Management Discussion & Analysis

December 31, 2013

Nanotech Security Corp.

Management's discussion & analysis
as at February 28, 2014

The following discussion and analysis should be read in conjunction with the comparative unaudited consolidated financial statements of the Company for the fiscal quarter ended December 31, 2013, and the notes relating thereto, as well as the Report to Shareholders and other management discussion in this management's discussion and analysis ("MD&A"). Additional information relating to the Company is filed on SEDAR at www.sedar.com.

This report includes forward-looking statements that are based on current expectations and are subject to risks and uncertainties. Statements herein which are directly or by implication forward-looking principally relate to the Company's views that its nano-optical technology will continue to show promise for mass production and commercial application. Other forward looking statements imply that the Company will remain capable of being financed and/or will be able to partner development until commercial sales are eventually realized. The principal risks related to these forward looking statements are that the Company's intellectual property claims will not prove sufficiently broad or enforceable to provide the necessary commercial protection and to attract the necessary capital and/or that the Company's products will not be able to displace entrenched hologram, metalized strip tagging and other conventional anti-counterfeiting technologies sufficiently to allow profitability.

General overview

Nanotech Security Corp. ("Nanotech") was incorporated under the laws of British Columbia in 1984 and has its corporate head office located in Burnaby, British Columbia. Nanotech's wholly owned subsidiary, Tactical Technologies Inc. ("Tactical"), has manufacturing facilities in Holmes, Pennsylvania.

Nanotech is developing what it hopes will prove to be commercially viable nanotechnology for use in anti-counterfeiting and commercial product authentication systems. The technology is being developed under a sublicense from its recently acquired 95% subsidiary, IDME Technologies Corp. IDME in turn holds its license rights pursuant to a 2009 technology sublicense from Simon Fraser University ("SFU") in Burnaby, British Columbia where the technology was originally conceived. The Company is developing specialized optical features using arrays of nano-holes in a substrate material such as polymer and metal, which yield unique light signatures that the Company believes cannot be easily reproduced by a counterfeiter. These optical features can be directly applied to banknotes and other valuable documents and products creating unique optical signatures that are both overt (naked-eye-visible) and machine (only) readable. These features are being designed to be suitable for a variety of other commercial security applications and formats. The sublicense from IDME is available for download at www.sedar.com filed February 4, 2011 and the License from Simon Fraser is now a material agreement of the (consolidated) Company and accordingly has been filed at www.sedar.com on or about the date hereof.

In February 2013, the Company established corporate offices and lab facilities in Burnaby, BC. The Company continued to conduct research through IDME at 4D LABS which is a Canadian federal government sponsored facility located at SFU. Expenditures for the quarter ended December 31, 2013 decreased to a reduced rate of $125,210, compared to $159,400 in same quarter in the previous year. Some of the R&D expenditures were augmented by matching funds from various government R&D incentive programs. The Company believes that work at 4D LABS represents highly cost effective research dollars given the Company is able to avoid the capital costs of a laboratory and certain highly specialized equipment.

The Company's current R&D focus is based on determining the ability of the replicated master shims (or wafer-dies) to transfer the nano-scale images onto selected substrates (continuous roll polymer sheets the width of kitchen wrap) over long production runs (measured in thousands of meters). These tests are being conducted by other third parties and to-date the tests have been very encouraging as described below. R&D work is also being done to enhance the image capabilities of the nanotechnology including color shifts and animation that are not seen with holographic technology. Patent applications and IP legal strategy efforts continued to constitute a significant portion of expenditures. The Company is engaging in follow-on co-operation agreement discussions with several potential users of the technology as well as potential product distribution channel partners.

General Overview (continued)

Since completing its first and second commercial-scale production test-run using its nanotechnology-based optical security feature, the Company has been doing other tests. These tests suggest that our advanced nano-optical technology could be seamlessly incorporated into standard security industry commercial scale manufacturing processes. A second generation of validation tests was also conducted. The production run showed that the Company's origination process and master shims (wafer-dies) used by the third parties' embossing equipment was able to transfer separate and continuous images accurately onto the substrate film over a commercial-scale run. The technology proved to be extremely robust in the high-volume, high-speed setting with the last ten meters performing as strongly as the first ten meters. Images of this film which represents a revolutionary optical-tagging system are available on the Company's website at:
www.nanosecurity.ca/press_imagesvideos.php

A number of trial wafers-dies were produced which have employed a variety of symbols and logos. Additional development was done on the nano-optics design and software that resulted in being able to create more complex colours and shading. A significant achievement from this development was the creation of a master wafer-die of National Geographic's iconic 1980s *Afghan Girl* portrait. Subsequently we experimented with further colour design and were able to create a larger, higher definition version of *Afghan Girl*. These new processes have allowed us to generate a new type of wafer-die that can support bolder, high intense colours as well as subtle colours such as skin tones.

In June 2013, the Company began research and development of a hand casting process for making re-combinations of the master wafer-dies and samples from the wafer-dies. Design and identification of the equipment required for the recombination process was begun and initial part orders were placed. The equipment will enable us to produce custom samples to support our commercial activities by being able to create relevant samples for potential clients. The equipment encompasses the first build out of machinery to be incorporated in our in-house laboratory at our facilities in Burnaby.

The Company's wholly-owned subsidiary, Tactical Technologies Inc. designs, manufactures and sells sophisticated communication, surveillance, intelligence gathering and officer safety equipment for the law enforcement and defense industries in the United States and Canada. The consolidated financial statements include the accounts of Nanotech and its wholly owned subsidiaries, Tactical and IDIT. The consolidated financial statements also include the accounts of 95% owned IDME and 100% owned IDIT Technologies Corp., a patent-holding affiliate. All inter-company transactions and balances have been eliminated on consolidation. Tactical's revenues include the gross amount billed to customers for sales of products delivered and related services provided. Cost of sales includes direct expenses related to the manufacture of products sold.

Results of operations

The consolidated financial statements for the quarter ended December 31, 2013 include the accounts of the Company and its wholly-owned subsidiaries, Tactical and IDIT, and 95% owned IDME. The Company derives substantially all of its revenues through Tactical in United States dollars.

Results of operations (continued)

Selected annual information

	2013	2012	2011
	$	$	$
Revenue	1,810,059	2,083,598	2,403,524
Cost of sales	1,381,398	1,642,612	1,689,671
Gross profit	428,661	440,986	713,853
Expenses	2,477,978	1,972,349	1,556,412
Net loss	(2,049,317)	(1,531,363)	(842,559)
Net loss per common share - basic and diluted	(0.07)	(0.05)	(0.03)

During the fiscal year ended September 30, 2013, the Company received net proceeds of $4,129,912 from the completion of an equity unit (share and warrant) placement.

	$
Use of proceeds from unit placement	
General working capital	2,429,912
Laboratory build out	1,100,000
Research and development	600,000
	4,129,912

Quarterly results – 2014

	December 31, 2013	September 30 2013	June 30 2013	March 31 2013
	$	$	$	$
Revenue	615,935	459,277	402,682	410,272
Net loss	(352,966)	(727,243)	(525,364)	(477,181)
Net loss per common share - basic and diluted	(0.01)	(0.02)	(0.02)	(0.02)

Quarterly results – 2013

	December 31 2012	September 30 2012	June 30 2012	March 31 2012
	$	$	$	$
Revenue	537,828	576,699	450,098	600,469
Net loss	(319,529)	(441,748)	(399,269)	(326,572)
Net loss per common share - basic and diluted	(0.01)	(0.01)	(0.01)	(0.01)

There are no seasonal effects or other trends in the Company's business over the quarters presented.

Results of operations (continued)

The revenues for the quarter ended December 31, 2013 increased by $78,107 or 15% to $615,935 compared to $537,828 in the quarter ended December 31, 2012. The increased revenues were mostly due to the receipt of IRAP grants recorded during the quarter of $55,336, related to the research and development salaries. Gross profit for the current quarter was 40% of revenues and $246,665 compared to 26% and $140,249 in the quarter ended December 31, 2012. The increase in gross profit in the current quarter was mainly due to the IRAP (government) technology grants.

During the first quarter of fiscal 2014, operating expenses increased $148,698 to $608,476 compared with $459,778 in the first quarter of fiscal 2013. The increased operating expenses for three month period are attributable to increased salaries, share-based compensation, professional fees, and investor relations for Nanotech's consolidated operations.

General and administration expense increased $140,053 due to increased management fees, office salaries, professional fees, premises costs and share-based compensation compared to the first fiscal quarter 2013. Sales and marketing expenses increased $28,800 to $127,303 for the current quarter compared to the first fiscal quarter 2013 due to an increase in investor relations fees and travel expenses. Foreign exchange in the first quarter of fiscal 2014 was a loss of $10,775 compared to a gain of $2,607 in 2013.

Liquidity

Working capital at December 31, 2013 was $3,199,144 compared to $1,175,310 at December 31, 2012 due to the September 2013 private placement net proceeds of $4,129,912.

Cash flow from operations

Cash used by operations in the quarter ended December 31, 2013 increased to $584,041 compared to $223,680 in the quarter ended December 31, 2012.

Investing activities

During the quarter ended December 31, 2013, the Company purchased equipment, net of disposals, totaling $9,491 (2012 - $Nil),

Financing activities

During the quarter ended December 31, 2012, the Company received $122,500 from the exercise of stock options by Directors.

Financial Condition / Capital resources

At December 31, 2013, the Company had working capital of $3,199,144, as compared to $1,175,310 at December 31, 2012. The Company has no long term debt or loans outstanding and had 38,756,136 common shares issued and outstanding at December 31, 2013 (diluted: 42,321,386) compared to 29,840,533 at December 31, 2012 (diluted: 31,078,944).

