Consolidated Financial Statements of

PHOTON CONTROL INC.

For the three months ended March 31, 2012 and 2011

(Unaudited)

NOTICE OF NO-AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

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

The Company’s external auditors, MNP LLP, have not performed a review of these financial statements.

PHOTON CONTROL INC.

Consolidated Statements of Financial Position

(Expressed in Canadian dollars)

As at March 31, 2012 and December 31, 2011

		March 31, 2012		December 31, 2011
Assets				
Current assets:				
Cash and cash equivalents	$	1,458,713	$	975,108
Trade accounts receivable and other		2,100,425		1,541,843
Note receivable - related (note 9a)		26,985		29,248
Due from related party (note 9a)		1,040,720		965,190
Inventory (note 4)		1,680,826		2,047,213
Prepaid expenses and deposits		23,846		48,078
		6,331,515		5,606,680
Property and equipment (note 5)		290,012		291,642
Intangible assets (note 6)		238,429		255,792
Internally generated intangible assets (note 2(h))		150,616		150,616
Long term rental deposits		34,695		34,695
Note receivable -related (note 9a)		156,519		159,373
Restricted cash (notes 14, 10(b))		953,744		953,744
Deferred Taxes (notes 17)		3,926,888		3,926,888
	$	12,082,418	$	11,379,430
Liabilities and Shareholders' Equity				
Current liabilities:				
Deferred revenue (note 9)	$	178,257	$	178,257
Accounts payable and accrued liabilities (note 16)		1,046,519		814,717
Due to related party (note 9a)		209,623		340,365
Bank indebtedness (note 14)		-		-
Provisions (note 10(b))		850,000		850,000
		2,284,399		2,183,339
Shareholders' equity (note 7):				
Share capital		28,246,173		28,246,173
Contributed surplus		2,008,403		1,997,903
Deficit		(20,456,557)		(21,047,985)
		9,798,019		9,196,091
Commitments and contingencies (notes 9 and 10)				
Subsequent events (note 18)				
	$	12,082,418	$	11,379,430

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board

"Christopher Weston", Director   "David C. Dueck", Director

PHOTON CONTROL INC.

Consolidated Statement of Comprehensive Income (Loss) and Deficit
(Expressed in Canadian dollars)

For the three months ended March 31, 2012 and 2011

		Three Months Ended March 31, 2012		Three Months Ended March 31, 2011
Revenue	$	3,071,727	$	3,250,303
Cost of sales		1,874,309		1,812,851
		1,197,418		1,437,452
Operating expenses (notes 9 and 11):				
General and administrative		389,005		662,769
Engineering		116,872		182,630
Business development		61,066		52,671
		566,943		898,070
Net earnings (loss) before other earnings and taxes		630,475		539,382
Other earnings (expenses):				
Interest and other earnings		5,467		2,166
Interest expense		(495)		-
Foreign exchange		(44,020)		(85,884)
		(39,048)		(83,718)
Net earnings (loss) from operating activities		591,427		455,664
Income Tax (expense) recovery		-		-
Net earnings and total comprehensive income		591,427		455,664
Basic and diluted earnings (loss) per share				
Weighted average common shares used in computing		102,909,518		102,333,056
Diluted average common shares used in computing		106,397,925		106,651,719
Basic earnings (loss) per share	$	0.01	$	0.01
Diluted earnings (loss) per share	$	0.01	$	0.01

See accompanying notes to consolidated financial statements.

PHOTON CONTROL INC

Consolidated Statements of Changes in Equity
(Expressed in Canadian dollars)
As at March 31, 2012 and 2011

	Share Capital		Contributed Surplus and Deficit		
	Number of Shares	Amount	Contributed Surplus	Deficit	Total
Balance at December 31, 2010	**102,909,518**	**$ 28,246,173**	**$ 1,951,100**	**$(25,695,606)**	**$ 4,501,667**
Stock based compensation to employees	-	-	46,803	-	46,803
Total comprehensive income (loss) for the period	-	-	-	4,647,621	4,647,621
Balance at December 31, 2011	**102,909,518**	**$ 28,246,173**	**$ 1,997,903**	**$(21,047,985)**	**$ 9,196,091**
Stock based compensation to employees	-	-	10,501	-	10,501
Total comprehensive income (loss) for the period	-	-	-	591,427	591,427
Balance at March 31, 2012	**102,909,518**	**$ 28,246,173**	**$ 2,008,404**	**$(20,456,558)**	**$ 9,798,019**

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

PHOTON CONTROL INC.

Consolidated Statement of Cash Flows

For the three months ended March 31, 2012 and 2011

As at March 31	**2012**	**2011**
Cash provided by (used in):		
Operations:		
Net earnings (loss)	$ 591,427	$ 455,664
Non-cash items:		
Amortization of property, equipment and intangibles	33,494	62,598
Stock-based compensation	10,501	22,812
Amortization of deferred development costs	-	-
Deferred rent and sublease deposits	-	(22,319)
Changes in non-cash operating working capital:		
Trade accounts receivable and other	(558,581)	(9,857)
Inventory	366,387	(743,353)
Prepaid expenses and deposits	24,232	(44,050)
Accounts payable and accrued liabilities	196,175	353,319
Due to/from related party	(170,808)	(118,501)
Received from related party	2,427	-
Long term receivables	-	-
Deferred revenue	2,852	-
	498,106	(43,687)
Financing:		
Advances under credit facility	-	-
Repayment of inter-company debt	-	-
Shares issued for cash	-	-
Proceeds from note receivable	-	-
	-	-
Investments:		
Restricted cash	-	-
Purchase of equipment	(14,501)	(48,751)
Purchase of intangible assets	-	(6,710)
Deferred development costs	-	-
	(14,501)	(55,461)
Increase (decrease) in cash and cash equivalents	483,605	(92,148)
Cash and cash equivalents, beginning of year	975,108	929,564
Cash and cash equivalents, end of year	1,458,713	837,416
Supplementary information:		
Cash received for interest	5,467	133
Cash paid for interest	(495)	-

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

1. Nature of business and continuing operations:

Photon Control Inc. (the Company) is a publically traded company listed on the TSX Venture Exchange and is incorporated under the laws of British Columbia, Canada. The Company's head office is 200-8363 Lougheed Highway, Burnaby, British Columbia, Canada, V5A 1X3. The address of the registered office and records office is Koffman Kalef LLP, 19th Floor, 885 West Georgia Street, Vancouver, BC, Canada, V6C 3H4.

