

METHES ENERGIES INTERNATIONAL LTD  
Form 10-Q  
July 14, 2014

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended May 31, 2014

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 001-35652

METHES ENERGIES INTERNATIONAL LTD.  
(Exact name of registrant as specified in its charter)

NEVADA	71-1035154
(State of other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3651 Lindell Road, Suite D-272, Las Vegas, Nevada, 89103  
(Address of principal executive offices)

(702) 932-9964  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES   
NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act:

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES  NO

As of July 14, 2014, the registrant has 11,435,431 shares of Common Stock issued and outstanding.

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## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This Form 10-Q contains “forward looking information” within the meaning of applicable securities laws. Such statements include, but are not limited to, statements with respect to the Company’s beliefs, plans, strategies, objectives, goals and expectations, including expectations about the future financial or operating performance of the Company and its projects, capital expenditures, capital needs, government regulation of the industry, environmental risks, limitations of insurance coverage, and the timing and possible outcome of regulatory matters, including the granting of patents and permits. Words such as “expect,” “anticipate,” “intend,” “attempt,” “may,” “will,” “plan,” “believe,” “s” “estimate” and variations of such words and similar expressions are intended to identify such forward looking information. These statements are not guarantees of future performance and involve assumptions, risks and uncertainties that are difficult to predict.

These statements are based on and were developed using a number of factors and assumptions including, but not limited to: stability in the U.S. and other foreign economies; stability in the availability and pricing of raw materials, energy and supplies; stability in the competitive environment; the continued ability of the Company to access cost effective capital when needed; and no unexpected or unforeseen events occurring that would materially alter the Company’s current plans. All of these assumptions have been derived from information currently available to the Company including information obtained by the Company from third party sources. Although management believes that these assumptions are reasonable, these assumptions may prove to be incorrect in whole or in part. As a result of these and other factors, actual results may differ materially from those expressed, implied or forecasted in such forward looking information, which reflect the Company’s expectations only as of the date hereof.

Factors that could cause actual results or outcomes to differ materially from the results expressed, implied or forecasted by the forward-looking information include risks associated with general business, economic, competitive, political and social uncertainties; risks associated with changes in project parameters as plans continue to be refined; risks associated with failure of plant, equipment or processes to operate as anticipated; risks associated with accidents or labor disputes; risks associated in delays in obtaining governmental approvals or financing, or in the completion of development or construction activities; risks associated with financial leverage and the availability of capital; risks associated with the price of commodities and the inability of the Company to control commodity prices; risks associated with the regulatory environment within which the Company operates; risks associated with litigation including the availability of insurance; and risks posed by competition. These and other factors that could cause actual results or outcomes to differ materially from the results expressed, implied or forecasted by the forward looking information are discussed in more detail in Item 1A under “Risk Factors” in Part I of our Annual Report on Form 10-K for the fiscal year ended November 30, 2013, as may be supplemented or amended from time to time and in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part I, Item 2 in this document.

The Company does not intend to, and the Company disclaims any obligation to, update any forward-looking information (including any financial outlooks), whether written or oral, or whether as a result of new information, future events or otherwise, except as required by law.

All references in this Form 10-Q to “Company,” “Methes,” “we,” “us,” or “our” refer to Methes Energies International Ltd. and its wholly owned subsidiaries Methes Energies Canada Inc. and Methes Energies USA Ltd. unless the context otherwise indicates.

We have rights to the trademarks Methes Energies and Design, Methes, The Biodiesel Company and Denami.



## PART I. FINANCIAL INFORMATION

## ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## METHES ENERGIES INTERNATIONAL LTD.

CONDENSED CONSOLIDATED BALANCE SHEETS AS OF NOVEMBER 30, 2013 AND MAY 31, 2014  
(EXPRESSED IN US\$)