At September 30, 2013, there were 1,045,000 stock options outstanding at a weighted average exercise price of $0.87.

The Company had no commitments for material capital expenditures as of December 31, 2013.

The Company has no lines of credit.

The Company has no exposure to asset backed commercial paper.

Results of operations (continued)

Management has reviewed its funding requirements and has determined that the Company has sufficient funds on hand to meet its requirements through September 2014.

Contractual obligations - premises lease		Payments due by period	
	Total	Less than 1 year	1-3 years
	$	$	$
NTS	107,512	33,834	73,678
TTI	308,622	91,919	216,703
Total contractual obligations	416,134 *	125,753 *	290,381 *

* Not including purchase commitments to suppliers

Capital and Reserves

a) Share Capital

	Number	Amount
		$
September 30, 2011	24,253,711	14,812,193
Private placement	1,844,822	1,586,729
Warrants exercised	2,517,000	354,669
September 30, 2012	28,615,533	16,753,591
Private placement	5,210,500	3,506,607
Acquisition of IDIT and IDME (Note 5)	3,705,103	4,853,685
Options exercised	1,225,000	184,584
Warrants expired	-	180,393
September 30, 2013 and December 31, 2013	**38,756,136**	**25,478,860**

b) Stock Option Plan

	Number of options	Exercise price	Expiry date
	#	$	
Outstanding, September 30, 2011	1,566,000	0.24	
Cancelled	(25,000)	0.10	
Outstanding, September 30, 2012	1,541,000	0.24	
Granted	690,000	0.80	February 27, 2016
Terminated	(46,000)	0.80	
Exercised	(1,225,000)	0.10	
Outstanding, September 30, 2013	960,000	0.80	
Granted	85,000	1.75	December 23, 2016
Outstanding, December 31, 2013	1,045,000	0.87	

Capital and Reserves (continued)

During the quarter ended December 31, 2013, a total of 85,000 stock options were granted to certain contractors of the Company at a price of $1.75 per share, exercisable for a term of three years. The fair value at the date of grant totaling $66,728 was estimated using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 60%; average risk-free interest rate of 1.19%; and an expected life of three years. The stock options vest in installments, whereby each installment is accounted for as a separate arrangement (known as "Graded Vesting"). To December 31, 2013, no options vested.

In the year ended September 30, 2013, a total of 690,000 stock options were granted to certain employees of the Company at a price of $0.80 per share, exercisable for a term of three years. The fair value at the date of grant totaling $257,405 was estimated using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 70%; average risk-free interest rate of 1.02%; and an expected life of three years. The stock options outstanding vest in installments, whereby each installment is accounted for as a separate arrangement (also known as "Graded Vesting"). To December 31, 2013, 477,875 options vested.

During the quarter ended December 31, 2013, the share-based payment was $27,946 (2012 - $Nil).

(c) Warrants

	Number of warrants	Weighted average exercise price	Fair value of warrants
	#	$	$
At September 30, 2011	2,517,000	0.10	102,969
Exercised	(2,517,000)	0.10	(102,969)
Granted	922,411	1.25	180,393
At September 30, 2012	922,411	1.25	180,393
Expired	(922,411)	1.25	(180,393)
Granted	2,605,250	0.90	623,305
At September 30, 2013 and December 31, 2013	2,605,250	0.90	623,305

During the year ended September 30, 2012, 2,517,000 warrants were exercised at a price of $0.10 for proceeds of $251,700.

During the year ended September 30, 2012, the Company issued warrants together with a private placement issuing 1,844,822 units. Each unit is comprised of one share and one-half warrant, exercisable for one year at $1.25. Commissions and finder's fees of $77,800 were paid in cash.

The fair values of warrants issued were determined using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 67.26%; average risk-free interest rate of 1.23%; and expected life of one year. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of one year.

During the year ended September 30, 2013, the Company issued warrants together with a private placement in two tranches issuing 5,210,500 units in total. Each unit is comprised of one share and one-half warrant, exercisable for eighteen months at $0.90. Commissions and finder's fees of $38,592 were paid in cash.

Capital and Reserves (continued)

The fair values of warrants issued were determined using the Black-Scholes option pricing model with the following assumptions: Tranche 1 no dividends are to be paid; average expected volatility of 53.77%; average risk-free interest rate of 1.22%; and expected life of 1.39 years. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of eighteen months. Tranche 2 no dividends are to be paid; average expected volatility of 53.43%; average risk-free interest rate of 1.29%; and expected life of 1.5 years. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of eighteen months.

During the year ended September 30, 2013, 922,411 warrants expired.

Off-balance sheet arrangements

The Company does not have any off-balance sheet arrangements in place.

Transactions with related parties

The remuneration of directors and other members of key management personnel are as follows:

	2013	2012
	$	$
Management and director fees	**72,990**	62,830
Legal fees	**19,764**	7,611
	92,754	70,441

Included in the above table

(a) Management fees of $62,490 (2012 - $58,330) were charged by Geni D Ventures Inc., a company controlled by Mr. Blakeway who is an officer or director of the Company. As of December 31, 2013, amounts owing to this company included in accounts payable and accrued liabilities were $Nil (2012 - $Nil).

(b) Fees of $19,764 (2012 - $7,611) in relation to legal services provided were paid to McMillan LLP, a law firm a partner of which was a related party during the year. The partner, Mr. Zinkhofer is a director of the Company. Neither Mr. Zinkhofer nor his firm receives any separate cash compensation for his services as a director.

The following transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

(c) As at December 31, 2013, $4,387 was a receivable from a director of the Company for amounts advanced by the Company to Canada Revenue Agency on his behalf. Interest of $182 was charged on this advance for the quarter.

(d) As at December 31, 2013, included in due to related party was $496,717 (2012 - $792) in advances, management fees and legal fees owing to officers and directors. The amounts owing are unsecured, non-interest bearing and have no fixed repayment terms.

Transactions with related parties (continued)

(e) The Company completed a unit private placement during the year ended September 30, 2012, issuing 1,844,822 units at $1.00 per unit (Note 14). Mr. Zinkhofer, the Company's corporate secretary and director participated in the placement and acquired less than 1% of the issued shares.

(f) During the quarter ended December 31, 2013, the Company paid $Nil (2012 - $120,000) for research and development to IDME, a company which has common shareholders and directors as Nanotech and on September 27, 2013, the Company acquired 95% of IDME (Note 5).

(g) During the year ended September 30, 2010, the Company acquired in consideration of an initial advance royalty payment, a license agreement from IDME, for the light based recognition nanotechnology being developed by the Company for use in anti-counterfeiting and authentication processes and products for currency, legal documents and commercial products. The advance royalty payments were required to be paid between June 15, 2010 and June 15, 2014 total $675,000 all of which has been expensed. Prior to the acquisition of IDME on September 27, 2013, $417,250 had been paid cumulatively and a further $37,500 was accrued in the current quarter.

Key sources of estimation uncertainty and key judgments

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are accounted for prospectively. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below:

(a) Useful lives of property and equipment

The depreciation method and useful lives reflect the pattern in which management expects the asset's future economic benefits to be consumed by the Company. During the year ended September 30, 2013 management changed the estimates of the useful lives of the Company's fixed assets and accordingly the depreciation rates were adjusted.

(b) Taxes

In assessing the probability of realizing deferred income tax assets, management makes estimates related to expectations of future taxable income, applicable tax opportunities, expected timing of reversals of existing temporary differences, and the likelihood that tax positions taken will be sustained upon examination by applicable tax authorities. In making its assessments, management gives additional weight to positive and negative evidence that can be objectively verified. Estimates of future taxable income are based on forecasted cash flows from operations and the application of existing tax laws in each jurisdiction. Forecasted cash flows from operations are based on projections internally developed and reviewed by management. Weight is attached to tax planning opportunities that are within the Company's control, and are feasible and implementable without significant obstacles. The likelihood that tax positions taken will be sustained upon examination by applicable tax authorities is assessed based on individual facts and circumstances of the relevant tax position evaluated in light of all available evidence. Where applicable tax laws and regulations are either unclear or subject to ongoing varying interpretations, it is reasonably possible that changes in these estimates can occur that materially affect the amounts of income tax assets recognized. At the end of each reporting period, the Company reassesses unrecognized income tax assets.

Key sources of estimation uncertainty and key judgments (continued)

(c) *Impairment of investment*

Significant management judgment is necessary to evaluate the impact of operating and macroeconomic changes on the available for sale investment in a private company. Critical assumptions include gross profit rates, operating and administrative expense, working capital fluctuations and capital expenditures.

(d) *Allocation of purchase consideration to acquired assets and assumed liabilities*

The Company determined and allocated the purchase price of an acquired company to the tangible and intangible assets acquired and liabilities assumed as of the business combination date in accordance with IFRS 3. The purchase price allocation process requires us to use significant estimates and assumptions, including fair value estimates, as of the acquisition date.

While management uses their best estimates and assumptions as a part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business combination date, the estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally one year from the acquisition date, management records adjustments to the assets acquired and liabilities assumed, with the corresponding offset to goodwill.

Key judgments include determination of functional currency, capitalization of development costs, determination of cash generating units and segments, and valuation of fair value for purposes of purchase price allocation for business combinations.