The Company designs and manufactures a wide range of optical sensors and instruments to measure temperature, pressure, position, and flow. These products are used by original equipment manufacturers (OEM) as well as end-users in the Semiconductor, Oil and Gas, Power, Life Science, and Manufacturing industries. On August 17, 2000, the Company completed an initial public offering of its common shares, which are listed on the TSX Venture Exchange ("TSX-V") under the trading symbol PHO. In 2002, the Company changed its name from Coldswitch Technologies Inc. to Photon Control Inc.

2. Significant accounting policies:

(a) Basis of presentation and statement of compliance:

These consolidated financial statements represent the first annual financial statements of the Company and its subsidiaries prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). The first date at which IFRS was applied was January 1, 2011. In accordance with IFRS, the Company has:

- provided comparative financial information; and
- applied the same accounting policies throughout all periods presented.

The Company's consolidated financial statements were previously prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP"). Canadian GAAP differs in some areas from IFRS. In preparing these financial statements, management has amended certain accounting methods previously applied in the Canadian GAAP financial statements to comply with IFRS.

These consolidated financial statements have been prepared on a going concern basis, under the historical cost convention, except for certain financial assets and financial liabilities which are measured at fair market value.

(b) Basis of consolidation:

The Company consolidates subsidiaries controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Inter-company balances and transactions, including any income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

2. Significant accounting policies (continued):

These consolidated financial statements include the accounts of the Company's wholly owned subsidiaries LAI Lightwave Aerospace Industries Ltd., CST Coldswitch Holdings Inc., The Lightswitch Company Inc., and Photon Control (Alberta) Inc., all of which are inactive.

(c) Cash and cash equivalents:

Cash and cash equivalents consist of highly liquid investments that are readily convertible to known amounts of cash. Short-term investments have maturity dates of three months or less from the date of purchase, or they are redeemable prior to maturity.

(c) Use of estimates:

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported revenue and expenses during the years. Significant items subject to such estimates and assumptions include the recoverable amount of equipment, deferred development costs and intangible assets, and valuation allowances for deferred income tax, receivables and inventory and assumptions used in determining the fair value of options and warrants.

These financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below.

(d) Inventory:

Inventory consists of optical, mechanical and electronic components and finished goods and is valued at the lower of cost or net realizable value. Cost is determined on a first in first out basis, and includes the cost of direct material, direct labour and other overhead costs. Labour costs are allocated to items based on actual labour rates. Fixed and variable overhead are allocated to production activities in converting materials to finished goods.

2. Significant accounting policies (continued):

(e) Property and equipment:

Property and equipment are stated at cost. Amortization is provided on the declining balance basis at the following annual rates:

Asset	Rate
Lab equipment	20%
Computers, office furniture and equipment	20%
Computer software	100%
Production equipment	30%
Leasehold improvements	Over the lesser of the initial term of the lease and the useful life of assets

(f) Intangible assets:

The costs of acquiring intangible assets, consisting of licenses, patents and trademarks are capitalized. Costs are amortized over the lesser of the estimated useful life of the intangible asset or the license term.

(g) Revenue recognition:

Revenue from sales of products is recognized when goods are shipped and title passes, there is persuasive evidence of an arrangement, collection is probable and fees are fixed and determinable. Cash collected prior to revenue recognition criteria being met is recorded as deferred revenue on the consolidated balance sheet.

(h) Research and development costs:

Research costs are expensed as incurred. Development costs are expensed as incurred unless all of the following can be demonstrated:

a. The technical feasibility of completing the intangible asset so that it will be available for use or sale;

b. The intention to complete the intangible asset and use or sell it;

c. The ability to use or sell the intangible asset;

d. How the intangible asset will generate probable future economic benefits;

e. The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset; and

f. The ability to measure reliably the expenditure attributable to the intangible asset during its development.

The Company amortizes costs, commencing with commercial production, over the expected future benefit period based upon quantities delivered compared to expected levels contracted to be delivered. The amount amortized in fiscal year 2012 to date was nil (2011 - nil).

2. Significant accounting policies (continued):

Company has a balance of internally generated intangible assets as at March 31, 2012 of $150,616 (March 31, 2011 - $152,724).

(i) Government assistance:

The Company makes periodic applications for financial assistance under available government incentive programs. Government assistance relating to capital expenditures is reflected as a reduction of the cost of such assets, while government assistance relating to current expenses is recorded as a reduction of such expenses. The benefits of government assistance are recognized when there is reasonable assurance that they will be realized. Reasonable assurance is considered to have occurred when the relevant authorities have indicated that the Company's research and development activities qualify for government assistance. The Company did not receive any government assistance during the year ended December 31, 2011 nor at March 31, 2012.

(j) Earnings (loss) per share:

Basic earnings (loss) per share amounts are calculated by dividing net earnings (loss) by the weighted average number of common shares outstanding during the year. Diluted earnings per share amounts are computed similarly to basic earnings per share except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of additional options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire shares of common stock at the average market price during the year.

