

# **CRS Electronics Inc.**

## **Management Discussion and Analysis**

**Third Quarter Report  
For the three and nine month period ended September 30, 2013**

November 25, 2013

The following information prepared as of November 25, 2013 is Management's Discussion and Analysis ("MD&A") of the financial condition and performance of CRS Electronics Inc. (the "Company" or "CRS") for the three and nine months ended September 30, 2013 and should be read in conjunction with the audited financial statements for the year ended December 31, 2012 which have been prepared in accordance with International Financial Reporting Standards ("IFRS"). All amounts are in United States (U.S.) dollars unless otherwise noted (tabular amounts are in thousands of U.S. dollars).

This MD&A is the responsibility of management. The Board of Directors carries out its responsibility for the review of this disclosure principally through its Audit Committee, of which half the members are independent. The Audit Committee reviews and prior to its publication, approves, pursuant to the authority delegated to it by the Board of Directors, this disclosure.

### **Forward-Looking Information**

The statements made in this MD&A, particularly those in the "Outlook" section that are not historical facts, contain forward-looking information that involves risk and uncertainties. All statements, other than statements of historical facts, which address CRS' expectations, should be considered forward-looking statements. Such statements are based on management's exercise of business judgment as well as assumptions made by management and with information currently available to management. When used in this document, the words "may", "will", "anticipate", "believe", "estimate", "expect", "intend" and words of similar import, are intended to identify any forward-looking statements. The forward-looking statements made in this MD&A describe management's expectations as at November 25, 2013.

You should not place undue reliance on these forward-looking statements. These statements reflect management's current view of future events and are subject to certain risks and uncertainties as contained in the Company's filings with Canadian securities regulatory authorities. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results could differ materially from those anticipated in these forward-looking statements. Management undertakes no obligation to reflect events or circumstances after the date hereof, or to reflect the occurrence of any unanticipated events. Although the Company believes that their expectations are based on reasonable assumptions, the Company can give no assurance that the forward-looking statements will materialize. Subject to applicable laws, the Company assumes no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or any other reason.

The material assumptions that were applied in making the forward-looking statements in this MD&A include: execution of the Company's existing plans and development programs for its product line, either of which may change due to changes in the views of the Company or if new information arises which makes it prudent to change such plans or programs; and the accuracy of current interpretation of market study results.

For a description of material factors that could cause actual results to differ materially from the forward-looking statements in this MD&A, please see the "Risk and Uncertainties" section.

## **Overview**

For over 14 years, CRS has been a developer and manufacturer of light emitting diode ("LED") light products. As a manufacturer of LED indicator lights for Blue Bird Corporation buses and other light applications, CRS realized that the improvement in LEDs created an opportunity for CRS to supply LED based indoor and outdoor lighting. Throughout 2007 to 2013 inclusive, CRS expended a significant amount of time and capital to develop, manufacture and market an LED MR16 halogen bulb replacement and LED PAR series of interior lights for the residential market sector. However, CRS was unable to earn positive margins due to high Canadian labour rates and severe residential price pressure through retailers.

CRS is currently focused on the expansion of its lamps to the North American interior light replacement market at a commercial level and has exited the residential market sector completely. The residential market value proposition did not align with CRS' considerable product features, market price or cost structure. CRS seeks to expand into the North American LED fixture market at a commercial level to leverage market leading intellectual property designed into its products. Converting the Welland, Ontario manufacturing facility to an Asian supply chain has also been a key 2013 objective. The North American commercial marketplace continues to adopt LED technology at a rapid pace. CRS management believes the marketplace will be fruitful for both LED lamps and fixtures for years to come.

## **Outlook**

For Fiscal 2013 the Company is focusing on finalizing the supply chain conversion to Asia, changing its Welland facility to the North American distribution center for LED lamps, and preparing a final assembly production line for LED fixtures to sell into the North American commercial market. Management added regional sales managers with LED commercial marketplace experience who have established strong relationships with electrical distributors, end users and lighting designers. The LED lamp portfolio has achieved the gold standard in 3<sup>rd</sup> party validation by achieving Energy Star® certification and ETL certification to support commercial sales efforts.