Looking forward

Nanotech is presently developing and seeking to market its authentication feature under several trademarks including *KolourOptik® NOtES®* (*Nano-Optic Technology for Enhanced Security*) technology and *Plasmogram®*. The Company anticipates that significant investment will be required to commercialize the technology. The Company may seek to involve third parties in joint venturing, partnering or otherwise funding such development activities failing which it will be required to seek to raise additional funds which will cause equity dilution to existing shareholders. The Company is currently presenting the technology to the bank note industry and other potential security authentication industry customers and is also working towards possible commercial licensing applications with third party specialists which supply security and brand recognition/protection features to the product marketplace. There can be no assurance that a successful product will be developed or that if developed any product will be commercially viable or competitive.

Tactical generated revenues of approximately $556,801 during the quarter ending December 31, 2013. Tactical had a backlog of approximately $532,713 at December 31, 2013, and at the date of filing of this MD&A has backlog orders of approximately $581,275.

Capital risk management

Management defines capital as long term debt, if any, plus shareholders' equity, which includes accumulated other comprehensive loss. Management's objectives when managing capital are to safeguard the Company's ability to continue as a going concern, to provide an adequate return to shareholders, to meet external capital requirements and preserve financial flexibility in order to benefit from potential opportunities that may arise. Management considers changes in economic conditions, risks that impact the consolidated operations and future significant capital investment opportunities in managing its capital.

Financial risk management

The Company's activities expose it to a variety of financial risks including market risk (interest rate risk and foreign exchange risk), credit risk and liquidity risk. Management reviews these risks on an ongoing basis to ensure that the risks are appropriately managed. The Company does not have a practice of trading derivatives and has none outstanding at December 31, 2013.

Interest rate risk

The Company's objective in managing interest rate risk is to monitor expected volatility in interest rates while also minimizing financing expense levels. Interest rate risk mainly arises from fluctuations of interest rates and the impact on the return earned on cash and the expense on floating rate debt. On an ongoing basis, management monitors changes in short term rates and considers long term forecasts to assess potential cash flow impacts to the Company. The Company does not currently hold any financial instruments to mitigate its interest risk. Cash earns interest based on market interest rates and there is no floating rate debt outstanding.

Foreign exchange risk

The Company operates on an international basis and is subject to foreign exchange risk exposures arising from transactions denominated in a foreign currency. The Company's objective is to minimize the impact of the volatility related to financial assets and liabilities denominated in a foreign currency where possible through effective cash flow management. Foreign currency exchange risk is limited to the portion of the Company's business transactions denominated in currencies other than Canadian dollars. On an ongoing basis, management monitors changes in foreign currency exchange rates as well as considering long term forecasts to assess the potential cash flow impact to the Company. The Company has elected not to actively manage the foreign exchange exposures at this time. The impact of a 10% change in foreign exchange rates between the Canadian and U.S. dollar on the Company's results of operations or financial position would not be significant.

Credit risk

Credit risk is the risk of a financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company is exposed to credit risk through its cash and accounts receivable. The Company manages the credit risk associated with its cash and cash equivalents by placing its funds with reputable financial institutions and investing in only highly rated securities that are traded on active markets and are capable of prompt liquidation. Credit risk for accounts receivables are managed through established credit monitoring activities. The Company also mitigates its credit risk on trade accounts receivable by obtaining cash deposits from certain customers. The Company has a concentration of customers in government agencies and law enforcement. Losses under trade accounts receivable have been historically insignificant. The credit worthiness of new customers is subject to review by management and that of existing customers is monitored.

The Company reviews its trade receivable accounts regularly and amounts are written down to their expected realizable value when the account is determined not to be fully collectible. The bad debt expense is charged to net income in the period that the account is determined to be doubtful. The Company does not currently have an allowance for doubtful accounts.

Liquidity risk

The Company's objective related to liquidity risk is to effectively manage cash flows to minimize the exposure that the Company will not be able to meet its obligations associated with financial liabilities. On an ongoing basis, management manages liquidity risk by maintaining adequate cash balances. Management believes that forecasted cash flows from operating activities will provide sufficient cash requirements to cover the Company's anticipated normal operating and capital expenditures.

Business risks

Although the market for our products appears to be expanding, our ability to remain competitive is dependent upon assessing changing markets and providing new products and capabilities. There can be no assurances that we will be able to do so or to meet changes in the marketplace or that the sale of new products will be profitable. Some of our competitors have greater financial resources and may be able to sustain recurring losses to establish market share at our expense.

The Company does not hold and has not entered into arrangements concerning market risk sensitive instruments for trading purposes.

The Company believes that inflation and other changes in prices have not had a material effect on the financial results as at December 31, 2013.

Accounting standards developments

The IASB has issued the following amendments and new standards, which had not been previously adopted by the Company. Each of the amendments and new standards is effective for the annual period beginning on or after October 1, 2013, unless otherwise indicated, with early adoption permitted.

The following is a description of the new or amended standards:

IFRS 9 Financial Instruments introduces the new requirements for the classification, measurement and de-recognition of financial assets and financial liabilities. Specifically, IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement to be subsequently measured at amortized cost or fair value, and all financial liabilities classified as subsequently measured at amortized cost except for financial liabilities as at fair value through profit or loss. The amendments are effective for the year beginning on or after October 1, 2015, with earlier application permitted.

IFRS 10 Consolidated Financial Statements replaces the consolidation requirements in IAS 27, Consolidated and Separate Financial Statements, and SIC-12 Consolidation - Special Purpose Entities. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. The effective date of IFRS 10 for the Company is the fiscal year commencing October 1, 2013. The adoption of this standard during the period did not have any material impact on the consolidated financial statements and notes to the financial statements.

IFRS 11 Joint Arrangements supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities - Non-Monetary Contributions by Venturer. IFRS 11 improves on IAS 31 by requiring a party to a joint arrangement to determine the type of joint arrangement in which it is involved by assessing its rights and obligations arising from the arrangement. The standard also addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities, namely the equity method. The effective date for the Company is the fiscal year commencing October 1, 2013. The adoption of this standard during the period did not have any material impact on the consolidated financial statements and notes to the financial statements.

IFRS 12 is a new standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. The effective date of the new standard is October 1, 2013 for the Company. The adoption of this standard during the period did not have any material impact on the consolidated financial statements and notes to the financial statements.

IFRS 13 is a new standard that defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure

Accounting standards developments (continued)

requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The effective date of IFRS 13 is October 1, 2013 for the company. The adoption of this standard during the period did not have any impact on the financial statements and notes to the financial statements.

IAS 1 - Presentation of Financial Statements: In June 2011, the IAS issued amendments to IAS 1 that requires an entity to group items presented in the statement of comprehensive income on the basis of whether they may be reclassified to earnings subsequent to initial recognition. For those items presented before taxes, the amendments to IAS 1 also require that the taxes related to the two separate groups be presented separately. The amendments are effective for annual periods beginning on or after July 1, 2012, with earlier adoptions permitted. The adoption of this amendment during the period did not have any impact on the financial statements and notes to the financial statements.

Subsequent Events

Ms. Frenny Bawa resigned her position at Nanotech as Chief Commercial Officer effective February 28th, 2014. Ms. Bawa expressed a desire to pursue personal activities.

Nanotech announced on February 25, 2014 that the Company's common shares commenced trading on the OTCQX® Market in the United States under the ticker symbol "NTSFF". The Company is pleased to have qualified for trading on OTCQX®, which will better enable Nanotech to provide U.S. investors with timely news and information. Additional information about Nanotech and its technologies can now be found at www.nanosecurity.ca or www.sedar.com or www.otcmarkets.com

There were no other subsequent events which constituted material changes in the Company's affairs.

Nanotech Outstanding Share Data

The Company's outstanding share data as at February 28, 2014:

Issued shares	38,756,136
Warrants	2,605,250
Stock options outstanding	1,045,000

"Doug H. Blakeway"

President & Chief Executive Officer

February 28, 2014

"Brian F. Causey"

Secretary & Chief Financial Officer

February 28, 2014

Financial Statements

December 31, 2013

Consolidated financial statements of

Nanotech Security Corp.

December 31, 2013

Nanotech Security Corp.

Consolidated statements of operations and comprehensive loss (Unaudited)
Periods ended December 31
(In Canadian dollars)

	2013	2012
	$	$
Revenue	**615,935**	537,828
Cost of sales	**369,270**	397,579
Gross profit	**246,665**	140,249
Operating expenses (Note 6)		
Research and development	**125,210**	159,400
General and administration	**343,134**	203,081
Sales and marketing	**127,303**	98,503
Foreign exchange (gain) loss	**10,775**	(2,607)
Finance charges	**2,054**	1,401
	608,476	459,778
Operating loss	**(361,811)**	(319,529)
Loss on write off of investment (Note 8)	**-**	-
Gain on sale of fixed asset	**8,845**	**-**
Net loss for the period	**(352,966)**	(319,529)
Other comprehensive loss		
Unrealized foreign exchange gains on translation of foreign operation	**27,467**	11,390
Total comprehensive loss for the period	**(325,499)**	(308,139)
Net Loss Attributable to:		
Nanotech Security Corp. shareholders	**(354,782)**	-
Non-controlling interest	**1,816**	-
	(352,966)	**-**
Comprehensive Loss Attributable to:		
Nanotech Security Corp. shareholders	**(327,315)**	-
Non-controlling interest	**1,816**	-
	(325,499)	**-**
Loss per share		
Basic and diluted	**(0.01)**	(0.01)
Weighted average number of common shares		
Basic and diluted	**38,756,136**	29,102,366

The accompanying notes to the consolidated financial statements are an integral part of this consolidated financial statement.

Nanotech Security Corp.