(k) Income taxes:

Tax expense comprises current and deferred tax. Tax is recognized in the consolidated statements of comprehensive income except to the extent it relates to items recognized in other comprehensive income or directly in equity.

Current income tax

Current tax expense is based on the results for the period as adjusted for items that are not taxable or not deductible. Current tax is calculated using tax rates and laws that were substantively enacted at the end of the reporting period. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. Provisions are established where appropriate on the basis of amounts expected to be paid to the tax authorities.

2. Significant accounting policies (continued):

Deferred tax

Deferred taxes are the taxes expected to be payable or recoverable on differences between the carrying amounts of assets in the Consolidated Statements of Financial Position and their corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet asset and liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences between the carrying amounts of assets and their corresponding tax bases. Deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets in a transaction that affects neither the taxable profit nor the accounting profit.

(l) Share issue costs:

The costs of issuing common shares are applied to reduce the stated value of such shares.

(m) Translation of foreign currencies:

Monetary items denominated in foreign currencies are translated to Canadian dollars at exchange rates in effect at the balance sheet dates and non-monetary items are translated at rates of exchange in effect when the assets were acquired or obligations incurred. Revenue and expenses are translated at rates in effect at the time of the transactions. Foreign exchange gains and losses are included in earnings.

(n) Stock-based compensation plans:

The Company has a stock-based compensation plan, which is described in Note 7(c). The fair value of the services rendered is determined indirectly by reference to the fair value of the equity instruments granted. Compensation cost attributable to options granted to employees and directors is measured at the fair value at the grant date using the Black-Scholes option pricing model. Compensation expense is recognized over the vesting period of the underlying option. Any consideration paid by employees on exercise of stock options or purchase of stock is credited to share capital. No compensation cost is recognized for options that employees forfeit if they fail to satisfy the service requirement for vesting. Compensation expense is recognized for stock-based payments to non-employees using the fair value of the goods or services received, unless the fair value of the equity instruments granted is more reliably determinable.

(o) Warranty provision estimate:

The Company accrues for the estimated obligation under warranty provisions at the time sales are recognized and any changes in estimates are recognized prospectively. The Company provides its customers with a limited right of return for defective products. All warranty returns must be authorized by the Company prior to acceptance.

2. Significant accounting policies (continued):

(p) Financial instruments:

The Company has classified its financial instruments as follows:

- Cash and cash equivalents and bank indebtedness, if any, as “held-for-trading”.
- Trade accounts receivable, the note receivable and amounts due from related parties are classified as ”loans and receivables”.
- Accounts payable and accrued liabilities, amounts due to related parties and advances under credit facility are classified as “other financial liabilities”.

All financial instruments are initially recognized at fair value and are subsequently accounted for based on their classification. The fair value of a financial instrument on initial recognition is the transaction price, which is the fair value of the consideration given or received. Subsequent to initial recognition, financial assets and liabilities classified as held-for-trading are measured at fair value with changes in fair value recorded in the Consolidated Statements of Operations. Financial assets classified as ”loans and receivables” and “other financial liabilities” are carried at amortized cost using the effective interest rate method. The fair values are based on quoted market bid process if available, otherwise fair value is obtained using discounted cash flow analysis. Transaction costs that are directly attributable to the issuance of financial assets or liabilities are accounted for as part of the carrying value at inception, and are recognized over the term of the assets or liabilities using the effective interest method.

(q) Impairment of property, equipment, intangibles and internally generated intangible assets:

At each date of the balance sheet, the Company’s carrying amounts of its assets are reviewed to determine whether there are any indications of impairment. If such indication exists, the recoverable amount of the assets is estimated using the higher of (a) fair value less costs to sell, and (b) value in use.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount is less than its carrying amount, the carrying amount is reduced to its recoverable amount and the impairment loss is recognized in profit or loss for the period. When there are indicators that the conditions giving rise to the impairment previously recognized have reversed, then the reversal of the impairment loss is reversed in that period.

(r) Comparative figures:

IFRS financial statement presentation was adopted on January 1, 2011. Comparative figures for both fiscal years 2011 and 2012 are thus both comparable and IFRS compliant.

3. Accounting standards issued but not yet effective:

Certain pronouncements were issued by the IASB or the International Financial Reporting Interpretations Committee ("IFRIC") that are mandatory for accounting periods after December 31, 2011. Pronouncements that are not applicable or do not have a significant impact to the Company have been excluded from the table below.

The following five new Standards were issued by the IASB in May 2011, and are effective for annual periods beginning on or after January 1, 2013. Early application is permitted if all five Standards are adopted at the same time.

Consolidated Financial Statements - IFRS 10 Consolidated Financial Statements ("IFRS 10") will replace existing guidance on consolidation in IAS 27 Consolidated and Separate Financial Statements, and SIC 12 Consolidation – Special Purpose Entities. The portion of IAS 27 that deals with separate financial statements will remain. IFRS 10 changes the definition of control, such that the same consolidation criteria will apply to all entities. The revised definition focuses on the need to have both "power" and "variable returns" for control to be present. Power is the current ability to direct the activities that significantly influence returns. Variable returns can be positive, negative or both. IFRS 10 requires continuous assessment of control of an investee in line with any changes in facts and circumstances.

Joint Arrangements - IFRS 11 Joint Arrangements ("IFRS 11") will replace IAS 31 Interests in Joint Ventures, and SIC 13 Jointly Controlled Entities – Non-monetary Contributions by Venturers. IFRS 11 defines a joint arrangement as an arrangement where two or more parties contractually agree to share control. Joint control exists only when the decisions about activities that significantly affect the returns of an arrangement require the unanimous consent of the parties sharing control. The focus is not solely on the legal structure of joint arrangements, but rather on how the rights and obligations are shared by the parties to the joint arrangement. IFRS 11 eliminates the existing policy choice of proportionate consolidation for jointly controlled entities. In addition, the Standard categorizes joint arrangements as either joint operations or joint ventures.