## **Business Objectives and Milestones**

CRS' overall business objective is to gain market share in the LED commercial lighting market to provide an economic return to its shareholders.

### ***Sales Objectives***

#### **1. Commercial LED lamp sales**

Our objective is to expand sales in the commercial lamp replacement market. CRS is beginning to introduce LED commercial lamps to North America. The company has strategically targeted the most commonly used commercial lamp categories for LED replacements: MR16, GU10, PAR 20, PAR 30, PAR 38, R20, BR30 and BR40 lamps. Independent laboratory testing confirms CRS LED lamps produce more light output, operate using less wattage, dim smoothly to 1% light output and are offered with a wider range of colour temperature than any other brand. These best in class products have been demonstrated by CRS regional managers to electrical distributors, end users and lighting specifiers throughout North America. The typical response has been overwhelmingly positive. Finished products are now being built and sold.

#### **2. Bus light business and contract LED light board manufacturing**

CRS continues to support our partners in these market segments. Over many years CRS has developed strong partnerships and the product lines deliver consistent gross margins. CRS plans to work with partners to meet their needs and maintain current sales volumes.

#### **3. Lighting fixture sales**

CRS will introduce LED light fixtures to North America. They will be represented by commercial lighting agents and sold through electrical distribution. Finalized designs are being prototyped with an expected launch in the first quarter of 2014. Designs include industry innovations in light output and maintenance. Initial market feedback has been extremely positive. Recruiting an experienced sales management and customer service staff is underway.

### ***Product Development Objectives***

#### **1. Product cost reduction**

CRS expects continued demand for lower cost offerings for customers. Therefore the Company has solidified our Asian supply chain and realized a significant decrease in product costs while maintaining CRS' high performance and specification standards.

## 2. Product development

Market research has shown that Energy Star® ratings have strong consumer recognition and provide confidence for selection of sound, energy efficient LED lamps. The Company has received Energy Star® certifications for the majority of its new family of LED lamps and continues to aggressively pursue certification on the remaining LED lamps. Preliminary results indicate that CRS' LED lamps will contain best in class light output and dimming compatibility which are two critical components of value in the marketplace. Fixtures require ETL certification. Both remaining certifications will be achieved by January 2014. CRS will work jointly with its strategic partners to provide performance specifications that are at the 'head of the class' for professional series commercial lights.

## **Performance of CRS**

### ***Key Performance Indicators***

The key performance indicators for CRS are revenue growth, gross profit, EBITDA, net income, and increasing patent protection on intellectual property.

The success of the Company to expand will be measured by revenue growth. Revenue growth will be dependent on the Company being able to expand production capacity to meet the anticipated demand for its products.

The Company is targeting gross margin percentages (defined as revenues less cost of sales and plant expenses as a percentage of revenues) of approximately 35.0% on an annual basis. Maintaining a consistent gross margin will be an indicator of how well the Company is managing its production costs and customer contract negotiations. The Company is looking at various product development and outsourcing alternatives to increase gross margin.

Management believes that EBITDA is a measure of how efficiently and effectively the business is operating. The Company is entering a period of rapid expansion and growth and therefore general and administrative costs have increased over the last eight quarters. To maintain an acceptable EBITDA, management will need to balance the increase in general and administrative costs and revenue growth. Net income is also viewed as an important measure for determining the value created for shareholders.

### ***Measurement***

Below in "Quarterly Results" and "Results of Operations" are two tables the Company uses to assess performance. "Quarterly Results" presents the Company's results for the last eight quarters, followed by a comparison of the Company's year to date results to those of the same period in Fiscal 2012.