Consolidated statements of changes in equity
Years ended December 31, 2013 and 2012
(In Canadian dollars)

	Number of shares	Share capital	Warrants reserve	Share based payments reserve	Reserve for contingent Shares to be Issued on Acquisition (Note 5)	Foreign currency translation reserve	Deficit	Total shareholders' equity
		$	$	$	$	$	$	$
Balance, September 30, 2011	24,253,711	14,812,193	102,969	463,809	-	3,684	(14,543,696)	838,959
Net loss	-	-	-	-	-	-	(1,531,363)	(1,531,363)
Unrealized foreign exchange loss on translation	-	-	-	-	-	(4,063)	-	(4,063)
Total comprehensive loss	-	-	-	-	-	(4,063)	(1,531,363)	(1,535,426)
Private placement	1,844,822	1,586,729	180,393	-	-	-	-	1,767,122
Share based payments	-	-	-	146,343	-	-	-	146,343
Exercise of warrants	2,517,000	354,669	(102,969)	-	-	-	-	251,700
Balance, September 30, 2012	28,615,533	16,753,591	180,393	610,152	-	(379)	(16,075,059)	1,468,698
Net loss							(319,529)	(319,529)
Unrealized foreign exchange loss on translation						11,390		11,390
Options exercised	1,225,000	184,584	-	(62,084)	-	-	-	122,500
Balance, December 31, 2012	29,840,533	16,938,175	180,393	548,068	-	11,011	(16,394,588)	1,283,059
Net loss	-	-	-	-	-	-	(1,729,788)	(1,729,788)
Unrealized foreign exchange loss on translation	-	-	-	-	-	(22,640)	-	(22,640)
Total comprehensive loss	-	-	-	-	-	(22,640)	(1,729,788)	(1,752,428)
Share consideration for the acquisition (Note 5)	3,705,103	4,853,685	-	-	307,715	-	-	5,161,400
Non-controlling interest on the acquisition								
Private placement (net of share issue costs of $38,592)	5,210,500	3,506,607	623,305	-	-	-	-	4,129,912
Share based payments	-	-	-	207,070	-	-	-	207,070
Warrants expired	-	180,393	(180,393)	-	-	-	-	-
Balance, September 30, 2013	38,756,136	25,478,860	623,305	755,138	307,715	(11,629)	(18,124,376)	9,029,013
Net loss	-	-	-	-	-	-	(354,782)	(354,782)
Unrealized foreign exchange loss on translation	-	-	-	-	-	27,467	-	27,467
Total comprehensive loss	-	-	-	-	-	27,467	(354,782)	(327,315)

The accompanying notes to the consolidated financial statements are an integral part of this consolidated financial statement.

Nanotech Security Corp.

Consolidated statements of financial position (Unaudited)

(In Canadian dollars)

	December 31, 2013	September 30, 2013 (Audited)
	$	$
Assets		
Current assets		
Cash and cash equivalents	**3,607,288**	4,155,811
Accounts receivable	**254,973**	362,111
Inventory (Note 7)	**261,026**	310,904
Prepaid expenses	**37,078**	11,743
	4,160,365	4,840,569
Investment (Note 8)	**-**	-
Property and equipment (Note 9)	**56,571**	61,897
Intangible assets (Note 10)	**5,227**	5,548
Other assets	**10,640**	10,302
Goodwill (Note 5 and 11)	**5,444,954**	5,444,954
	9,677,757	10,363,270
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**459,098**	809,620
Due to related party (Note 12)	**496,717**	533,812
Deposits	**5,406**	5,749
	961,221	1,349,181
Nature of operations (Note 1)		
Commitments (Note 20)		
Shareholders' equity		
Share capital (Note 14)	**25,478,860**	25,478,860
Warrants reserve (Note 14)	**623,305**	623,305
Share based payments reserve	**783,084**	755,138
Shares issuable reserve	**307,715**	307,715
Foreign currency translation reserve	**15,838**	(11,629)
Deficit	**(18,479,158)**	(18,124,376)
Equity attributable to shareholders of the Company	**8,729,644**	9,029,013
Non-controlling interests (Note 16)	**(13,108)**	(14,924)
Total equity	**8,716,536**	9,014,089
	9,677,757	10,363,270

Approved by the Directors on February 28, 2014

(Signed) D.H. Blakeway, _____ D.H. Blakeway, Director

(Signed) K.R. Tolmie, _______ K.R. Tolmie, Director

The accompanying notes to the consolidated financial statements are an integral part of this consolidated financial statement.

Nanotech Security Corp.

Consolidated statements of cash flows
Periods ended December 31
(In Canadian dollars)

	2013	2012
	$	$
Operating activities		
Net loss	**(352,966)**	(319,529)
Items not involving cash		
Depreciation and amortization	**6,441**	5,475
Stock-based compensation	**27,946**	-
Gain on sale of asset	**(8,845)**	-
	(327,424)	(314,054)
Non-cash working capital changes (Note 15)	**(256,617)**	90,374
	(584,041)	(223,680)
Investing activities		
Purchase of property and equipment, net of disposals	**9,491**	-
	9,491	-
Financing activities		
Issuance of shares for options exercised	**-**	122,500
	-	122,500
Effect of foreign exchange on cash and cash equivalents	**26,027**	10,907
Net decrease in cash and cash equivalents	**(548,523)**	(90,273)
Cash and cash equivalents, beginning of period	**4,155,811**	1,254,449
Cash and cash equivalents, end of period	**3,607,288**	1,164,176

Supplemental cash flow disclosure (Note 15)

The accompanying notes to the consolidated financial statements are an integral part of this consolidated financial statement.

1. Summary of business and nature of operations

(a) *Nature of business*

Nanotech Security Corp. (the "Company") is incorporated under the laws of British Columbia and is listed on the TSX Venture Exchange (Tier 1, trading symbol: NTS-V) and is listed in the USA on the OTCQX Market (trading symbol: NTSFF). The Company is developing light based recognition nanotechnology for potential use in anti-counterfeiting and authentication processes and products including currency, legal documents and commercial products. Its wholly-owned subsidiary, Tactical Technologies Inc. ("TTI"), designs and sells sophisticated communication surveillance and intelligence gathering equipment for the law enforcement and defense industries in the United States and Canada.

The Company's head office is located at #308 - 2999 Underhill Street, Burnaby, BC, Canada V5A 3C2 and the registered and records office is Suite 1500 - 1055 West Georgia, Vancouver, BC, Canada V6E 4N7.

These interim consolidated financial statements have been prepared on the basis that the Company will continue as a going concern. The Company has recurring operating losses and an accumulated deficit of $18,479,158 as of December 31, 2013. The Company also expects to continue to incur substantial expenses relating to its research and development efforts in light based recognition nanotechnology. As a result, the Company expects to incur significant losses in the next year unless it is able to realize revenue after commercialization of its products under development. The timing and amount of such revenues, if any, cannot be predicted with certainty. The Company's ability to continue as a going concern is dependent on its ability to obtain significant additional financing in order to meet its planned business objectives and to be able to develop and commercialize products currently in development. The Company will need to raise funds and is pursuing additional funds through grants, strategic collaborations, public or private equity or debt financing or other funding sources. This funding may not be available on acceptable terms, or at all, and may be dilutive to shareholder interests. However, there can be no assurance that the Company will be able to obtain additional financial resources. If the Company is unable to generate positive cash flows or obtain adequate financing, the Company will need to curtail operations and development activities. These factors may cast significant doubt regarding the Company's ability to continue as a going concern. Should the Company be unable to realize its assets and discharge its liabilities in the normal course of business the net realizable value of its assets may be materially less than the amounts on the statement of financial position.

(b) *Basis of preparation and statement of compliance*

These interim consolidated financial statements are expressed in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards (IFRS). The policies set out below were consistently applied to all the periods presented unless otherwise noted below. These financial statements were prepared on a going concern basis, under the historical cost convention, except for certain financial assets and financial liabilities recorded at fair value through profit or loss. The financial statements were approved by the Company's Board of Directors and authorized for issue on February 28, 2014.

2. Significant accounting policies

(a) *Basis of consolidation*

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, TTI, and IDIT. These consolidated financial statements also include the accounts of IDME, of which the Company owns 95% of the shares. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Intercompany balances, transactions, revenues and expenses have been eliminated on consolidation.

2. Significant accounting policies (continued)

(b) Inventory

Raw materials are valued at the lower of cost and net realizable value. Cost is determined on a weighted average basis. Work in process and finished goods are valued at the lower of cost and net realizable value. The cost of work in process and finished goods includes the cost of raw material, direct labour and an allocation of related overheads. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(c) Foreign currency translation

The functional and presentation currency of the Company and its Canadian subsidiaries is the Canadian dollar. TTI's functional currency is the U.S. dollar. The assets and liabilities of TTI are translated to Canadian dollars at exchange rates at the reporting date. The income and expenses of TTI are translated to Canadian dollars using average exchange rates for the month during which the transactions occurred. Foreign currency differences are recognized as a separate component in other comprehensive income.

Transactions in currencies other than the functional currency are recorded at the rates of exchange at the date of the transaction. At each financial position reporting date, monetary assets and liabilities that are denominated in foreign currencies are translated at the rates prevailing at the period end date. Non-monetary items that are measured in terms of historical cost are translated using the historical rates. All gains and losses on translation of those foreign currency transactions are recorded in comprehensive income.

(d) Property and equipment and amortization

Property and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. The initial cost of an asset comprises its purchase price and any costs directly attributable to bringing the asset into working condition for its intended use.

Repairs and maintenance costs are charged directly to the statement of operations as incurred. Depreciation is calculated using the following methods and annual rates:

Manufacturing, office and computer equipment	20%-100% declining balance
Leasehold improvements	lesser of lease term and 20% straight-line

(e) Intangible assets

Intangible assets with finite lives are stated at the amount initially recognized less accumulated amortization and accumulated impairment losses. Amortization is computed using the straight-line method over the term of licensing agreements.

