established an option plan (the "Plan") whereby the Company may grant options to purchase common shares to directors, officers, employees, and consultants. Options generally vest over a 3-year period with 1/6 vesting every 6 months. The Company's plan allows for a maximum term on any options to be ten years. The Company, at the discretion of the Board of Directors, may issue options to a maximum of 32,894,324 which was approved by the shareholders on September 2, 2010 has a fixed option plan The minimum price being the closing price on the TSX Venture Exchange on the date of issue.

	Number of options to employees	Weighted average price to employees \$	Number of options to non-employees	Weighted average price to non-employees \$
Balance, October 1, 2010	14,644,672	0.20	1,292,300	0.23
Forfeited	(1,491,667)	0.30	-	-
<b>Balance, September 30, 2011</b>	<b>13,153,005</b>	<b>0.18</b>	<b>1,292,300</b>	<b>0.23</b>
Forfeited	(1,000,000)	0.21	-	-
<b>Balance, December 31, 2011</b>	<b>12,153,005</b>	<b>0.18</b>	<b>1,292,300</b>	<b>0.23</b>

The following summarizes information about stock options outstanding as at December 31, 2011:

	Outstanding options			Exercisable options	
	Options	Weighted average price \$	Weighted average years to expiry	Options	Weighted average price \$
	5,225,000	0.15	8.00	3,758,335	0.15
	3,370,305	0.18	4.41	3,236,973	0.18
	4,250,000	0.21	6.63	3,729,168	0.22
	400,000	0.35	6.70	400,000	0.35
	200,000	0.40	8.28	100,000	0.40
<b>Balance December 31, 2011</b>	<b>13,445,305</b>	<b>0.18</b>		<b>11,224,476</b>	<b>0.19</b>

The total share-based compensation calculated for the three months ended December 31, 2011 was \$26,751 (2010 - \$87,746).

There have been no modifications to the above stock option plan for the three months ended December 31, 2011 or the year ended September 30, 2011.

# Sustainable Energy Technologies Ltd.

Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

## 12. Preferred shares

Series 7	Debt component	Equity component of preferred shares	Warrant component	Option component	Total
	\$	\$	\$	\$	\$
Balance at October 1, 2010	4,869,083	2,704,631	1,278,482	-	8,852,196
Accretion	1,760,363	-	-	-	1,760,363
Gain on preferred shares	(1,787,830)	-	-	-	(1,787,830)
Conversion of preferred shares	(42,241)	(33,536)	-	-	(75,777)
<b>Balance at September 30, 2011</b>	<b>4,799,375</b>	<b>2,671,095</b>	<b>1,278,482</b>	-	<b>8,748,952</b>
Accretion	396,208	-	-	-	396,208
Conversion of preferred shares	(6,321)	(5,019)	-	-	(11,340)
<b>Balance at December 31, 2011</b>	<b>5,189,262</b>	<b>2,666,076</b>	<b>1,278,482</b>	-	<b>9,133,820</b>

Series 9	Debt component	Equity component of preferred shares	Warrant component	Option component	Total
	\$	\$	\$	\$	\$
Balance at October 1, 2010	373,594	107,824	<b>77,053</b>	-	558,471
Accretion	94,108	-	-	-	94,108
Gain on preferred shares	(99,244)	-	-	-	(99,244)
Conversion of preferred shares	(26,121)	(7,843)	-	-	(33,964)
Balance at September 30, 2010	<b>342,337</b>	<b>99,981</b>	<b>77,053</b>	-	<b>519,371</b>
Accretion	20,478	-	-	-	20,478
<b>Balance at December 31, 2011</b>	<b>362,815</b>	<b>99,981</b>	<b>77,053</b>	-	<b>539,849</b>

Series 10	Debt component	Equity component of preferred shares	Warrant component	Option component	Total
	\$	\$	\$	\$	\$
Balance at October 1, 2010	-	-	-	-	-
Preferred shares	350,311	413,307	-	-	763,618
Accretion	90,584	-	-	-	90,584
<b>Balance at September 30, 2011</b>	<b>440,895</b>	<b>413,307</b>	-	-	<b>854,202</b>
Accretion	26,456	-	-	-	26,456
<b>Balance at December 31, 2011</b>	<b>467,351</b>	<b>413,307</b>	-	-	<b>880,658</b>



# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

Series 11	Debt component	Equity component of preferred shares	Warrant component	Option component	Total
	\$	\$	\$	\$	\$
Balance at September 30, 2011	-	-	-	-	-
Preferred shares	208,626	156,807	98,411	-	463,844
Accretion	12,058	-	-	-	12,058
<b>Balance at December 31, 2011</b>	<b>220,684</b>	<b>156,807</b>	<b>98,411</b>	<b>-</b>	<b>475,902</b>

Series 12	Debt component	Equity component of preferred shares	Warrant component	Option component	Total
	\$	\$	\$	\$	\$
Balance at September 30, 2010	-	-	-	-	-
Preferred shares	224,888	275,112	-	-	500,000
Accretion	3,337	-	-	-	3,337
<b>Balance at December 31, 2011</b>	<b>228,225</b>	<b>275,112</b>	<b>-</b>	<b>-</b>	<b>503,337</b>
<b>Total preferred shares</b>	<b>6,468,607</b>	<b>3,611,283</b>	<b>1,453,946</b>	<b>-</b>	<b>11,533,836</b>
Total preferred shares 2010	6,190,627	3,063,725	1,355,535	-	10,608,392

On May 8, 2009, the Company issued 450,000 Class A Units and 313,500 Class B Units at a price of \$10.00 per unit. Each Class A Unit consisted of one (1) redeemable 8%, voting, First Preferred Share, Series 7 ("Series 7 Preferred Shares") and 28 detachable warrants ("Warrants") to acquire one (1) non-voting common share at an exercise price of \$0.30 per share until May 7, 2013. Each Class B Unit consisted of one (1) Series 7 Preferred Share and 22 warrants to acquire one (1) voting common share at \$0.30 per share until May 7, 2013. On May 22, 2009 the Company issued an additional 126,500 Class B Units.