**Quarterly Results**

	Fiscal 2013			Fiscal 2012			Fiscal 2011	
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
<i>In thousands of dollars</i>	USD	USD	USD	USD	USD	USD	USD	USD
Sales	437.0	565.3	738.5	463.3	607.1	687.7	1,312.0	526.6
Gross loss	(243.2)	(109.1)	(262.3)	(750.1)	(348.1)	(277.3)	(357.6)	(384.1)
<i>Gross loss%</i>	(55.7%)	(19.3%)	(35.5%)	(161.9%)	(57.3%)	(40.3%)	(27.3%)	(72.9%)
Select expenses								
Selling and marketing	236.4	118.8	129.5	446.2	118.0	278.9	571.6	352.7
General and administrative	442.1	571.5	386.5	566.7	719.5	453.2	512.0	427.4
Engineering and research	187.1	236.5	132.3	61.0	103.2	106.5	112.8	175.8
Foreign exchange (gain) loss	(68.7)	108.2	77.2	49.6	(175.6)	(147.6)	30.1	(57.4)
Total expenses	796.9	1,035.0	725.5	1,123.5	765.1	691.0	1,226.5	898.5
Income (loss) from operations	(1,040.1)	(1,144.1)	(987.8)	(1,873.6)	(1,113.2)	(968.3)	(1,584.1)	(1,282.6)
Add back: Depreciation and amortization	80.9	79.6	76.0	107.5	109.4	112.3	111.8	125.1
EBITDA Loss	(959.2)	(1,064.5)	(911.8)	(1,766.1)	(1,003.8)	(856.0)	(1,472.3)	(1,157.5)
Finance costs	(12.6)	(12.4)	(7.3)	(10.1)	2.8	(34.3)	(23.2)	(18.9)
Refundable tax credit expense	-	-	-	-	-	-	-	(41.3)
Depreciation of equipment, furniture and leaseholds	(46.4)	(46.2)	(44.4)	(70.6)	(72.2)	(75.7)	(76.1)	(67.5)
Amortization of intangibles	(27.6)	(26.6)	(24.8)	(28.5)	(28.8)	(28.7)	(28.0)	(27.5)
Amortization of patents and trademarks	(6.9)	(6.8)	(6.8)	(8.4)	(8.4)	(7.9)	(7.7)	(30.1)
(Loss) Gain on disposal of intangible assets	(0.9)	-	-	-	1.4	-	-	(456.0)
Loss on disposal of patents and trademarks	(3.5)	-	-	(21.8)	-	-	-	(258.2)
Loss on disposal of equipment, furniture and leaseholds	(37.5)	-	-	(237.4)	(13.8)	(5.3)	(0.3)	-
Change in warrant liability	103.6	(54.8)	38.0	170.7	(50.9)	26.3	462.1	13.3
Income taxes recovery	-	-	-	-	-	-	-	-
Net (loss) income	(991.0)	(1,211.3)	(957.1)	(1,972.2)	(1,173.7)	(981.6)	(1,145.5)	(2,043.7)
Loss per share	(0.01)	(0.02)	(0.01)	(0.03)	(0.02)	(0.02)	(0.03)	(0.05)

## Results of Operations

The following table sets out the Company's results for the nine months ended September 30, 2013 compared with the prior year's period then ended.

<i>In thousands of U.S. dollars</i> <sup>(1)</sup>	Nine Months Ended September 30		Increase (Decrease)	% Increase (Decrease)
	2013	2012		
Sales	1,740.8	2,606.8	(866.0)	(33.2%)
Gross profit (loss)	(614.6)	(983.0)	368.4	(37.5%)
<i>Gross profit (loss) percentage</i>	(35.3%)	(37.7%)		
Selling and marketing	484.7	968.5	(483.8)	(50.0%)
<i>As a % of sales</i>	27.8%	37.2%		
General and administrative	1,400.1	1,684.6	(284.5)	(16.9%)
<i>As a % of sales</i>	80.4%	64.6%		
Engineering and research	555.9	322.4		
Foreign exchange (gain) loss	116.7	(293.1)		
<i>Total operating expenses</i>	2,557.4	2,682.4		
<i>Income (loss) from operations</i>	(3,172.0)	(3,665.4)		
Add back amortization	236.5	333.5		
<b>EBITDA Loss</b>	<b>(2,935.5)</b>	<b>(3,331.9)</b>	<b>396.4</b>	<b>(11.9%)</b>
Finance costs	(32.3)	(54.8)		
Depreciation of equipment, furniture and leaseholds	(137.0)	(223.9)		
Amortization of intangibles	(79.0)	(85.6)		
Amortization of patents and trademarks	(20.5)	(24.0)		
(Loss) Gain on disposal of intangible assets	(0.9)	1.4		
Loss on disposal of patents and trademarks	(3.5)	-		
Loss on disposal of equipment, furniture and leaseholds	(37.5)	(19.4)		
Change in warrant liability	86.9	437.4		
<b>Net loss</b>	<b>(3,159.3)</b>	<b>(3,300.8)</b>		

<sup>(1)</sup> Information for 2013 and 2012 is prepared in accordance with IFRS.