Intangible assets acquired in a business combination and recognized separately from goodwill are initially recognized at their fair value at the acquisition date (which is regarded as their cost).

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortization and accumulated impairment losses, on the same basis as intangible assets that are acquired separately. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at the end of each year end.

2. Significant accounting policies (continued)

(f) Impairment of long-lived assets

Long-lived assets are assessed for impairment at the end of each reporting period and whenever events or changes in circumstances indicate that their carrying value may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(g) Provisions

Provisions represent liabilities for which the amount or timing is uncertain. Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where appropriate, the future cash flow estimates are adjusted to reflect risks specific to the liability.

(h) Income taxes

Income tax on the results for the years presented comprises current and deferred tax. Income tax is recognized in profit or loss except to the extent that it relates to items recognized in other comprehensive income or directly in equity, in which case the tax expense is recognized in other comprehensive income or in equity.

Current tax expense is based on the results for the period as adjusted for items that are not taxable or not deductible for tax purposes. Current tax is calculated using tax rates and laws that were enacted or substantively enacted at the financial position date.

Deferred tax is recorded using the liability method of accounting for income taxes. Under this method, the Company calculates all unused tax losses, unused tax credits and temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the period end date.

Deferred tax is calculated based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates that are expected to apply to the year of realization or settlement based on tax rates and laws enacted or substantively enacted at the period end date.

Deferred tax assets are recognized to the extent it is probable that taxable profits will be available against which the unused tax losses, unused tax credits, and deductible temporary differences can be utilized. The carrying amount of deferred tax assets is reviewed at each date of financial position and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

2. Significant accounting policies (continued)

(i) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable.

Revenue from the sale of products is recognized when all of the following conditions have been met:

- title and risk involving the products are transferred to the buyer;
- the Company's managerial involvement over the goods ceases to exist;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Company; and
- the costs incurred in respect of the transaction can be measured reliably.

If there is a requirement for customer acceptance of any products shipped, revenue is recognized only after customer acceptance has been received. Payments received in advance of the satisfaction of the Company's revenue recognition criteria are recorded as deferred revenue.

Provisions are established for estimated product returns and warranty costs at the time revenue is recognized based on historical experience for the product.

(j) Share-based payments

The Company makes share-based payments to directors and employees and the compensation expense for share-based payment is determined based on the fair value at the grant date using the Black-Scholes option-pricing model and is recorded in the statement of operations over the vesting period. When stock options are exercised, any consideration paid by employees, as well as the related stock-based compensation, is credited to share capital.

(k) Investment tax credits

The Company is entitled to certain non-refundable Canadian investment tax credits for qualifying research and development activities in Canada. Investment tax credits are accounted for as a reduction of the related expenditure for items of a current expense nature or as a reduction of property and equipment for items of a capital nature when the amount is reliably estimable and the Company has reasonable assurance regarding compliance with the relevant conditions and that the credit will be realized.

(l) Financial instruments

Financial instruments are classified into one of the following categories: (1) Fair value through profit and loss ("FVTPL"), (2) held-to maturity ("HTM"), (3) loans and receivables, (4) available-for-sale ("AFS") financial assets or (5) other financial liabilities. The classification determines the accounting treatment of the instrument. The Company determines the classification when the financial instrument is initially recorded, based on the underlying purpose of the instrument.

Financial assets

Cash and cash equivalents

Cash and cash equivalents comprise cash on deposit and short term, highly liquid investments that are readily convertible to a known amount of cash with an original maturity of less than three months and that are subject to an insignificant risk of changes in value. Cash and cash equivalents are classified as loans and receivables and are measured at amortized cost.

2. Significant accounting policies (continued)

(l) Financial instruments (continued)

Financial assets (continued)

Accounts receivables

Accounts receivables do not incur any interest, are short term in nature and are measured at their nominal value net of appropriate allowance for estimated amounts that are not expected to be recovered. Such allowances are raised based on an assessment of debtor ageing, past experience or known customer circumstances.

Investments

Investments, other than investments in subsidiaries and associates, are financial asset investments and are initially recognized at fair value. At subsequent reporting dates, financial assets that the Company has the expressed intention and ability to hold to maturity (held to maturity) as well as loans and receivables are measured at amortized cost, less any impairment losses. The amortization of any discount or premium on the acquisition of a held to maturity investment is recognized in the statement of operations in each period using the effective interest method. Investments other than those classified as held to maturity or loans and receivables are classified as either at fair value through profit or loss (which includes investments held for trading) or available for sale financial assets. Both categories are subsequently measured at fair value. For available for sale investments, realized/unrealized gains and losses are recognized in equity until the investment is disposed or impaired, at which time the cumulative gain or loss previously recognized in equity is included in the statement of operations.

Impairment of financial assets (including receivables)

A financial asset not measured at fair value through profit or loss is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated cash flows discounted at the asset's original effective interest rate. Losses are recognized in the statement of operations. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through the statement of operations. Impairment losses relating to available for sale investments are recognized when the decline in fair value is considered significant or prolonged. These impairment losses are recognized by transferring the cumulative loss that has been recognized in comprehensive loss to net loss. The loss recognized in the statement of operations is the difference between the acquisition cost and the current fair value.

Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified and accounted for as debt or equity according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

2. Significant accounting policies (continued)

(l) Financial instruments (continued)

Financial assets (continued)

Accounts payables and accrued liabilities, and deposits

Accounts payables and accrued liabilities, and deposits are not interest bearing and are measured at their nominal value until settled.

De-recognition of financial assets and financial liabilities

Financial assets are derecognized when the rights to receive cash flows from the asset have expired, the right to receive cash flows has been retained but an obligation to pay them in full without material delay has been assumed or the right to receive cash flows has been transferred together with substantially all the risks and rewards of ownership. Financial liabilities are derecognized when the associated obligation has been discharged, cancelled or has expired.

(m) Earnings per common share

Basic net loss per common share has been calculated using the weighted average number of common shares outstanding during the year. The diluted net loss per share reflects the potential dilution of common share equivalents, such as outstanding stock options, in the weighted average number of common shares outstanding during the year, if dilutive. For this purpose, the "treasury stock method" is used for the assumed proceeds upon the exercise of outstanding stock options that are used to purchase common shares at the average market price during the period.

(n) Research and development

Research costs are charged to operations when they are incurred less investment tax credits. Development costs are charged to operations in the period incurred unless the Company can demonstrate that a development project meets certain criteria for capitalization and amortization. The Company has not capitalized any development costs during the three months ended December 31, 2013 or 2012.

(o) Business combination

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Company, liabilities incurred by the Company to the former owners of the acquiree and the equity interests issued by the Company in exchange for control of the acquiree. Acquisition-related costs are generally recognized in profit or loss as incurred.

At the acquisition date, the identifiable assets acquired and the liabilities assumed are recognized at their fair value, except that:

- deferred tax assets or liabilities, and assets or liabilities related to employee benefit arrangements are recognized and measured in accordance with IAS 12 Income Taxes and IAS 19 respectively;
- liabilities or equity instruments related to share-based payment arrangements of the acquiree or share-based payment arrangements of the Group entered into to replace share-based payment arrangements of the acquiree are measured in accordance with IFRS 2 at the acquisition date; and assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations are measured in accordance with that Standard.

2. Significant accounting policies (continued)

(o) Business combination (continued)

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If, after reassessment, the net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held interest in the acquiree (if any), the excess is recognized immediately in profit or loss as a bargain purchase gain.

Non-controlling interests that are present ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at fair value or at the non-controlling interest's proportionate share of the recognized amounts of the acquiree's identifiable net assets. The choice of measurement basis is made on a transaction-by-transactions basis. Other types of non-controlling interests are measured at fair value or, when applicable, on the basis specified in another IFRS.

When the consideration transferred by the Company in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with corresponding adjustments against goodwill. Measurement period adjustments are adjustments that arise from additional information obtained during the "measurement period" (which cannot exceed one year from the acquisition date) about facts and circumstances that existed at the acquisition date.

The subsequent accounting for changes in the fair value of the contingent consideration that do not qualify as measurement period adjustments depends on how the contingent consideration is classified. Contingent consideration that is classified as equity is not re-measured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Contingent consideration that is classified as an asset or a liability is re-measured at subsequent reporting dates in accordance with IAS 39, or IAS 37 Provisions, Contingent Liabilities and Contingent Assets, as appropriate, with the corresponding gain or loss being recognized in profit or loss.

If the initial accounting for the business combination is incomplete by the end of the reporting period in which the combination occurs, the Company reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period, or additional assets or liabilities are recognized, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognized at that date.

2. Significant accounting policies (continued)

(p) Goodwill

Goodwill arising on an acquisition of a business is carried at cost as established at the date of acquisition of the business less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to each of the Company's cash-generating units (or groups of cash-generating units) that is expected to benefit from the synergies of the combination. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently when there is indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata based on the carrying amount of each asset in the cash generating unit. Any impairment loss for goodwill is recognized directly in profit or loss in the consolidated statement of comprehensive income. An impairment loss recognized for goodwill is not reversed in subsequent periods. Management evaluates goodwill for impairment annually as of September 30th.

On disposal of the relevant cash-generating unit, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

3. Key sources of estimation uncertainty and key judgments

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are accounted for prospectively. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below:

(a) Useful lives of property and equipment

The depreciation method and useful lives reflect the pattern in which management expects the asset's future economic benefits to be consumed by the Company. During the year ended September 30, 2013 management changed the estimates of the useful lives of the Company's fixed assets and accordingly the depreciation rates were adjusted.