Holders of Series 7 Preferred Shares are entitled to receive as and when declared by the Board of Directors out of moneys of the Company applicable to the payment of annual dividends an amount equal to 8% of the then applicable Series 7 Redemption Price payable semi-annually, the first of such dividends to become payable October 15, 2009. In the event the annual 8% dividend is not declared and paid, such dividend shall be accretive to the Series 7 Redemption Price.

The Series 7 Preferred Shares may not be redeemed by the Company prior to October 15, 2011. After October 14, 2011, if within the 90 day period preceding the date of notice of redemption, the weighted average trading price has exceeded \$0.60 per share for at least 30 consecutive trading days and the average trading volume for such 30 consecutive trading days is at least \$200,000, the Company may redeem all but not less than all the Series 7 Preferred Shares at the then applicable Series 7 Redemption Price subject to the prior right of holders to exercise their right to convert the Series 7 Preferred Shares into common shares of the Company.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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### 12. Preferred shares (continued)

Holders of the Series 7 Preferred Shares may convert, at any time, the Series 7 Preferred Shares into that number of fully paid and non-assessable common shares equal to the then applicable Series 7 Redemption Price divided by the conversion price of \$0.15 per share. Series 7 Preferred Shares are automatically converted into common shares if (i) approved by a majority of the Series 7 Preferred Shares or (ii) the Company undertakes an underwritten public offering pursuant to a receipted prospectus or similar document for aggregate proceeds of \$20 million at a price per share of at least \$0.45.

On May 8, 2009, the subscriber for the Class A Units was also issued one (1) First Preferred Shares Series 8, and an option (the "Option") to acquire up to 10,000,000 common shares at \$0.15 per share, exercisable until November 7, 2009, at a price of \$1.00. The 1 First Preferred Share Series 8, entitles the holder to designate a representative to the board of directors of the Company for so long as the holder owns in the aggregate more than 10% of the issued and outstanding common shares of the Company on a fully diluted basis. The share is redeemable at a price of \$1.00, at the option of the holder.

The Class A and Class B Units were accounted for on the basis of their substance and are presented in their component parts of debt, warrants and equity. The debt component was measured at the issue date at the present value of the cash payment of dividends and principal under the terms of the preferred shares using a discount rate of 35%. The difference between the debt component, the warrants and the face value of preferred shares is classified as equity. The debt component is accreted to its face value through a charge to earnings using the effective interest method. Issue costs have been allocated between the debt and the equity components of the preferred shares. Cash transaction costs of approximately \$962,310 were allocated on a pro rata basis to the carrying values.

On August 23, 2010, the Company issued 68,736 First Preferred Shares Series 9 for gross proceeds of \$687,360. The Series 9 preferred shares are similar and rank pari passu to the Series 7 preferred shares, with the exception of the detachable warrants which were not issued as part of the Series 9 preferred shares. The Series 9 shares are convertible at a price of \$0.155. The Series 9 preferred shares (50,000) issued to Doughty Hanson have a 4 month hold expiring December 23, 2010. Doughty Hanson was also given 5,161,290 warrants exercisable for 1 year at \$0.155 and with a 4 month hold as partial compensation for underwriting the equity commitment of \$3,000,000.

The debt component was measured at the issue date at the present value of the cash payment of dividends and principal under the terms of the preferred shares using a discount rate of 20% and a five year term. The difference between the debt and warrant components and the face value of preferred shares is classified as equity. Transaction costs of \$143,388 were allocated on a pro rata basis to the carrying values,

On October 5, 2010, the Company issued 80,000 First Preferred Shares Series 10 to Doughty Hanson, pursuant to a commitment agreement dated August 23, 2010, which are similar to and rank pari passu with the Series 7 and Series 9 preferred shares, with the exception of the detachable warrants which were not issued as part of the Series 10 preferred shares. The Series 10 preferred shares resulted in a cash inflow of \$800,000 and they are convertible at a price of \$0.14 and mature 5 years and 1 day from the date of issuance. The debt component was measured at the issue date at the present value of the cash payment of dividends and principal under the terms of the preferred shares using a discount rate of 25% and a five year term. The difference between the debt component and the face value of preferred shares is classified as equity. The debt component is accreted to its face value through a charge to earnings using the effective interest method. Transaction costs were \$36,382.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 12. Preferred shares (continued)

On October 25, 2011, the Company issued 50,000 First Preferred Shares Series 11 to Doughty Hanson, pursuant to a commitment agreement dated October 19, 2011, which are similar to and rank pari passu with the Series 7 and Series 9 preferred shares. The Series 11 preferred shares resulted in a cash inflow of \$500,000 and they are convertible at a price of \$0.115 and mature 5 years and 1 day from the date of issuance. The debt component was measured at the issue date at the present value of the cash payment of dividends and principal under the terms of the preferred shares using a discount rate of 23% and a five year term. The difference between the debt component and the face value of preferred shares is classified as equity. The debt component is accreted to its face value through a charge to earnings using the effective interest method. The transaction costs were \$36,156.