**Revenues**

Revenues for the three months ended September 30, 2013 decreased 28.0% to \$437,000 from \$607,100 for the same period in 2012.

Revenue from bus light sales during the three months ended September 30, 2013 decreased 1.5% to \$249,300 from \$253,200 for the same period in 2012. Revenues from contract manufacturing for the three months ended September 30, 2013 increased 31.1% to \$167,300 from \$127,600 in 2012.

Commercial LED revenue for the three months ended September 30, 2013 stemmed from LED MR16 sales that decreased 90.8% to \$20,400 from \$221,900 during the same period in 2012.

Retail LED revenue for the three months ended September 30, 2013 stemmed from LED MR16, GU10, PAR 20, 31, 38, and A19 sales decreased 100% to nil from \$4,400 during the same period in 2012.

Revenues for the nine months ended September 30, 2013 decreased 33.2% to \$1,740,800 from \$2,606,800 for the same period in 2012.

Revenue from bus light sales during the nine months ended September 30, 2013 decreased 1.4% to \$809,700 from \$821,500 for the same period in 2012. Revenues from contract manufacturing for the nine months ended September 30, 2013 increased 122.9% to \$557,700 from \$250,200 in 2012.

Commercial LED revenue for the nine months ended September 30, 2013 stemmed from LED MR16 sales that decreased 62.4% to \$180,100 from \$479,500 during the same period in 2012.

Retail LED revenue for the nine months ended September 30, 2013 stemmed from LED MR16, GU10, PAR 20, 31, 38, and A19 sales that decreased 81.7% to \$193,300 from \$1,055,700 during the same period in 2012.

**Cost of Sales and Gross Loss**

The cost of sales is inclusive of direct material costs, plant labour, plant overheads, plant management salaries, amortization of plant equipment and the amortization of product development costs.

For the three months ended September 30, 2013, gross loss percentage was (55.7%) compared to (57.3%) in the same period last year. For the nine months ended September 30, 2013, gross loss percentage was (35.3%) compared to (37.7%) in the same period last year. The overall decrease in gross loss is primarily attributed to the exit of the Company's retail sales strategy which generated negative margins as the Company transitions to increase sales in the commercial LED market.



***Selling and Marketing Expenses***

For the three months ended September 30, 2013 selling and marketing expenses increased 100.3% to \$236,400 from \$118,000 for the same period in 2012. The increase is a result of establishing a North American commercial market regional management sales team. For the nine months ended September 30, 2013 selling and marketing expenses decreased 50.0% to \$484,700 from \$968,500 for the same period in 2012. This overall decrease reflects the retraction out of the retail sales market and current transition into selling exclusively to the commercial sales market which requires significantly less marketing expenses to be incurred.

***General and Administrative Expenses***

For the three months ended September 30, 2013 general and administrative expenses decreased 38.6% to \$442,100 from \$719,500 for the same period in 2012. For the nine months ended September 30, 2013 general and administrative expenses decreased 16.9% to \$1,400,100 from \$1,684,600 for the same period in 2012. The changes relate primarily to the changes in stock based compensation awarded during the comparative periods.

***Engineering and Research***

Research costs are expensed in the month the costs are incurred. When a product is likely to be commercially viable in the form developed, the costs to complete the development are capitalized on the statement of financial position. When commercial sales begin the development costs are amortized over the expected life of the product.

For the three months ended September 30, 2013 net research and development expenses increased to \$187,100 from \$103,200 for the same period in 2012. For the nine months ended September 30, 2013 net research and development expenses increased to \$555,900 from \$322,400 for the same period in 2012. The Company has incurred additional research and development costs in relation to its commercial lamp and lighting fixture projects developed during the period.