Disclosure of Interests in Other Entities - IFRS 12 Disclosure of Interests in Other Entities ("IFRS 12") is the new Standard for disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. Matters covered include information about the significant judgments and assumptions that any entity has made in determining whether it has control, joint control or significant influence over another entity.

Separate Financial Statements - IAS 27 Separate Financial Statements ("IAS 27") has been updated to require an entity presenting separate financial statements to account for those investments at cost or in accordance with IFRS 9 Financial Instruments. The amended IAS 27 excludes the guidance on the preparation and presentation of consolidated financial statements for a group of entities under the control of a parent currently within the scope of current IAS 27 Consolidated and Separate Financial Statements replaced by IFRS 10.

3. Accounting standards issued but not yet effective (continued):

Investments in Associates and Joint Ventures - IAS 28 Investments in Associates and Joint Ventures (“IAS 28”) has been revised and it is to be applied by all entities that are investors with joint control of, or significant influence over, an investee. The scope of IAS 28 Investments in Associates does not include joint ventures.

IFRS 13 Fair Value Measurement (“IFRS 13”) was issued by the IASB in May 2011, and is effective for annual periods beginning on or after January 1, 2013. Early application is permitted. IFRS 13 was issued to remedy the inconsistencies in the requirements for measuring fair value and for disclosing information about fair value measurement in various current IFRSs. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. an exit price.

The IASB has issued an amendment to IFRS 7, Financial Instruments: Disclosures (“IFRS 7”), requiring incremental disclosures regarding transfers of financial assets. This amendment is effective for annual periods beginning on or after July 1, 2011. The Company will apply the amendment at the beginning of its 2012 financial year. The Company does not expect the implementation to have a significant impact on the Company’s disclosures.

The IASB has issued a new standard, IFRS 9, Financial Instruments (“IFRS 9”), which will ultimately replace IAS 39, “Financial Instruments: Recognition and Measurement” (“IAS 39”). The replacement of IAS 39 is a multi-phase project with the objective of improving and simplifying the reporting for financial instruments and the issuance of IFRS 9 is part of the first phase of this project. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. IFRS 9 requires a single impairment method to be used, replacing multiple impairment methods in IAS 39. For financial liabilities measured at fair value, fair value changes due to changes in an entity’s credit risk are presented in other comprehensive income. IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Company does not expect the implementation to have a significant impact on the Company’s results of operations, financial position and disclosures.

The IASB has issued an amendment to IAS 1, Presentation of Financial Statements (“IAS 1”), which requires entities to group items presented in other comprehensive income (OCI) on the basis of whether they might at some point be reclassified from OCI to profit or loss at a later date when specified conditions are met. By requiring items of OCI to be grouped on this basis, their potential effect on profit or loss in future periods will be clearer. This amendment is effective for annual periods beginning on or after July 1, 2012 and requires full retrospective application. The Company does not expect IAS 1 to have a material impact on the financial statements.

(Expressed in Canadian dollars, unless specifically indicated otherwise)

4. Inventory:

As at March 31	2012	2011
Raw materials	$ 893,383	$ 869,984
Work in process	431,824	693,820
Finished goods	355,619	318,405
	$ 1,680,826	$ 1,882,209

For the three months ended March 31, 2012, inventory recognized as an expense in cost of sales amounted to $1,216,099 (March 31, 2011 - $1,166,547). Included in the above amounts were inventory write downs of $ Nil (2011 - $ Nil). There were no reversals of previously recorded inventory write downs for 2012 (2011 - $ Nil). As of March 31, 2012, the Company anticipates the net inventory will be realized within one year.

5. Property and equipment:

	Laboratory equipment	Computers, office furniture and equipment	Production equipment	Leasehold improvements		Total
Asset Cost						
Balance January 1, 2011	317,153	307,403	333,057	370,184	-	**1,327,797**
Reclasses						
Additions	29,293	3,695	3,193	1,226		**37,407**
Disposals						-
Balance December 31, 2011	**346,446**	**311,098**	**336,250**	**371,410**		**1,365,204**
Additions	-	-	2,000	12,500		**14,500**
Disposals			-			-
Balance March 31, 2012	**346,446**	**311,098**	**338,250**	**383,910**		**1,379,704**
Accumulated amortization						
Balance January 1, 2010	201,603	178,458	247,555	297,218	-	**924,834**
Reclasses		-				
Amortization for period	22,495	25,900	26,141	74,192		**148,728**
Disposals						-
Balance December 31, 2011	**224,098**	**204,358**	**273,696**	**371,410**		**1,073,562**
Amortization for period	2,610	5,337	7,767	416		**16,130**
Disposals						-
Balance March 31, 2012	**226,708**	**209,695**	**281,463**	**371,826**		**1,089,692**
Carrying Amounts						
At January 1, 2011	115,550	128,945	85,502	72,966		**402,963**
At December 31, 2011	122,348	106,740	62,554	-		**291,642**
At March 31, 2012	119,738	101,403	56,787	12,084		**290,012**

PHOTON CONTROL INC.