(b) Taxes

In assessing the probability of realizing deferred income tax assets, management makes estimates related to expectations of future taxable income, applicable tax opportunities, expected timing of reversals of existing temporary differences, and the likelihood that tax positions taken will be sustained upon examination by applicable tax authorities. In making its assessments, management gives additional weight to positive and negative evidence that can be objectively verified. Estimates of future taxable income are based on forecasted cash flows from operations and the application of existing tax laws in each jurisdiction. Forecasted cash flows from operations are based on projections internally developed and reviewed by management. Weight is attached to tax planning opportunities that are within the Company's control, and are feasible and implementable without significant obstacles. The likelihood that tax positions taken will be sustained upon examination by applicable tax authorities is assessed based on individual facts and circumstances of the relevant tax position evaluated in light of all available evidence. Where applicable tax laws and regulations are either unclear or subject to ongoing varying interpretations, it is reasonably possible that changes in these estimates can occur that materially affect the amounts of income tax assets recognized. At the

3. Key sources of estimation uncertainty and key judgments (continued)

end of each reporting period, the Company reassesses unrecognized income tax assets.

(c) Impairment of investment

Significant management judgment is necessary to evaluate the impact of operating and macroeconomic changes on the available for sale investment in a private company. Critical assumptions include gross profit rates, operating and administrative expense, working capital fluctuations and capital expenditures.

(d) Allocation of purchase consideration to acquired assets and assumed liabilities

The Company determined and allocated the purchase price of an acquired company to the tangible and intangible assets acquired and liabilities assumed as of the business combination date in accordance with IFRS 3. The purchase price allocation process requires us to use significant estimates and assumptions, including fair value estimates, as of the acquisition date.

While management uses their best estimates and assumptions as a part of the purchase price allocation process to accurately value assets acquired and liabilities assumed at the business combination date, the estimates and assumptions are inherently uncertain and subject to refinement. As a result, during the purchase price allocation period, which is generally one year from the acquisition date, management records adjustments to the assets acquired and liabilities assumed with the corresponding offset to goodwill.

Key judgments include determination of functional currency, capitalization of development costs, determination of cash generating units and segments, and valuation of fair value for purposes of purchase price allocation for business combinations.

4. Accounting standards developments

The IASB has issued the following amendments and new standards, which had not been previously adopted by the Company. Each of the amendments and new standards is effective for the annual period beginning on or after October 1, 2013, unless otherwise indicated, with early adoption permitted.

The following is a description of the new or amended standards:

IFRS 9 Financial Instruments introduces the new requirements for the classification, measurement and de-recognition of financial assets and financial liabilities. Specifically, IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement to be subsequently measured at amortized cost or fair value, and all financial liabilities classified as subsequently measured at amortized cost except for financial liabilities as at fair value through profit or loss. The amendments are effective for the year beginning on or after October 1, 2015, with earlier application permitted.

IFRS 10 Consolidated Financial Statements replaces the consolidation requirements in IAS 27, Consolidated and Separate Financial Statements, and SIC-12 Consolidation - Special Purpose Entities. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. The effective date of IFRS 10 for the Company is the fiscal year commencing October 1, 2013. The adoption of this standard during the period did not have any material impact on the consolidated financial statements and notes to the financial statements.

4. Accounting standards developments (continued)

IFRS 11 Joint Arrangements supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities - Non-Monetary Contributions by Venturer. IFRS 11 improves on IAS 31 by requiring a party to a joint arrangement to determine the type of joint arrangement in which it is involved by assessing its rights and obligations arising from the arrangement. The standard also addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities, namely the equity method. The effective date for the Company is the fiscal year commencing October 1, 2013. The adoption of this standard during the period did not have a material impact on the consolidated financial statements and notes to the financial statements.

IFRS 12 is a new standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. The effective date of the new standard is October 1, 2013 for the Company. The adoption of this standard during the period did not have a material impact on the consolidated financial statements and notes to the financial statements.

IFRS 13 is a new standard that defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The adoption of this standard during the period did not have a material impact on the consolidated financial statements and notes to the financial statements.

IAS 1 - Presentation of Financial Statements: In June 2011, the IAS issued amendments to IAS 1 that requires an entity to group items presented in the statement of comprehensive income on the basis of whether they may be reclassified to earnings subsequent to initial recognition. For those items presented before taxes, the amendments to IAS 1 also require that the taxes related to the two separate groups be presented separately. The amendments are effective for annual periods beginning on or after July 1, 2012, with earlier adoptions permitted. The application of the amendments to IAS 1 did not have a material impact on the consolidated financial statements.

5. Acquisitions of IDME and IDIT

Pursuant to a share exchange agreement for a combined transaction, the Company completed the acquisition of controlling interests in two privately held British Columbia corporations, IDIT Technologies Corp. ("IDIT") and IDME Technologies Corp. ("IDME"), from whom the Company sublicenses its anti-counterfeiting technology, on September 27, 2013. As consideration the Company agreed to issue a total of 3,940,000 common shares in exchange for 100% of the issued and outstanding common shares of IDIT and 95% of the issued and outstanding common shares of IDME. The fair value of the equity shares issued was based on the market value of Nanotech's traded shares on September 27, 2013, the acquisition date.

The fair value the net assets acquired does not include certain common shares of the Company still registered in the name of IDME as of September 30, 2013 because these shares had been reserved for distribution to the former shareholders of IDME prior to the date of acquisition. These shares will be distributed to the former IDME shareholders in future either directly as a dividend or indirectly by issuance of the equivalent number of new shares from the Company's treasury against cancellation of the same number of shares held by IDME on a wind-up of IDME.

5. Acquisitions of IDME and IDIT (continued)

Three of the Company's directors were among the vendors of the IDIT and IDME common shares as follows: Doug Blakeway Director and CEO, (1,632,033 shares), Dr. Bozena Kaminska, Director and CSO (1,674,634 shares) and Clint Landrock, Executive VP Products (433,333 shares), for a total of 3,740,000 shares. Included in the 3,940,000 common shares issuable are 234,897 common shares issuable subject to prior approval of the Company's disinterested shareholders (the "contingent shares") as the Company did not have sufficient authorized shares. All common shares issued by the Company in connection with the acquisition will be escrowed and the escrow will allow for 25% semi-annual releases over two years from closing starting six months from closing.

The acquisition will eliminate a 6% gross revenue royalty on product sales and will also result in the Company acquiring direct ownership of the principal nanotechnology patents as well as ownership of additional intellectual property in related fields which the private corporations now hold. The Company's products and services will then be subject only to a 3% sales royalty in favour of Simon Fraser University ("SFU") where elements of the nanotechnology originated. SFU also remains as the non-controlling 5% interest in IDME.

The acquisition of IDIT and IDME in a combined transaction, have been accounted for using the purchase method with the provisional fair values of the assets acquired, and liabilities assumed:

	$
3,705,103 common shares at $1.31 per share	4,853,685
234,897 contingent common shares at $1.31 per share	307,715
Fair value of equity consideration	5,161,400
Non-controlling interest - proportionate share of net assets	14,924
Recognized amounts of identifiable net assets:	
Bank overdraft	(18)
Receivables	487,424
Property and equipment	2,550
Liabilities assumed	(788,434)
Net identifiable liabilities	(298,478)
Goodwill	5,444,954

The purchase price allocation as of December 31, 2013, unchanged from September 30, 2013, has been prepared on a provisional basis based on management's best estimates of the fair value of the assets acquired, liabilities assumed and consideration paid as of the date of finalization of these consolidated financial statements. Management is still in the process of allocating value to the acquired intangible assets. Management is unable to allocate the provisional goodwill as of December 31, 2013 as it is still assessing whether it will create a new cash generating unit for the additional technology acquired.

Acquisition related costs totaling $14,852 have been excluded from the determination of the consideration transferred and have been included within general and administrative expenses in consolidated statement of loss and comprehensive loss.

None of the goodwill arising on these acquisitions is expected to be deductible for tax purposes.

6. Nature of expenses

Operating expenses are comprised of the following:

	Three Months Ended December 31 2013	Three Months Ended December 31 2012
	$	$
Advertising and promotion	**2,956**	7,302
Depreciation of property and equipment	**3,453**	3,056
Equipment maintenance and lease	**281**	486
Finance charges	**2,054**	1,401
Insurance	**5,831**	5,076
Investor and public relations	**43,973**	18,850
Legal and professional fees	**55,391**	39,694
Consulting fees	**29,286**	-
Office and general	**36,105**	15,107
Product research and development	**117,207**	158,889
Rent	**22,009**	6,035
Salaries	**222,635**	195,444
Share-based compensation expense (Note 14)	**27,946**	-
Travel and entertainment	**28,574**	11,045
Foreign exchange (gain) loss	**10,775**	(2,607)
	608,476	459,778

7. Inventory

	December 31 2013	December 31 2012
	$	$
Raw materials	**154,931**	244,189
Work in progress	**106,095**	56,429
	261,026	300,618

During the three months ended December 31, 2013, the Company recorded cost of sales of $256,575 (2012 - $252,460) related to the sale of inventories.

8. Investment

In January 2009, the Company acquired 1.58% of the Class A common shares of RFind Systems Inc. (“RFind”), a non-publicly traded company. During the year ended September 30, 2013, the Company wrote down its $50,000 investment in RFind Systems Inc. to nil as a result of RFind selling off part of its business interests in 2013 to repay debts and is presently operating with limited cash and personnel. Upon assessment, the Company does not expect to recover its investment in RFind.