***Finance Costs***

Interest costs are lower during 2013 due to lower average principal outstanding on long-term debt. This is primarily attributable to the finalization of two outstanding loans during January 2013. Accretion expense is related to the non-interest bearing loan from the Southern Ontario Development Program. These expenses are partially offset by interest revenues. The 2013 revenues were due to two redeemable term deposits purchased by the Company with proceeds from the private equity placement issuance of common shares on June 8, 2012. Interest on the term deposits compounded annually at a rate of 1.3% and 1.536%. The 1.3% and 1.536% term deposits matured during July 2013. The funds were re-invested

into a 1.4% term deposit which matured on October 22, 2013 and is discussed below in “Subsequent Events”.

	Three months ended		Nine months ended	
	September 30		September 30	
	2013	2012	2013	2012
Interest on long term debt	\$9,400	\$9,800	\$37,200	\$48,200
Accretion expense	7,300	6,400	23,700	28,900
Less:				
Interest revenue	(4,100)	(19,000)	(28,600)	(22,300)
Net finance costs:	\$12,600	(\$2,800)	\$32,300	\$54,800

Net finance costs for the three month period ended September 30, 2013 increased \$15,400 to \$12,600 from (\$2,800) for the same period in 2012. Net finance costs for the nine month period ended September 30, 2013 decreased \$22,500 to \$32,300 from \$54,800 for the same period in 2012. Finance costs are attributable to a mix of long and short term debt obligations as follows:

Interest on long-term debt decreased 4.1% to \$9,400 during the three months ended September 30, 2013 from \$9,800 during the same period in 2012. Interest on long-term debt decreased 22.8% to \$37,200 during the nine months ended September 30, 2013 from \$48,200 during the same period in 2012. The decrease is related to the finalization of loans which occurred in Q1 2013.

Accretion expense increased 14.1% to \$7,300 during the three month period ended September 30, 2013 from \$6,400 during the same period in 2012. Accretion expense decreased 18.0% to \$23,700 during the nine month period ended September 30, 2013 from \$28,900 during the same period in 2012. The decrease relates to the continued repayment of the loan provided through the Southern Ontario Development Program.

Interest revenue decreased 78.4% to \$4,100 during the three month period ended September 30, 2013 from \$19,000 during the same period in 2012. Interest revenue increased 28.3% to \$28,600 during the nine month period ended September 30, 2013 from \$22,300 during the same period in 2012. The increase relates to the additional interest earned on the redeemable term deposits purchased by the Company with proceeds from the private equity placement on June 8, 2012.

#### ***Depreciation of Equipment, Furniture and Leaseholds***

Depreciation decreased 35.7% to \$46,400 during the three months ended September 30, 2013 from \$72,200 during the same period in 2012. Depreciation decreased 38.8% to \$137,000 during the nine months ended September 30, 2013 from \$223,900 during the same period in 2012. The decrease is related primarily to a disposal of redundant production equipment realized during Fiscal 2012.

***Amortization of Intangible Assets***

The amortization expense decreased \$1,200 to \$27,600 during the three months ended September 30, 2013 from \$28,800 during the same period in 2012. The amortization expense decreased \$6,600 to \$79,000 during the nine months ended September 30, 2013 from \$85,600 during the same period in 2012.

***Amortization of Patents and Trademarks***

The amortization expense decreased \$1,500 to \$6,900 during the three months ended September 30, 2013 from \$8,400 during the same period in 2012. The amortization expense decreased \$3,500 to \$20,500 during the nine months ended September 30, 2013 from \$24,000 during the same period in 2012.

***Foreign Exchange Losses/Gains***

The US dollar is the functional currency of the Company and is also the currency in which it presents these financial statements. The Company recognizes transactions in currencies other than the US dollar (foreign currencies) at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, it retranslates monetary items denominated in foreign currencies at the rates prevailing at that date. It does not retranslate non-monetary items measured in terms of historical cost in a foreign currency. It recognizes exchange differences on monetary items in profit or loss in the period in which they arise. For the three months ended September 30, 2013, CRS incurred a foreign currency gain of \$68,700 compared to a gain of \$175,600 in 2012. For the nine months ended September 30, 2013, CRS incurred a foreign currency loss of \$116,700 compared to a gain of \$293,100 in 2012.