Notes to Consolidated Financial Statements
(Expressed in Canadian dollars, unless specifically indicated otherwise)

For the three months ended March 31, 2012 and 2011

6. Intangible assets:

	Patents	Trademarks	Computer software	Computer system (SW)	Total
Asset Cost					
Balance January 1, 2011	363,450	28,602	90,573	98,888	**581,513**
Additions	13,568	-		46,264	**59,832**
Disposals					-
Balance December 31, 2011	**377,018**	**28,602**	**90,573**	**145,152**	**641,345**
Additions	-	-		-	**-**
Disposals	-				-
Balance March 31, 2012	**377,018**	**28,602**	**90,573**	**145,152**	**641,345**
Accumulated amortization					
Balance January 1, 2011	192,060	22,436	90,573	-	**305,069**
Amortization for period	44,077	1,541	-	34,866	**80,484**
Disposals					-
Balance December 31, 2011	**236,137**	**23,977**	**90,573**	**34,866**	**385,553**
Amortization for period	9,093	-		8,270	**17,363**
Disposals					-
Balance March 31, 2012	**245,230**	**23,977**	**90,573**	**43,136**	**402,916**
Carrying Amounts					
At January 1, 2011	171,390	6,166	-	98,888	**276,444**
At December 31, 2011	140,881	4,625	-	110,286	**255,792**
At March 31, 2012	131,788	4,625	-	102,016	**238,429**

(Expressed in Canadian dollars, unless specifically indicated otherwise)

7. Share capital:

(a) Authorized:

Unlimited number of common shares without par value

(b) Issued and outstanding:

Common shares:

		Number of shares	Stated values
Issued and outstanding as at December 31, 2010	$	102,909,518	$ 28,246,173
Shares issued in 2011		-	-
Issued and outstanding as at December 31, 2011	$	102,909,518	$ 28,246,173
Shares issued in 2012		-	-
Issued and outstanding as at March 31, 2012	$	102,909,518	$ 28,246,173

Contributed Surplus:

	Amount
Balance, December 31, 2011	$ 1,951,100
Stock-based compensation to employees	46,803
Balance, December 31, 2012	$ 1,997,903
Stock-based compensation to employees	10,500
Fair value of options exercised	-
Balance, March 31, 2012	$ 2,008,403

(Expressed in Canadian dollars, unless specifically indicated otherwise)

7. Share capital (continued):

(c) Stock options:

The number of options reserved for issuance under the Company's stock option plan is equal to 10% of the issued and outstanding shares in the Company. Accordingly, as at December 31, 2011, the Company's board of directors had reserved 10,290,952 options for issuance under the Company's stock option plan. As of December 31, 2011, there was no change in either the number of shares or the reserved 10,290,095 options. The stock option plan provides that options may be granted with an exercise price of no less than the market price of the Company's stock on the grant date less applicable discounts permitted by the TSX-V. The stock option plan also provides that the term of the options shall not exceed five years.

Stock option transactions are summarized as follows:

	Number of share options	Weighted average exercise price
Outstanding, December 31, 2010	4,592,500	$ 0.10
Granted	20,000	0.12
Granted	10,000	0.11
Granted	20,000	0.10
Cancelled	(575,000)	0.10
Expired	(535,000)	0.10
Exercised	-	0.00
Outstanding, December 31, 2011	3,532,500	$ 0.10
Granted	-	0.00
Cancelled	(92,500)	0.10
Expired	-	0.00
Exercised	-	0.00
Outstanding, March 31, 2012	3,440,000	$ 0.10

Nil stock options were granted during the month ended March 31, 2012 (March 31, 2011 – Nil options granted).

(Expressed in Canadian dollars, unless specifically indicated otherwise)

7. Share capital (continued):

(c) Stock options (continued):

The following table summarizes the stock options outstanding at March 31, 2012:

	Options outstanding			Options exercisable	
Exercise price	Number of shares	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
$0.10	3,390,000	1.84	$ 0.100	2,015,000	$ 0.100
$0.105	10,000	3.50	$ 0.105	2,500	$ 0.105
$0.11	20,000	3.85	$ 0.110	2,500	$ 0.110
$0.115	10,000	3.70	$ 0.115	2,500	$ 0.115
$0.135	10,000	4.15	$ 0.135	-	$ 0.135
	3,440,000	1.87	$ 0.100	2,022,500	$ 0.100

The options outstanding at March 31, 2012 expire between October 8, 2012 and September 21, 2016.

The fair value of options granted was estimated on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	2012	2011
Expected option lives	5 years	5 years
Risk-free interest rate	1.44% to 2.59%	1.44% to 2.59%
Dividend yield	0%	0%
Volatility	123% to 371%	150% to 370%

During the three months ended March 31, 2012, the Company recorded $10,500 (2011 - $22,812) of compensation expense representing the fair value of the options and shares vesting during the year with a corresponding increase to contributed surplus.

7. Share capital (continued):

(d) Net earnings (loss) per share:

The weighted average number of shares outstanding as at March 31, 2012 of 102,909,518 (March 31, 2011 - 102,333,056) was used in the calculation of basic earnings per share and 106,379,925 (March 31, 2011 - 106,651,719) was used in the calculation of diluted earnings per share.

8. Adoption of IFRS:

The Company's financial statements have been prepared to comply with IFRS (International Financial Reporting Standards) for the three months ending March 31, 2012.

The year ending December 31, 2011 were the first annual financial statements to be IFRS compliant.

9. Related party balances and transactions:

(a) Related company balances and transactions:

All transactions with related parties have been translated in the normal course of operations and have been measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. Related party transactions include transactions with Photon Control R&D Ltd. Photon Control R&D Ltd. commenced providing engineering consulting and research and development services to the Company on October 1, 2008 and, as a result, the Company has reduced its internal research and development operations. The Company subleases space to Photon Control R&D Ltd. at the same facility. The Company charges Photon Control R&D Ltd. premises and related expenses to recover the Company's costs. Amounts outstanding with Photon Control R&D Ltd. are non-interest bearing, unsecured and due on demand. This account is active and payments are received on a monthly basis, and the balance is paid out at least twice during the year.