On December 19, 2011, the Company issued 50,000 First Preferred Shares Series 12 to Doughty Hanson, pursuant to a commitment agreement dated October 19, 2011, which are similar to and rank pari passu with the Series 7, Series 9 and Series 11 preferred shares with the exception of the detachable warrants which were not issued as part of the Series 12 preferred shares. The Series 12 preferred shares resulted in a cash inflow of \$500,000 and they are convertible at a price of \$0.08 and mature 5 years and 1 day from the date of issuance. The debt component was measured at the issue date at the present value of the cash payment of dividends and principal under the terms of the preferred shares using a discount rate of 23% and a five year term. The difference between the debt component and the face value of preferred shares is classified as equity. The debt component is accreted to its face value through a charge to earnings using the effective interest method.

### 13. Warrants

Changes in the Company's purchase warrants are as follows:

	Issued with common or preferred shares	Broker warrants	Total purchase warrants	Allocated fair market value
	\$	\$	\$	\$
Balance, October 1, 2010	27,353,290	-	27,353,290	1,355,535
Warrants issued	12,944,913	2,190,501	15,135,414	996,936
Warrants expired	(5,161,290)		(5,161,290)	(77,053)
Balance September 30, 2011	35,136,913	2,190,501	37,327,414	2,275,418
Warrants expired		(1,127,001)	(1,127,001)	(66,572)
Warrants issued	6,347,826		6,347,826	98,411
<b>Balance, December 31, 2011</b>	<b>41,484,739</b>	<b>1,063,500</b>	<b>42,548,239</b>	<b>2,307,257</b>

- An additional 1,710,000 purchase warrants were issued March 18, 2011 representing the right to purchase common shares on a one to one basis with a price of \$0.20 per share for a two year term. The fair value of warrants outstanding was estimated as at the date of issuance of the warrant using the Black-Scholes option-pricing model and using a 1.6% risk free rate for the two year term of the warrants, and expected volatility of approximately 87% and expected dividend yield of nil. The fair market value of the warrants was \$116,280.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 13. Warrants (continued)

- An additional 1,661,071 purchase warrants were issued March 29, 2011 representing the right to purchase common shares on a one to one basis with a price of \$0.20 per share for a two year term. The fair value of warrants outstanding was estimated as at the date of issuance of the warrant using the Black-Scholes option-pricing model and using a 1.6% risk free rate for the two year term of the warrants, and expected volatility of approximately 86% and expected dividend yield of nil. The fair market value of the warrants at issuance was \$106,308.
- An additional 632,143 purchase warrants were issued March 22, 2011 representing the right to purchase common shares on a one to one basis with a price of \$0.20 per share for a two year term. The fair value of warrants outstanding was estimated as at the date of issuance of the warrant using the Black-Scholes option-pricing model and using a 1.6% risk free rate for the two year term of the warrants, and expected volatility of approximately 86% and expected dividend yield of nil. The fair market value of the warrants at issuance was \$44,882.
- An additional 3,082,500 purchase warrants were issued March 21, 2011 representing the right to purchase common shares on a one to one basis with a price of \$0.20 per share for a two year term. The fair value of warrants outstanding was estimated as at the date of issuance of the warrant using the Black-Scholes option-pricing model and using a 1.6% risk free rate for the two year term of the warrants, and expected volatility of approximately 86% and expected dividend yield of nil. The fair market value of the warrants at issuance was \$228,105.
- The Company issued 1,063,500 broker warrants exercisable for a period of two years at \$0.14. These warrants were partial compensation for the unit equity offering concluded April 2011. The Black Scholes option model was used to calculate the fair value of the warrants using a nil dividend yield, a 1.68% interest rate and a volatility of 86%. The fair market value at issuance was \$76,572.
- The Company issued 4,848,484 purchase warrants for a one year term at \$0.165 to Doughty Hanson in March 2011 as compensation for placing a guarantee with the bank for the Company's \$1,500,000 line of credit. The Black Scholes option model was used to calculate the fair value of the warrants using a nil dividend yield, a 1.19% interest rate and a volatility of 86%. The fair market value at issuance was \$300,606.
- The Company issued 1,010,715 purchase warrants exercisable for a period of two years at \$0.20. These warrants were partial compensation for the unit equity offering concluded April 2011. The Black Scholes option model was used to calculate the fair value of the warrants using a nil dividend yield, a 1.84% interest rate and a volatility of 86%. The fair market value at issuance was \$57,610.
- The Company issued 6,347,826 additional warrants to Doughty Hanson exercisable for a period of one year at \$0.115. These warrants were partial compensation for underwriting the equity commitment of \$1,500,000 in October 2011. The Black-Scholes option model was used to calculate the fair value of the warrants using a nil dividend yield, a 1.18% interest rate and a volatility of 100%. The fair market value at issuance was \$98,611.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 14. Share-based payment reserve

The following schedule shows the continuity of the share-based payment reserve:

	\$
Balance, October 1, 2010	4,445,087
Share based payments	296,926
Exercised additional warrants	77,054
<b>Balance September 30, 2011</b>	<b>4,819,067</b>
Expired broker warrants (note 13)	66,672
Share based payments (note 11)	26,751
<b>Balance, December 31, 2011</b>	<b>4,912,490</b>

### 15. Capital management

The Company's objectives when managing capital is to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders. The Company sets the amount of capital in proportion to risk. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company's objective is met by retaining adequate equity to provide for the possibility that cash flows from operations will not be sufficient to meet future cash flow requirements. The Board of Directors does not establish quantitative return on capital criteria for management; but rather promotes year over year sustainable profitable growth. The Company is subject to bank imposed covenants regarding the bank debt (note 17).