***Loss before Income Taxes, Depreciation and Amortization (“EBITDA”)***

The negative EBITDA loss for the three and nine months ended September 30, 2013 were (\$959,200) and (\$2,935,500) compared to (\$1,003,800) and (\$3,331,900) for the same periods in 2012 as a result in a significant change in foreign exchange loss and decrease in general and administrative expenses during the year.

***Net Losses***

As a result of the above activities, the net loss for the three months ended September 30, 2013 was (\$991,000) or (\$0.01) per share compared to a loss of (\$1,173,700), or (\$0.02) per share for the same period 2012. The net loss for the nine months ended September 30, 2013 was (\$3,159,300), or (\$0.04) per share compared to a loss of (\$3,300,800), or (\$0.06) per share for the same period 2012. The changes in net losses are a result of the increase in foreign exchange losses and research and development and a decrease in depreciation and amortization and warrant liabilities from 2012 to 2013.

## Liquidity and Capital Resources

The following table summarizes the key financial ratios of the Company.

<i>(in U.S. dollars except for ratios)</i>	<b>September 30 2013</b>	September 30 2012
Current Ratio	<b>2.17:1</b>	5.4:1
Cash	<b>\$1,471,817</b>	\$5,780,341
Available Operating Line	<b>\$763,595</b>	N/A
Net Working Capital	<b>\$1,537,561</b>	\$6,336,153
Total Assets	<b>\$3,745,600</b>	\$9,092,089
Total Debt	<b>\$1,711,409</b>	\$2,863,122
Total Equity	<b>\$2,034,191</b>	\$6,228,967
Debt to Equity Ratio	<b>0.84:1</b>	0.46:1

### **Cash Flows**

During the nine month period ended September 30, 2013, CRS experienced negative cash flows used in operations of \$2,678,800 compared to a negative cash flow of \$2,992,200 for the same period in 2012. The decrease in accounts receivable and increase in accounts payable increased the cash flows from operations compared to the same period in 2012. The Company made investments in computer software of \$42,100 and equipment, furniture and leasehold of \$145,800. The Company's various financing activities used \$173,200 compared to providing \$8,044,100 in the same period in Fiscal 2012. The decrease is a result of the large private placement which the company entered into in the same period in Fiscal 2012.

## Outstanding Share Data

As at September 30, 2013 the Company had the following items issued and outstanding:

- Common shares: 71,399,844
- Stock options: 5,600,836

Range of exercise prices (CAD\$)	Number outstanding	Weighted- average remaining contractual life	Weighted- average exercise price (CAD\$)
\$0.24 - \$0.48	5,117,502	49	\$0.25
\$0.58 - \$0.59	483,334	13	\$0.58
<b>Total</b>	<b>5,600,836</b>	<b>46</b>	<b>\$0.28</b>

1,214,170 options are exercisable as at September 30, 2013. The weighted average exercise price of these options is \$0.43.

In March 27, 2008, charitable options to purchase 66,486 common shares were granted to an eligible

charitable organization. These options are exercisable at CAD \$0.30 per share with an expiry date as of March 27, 2018.

## **Commitments and Contingencies**

Due to the nature of the business, the Company may have unspecified contingent liabilities that are not known to the Company at the end of the period. The Company will recognize contingent liabilities in a future period when they become known to the Company.

The Company has the following commitments outstanding:

1. The Company amended its exclusive license agreement with Eveready Battery Company, Inc. (the “Exclusive Agreement”), a subsidiary of Energizer Holdings, Inc., for the Company to manufacture a suite of LED lighting products under the brand name Energizer. The term of the Exclusive Agreement was from January 1, 2011 to December 31, 2015 and is amended to expire at December 31, 2013.

In accordance with the Exclusive Agreement, the minimum guaranteed royalty to be paid by the Company over the remaining term thereof is as follows:

<u>Year</u>	<u>Minimum Guaranteed Royalty</u>
2013	\$ 148,125

2. The Company signed a service agreement with Niagara Regional Broadband Network Limited, for high-speed fiber optic network bandwidth and related management services for the Welland plant. The term of the agreement is from April 1, 2011 to March 31, 2016.