9. Property and equipment

	December 31 2013	September 30 2013
	$	$
Carrying amounts of		
Manufacturing, office and computer equipment	**56,571**	43,907
Leasehold improvements	**-**	1,562
	56,571	45,469

	Manufacturing, office and computer equipment	Leasehold improvements
	$	$
Cost		
Balance at September 30, 2011	366,928	25,472
Additions	10,151	-
Effect of foreign currency exchange differences	(18,209)	(1,580)
Balance at September 30, 2012	358,870	23,892
Additions	44,381	-
Effect of foreign currency exchange differences	16,272	1,145
Balance at September 30, 2013	419,523	25,037
Additions	1,150	-
Disposals	(14,364)	-
Effect of foreign currency exchange differences	12,340	819
Balance at December 31, 2013	**418,649**	**25,856**
Accumulated depreciation		
Balance at September 30, 2011	300,702	19,919
Depreciation expense	29,940	3,736
Effect of foreign currency exchange differences	(15,679)	(1,325)
Balance at September 30, 2012	314,963	22,330
Depreciation expense	27,742	1,637
Effect of foreign currency exchange differences	14,921	1,070
Balance at September 30, 2013	357,626	25,037
Disposals	(12,568)	**-**
Depreciation expense	5,939	**-**
Effect of foreign currency exchange differences	11,081	819
Balance at December 31, 2013	**362,078**	**25,856**

10. Intangible assets

	December 31 2013	September 30 2013
	$	$
Carrying amounts of		
Licenses	**5,227**	7,323

	Licenses
	$
Cost	
Balance at September 30, 2011	57,998
Additions	1,855
Effect of foreign currency exchange differences	(3,632)
Balance at September 30, 2012	56,221
Effect of foreign currency exchange differences	2,693
Balance at September 30, 2013	58,914
Effect of foreign currency exchange differences	1,927
Balance at December 31, 2013	**60,841**
Accumulated amortization	
Balance at September 30, 2011	49,913
Amortization expense	2,130
Effect of foreign currency exchange differences	(3,145)
Balance at September 30, 2012	48,898
Amortization expense	2,096
Effect of foreign currency exchange differences	2,372
Balance at September 30, 2013	53,366
Amortization expense	502
Effect of foreign currency exchange differences	1,746
Balance at December 31, 2013	**55,614**

11. Goodwill

The goodwill arose from the acquisitions of IDIT and IDME during the year ended September 30, 2013.

	$
Balance at October 1, 2012	-
Goodwill on acquisitions of IDIT and IDME (Note 5)	5,444,954
Balance at September 30, 2013 and December 31, 2013	**5,444,954**

Goodwill is assessed for impairment annually as at September 30, or when circumstances indicate there may be impairment, and is allocated to cash generating units ("CGUs") on the basis of management's internal review. The provisional goodwill from the acquisition of IDIT and IDME has not been allocated to a CGU yet as management is still assessing whether there will be a new CGU established. See Note 5.

12. Transactions with related parties

The remuneration of directors and other members of key management personnel are as follows:

	December 31 2013	December 31 2012
	$	$
Management and director fees	**72,990**	62,830
Legal fees	**19,764**	7,611
	92,754	70,441

Included in the above table

(a) Management fees of $62,490(2012 - $58,330) were charged by Geni D Ventures Inc., a company controlled by Mr. Blakeway who is an officer or director of the Company. As of December 31, 2013, amounts owing to this company included in accounts payable and accrued liabilities were $Nil (2012 - $Nil).

(b) Fees of $19,764 (2012 - $7,611) in relation to legal services provided were paid to McMillan LLP, a law firm a partner of which was a related party during the year. The partner, Mr. Zinkhofer is a director of the Company.

The following transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

i) As at December 31, 2013, $4,387 was receivable from a director of the Company for amounts advanced by the Company to Canada Revenue Agency on his behalf. Interest of $182 was charged on this advance during the quarter.

ii) As at December 31, 2013, included in due to related party was $496,717 (2012 - $792) in advances, management fees and legal fees owing to officers and directors. The amounts owing are unsecured, non-interest bearing and have no fixed repayment terms.

iii) The Company completed a unit private placement during the year ended September 30, 2012, issuing 1,844,822 units at $1.00 per unit (Note 14). Mr. Zinkhofer, the Company's corporate secretary and director participated in the placement and acquired less than 1% of the issued shares.

iv) During the quarter ended December 31, 2013, the Company paid $Nil (2012 - $120,000) for research and development to IDME, a company which has common shareholders and directors as Nanotech and on September 27, 2013, the Company acquired 95% of IDME (Note 5).

v) During the year ended September 30, 2010, the Company acquired in consideration of an initial advance royalty payment, a license agreement from IDME, for the light based recognition nanotechnology being developed by the Company for use in anti-counterfeiting and authentication processes and products for currency, legal documents and commercial products. The advance royalty payments were required to be paid between June 15, 2010 and June 15, 2014 total $675,000 all of which has been expensed. Prior to the acquisition of IDME on September 27, 2013, $417,250 had been paid cumulatively and a further $37,500 was accrued in the current quarter.

13. Income taxes

The Company has approximately $9.5 million in Canadian tax loss carry forwards with expiry dates from 2014-2032, the tax effect of which has not been recognized in the accounts. Income tax loss carry forwards are reported on an annual basis.

14. Share capital

(a) Share capital

	Number	Amount
		$
September 30, 2011	24,253,711	14,812,193
Private placement	1,844,822	1,586,729
Warrants exercised	2,517,000	354,669
September 30, 2012	28,615,533	16,753,591
Private placement	5,210,500	3,506,607
Acquisition of IDIT and IDME (Note 5)	3,705,103	4,853,685
Options exercised	1,225,000	184,584
Warrants expired	-	180,393
September 30, 2013 and December 31, 2013	**38,756,136**	**25,478,860**

The Company completed a private placement in in two tranches, on August 20, 2013 and September 3, 2013 with several arm's length investors for total proceeds of $4,168,400 by the issuance of subscription receipts convertible into equity units at $0.80 each. Each unit comprising a common share and 0.5 warrants exercisable for 18 months at $0.90. These units were converted to common shares and warrants on the completion of the acquisition of IDME and IDIT (Note 5). Share issuance costs of $38,592 were incurred in relation to the private placement.

(b) Stock option plan

	Number of options	Exercise price	Expiry date
		$	
Outstanding, September 30, 2011	1,566,000	0.24	
Cancelled	(25,000)	0.10	
Outstanding, September 30, 2012	1,541,000	0.24	
Granted	690,000	0.80	February 27, 2016
Forfeited	(46,000)	0.80	
Exercised	(1,225,000)	0.10	
Outstanding, September 30, 2013	960,000	0.80	
Granted	85,000	1.75	December 23, 2016
December 31, 2013	1,045,000	0.87	

During the quarter ended December 31, 2013, a total of 85,000 stock options were granted to certain contractors of the Company at a price of $1.75 per share, exercisable for a term of three years. The fair value at the date of grant totaling $66,728 was estimated using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 60%; average risk-free interest rate of 1.19%; and an expected life of three years. The stock options vest in installments, whereby each installment is accounted for as a separate arrangement (known as "Graded Vesting"). To December 31, 2013, no options vested.

In the year ended September 30, 2013, a total of 690,000 stock options were granted to certain employees of the Company at a price of $0.80 per share, exercisable for a term of three years. The fair value at the date of grant totaling $257,405 was estimated using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 70%; average risk-free interest rate of 1.02%; and an expected life of

14. Share capital (continued)

(c) Stock option plan (continued)

three years. The stock options outstanding vest in installments, whereby each installment is accounted for as a separate arrangement (also known as "Graded Vesting"). To December 31, 2013, 477,875 options vested.

During the three months ended December 31, 2013, the share based payment was $27,946 (2012 - $Nil).

(d) Warrants

	Number of warrants	Weighted average exercise price	Fair value of warrants
		$	$
At September 30, 2011	2,517,000	0.10	102,969
Exercised	(2,517,000)	0.10	(102,969)
Granted	922,411	1.25	180,393
At September 30, 2012	922,411	1.25	180,393
Expired	(922,411)	1.25	(180,393)
Granted	2,605,250	0.90	623,305
At September 30, 2013 and December 31, 2013	**2,605,250**	**0.90**	**623,305**

During the year ended September 30, 2012, 2,517,000 warrants were exercised at a price of $0.10 for proceeds of $251,700.

During the year ended September 30, 2012, the Company issued warrants together with a private placement issuing 1,844,822 units. Each unit is comprised of one share and one-half warrant, exercisable for one year at $1.25. Commissions and finder's fees of $77,800 were paid in cash.

The fair values of warrants issued was determined using the Black-Scholes option pricing model with the following assumptions: no dividends are to be paid; average expected volatility of 67.26%; average risk-free interest rate of 1.23%; and expected life of one year. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of one year.

During the year ended September 30, 2013, the Company issued warrants together with a private placement in two tranches issuing 5,210,500 units in total. Each unit is comprised of one share and one-half warrant, exercisable for eighteen months at $0.90. Commissions and finder's fees of $38,592 were paid in cash.

The fair values of warrants issued was determined using the Black-Scholes option pricing model with the following assumptions: Tranche 1 no dividends are to be paid; average expected volatility of 53.77%; average risk-free interest rate of 1.22%; and expected life of 1.5 years. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of eighteen months. Tranche 2 no dividends are to be paid; average expected volatility of 53.43%; average risk-free interest rate of 1.29%; and expected life of 1.5 years. The expected annualized volatility was calculated using the Company's historic common share prices with a reference period equal to the expected life of eighteen months.