The Company defines capital as the aggregate of total shareholders' equity and cash and cash equivalents as follows:

	December 31, 2011	September 30, 2011
Total shareholders' equity (deficiency)	\$(3,985,351)	\$ (2,981,339)
Cash and cash equivalents	225,072	328,821
Bank loan	(1,121,690)	(1,346,662)
<b>Total capital</b>	<b>\$(4,881,969)</b>	<b>\$(3,999,180)</b>

There have been no changes to the Company's objectives in managing capital or in the management of capital since September 30, 2011. The decrease in equity has no immediate effect on the Company. The decrease in the shareholders' equity (deficiency) is because the Company's comprehensive loss surpasses the equity injections and increased sales at December 31, 2011.

### 16. Financial instruments and financial risk management

The Company has exposure to the following risks from its use of financial instruments: credit risk, liquidity risk and market risk. This note presents information about the Company's exposure to each of these risks and the Company's objectives, policies and processes for measuring and managing risk. Further quantitative disclosures are included throughout these condensed interim consolidated financial statements.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 16. Financial instruments and financial risk management (continued)

The Board of Directors has overall responsibility for the establishment and oversight of the Company's financial risk management framework and monitors risk management activities. The Company identifies and analyzes the risks faced by the Company and may utilize financial instruments to mitigate these risks.

#### *Credit risk*

Credit risk arises when a failure by counterparties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date. Allowances are considered by management on a case by case basis and the payment terms from customers are carefully reviewed. The Company does not have any significant credit risk exposure to any single counterparty or any group of counterparties having similar characteristics at December 31, 2011. The credit risk on cash and cash equivalents is considered to be limited because the counterparties are financial institutions with high credit ratings assigned by international credit rating agencies. The Company submits all credit applications to the Export Development Corporation (EDC) for accounts receivable insurance and has a cash only policy if credit approval is not granted by EDC.

The following table illustrates the Company's receivables and advances:

	As at December 31, 2011	As at September 31, 2011
Trade	\$ 666,015	\$ 757,509
Taxation authorities	315,020	34,928
Employee advances	94	944
	<b>\$ 981,129</b>	<b>\$ 1,093,381</b>

The Company assesses quarterly if there should be any impairment of the financial assets of the Company. During the period ended December 31, 2011, there was no impairment or allowance required on any of the financial assets of the Company.

The maximum exposure to credit risk is represented by the carrying amount on the balance sheet. There are no material financial assets that the Company considers past due, as the \$348,366 over 90 days past due has EDC insurance against it and the accounts have since been collected.

#### *Credit risk (continued)*

The following is a schedule of trade receivables:

	As at December 31, 2011	As at September 31, 2011
Neither impaired nor past due	\$ 262,753	\$ 613,641
Not impaired but past due in the following periods	-	-
31 – 60 days	54,896	34,857
61 – 90 days	-	25,466
90 and over	348,366	83,545
	<b>\$ 666,015</b>	<b>\$ 757,509</b>

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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(Unaudited)

### 16. Financial instruments and financial risk management (continued)

#### *Liquidity risk*

Liquidity risk includes the risk that, as a result of our operational liquidity requirements:

- The Company will not have sufficient funds to settle a transaction on the due date;
- The Company will be forced to sell financial assets at an amount which is less than what they may be worth; or
- The Company may be unable to settle or recover a financial assets at all

The Company's operating cash requirements, including amounts projected to complete the Company's existing capital expenditure program, are continuously monitored and adjusted as input variables change. These variables include but are not limited to available bank lines and government assistance. As these variables change, liquidity risks may necessitate the need for the Company to conduct equity issues or obtain project debt financing. There is no assurance that adequate funds from equity or debt markets will be available to the Company in a timely manner. The company also mitigates liquidity risk by maintaining an insurance program to minimize exposure to insurable losses.

The following are the contractual maturities of financial liabilities at December 31, 2011:

<u>Financial liability</u>	<u>&lt; 1 Year</u>	<u>1-3 Years</u>	<u>Thereafter</u>	<u>Total</u>
Accounts payable and accrued liabilities	1,156,201	-	-	1,156,201
Bank loan	1,121,690	-	-	1,121,690
Energy Northwest obligation	271,366	-	1,085,464	1,356,830
Commitments (Note 22)	363,275	600,992	-	964,267
Preferred shares Series 7,9,10, 11 and 12	-	9,133,820	2,400,016	11,533,836
<b>Total</b>	<b>2,912,532</b>	<b>9,734,812</b>	<b>3,485,480</b>	<b>16,132,824</b>

#### *Market risk*

Market risk is the risk that changes in market factors, such as foreign exchange rates and interest rates will affect the Company's cash flows, net income, liquidity or the value of financial instruments. The objective of market risk management is to mitigate market risk exposures where considered appropriate and maximize returns. The Company does not utilize derivative instruments to manage market risk. The Board of Directors periodically reviews the results of all risk management activities and all outstanding positions.