In accordance with the Agreement, the service cost to be paid by the Company over the remaining term thereof is as follows:

<u>Year</u>	<u>IT Hosting Fees</u>
2013	\$ 2,186
2014	8,744
2015	8,744
2016	2,186

3. The Company signed a service agreement with Activo Inc., for high-speed fiber optic network bandwidth and related management services for the Richmond Hill office. The term of the agreement is from August 1, 2012 to June 30, 2016.

In accordance with the Agreement, the service cost to be paid by the Company over the remaining term thereof is as follows:

<u>Year</u>	<u>IT Hosting Fees</u>
2013	\$ 564
2014	2,255
2015	2,255
2016	1,128

4. The Company signed a tenant lease agreement for the use of office space located at 9120 Leslie Street, Suite 102, Richmond Hill, Ontario. The tenant agreement covers general rent of office space, operating costs, utilities and realty taxes. The term of the agreement is from August 1, 2012 to July 31, 2015.

In accordance with the Agreement, the service cost to be paid by the Company over the remaining term thereof is as follows:

<u>Year</u>	<u>Rent</u>
2013	\$ 10,240
2014	43,617
2015	25,673

5. The Company signed a lease agreement for the use of a vehicle. The term of the agreement is from March 20, 2013 to March 20, 2016. In accordance with the agreement, the service cost to be paid by the Company over the remaining term thereof is as follows:

<u>Year</u>	<u>Rent</u>
2013	\$ 2,510
2014	10,040
2015	10,040
2016	1,673

6. On December 28, 2012, GE Lighting Solutions, LLC (“GE”) filed a lawsuit against the Company claiming CRS has infringed two GE patents and has asked for an Order to have CRS destroy all infringing products and related moulds, machine, tooling or other equipment used in their manufacture, to prevent CRS from importing, manufacturing, using, selling and/or offering all infringing products and to have CRS pay damages to GE, together with costs and prejudgment and post-judgment interest. The amount of the claim for damages and costs was not stipulated in the lawsuit. CRS denies any wrongdoing or infringement of any patent owned by GE, believes the claim to be without merit and intends to vigorously defend against the GE lawsuit. No accruals have been made as a result.

## **Financial Instruments**

### ***Fair Value***

The carrying values of cash and cash equivalents, accounts receivable, government incentives receivable, trade and other payables and notes payable do not materially differ from their fair values given their short-term period to maturity. The fair values of finance lease obligations and debt obligations approximate carrying value as the instruments bear interest or are discounted at market rates. The derivative liability is updated each reporting period for changes in its fair value.

### ***Credit Risk***

The Company is exposed to credit risk in the event of non-performance by customers in paying outstanding trade accounts receivable. The three largest accounts receivable balances relate to a bus manufacturer based in the United States, an LED lighting manufacturer based in Canada, and a major Canadian retailer which hold 33%, 7% and 45% of the trade accounts receivable on September 30, 2013, respectively (28.7%, 20.3% and 10.3% on December 31, 2012). The Company has purchased insurance from Export Development Canada to compensate for this risk in addition to monitoring the status of accounts on a regular basis.

Trade accounts receivable are past due when a customer fails to make a payment when contractually due. The Company specifically identifies customers with past due balance (over normal credit term) and provides for these accounts where appropriate. The following is an aging of trade accounts receivable:

	Current	30-60	60-90	over 90	Total
September 30, 2013	79,709	96,684	46,212	219,560	442,165

### ***Interest Rate Risk***

The Company is exposed to interest rate risk on its short-term credit facilities and on a portion of its long-term debt, since the interest rate charged on these facilities fluctuates with the general level of interest rates. However, in management's opinion, this risk is not significant as the short term credit facilities do not represent a significant amount of financing.

***Foreign Currency Risk***

The Company is exposed to currency risk because it makes purchases and sales transacted in Canadian currency. The following accounts were denominated in Canadian dollars:

	<b>September 30</b>	December 31
	<b>2013</b>	2012
Cash	<b>2,298</b>	4,392,331
Trade accounts receivable	<b>255,781</b>	236,628
Trade accounts payable	<b>(11,694)</b>	(60,481)
Bank indebtedness	<b>(128,130)</b>	-
Short-term notes payable	-	(32,256)
Debt obligations	<b>(420,418)</b>	(669,832)

**Subsequent Events**

On October 22, 2013 the ninety day term deposit of 1.4% per annum matured. Of the proceeds received, CAD \$1,000,000 was reinvested into a 90 day 1.4% short term secured investment and CAD \$200,000 was reinvested into a 35 day 1.2% short term secured investment.