(Expressed in Canadian dollars, unless specifically indicated otherwise)

9. Related party balances and transactions (continued):

As at March 31	2012	2011
Balance Sheet		
Accounts receivable	$ 1,040,720	$ 937,299
Note receivable	183,504	191,637
Accounts payable and accrued liabilities	209,623	279,540
Statement of Operations		
Recovery of premises and related expenses	$ 50,044	$ 55,586
Payroll Reimbursement	358,674	335,967
Engineering, research and development services expenses	97,740	127,259
Royalty expenses	112,598	47,863
Revenue from sales of products and services	38,552	65,412

The Company indemnifies its directors and officers against any and all claims or losses reasonably incurred in the performance of their service to the Company to the extent permitted by law. The Company has acquired and maintains liability insurance for directors and officers of the Company.

During 2009, the Company finalized and amended the terms of its agreement to transfer its R&D workforce to Photon Control R&D Ltd. Under the finalized terms, Photon Control R&D Ltd. issued a $315,000 promissory note to the Company as consideration for the transfer. The promissory note bears a coupon rate of 3% per annum, is repayable in equal monthly instalments of $3,089 beginning April 1, 2010 and matures March 1, 2020. For accounting purposes, the transaction was recognized at the exchange amount and the promissory note was discounted at an estimated market rate of 10% resulting in a carrying value of the note receivable at issuance of $217,487 and a deferred gain as at March 31, 2010. The deferred gain of $24,668 was recognized in income as principal payments on the note receivable, collected by the Company. The promissory note receivable is being accreted up to its face value of $315,000 by the effective interest method and as at March 31, 2012, $18,025 (2011 - $4,148) in accretion was recognized in interest income.

(Expressed in Canadian dollars, unless specifically indicated otherwise)

9. Related party balances and transactions (continued):

As at March 31	2012	2011
Promissory note receivable – face value	$ 315,000	$315,000
Less: discount	(97,513)	(97,513)
	217,487	217,487
Accretion	18,025	4,184
Principal repayment	(52,008)	(30,034)
Carrying amount	183,504	191,637
Current portion	(26,985)	(29,600)
Long-term portion	$156,519	$162,037

(b) Compensation of key management personnel:

The Company's key management personnel have authority and responsibility for overseeing, planning, directing and controlling the activities of the Company and consist of the Company's Board of Directors and the Company's Executive Leadership Team. The Executive Leadership Team consists of the CEO and President, and the Chairman. (Compensation for 2012 below reflects departure of Chief Technology Officer.)

Total compensation expense for key management personal and the composition thereof, is as follows:

As at March 31	2012	2011
Short term benefits	$ 54,120	$ 104,120
Post-employment benefits	-	-
Termination benefits	-	-
Share-based compensation	-	-
Carrying amount	$ 54,120	$ 400,236

(Expressed in Canadian dollars, unless specifically indicated otherwise)

10. Commitments and contingencies:

(a) Leases:

The Company has entered into premises leases requiring the following minimum lease payments and related costs as follows:

2012 (as at March 31)	$	472,260
2013		674,852
2014		720,572
2015		766,245
2016		812,047
	$	3,445,976

For the year ended March31, 2012, lease payments and related costs recognized as an expense amounted to $157,420 (2011 - $148,489)

(b) Litigation:

In October 2001, a former member of management and President of the Company (the "Claimant") initiated an arbitration proceeding asserting that certain amounts were owing to him by the Company. The Company had commenced an action against the Claimant for a declaration that it had properly rescinded a loan agreement between the Company and the Claimant dated March 5, 2001 (the "Loan Agreement") and that the debt owed to the Claimant (the "Claimant Debt"), being $340,887 as at the date of the Loan Agreement, was repayable in shares of the Company at a rate of one share per dollar of debt.

In addition, the Claimant has filed a claim against the Company seeking unspecified damages for wrongful dismissal. The Company considered the allegations in the lawsuit to be without merit and subsequently proceeded to defend the action.

The Company's application to dismiss the claim was denied in September 2009. The trial commenced on May 9, 2011 but did not complete on May 20, 2011 as scheduled. The trial resumed on June 13 and was completed on June 17, 2011.

As announced in the News Release dated August 2, 2011, the Supreme Court of British Columbia has released a decision that the Company did not have the right to rescind the Loan Agreement and that this debt is repayable in accordance with the Loan Agreement. The amount of the Claimant Debt payable is $374,562 including interest as at September 30, 2010 plus interest thereafter. The Court also ruled that the Claimant was dismissed without cause in 2001 and awarded 18 months notice at $130,000 per year in salary plus the value of the benefits payable to him.

10. Commitments and contingencies (continued):

As announced in the News Release dated September 12, 2011, Photon Control has filed a Notice of Appeal from the decision of the Supreme Court of British Columbia, and the appeal is from the Court's decision on both rescission of the loan agreement and the dismissal of the Claimant from the Company. Subsequently, the Company's appeal of both the loan agreement decision and the wrongful dismissal decision was heard by the British Columbia Court of Appeal on March 15 and 16, 2012. At the end of the hearing, judgement was reserved, without any indication as to how long the Court of Appeal's judgment may be reserved therefore appropriate adjustments to the charge will be made in the Company's future 2012 financial statements to reflect the decision of the Court.

A charge for the Claimant Debt in the amount of $310,499 was previously taken by the Company as a long term liability and was reported on the Company’s previous financial statements. Subsequently, the Company recorded an additional $539,501 in Q4 2011 to reflect the decision of the Court and the current estimate of this claim. Both of these amounts, totalling $850,000, were classified in Q4 2011 as a contingent liability (dependent upon the results of the appeal in the current fiscal 2012) per IAS 37. Related to this issue, the Company has provided a $850,000 standby irrevocable letter of credit as a guarantee against this lawsuit (included on restricted cash).