#### *Foreign currency risk*

Foreign currency risk is the risk that a variation in the exchange rate between Canadian and foreign currencies will affect the Company's results. The Company is subject to risk associated with its cash and cash equivalents, long term asset, the Energy Northwest obligation and from the sale and purchase of equipment, inventory components and services denominated in foreign currencies.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 16. Financial instruments and financial risk management (continued)

#### *Foreign currency risk (continued)*

Assuming all other variables remain constant, a \$0.05 change in the Canadian/US exchange rate would affect the Company's net loss by approximately \$67,609 for the quarter ended December 31, 2011 (December 31, 2010 - \$55,735). Assuming all other variables remain constant, a \$0.05 change in the Canadian/Euro exchange rate would change the Company's net loss by approximately \$31,719 for the quarter ended December 31, 2011 (December 31, 2010 - \$52,967). An opposite change in the Canadian/Euro exchange rate will result in an opposite impact on net loss. The Company had no forward exchange rate contracts in place as at or during the quarter ended December 31, 2011.

#### *Interest rate risk*

Interest rate risk refers to the risk that cash flows associated with the instrument will fluctuate due to changes in market interest rates. The Company currently does not use interest rate hedges, fixed interest rate contracts or variable rate debt to manage the Company's exposure to interest rate fluctuations.

#### *Fair value of financial instruments*

The Company's financial instruments include cash and cash equivalents, accounts receivable and advances, accounts payable and accrued liabilities, bank debt, Energy Northwest obligation and preferred shares. The carrying value and fair value of these financial instruments at December 31, 2011 is disclosed below by financial instrument category, as well as any related gain, loss, expense or revenue for the three months ended December 31, 2011:

<b>Financial instrument</b>	<b>Carrying value</b>	<b>Fair value</b>	<b>Gain/(loss)</b>	<b>Finance expense</b>
	\$	\$	\$	\$
Accounts receivable	981,128	981,128	-	-
Accounts payable and accrued liabilities	1,156,201	1,156,201	-	-
Bank loan	1,121,689	1,121,689	-	16,924
Energy Northwest obligation	1,356,830	695,000	661,830	65,569
Preferred shares	6,468,607	6,468,607		461,895
				544,388

The Company categorizes its financial instruments carried at fair value into one of three different levels depending on the observability of the inputs employed in the measurement. At December 31, 2011, the Company valued cash and cash equivalents using Level 1 input. At December 31, 2011 the Company did not have any assets and liabilities measured at a fair value using level 2 and 3 inputs.

- Level 1 - Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 - Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
- Level 3 - Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.



# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 17. Bank debt

The Company arranged a \$1,500,000 operating line of credit with the bank in March 2011. The operating line is fully secured by Doughty Hanson through an Equity Commitment Agreement. Interest is payable at the bank's prime rate plus 2.5% and amounts outstanding are repayable upon demand. The loan is subject to two covenants, a Current Asset to Current Liabilities ratio of 1.25:1.00 and Tangible Net Worth not to be less than \$2.5 million at any time. The Company was not in compliance with all covenants as of December 31, 2011. The Company is currently negotiating new covenants with the bank.

### 18. STG markets limited partnership

STG Markets Limited Partnership ("STGLP") (formerly Solar Markets Limited Partnership ("SMLP")) is an Alberta Limited Partnership which carries on the business of commercializing manufacturing and marketing inverters under license from Sustainable Energy and certain of Sustainable Energy's subsidiaries. The General Partner of STGLP is SES which exercises control over STGLP's operations. The Limited Partners of STGLP are Sustainable Energy, and from time to time, private investors who have provided capital to STGLP by purchasing limited partnership units ("LP Units") at a price of \$10,000 per LP Unit.

As Limited Partners of the Partnership on December 31 of each year, the investors are entitled to deduct their share of non capital losses of the Partnership for the year to a maximum of \$10,000 per LP Unit. As a result, 99.99% of non-capital losses are not available to Sustainable Energy to offset future taxable income realized by it.

The financial results of STGLP have been consolidated with the financial results of Sustainable Energy since inception as SES has full control over the operations of STGLP and Sustainable Energy has at all times the right to acquire all the LP Units not held by it directly.

### 19. Related party transactions

Other than as disclosed elsewhere in the consolidated financial statements, the Company had the following related party transaction:

Included in general and administration expenses is remuneration and fees for key management personnel and directors. For the period ending December 31, 2011, the Company has expensed \$147,042 as salary and \$17,366 as salary based compensation.

Revenue and expense transactions are in the normal course of operations and have been valued in these consolidated financial statements at fair value.

### 20. Government grants

Sustainable Energy has received contributions related to the development of its technologies and to marketing from U.S. and Canadian Government agencies. The contributions have been deducted in calculating the Company's investment in technology development or from the expense to which they relate. These amounts, plus, in certain cases, an implied return on the investment, are repayable as a percentage of the Company's revenues. Since the repayments are tied to the amount of revenues that may be earned in future periods, repayment of these contributions will be treated as a royalty expense in the period in which the revenue is earned.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 20. Government grants (continued)

#### *National Research Council*

The Company has entered into an agreement with the National Research Council to fund 60% of the salaries it incurs to commercialize the universal electronic platform to a maximum of \$245,241 from December 12, 2005 to June 30, 2008. The Company has received \$69,636 (2007 - \$108,814) and has credited this amount to operating expense. A royalty of 1.9% of gross revenue after October 1, 2008 is payable until TPC has recovered one and a half times the amount advanced to the Company or ten years after the beginning of the repayment schedule if the amount repaid is less than the full amount at September 30, 2011. The company has recorded in the books \$Nil during the three months ended December 31, 2011 (2010 - \$18,895). The royalty potentially payable is \$325,443. The Company needs to achieve cumulative gross sales over \$17.1 million to cause the maximum repayment. The National Research Council has agreed to forego the royalty expense for fiscal 2012.