On November 13, 2013 the Company announced a proposed private placement to CJL Holding Inc., a corporation related to the Company's Executive Chairman, at a price of \$0.20 per common share for total aggregate proceeds to the company of \$3 million. The investor currently holds approximately 42.6% of the issued and outstanding common shares of the Company. The private placement is subject to satisfaction of customary closing conditions, including receipt of all necessary regulatory approvals, and is expected to close on December 31, 2013.

**Off-Balance Sheet Arrangements**

The Company does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the results of operations or financial condition of CRS including, without limitation, such considerations as liquidity and capital resources that have not previously been discussed.

**Proposed Transactions**

CRS is not a party to any proposed transactions, other than the financing initiatives being pursued as described elsewhere in this document, which may have an effect on the financial condition, results of operations or cash flows or proposed asset or business acquisition or disposition.



## **Critical Accounting Policies**

This MD&A should be read in conjunction with the Company's unaudited condensed interim financial statements for the three and nine months ended September 30, 2013, and the audited annual financial statements for the year ended December 31, 2012. Those financial statements outline the accounting principles and policies used to prepare this MD&A. Accounting policies are critical if they rely on a substantial amount of judgment in their application or if they result from a choice between accounting alternatives and that choice has a material impact on reported results or financial position. There was no significant change to the critical accounting policies from the year ended December 31, 2012 during the three and nine months period ended September 30, 2012.

### ***Accounting standards issued but not yet effective***

Certain pronouncements were issued by the IASB that are mandatory for accounting periods beginning after January 1, 2013 or later periods.

The following new standards, amendments and interpretations have been considered by the Company:

#### **IFRS 9, Financial Instruments (“IFRS 9”):**

In October 2010, the IASB issued IFRS 9. IFRS 9, which replaces IAS 39, Financial Instruments: Recognition and Measurement, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows. This new standard is effective for the Company's financial statements commencing January 1, 2015. The Company is assessing the impact of this new standard on its consolidated financial statements.

#### **IFRS 10, Consolidated Financial Statement (“IFRS 10”):**

In May 2011, the IASB issued IFRS 10. IFRS 10, Consolidated Financial Statements, which replaces the consolidated requirements of SIC-12 Consolidation – Special Purpose Entities and IAS 27 Consolidated and Separate Financial Statements, establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. This new standard is effective for the Company's financial statements commencing January 1, 2013. There are no material changes to the consolidated financial statements as a result of this new standard.

**IFRS 12, Disclosure of Interests in Other Entities (“IFRS 12”):**

In May 2011, the IASB issued IFRS 12. IFRS 12, Disclosure of Interests in Other Entities, establishes new and comprehensive disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. This new standard is effective for the Company's financial statements commencing January 1, 2013. There are no material changes to the consolidated financial statements as a result of this new standard.

**IFRS 13, Fair Value Measurement (“IFRS 13”):**

In May 2011, the IASB issued IFRS 13. IFRS 13, Fair Value Measurement, replaces the fair value guidance contained in individual IFRSs with a single source of fair value measurement guidance. This new standard is effective for the Company's financial statements commencing January 1, 2013. There are no material changes to the consolidated financial statements as a result of this new standard.

**Risk and Uncertainties**

CRS operates in the LED lighting market and is exposed to a variety of risk factors and uncertainties in the normal course of operations. The risks and uncertainties that could materially affect our business, financial condition and results of operations are described in our Annual Report for the fiscal year 2012 which has been filed with Canadian securities regulatory authorities and is available at [www.sedar.com](http://www.sedar.com) under the corporate name CRS Electronics Inc. The risks disclosed in our annual report are not necessarily the only risks and uncertainties we face. Additional risks and uncertainties not presently known to us, or that we currently believe to be immaterial, may also adversely affect our business.

There was no significant change to these risks and uncertainties during the period ended September 30, 2013 other than those described elsewhere in this MD&A.