(Expressed in Canadian dollars, unless specifically indicated otherwise)

11. Supplementary information:

As at March 31	2012	2011
General and administrative:		
Salaries and fees	$ 175,726	$ 172,183
Office premises expenses	62,760	73,642
Legal, filing fees and auditing	58,416	288,695
Legal judgements (Contingent)	-	-
Audit	15,000	39,033
Insurance	43,673	41,062
Stock option compensation expense	-	-
Depreciation and amortization	8,302	3,735
Other expenses	25,128	44,419
	$ 389,005	$ 662,769
Engineering expenses:		
Salaries and fees	$ 4,601	54,692
Materials	-	679
Certification and testing	5,149	-
Travel and entertainment	-	-
Consulting fees	97,740	127,259
Depreciation and amortization	8,793	-
Other expenses	589	-
	$ 116,872	$ 182,630
Business development and marketing:		
Salaries and consulting fees	$ 38,615	$ 14,826
Travel expenses	5,799	743
Trade shows	12,691	-
Promotion	3,661	37,054
Depreciation and amortization	300	-
Other expenses		48
	$ 61,066	$ 52,671

(Expressed in Canadian dollars, unless specifically indicated otherwise)

12. Financial instruments:

Fair Value of Financial Assets and Liabilities:

The Company has no financial instruments recorded fair value as at March 31, 2012, nor as at December 31, 2011.

The note receivable from related party is measured at amortized cost. Its market value was determined at inception based upon discounting contractual cash flows at estimated market discount rates considering the credit risk of the counterparty. The estimated market value as at March 31, 2012 is estimated to approximate its carrying value.

The fair value of the Company's cash and cash equivalents, trade accounts receivable and other amounts due under credit facility, amounts due to and from related parties, accounts payable and accrued liabilities approximate their respective carrying amounts due to their short maturities or are discounted at market interest rates.

Risk Management:

(a) Credit and interest rate risk:

The Company is exposed to credit risk associated with its trade accounts receivable and related party receivables. Credit risk is minimized substantially by ensuring the credit worthiness of the entities with which it carries on business. In November 2009, the Company entered into an agreement with Export Development Canada to insure its non-Canadian accounts receivable up to a maximum of USD $1,500,000. As at March 31, 2012 the maximum credit risk, which is the total of its uninsured trade receivables (primarily Canadian based customers and intercompany), was $1,146,974 or 36% (March 31, 2011 - $ 687,235 or 29%) of the total outstanding accounts receivable balances.

The following table provides information regarding the ageing of trade receivables as at March 31, 2012:

Current	31-60 days	61-90 days	91 days +
50%	36%	4%	10%

The following table provides information regarding the aging of trade receivables as at March 31, 2011:

Current	31-60 days	61-90 days	91 days +
47%	23%	9%	21%

The Company holds its cash and cash equivalents at a major Canadian banking institution. As at March 31, 2012, the Company was not exposed to significant credit or interest rate risk.

12. Financial instruments (continued):

Allowance for Doubtful Accounts

At each period end, the Company reviews the collectability of outstanding receivables. The specific accounts are only written off once all the collection avenues have been explored or when legal bankruptcy has occurred. The following is a reconciliation of the allowance account.

Reconciliation of the allowance for doubtful accounts	March 31, 2012	March 31, 2011
Balance, beginning of the year	$ 143,135	$ 108,130
Write-offs of specific accounts	-	-
Change in provision-	-	-
Balance, as at March 31	$ 143,135	$ 108,130

The following table identifies the percentage of trade accounts receivable from individual customers comprising 10% or more of the Company's trade receivables:

	2012	2011
Customer A	46%	31%
Customer B	23%	17%
Customer C	-	11%

(b) Market, interest and foreign exchange risk:

Market risk is the risk that changes in market prices such as foreign exchange rates and interest rates will affect the Company's net earnings or the values of financial instruments. The Company is exposed to interest rate risk with regard to the cash, cash equivalents and amounts due under credit facility and its related party note receivable. The majority of the Company's sales revenues and trade receivables are denominated in United States dollars. As such, the Company may be subject to material, realized and unrealized exchange gains or losses resulting from above average changes in exchange rates between the Canadian and the United States dollar. As at March 31, 2012, the Company did not utilize any forward exchange contracts to mitigate any of the risks as mentioned above. The following table lists the United States dollar balances of monetary items denominated in United States dollars as at March 31:

Amounts denominated in U.S. dollars as at March 31	2012	2011
Cash	$ 1,285,172	$ 933,898
Trade accounts receivable	1,985,489	2,192,085
Trade accounts payable	55,513	333,653

(Expressed in Canadian dollars, unless specifically indicated otherwise)

12. Financial instruments (continued):

The estimated impact on net earnings at March 31, 2012 with a +/- 10% change in foreign exchange rates is $312,514 (March 31, 2011 - $279,233).

The above sensitivity demonstrates the effect of a change in foreign exchange rates in isolation. In reality, there may be other contributing factors that will materially alter the estimated outcome. Furthermore, the financial position of the Company may vary at the time that a change in foreign currency exchange rates occurs, again, causing the impact on the Company's results to differ materially from the estimated outcome shown above.

(c) Liquidity risk:

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The ability to do this relies on the Company being able to successfully rely on external financing as well as the timely collection of its outstanding trade accounts receivable. As at March 31, 2012, the Company's accounts trade payable and accrued liabilities were $1,046,519 (2011 - $1,547,361) which fall due for payment within twelve months of the balance sheet date. As at March 31, 2012, the Company had an unutilized credit facility of $500,000 (unutilized as at March 31, 2011). The Company has recorded a provision (contingent liability) of $850,000 (March 31, 2011 - $310,499) which may become due in 2012. However, a $850,000 standby irrevocable letter of credit has been provided as a guarantee against this lawsuit (included on restricted cash).