### 21. Supplemental information

The changes in non-cash working capital for the three months ended December 31, 2011 and 2010 are as follows:

Operating activities		
Decrease (increase) in assets		
Accounts receivable and advances	112,252	215,965
Prepaid expense and deposits	136,968	12,426
Inventory	250,098	(447,600)
Other assets	75,152	17,529
	<b>574,470</b>	<b>(201,680)</b>
Increase (decrease) in liabilities		
Accounts payable	(485,220)	(614,151)
	<b>89,250</b>	<b>(815,831)</b>

### 22. Commitments

- (a) At December 31, 2011, Sustainable Energy had commitments for premise, equipment leases, investor relation agreements, and software installation as follows:

	\$
2012	363,275
2013	322,948
2014	230,870
2015	47,174

- (b) Consulting services were provided in fiscal 1998 to the Company. Repayment including interest at an annual rate of 20% per year is contingent upon SEL achieving sales (\$Nil to date) or capital funding of \$2,000,000 US (\$342,000) US has been received to December 31, 2011). At December 31, 2011, the total contingent amount payable including accrued interest was approximately \$429,768 (\$373,911US) (2010 - \$385,313, \$315,212 US).

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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- (c) There is a legal action for which the ultimate result cannot be ascertained at this time. Management does not expect the outcome of these proceedings to have a material effect on the financial position or results of operations.
- (d) The Company is party to an employment agreement with a director of the Company, where payment of a portion of the director's compensation is contingent upon the Company realizing positive earnings for any one fiscal quarter before interest, taxes, depreciation and amortization, a change of control of the Company, liquidation or receivership of the Company or termination of the employment relationship. At December 31, 2011, the total contingent amount payable was approximately \$112,500 (2010 - \$Nil).

### 23. Segmented information

#### *Geographic disclosures*

	As at December 31, 2011		As at September 30, 2011	
	Revenues	Assets *	Revenues	Assets *
Canada	649,732	115,069	2,2714,536	135,098
United States	-	1,291,281	-	1,393,176
Europe	371,492	14,865	1,153,374	17,438
	<b>1,021,224</b>	<b>1,421,215</b>	<b>\$3,867,910</b>	<b>1,545,712</b>

\* Assets refer to the Company's development costs and capital assets.

#### *Major customers*

The Company had two customers where product sales were greater than 10% in the period. One customer had attributed sales of \$347,576 and the other had attribute sales of \$230,287 (2010 – three customers, \$391,081, \$170,903 and \$119,482).

### 24. First-time adoption of international financial reporting standards

As stated in note 2, these are the Company's first condensed interim consolidated financial statements for the period covered by the first annual consolidated financial statements to be prepared in accordance with IFRS.

#### *IFRS 1 Exemptions Applied and Mandatory Exceptions*

IFRS 1, First-Time Adoption of International Financial Reporting Standards allows first-time adopters certain exemptions from the general requirement to apply IFRS for September 30, 2012 year ends retrospectively. IFRS 1 also includes mandatory exceptions to the retrospective application of IFRSs. In addition to the exemptions noted above, the Company has applied the following exemptions:

- The Company has elected under IFRS 1 to capitalize borrowing costs prospectively for projects commencing subsequent to October 1, 2010; all borrowing costs prior to October 1, 2010 will remain expensed.
- The Company has applied the transitional provision in IFRIC 4 Determining whether an Arrangement contains a lease and has assessed all arrangements as at the date of transition. Consequently the Company has assessed its arrangements as at October 1, 2010 instead of the

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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date of the original arrangement. Since the arrangements have been treated similarly under both Canadian GAAP and IFRS, this has had no effect on the financial statements.

- IFRS 3 Business Combinations has not been applied retrospectively to business combinations that occurred before the date of transition to IFRS (October 1, 2010). Prior business combinations have been accounted for under Canadian GAAP.
- IFRS 1 allows first-time adopters to not comply with the requirement to retrospectively determine cumulative currency translation differences in accordance with IAS 21 from the date a subsidiary was formed and allows the cumulative translation balance to be reset to zero at transition. Accordingly, the Company elected to reset all cumulative translation balances to zero in opening deficit at October 1, 2010.

### *IFRS 1 Exemptions Applied and Mandatory Exceptions*

- IFRS encourages, but does not require, first-time adopters to apply IFRS 2 Share-based Payment to equity instruments that were granted on or before November 7, 2002 or equity instruments that were granted subsequent to November 7, 2002 and vested before the date of transition to IFRS. The Company has elected to apply IFRS 2 to stock options that have not vested prior to October 1, 2010. The effect is to increase the share-based payment reserve and increase the deficit at transition date.
- At the date of transition, in accordance with IFRS 1, the Company elected deemed cost as fair value for its capital assets and development costs as at the transition date.

IFRS 1 contains four mandatory exceptions to the retrospective application of IFRSs which relate to (a) the derecognition of financial assets and liabilities, (b) hedge accounting, (c) estimates and (d) assets classified as held for sale and discontinued operations. These mandatory exceptions have not had a material impact on the consolidated financial statements.

### *Effects on cash flows*

Under Canadian GAAP, financing costs paid were classified as operating cash flows. Under IFRS financing costs paid can be classified as financing cash flows. This reclassification had no effect on operating cash flows or financing cash flows for the three months ended December 31, 2010.

### *Reconciliation of Canadian GAAP to IFRS*

The Company has prepared the following reconciliations of its previously reported Canadian GAAP balances to IFRS:

- Equity at October 1, 2010, December 31, 2010, and September 30, 2011;
- Consolidated statements of financial position at October 1, 2010, December 31, 2010 and September 30, 2011; and
- Consolidated statements of comprehensive loss for the three month periods ended December 31, 2010 and the year ended September 30, 2011.