During the year ended September 30, 2013, 922,411 warrants expired unexercised.

15. Supplementary cash flow information

(a) Change in non-cash operating working capital

	2013	2012
	$	$
Accounts receivable	**107,138**	71,174
Inventory	**49,878**	(13,780)
Prepaid expenses	**(25,335)**	(37,204)
Accounts payable	**(350,522)**	110,109
Current provisions	**-**	(32,448)
Due to related party	**(37,095)**	-
Deposits	**(343)**	(7,360)
Other assets	**(338)**	(117)
	(256,617)	90,374

(b) Interest and income taxes

During the quarter ended December 31, 2013 and 2012, the Company did not pay or receive any interest or income taxes.

(c) Cash and cash equivalents

Cash and cash equivalents are comprised of:

	2013	2012
	$	$
Cash	**378,190**	908,619
Money market funds	**3,229,098**	255,557
	3,607,288	1,164,176

(d) Non-cash investing and financing activities

During the year ended September 30, 2013, the Company issued 3,705,103 shares and agreed to issue an additional 234,897 shares subject to disinterested shareholders' approval for the acquisition of IDME and IDIT. See Note 5.

16. Non-controlling interest

	2013	2012
	$	$
Balance, September 30, 2013	**(14,924)**	-
Non-controlling interest	**1,816**	-
Balance, December 31, 2013	**(13,108)**	-

17. Capital risk management

The Company defines capital as long-term debt plus shareholders' equity. The Company's objectives when managing capital are to safeguard the ability to continue as a going concern, to provide an adequate return to shareholders, to meet external capital requirements and preserve financial flexibility in order to benefit from potential opportunities that may arise. The Company's officers are responsible for managing the Company's capital and do so through quarterly meetings and regular review of financial information. The Board of Directors is responsible for overseeing

17. Capital risk management (continued)

this process. In managing its capital, the Company considers changes in economic conditions, risks that impact the consolidated operations and future significant capital investment opportunities.

18. Financial instruments

Financial risk management

The Company's activities expose it to a variety of financial risks including market risk (foreign exchange and interest rate risk), credit risk and liquidity risk. Management reviews these risks on an ongoing basis to ensure that the risks are appropriately managed. The Company may use foreign exchange forward contracts to manage exposure to fluctuations in foreign exchange from time to time. The Company does not have a practice of trading derivatives and has none outstanding at December 31, 2013.

(a) *Interest rate risk*

The Company's objective in managing interest rate risk is to monitor expected volatility in interest rates while also minimizing financing expense levels. Interest rate risk mainly arises from fluctuations of interest rates and the impact on the return earned on cash and cash equivalents. On an ongoing basis, management monitors changes in short-term rates and considers long-term forecasts to assess potential cash flow impacts to the Company. The Company does not currently hold any financial instruments to mitigate its interest risk. Cash and cash equivalents earns interest based on market interest rates

(b) *Foreign exchange risk*

The Company operates on an international basis and is subject to foreign exchange risk exposures arising from transactions denominated in a foreign currency. The Company's objective is to minimize the impact of the volatility related to financial assets and liabilities denominated in a foreign currency where possible through effective cash flow management. Foreign currency exchange risk is limited to the portion of the Company's business transactions denominated in currencies other than Canadian dollars. On an ongoing basis, management monitors changes in foreign currency exchange rates as well as considering long-term forecasts to assess the potential cash flow impact to the Company. The Company has elected not to actively manage the foreign exchange exposures at this time. The impact of a 10% change in foreign exchange rates between the Canadian and U.S. dollar on the Company's results of operations or financial position would not be significant.

U.S. dollar balances subject to this risk as follows:

	2013	2012
	$	$
Cash and cash equivalents	**290,758**	826,090
Accounts receivable	**108,516**	136,149
Accounts payable	**(142,852)**	(109,729)
Deposits	**(5,080)**	(2,460)
	251,342	850,050

18. Financial instruments (continued)

(c) Credit risk

Credit risk is the risk of a financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company is exposed to credit risk through its cash and cash equivalents and accounts receivable. The Company manages the credit risk associated with its cash by placing its funds with reputable financial institutions and investing in only highly rated securities that are traded on active markets and are capable of prompt liquidation.

Credit risk for accounts receivable is managed through established credit monitoring activities. The Company also mitigates its credit risk on trade accounts receivable by obtaining cash deposits from certain customers.

	2013	2012
	$	$
Cash	**3,607,288**	1,164,176
Accounts receivable	**254,973**	170,689
	3,862,261	1,334,865

The Company has a concentration of customers in government agencies and law enforcement. Losses under trade accounts receivable have been historically insignificant. The credit worthiness of new customers is subject to review by management, and that of existing customers is monitored. The Company reviews its trade receivable accounts regularly and amounts are written down to their expected realizable value when the account is determined not to be fully collectible. The bad debt expense is charged to net income in the period that the account is determined to be doubtful. The Company does not currently have an allowance for doubtful accounts.

Substantially all accounts receivable are less than 60 days old.

(d) Liquidity risk

The Company's objective related to liquidity risk is to effectively manage cash flows to minimize the exposure that the Company will not be able to meet its obligations associated with financial liabilities as they fall due. On an ongoing basis, the Company manages liquidity risk by maintaining adequate cash balances.

(e) Fair values

The carrying amounts of accounts receivables, accounts payables and accrued liabilities and provisions approximate fair value due to the short term nature of these financial instruments. Fair values of other financial instruments are classified using the following fair values hierarchy:

Level 1 - inputs are unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 - inputs are other than quoted prices in Level 1 that are observable for the asset or liability, either directly or indirectly; and

Level 3 - inputs for the asset or liability that are not based on observable market data.

18. Financial instruments (continued)

The Company's financial instruments, carried at fair value, are classified into the above hierarchy as follows:

	Level 1	Level 2	Level 3	Total
Financial assets				
Cash and cash equivalents	**3,607,288**	-	**-**	**3,607,288**

19. Segmented information

Information reported to the chief operating decision maker for the purposes of resource allocation and assessment of segment performance focuses on the types of products or services delivered or provided. The directors of the Company have chosen to organize the Company around differences in products and services. Specifically the Company's reportable segments under IFRS 8 are: Tactical which designs, manufactures and sells sophisticated wireless radio frequency ("RF") communication, surveillance, intelligence gathering and officer safety equipment and Nanotechnology which is developing anti-counterfeiting authentication processes using nano-hole light based recognition nanotechnology. The Company has revenues from Tactical's operations but has not yet earned revenues related to the light based recognition nanotechnology.

Tactical's major customers are local, state and federal law enforcement agencies located primarily in the United States. Nanotech does not have customers at the present time.

No customer represents in excess of 10% of total revenue in both 2013 and 2012.

			2013
	Nanotechnology	**Tactical**	**Consolidated**
	$	**$**	**$**
Total current assets	**3,485,546**	**674,819**	**4,160,365**
Property and equipment	**22,270**	**34,301**	**56,571**
Intangible assets	**-**	**5,227**	**5,227**
Other assets	**-**	**10,640**	**10,640**
Total liabilities	**803,821**	**157,400**	**961,221**
Non-controlling interests	**13,108**	**-**	**13,108**
Capital expenditures	**1,149**	**(10,640)**	**(9,491)**

19. Segmented information (continued)

			2012
	Nanotechnology	Tactical	Consolidated
	$	$	$
Total current assets	994,735	686,845	1,681,580
Property and equipment	9,887	31,016	40,903
Investment	50,000	-	50,000
Intangible assets	-	6,897	6,897
Other assets	-	9,949	9,949
Total liabilities	394,650	111,620	506,270

			2013
	Nanotechnology	**Tactical**	**Consolidated**
	$	**$**	**$**
Operating revenue	**59,134**	**556,801**	**615,935**
Cost of sales	**463**	**368,807**	**369,270**
Gross profit (loss)	**58,671**	**187,994**	**246,665**
Operating expenses	**423,117**	**185,359**	**608,476**
Gain on sale of fixed asset	**-**	**8,845**	**8,845**
Net profit (loss)	**(364,446)**	**11,480**	**(352,966)**
Unrealized foreign exchange (loss) gain on translation of foreign operation	**27,467**	**-**	**27,467**
Total comprehensive loss	**(336,979)**	**11,480**	**(325,499)**

			2012
	Nanotechnology	Tactical	Consolidated
	$	$	$
Operating revenue	539	537,289	537,828
Cost of sales	37,500	360,079	397,579
Gross profit	(36,961)	177,210	140,249
Operating expenses	270,482	189,296	459,778
Net loss	(307,443)	(12,086)	(319,529)
Unrealized foreign exchange (loss) gain on translation of foreign operation	11,390	-	11,390
Total comprehensive loss	(296,053)	(12,086)	(308,139)

20. Commitments

The minimum annual rentals payable under the terms of operating leases for premises are as follows:

	Total
	$
2014	232,159
2015	135,670
Thereafter	167,460
	535,289

21. Subsequent Events

Ms. Frenny Bawa resigned her position at Nanotech as Chief Commercial Officer effective February 28th, 2014. Ms Bawa expressed a desire to pursue personal activities.

Nanotech announced on February 25, 2014 that the Company's common shares commenced trading on the OTCQX® Market in the United States under the ticker symbol "NTSFF". The Company is pleased to have qualified for trading on OTCQX®, which will better enable Nanotech to provide U.S. investors with timely news and information. Additional information about Nanotech and its technologies can now be found at www.nanosecurity.ca or www.sedar.com or www.otcmarkets.com

There were no other subsequent events which constituted material changes in the Company's affairs.