Significant cash commitments in years subsequent to March 31, 2012 are as follows:

	1 year	2 years	3 years	4 years	5 years	Total
Accounts trade payable and accrued liabilities	$1,046,519	$ -	$ -	$ -	$ -	$1,046,519
Due to related party	209,623	-	-	-	-	209,623
Lease obligation	472,260	674,852	720,572	766,245	812,047	3,445,976
Credit facility	-	-	-	-	-	

13. Capital disclosure:

The Company's objectives when managing capital are:

- To maintain its ability to continue as a going concern.
- To provide adequate working capital.
- To maintain cash on hand in highly liquid and highly rated financial instruments.
- Meet the debt covenants imposed by the Company's banking institution.

(Expressed in Canadian dollars, unless specifically indicated otherwise)

13. Capital disclosure (continued):

The Company includes the following items in the management of capital: cash, cash equivalents, credit facility and shareholders' equity comprised of issued capital, contributed surplus and deficit. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions. The Company may adjust its capital structure in the future, by issuing shares and adjusting debt utilization. As at March 31, 2012, the Company's capital is as follows:

As at March 31	2012	2011
Credit facility	$ -	$ -
Cash	1,458,713	837,416
Net cash (debt)	1,458,713	837,416
Shareholders' equity	9,798,019	4,980,142
	$ 11,256,732	$ 5,817,558

The Company is subject to the following capital requirements relating to the covenants and conditions of its bank line of credit:

- The working capital ratio shall not be less than 1.1:1.
- The debt to tangible net worth ratio shall not at any time exceed 2.75:1.
- There will be no dividends, reduction in loans from shareholders, subsidiaries or related parties, or other withdrawals of similar nature without the prior consent of the bank.
- The bank reserves the right to require foreign receivables to be insured by the EDC with direction by the Company to pay all insurance proceeds to the bank.

The Company was in compliance with the above noted covenants as at March 31, 2011, and at March 31, 2012.

14. Bank credit facility and restricted cash:

In November 2007, the Company secured a bank operating line credit facility of up to $500,000 under the Export Development Canada's Master Accounts Receivable Guarantee (MARG) program. This credit facility is secured by a cash deposit of $50,000 plus interest earned thereon, a general security agreement, a general assignment of book debts and a $450,000 MARG program with Export Development Canada and assignment of all risk insurance coverage. This facility bears interest at the bank's prime plus 1.25% per annum.

(Expressed in Canadian dollars, unless specifically indicated otherwise)

14. Bank credit facility and restricted cash (continued):

The Company also obtained a corporate credit card in June 2007. The credit card is secured by a $51,750 cash deposit. The deposit earns interest at prime minus 2.35%. The facility is subject to periodic review by the bank not less frequently than annually. All amounts outstanding under the credit facility are due on demand.

In addition, restricted cash also includes $850,000 as a guarantee against a lawsuit for which judgement in 2011 was rendered in favour of the Plaintiff. (See Note 10 (b) Litigation.)

As at March 31	2012	2011
Bank operating line of credit cash deposit	$ 50,000	$ 50,000
Credit card cash deposit	53,744	53,744
Change in provisions	850,000	-
Balance as at March 31	$ 953,744	$ 103,744

15. Segmented information:

Photon Control Inc. designs and manufactures a wide range of optical sensors and instruments to measure temperature, pressure, position, and flow. These products are used by original equipment manufacturers (OEM) as well as end-users in the Semiconductor, Oil and Gas, Power, Life Science, and Manufacturing industries. Photon Control's products have competitive advantages in both performance and cost. Photon Control's approach to creating shareholder value has been to pursue Original Equipment Manufacturer (OEM) sales whether directly or through a distributor and to investigate the market potential of products by working directly with customers in select industries to foresee their sectors' requirements. These collaborations often include commitments to conduct trials of the new products on industrial sites.

(a) Geographic information:

Information regarding revenue earned from major customers by geographic segments, based on the location of the customer, is as follows:

	For the three months ended	
	March 31, 2012	**March 31, 2011**
Revenue:		
Canada	$ 100,344	$ 108,781
United States	2,011,851	2,362,007
Europe	5,630	5,698
Taiwan	-	4,456
China	840,493	540,317
Russia	84,903	10,550
Other	28,506	218,494
Total	$ 3,071,727	$ 3,250,303

(Expressed in Canadian dollars, unless specifically indicated otherwise)

15. Segmented information (continued):

All of the Company's equipment and intangible assets are located in Canada.

(b) Major customers:

The following table identifies the percentage of revenue generated from individual customers comprising 10% or more of the Company's revenue:

As at March 31	2012	2011
Entity A	44%	40%
Entity B	27%	17%
Entity C	10%	10%
Entity D	5%	9%
	86%	76%

16. Trade payables and accrued liabilities

As at March 31	2012	2011
Trade payables	$ 548,575	$ 922,854
Accrued liabilities	366,354	415,862
Warranty provision	131,590	208,646
	$ 1,046,519	$ 1,547,362

The following is a reconciliation of the warranty provision during the year.

Reconciliation of warranty provision as at March 31	2012	2011
Provision as at March 31, beginning of the year	$ 137,792	$ 193,851
Warranty Costs incurred	(37,225)	(18,057)
Warranty provision - additions or changes	31,023	32,852
Balance as at March 31	$ 131,590	$ 208,646

Due to the uncertainty surrounding the timing of warranty returns, the entire provision has been classified as current.

17. Subsequent Events:

See Note 10 (b) for subsequent events with respect to litigation issues.