Notes describing the details of the adjustments follow the reconciliations.

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

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### 24. First-time adoption of international financial reporting standards (continued)

Consolidated statement of financial position reconciliation as at October 1, 2010:

	IFRS adjustments			IFRS
	Canadian GAAP	Foreign exchange (Note a)	Share-based expense (Note b)	
	\$	\$	\$	\$
<b>Assets</b>				
Current assets				
Cash and cash equivalents	561,373			561,373
Accounts receivable and advances	978,192			978,192
Inventory	2,741,574			2,741,574
Prepaid expenses and deposits	601,645			601,645
Non-current assets				
Development costs	2,137,349	(569,921)		1,567,428
Capital assets	261,507	(2,069)		259,438
Other long term assets	243,783			243,783
	<u>7,525,423</u>	<u>(571,990)</u>	<u>-</u>	<u>6,953,433</u>
<b>Liabilities</b>				
Current liabilities				
Accounts payable and accrued liabilities	2,206,264			2,206,264
Provisions	-			-
Bank debt	-			-
Energy Northwest obligation, current portion	217,826			217,826
Noncurrent liabilities				
Energy Northwest obligation	871,303			871,303
Preferred shares	5,242,677			5,242,677
	<u>8,538,070</u>	<u>-</u>	<u>-</u>	<u>8,538,070</u>
<b>Equity</b>				
Share capital	30,393,463			30,393,463
Warrants	1,355,535			1,355,535
Equity component of preferred shares preferred shares	2,812,455			2,812,455
Share-based payment reserve	4,158,830		286,257	4,445,087
Deficit	(39,732,930)	(571,990)	(286,257)	(40,591,177)
	<u>(1,012,647)</u>	<u>(571,990)</u>	<u>-</u>	<u>(1,584,637)</u>
	<u>7,525,423</u>	<u>(571,990)</u>	<u>-</u>	<u>6,953,433</u>

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 24. First-time adoption of international financial reporting standards (continued)

Consolidated statement of financial position reconciliation as at December 31, 2010:

	IFRS adjustments			IFRS
	Canadian GAAP	Foreign exchange (Note a)	Share-based expense (Note b)	
	\$	\$	\$	\$
<b>Assets</b>				
Current assets				
Cash and cash equivalents	1,025,375			1,025,375
Accounts receivable and advances	762,226			762,226
Inventory	3,189,175			3,189,175
Prepaid expenses and deposits	589,219			589,219
Non-current assets				
Development costs	2,070,558	(591,748)		1,478,810
Capital assets	227,828	(3,978)		223,850
Other long term assets	226,254			226,254
	<u>8,090,635</u>	<u>(595,726)</u>	<u>-</u>	<u>7,494,909</u>
<b>Liabilities</b>				
Current liabilities				
Accounts payable and accrued liabilities	1,592,113			1,592,113
Provision	-			-
Bank debt	-			-
Energy Northwest obligation, current portion	221,158			221,158
Noncurrent liabilities				
Energy Northwest obligation	884,630			884,630
Preferred shares	6,190,627			6,190,627
	<u>8,888,528</u>	<u>-</u>	<u>-</u>	<u>8,888,528</u>
<b>Equity</b>				
Share capital	32,700,145			32,700,145
Warrants	1,422,107			1,422,107
Equity component of preferred shares preferred shares	3,063,725			3,063,725
Share-based payment reserve	4,204,712		328,121	4,532,833
Foreign currency translation reserve		54,599		54,599
Deficit	(42,188,582)	(650,325)	(328,121)	(43,167,028)
	<u>(797,893)</u>	<u>(595,726)</u>	<u>-</u>	<u>(1,393,619)</u>
	<u>8,090,635</u>	<u>(595,726)</u>	<u>-</u>	<u>7,494,909</u>

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

### 24. First-time adoption of international financial reporting standards (continued)

Consolidated statement of comprehensive loss reconciliation for the three month period ended December 31, 2010:

	Canadian GAAP	Foreign exchange (Note a)	Share based expenses (Note b)	Reclassification (Note c)	IFRS
	\$	\$	\$	\$	\$
Sale	994,465				994,465
Cost of sales	872,512				872,512
Gross margin	121,953	-	-	-	121,953
Expenses					
Repayment of government contributions	18,895			(18,895)	-
Product research and development	1,188,208			(1,032,863)	155,345
Selling and marketing				630,621	630,621
Operations	-			469,319	469,319
General and administrative	822,640		41,864	75,601	940,105
Interest	56,683			(56,683)	-
Finance cost	454,562			56,683	511,245
Amortization of capital assets and development costs	128,492	(18,610)		(109,882)	-
Foreign exchange loss	64,017	(50,116)		(13,901)	-
	2,733,497	(68,726)	41,864	-	2,706,635
<b>Loss before undernoted items</b>	(2,611,544)	68,726	(41,864)	-	(2,584,682)
Interest and other	8,831				8,831
	(2,602,713)				(2,575,851)
Foreign currency adjustment to equity	-	76,458	-	-	76,458
<b>Total comprehensive loss</b>	(2,602,713)	145,184	(41,864)	-	(2,499,393)

### 24. First-time adoption of international financial reporting standards (continued)

# Sustainable Energy Technologies Ltd.

## Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

Consolidated statement of financial position reconciliation as at September 30, 2011:

	IFRS adjustments			IFRS
	Canadian GAAP	Foreign exchange (Note a)	Share-based expense (Note b)	
	\$	\$	\$	\$
<b>Assets</b>				
Current assets	<b>328,821</b>			<b>328,821</b>
Cash and cash equivalents				
Accounts receivable and advances	<b>1,093,381</b>			<b>1,093,381</b>
Inventory	<b>3,590,075</b>			<b>3,590,075</b>
Prepaid expenses and deposits	<b>212,401</b>			<b>212,401</b>
Non-current assets				
Development costs	<b>1,870,186</b>	<b>(477,010)</b>		<b>1,393,176</b>
Capital assets	<b>154,851</b>	<b>(2,315)</b>		<b>152,536</b>
Other long term assets	<b>150,303</b>			<b>150,303</b>
	<b>7,400,018</b>	<b>(479,325)</b>	<b>-</b>	<b>6,920,693</b>
<b>Liabilities</b>				
Current liabilities				
Accounts payable and accrued liabilities	<b>1,641,421</b>			<b>1,641,421</b>
Bank debt	<b>1,346,662</b>			<b>1,346,662</b>
Energy Northwest obligation, current portion	<b>266,268</b>			<b>266,268</b>
Noncurrent liabilities				
Energy Northwest obligation	<b>1,065,073</b>			<b>1,065,073</b>
Preferred shares	<b>5,582,607</b>			<b>5,582,607</b>
	<b>9,902,031</b>	<b>-</b>	<b>-</b>	<b>9,902,031</b>
<b>Equity</b>				
Share capital	<b>34,258,068</b>			<b>34,258,068</b>
Warrants	<b>2,275,418</b>			<b>2,275,418</b>
Equity component of preferred shares	<b>3,184,383</b>			<b>3,184,383</b>
Share-based payment reserve	<b>4,629,367</b>		<b>189,700</b>	<b>4,819,067</b>
Foreign currency translation reserve		<b>(171,906)</b>		<b>(171,906)</b>
Deficit	<b>(46,849,249)</b>	<b>(307,419)</b>	<b>(189,700)</b>	<b>(47,346,368)</b>
	<b>(2,502,013)</b>	<b>(479,325)</b>	<b>-</b>	<b>(2,981,338)</b>
	<b>7,400,018</b>	<b>-</b>	<b>-</b>	<b>6,920,693</b>



# Sustainable Energy Technologies Ltd.

Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

## 24. First-time adoption of international financial reporting standards (continued)

Consolidated statement of comprehensive loss reconciliation for the year ended September 30, 2011:

Sales	3,867,910			3,867,910
Cost of sales	2,920,509			2,920,509
Gross margin	947,401	-	-	947,401
Expenses				
Repayment of government contributions	119,052		(119,052)	-
Selling and marketing	4,316,908		(2,327,835)	1,989,073
Product research and development			1,126,131	1,126,131
Operations	-		1,709,276	1,709,276
Inventory write down	198,987		(198,987)	-
General and administrative	2,066,708	(96,557)	596,729	2,566,880
Share-based payments	393,483		(393,483)	-
Finance cost	2,209,417			2,209,417
Amortization of capital assets and development costs	451,715	(77,633)	(374,082)	-
Foreign exchange loss	205,633	(186,936)	(18,697)	-
	9,961,903	(264,569)	(96,557)	9,600,777
Loss before undernoted items	(9,014,502)			(8,653,376)
				-
Gain on preferred shares	1,887,074			1,887,074
Interest and other	11,109			11,109
	1,898,183	-	-	1,898,183
Loss before translation of foreign operations	(7,116,319)			(6,755,193)
Foreign currency adjustment to equity	-	(171,906)	-	(171,906)
Total comprehensive loss	(7,116,319)	(436,475)	(96,557)	(6,927,099)

# Sustainable Energy Technologies Ltd.

Notes to the condensed interim consolidated financial statements

December 31, 2011

(Unaudited)

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## 24. First-time adoption of international financial reporting standards (continued)

### *Notes to the financial statement reconciliations*

- (a) In accordance with IAS 21, The Effect of Changes in Foreign Exchange Rates, the assets and liabilities of Sustainable's subsidiaries are expressed in Canadian dollars using the exchange rate prevailing at the balance sheet date. Income and expense items are translated at the average exchange rate for the period, unless exchange rates fluctuated significantly during the period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are classified as other comprehensive profit and recognized in the Company's foreign currency translation reserve.

Under Canadian GAAP, monetary assets and liabilities of the subsidiaries were translated at the exchange rate in effect at the balance sheet date. Non-monetary assets and liabilities are translated at historical rates. Revenues and expenses were translated using the average rate of exchange of the period being reported. Translation adjustments are recorded in earnings.

The Company applied the first-time IFRS adoption exemption to reset the cumulative translation differences to nil on the transition date.

- (b) IFRS requires forfeitures be estimated and recognized on the grant date and revised prospectively in subsequent periods for actual experiences; while under Canadian GAAP forfeitures of awards could be recognized as they occurred.

The Company had previously accounted for forfeitures of share-based compensation in the period that they occurred. IFRS 2, "Share-based payments", requires the Company to account for the fair value of options expected to be exercised at the date of grant. Consequently the Company has adjusted the IFRS financial statements to account for expected forfeitures of 14%.

IFRS 2, "Share-based payments", requires the Company to expense share-based payments based on graded vesting. As a result of applying this methodology retroactively the share-based payment reserve has been increased by \$286,257 as at September 30, 2010.

- (c) The terms, descriptions, classifications and presentation used throughout the financial statements have been changed to conform to those generally used under IFRS.