ASSETS	November 30, 2013 (Unaudited)	May 31, 2014 (Unaudited)
Current assets		
Cash and cash equivalents	\$ 174,084	\$ 4,048,226
Accounts receivable, net (notes 10 and 12)	1,154,916	136,637
Inventories (note 3)	801,063	249,728
Prepaid expenses and deposits	84,990	402,768
Deferred financing fees	49,139	6,424
<b>Total current assets</b>	<b>2,264,192</b>	<b>4,843,783</b>
Deposits	30,398	28,199
Property, plant and equipment, net (note 4)	8,178,694	8,056,626
Intangible assets, net	393,015	382,913
<b>Total assets</b>	<b>\$ 10,866,300</b>	<b>\$ 13,311,521</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities		
Credit facility (note 7)	\$ 1,019,513	\$ —
Accounts payable (note 10)	2,766,661	1,740,695
Accrued liabilities	211,296	224,664
Customer deposits (note 10)	8,185	9,104
Payable to related parties and others (note 5)	2,251,402	745,750
Short-term loans (note 6)	1,961,651	3,394,039
<b>Total liabilities</b>	<b>8,218,708</b>	<b>6,114,252</b>
Stockholders' equity		
Preferred stock, \$0.001 par value, 10,000,000 shares authorized; 260,782 and 111,822 shares issued and outstanding as at November 30, 2013 and May 31, 2014, respectively (note 8)	261	112
Common stock, \$0.001 par value, 75,000,000 shares authorized; 7,231,417 and 11,435,431 shares issued and outstanding at November 30, 2013 and May 31, 2014, respectively (note 8)	7,231	11,435
Additional paid-in capital	18,532,803	26,142,945
Accumulated deficit	(15,892,703)	(18,957,223)
<b>Total stockholders' equity</b>	<b>2,647,592</b>	<b>7,197,269</b>

Total liabilities and stockholders' equity	\$ 10,866,300	\$ 13,311,521
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Commitments (note 11)

See accompanying notes to unaudited condensed consolidated financial statements

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## METHES ENERGIES INTERNATIONAL LTD.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)  
FOR THE THREE AND SIX MONTHS ENDED MAY 31, 2013 AND MAY 31, 2014  
(EXPRESSED IN US\$)

	Three Months Ended May 31, 2013	Three Months Ended May 31, 2014	Six Months Ended May 31, 2013	Six Months Ended May 31, 2014
Revenue				
Biodiesel sales	\$ 2,080,304	\$ 316,294	\$ 2,210,740	\$ 625,831
Feedstock sales	40,802	69,719	84,988	96,341
Glycerin sales	22,635	10,649	36,441	23,847
Government incentives (note 12)	170,124	25,557	179,004	38,592
Equipment sales	2,657	750	2,657	1,397
Royalties	2,793	11,454	6,775	11,454
Others	9,039	4,982	17,860	20,421
	2,328,354	439,405	2,538,465	817,883
Cost of goods sold	2,221,184	371,921	2,410,713	664,540
Gross profit	107,170	67,484	127,752	153,343
Operating expenses				
Selling, general and administrative expenses (note 4, 8 and 9)				
	1,476,838	1,442,291	2,767,926	2,907,700
Loss before interest and taxes	(1,369,668)	(1,374,807)	(2,640,174)	(2,754,357)
Other expenses				
Interest expense (notes 5, 6 and 7)	(122,143)	(192,035)	(242,969)	(293,927)
Loss before income taxes	(1,491,811)	(1,566,842)	(2,883,143)	(3,048,284)
Income taxes				
Net loss for the period	\$ (1,491,811)	\$ (1,566,842)	\$ (2,883,143)	\$ (3,048,284)
Net Loss Per Common Share - Basic and Diluted	\$ (0.21)	\$ (0.18)	\$ (0.42)	\$ (0.36)
Weighted average number of common shares - Basic and Diluted	6,978,169	8,702,605	6,790,324	8,411,002

See accompanying notes to unaudited condensed consolidated financial statements



## METHES ENERGIES INTERNATIONAL LTD.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (Unaudited)  
FOR THE YEAR ENDED NOVEMBER 30, 2013 AND THE SIX MONTHS ENDED MAY 31, 2014  
(EXPRESSED IN US\$)

	Common Stock		Preferred Stock		Additional	Accumulated	Total
	Shares	Amount	Shares	Amount	Paid-in Capital	Deficit	
Balance at November 30, 2012	6,553,169	\$ 6,553	—	—\$	—\$ 16,033,123	\$ (10,241,029)	\$ 5,798,647
Issuance of common stock units under private placement	653,248	653	—	—	2,149,347	—	2,150,000
Issuance cost – common stock under private placement	—	—	—	—	(368,611)	—	(368,611)
Issuance of Common stock for services	25,000	25	—	—	51,975	—	52,000
Issuance of preferred stock units under private placements	—	—	260,782	261	622,239	—	622,500
Issuance cost – preferred stock under private placement	—	—	—	—	(149,330)	—	(149,330)
Stock-based compensation	—	—	—	—	155,578	—	155,578
Dividends payable on preferred stock units	—	—	—	—	—	(9)	(9)
Issuance of common stock options to employees and officer	—	—	—	—	38,482	—	38,482
Net loss for the period	—	—	—	—	—	(5,651,665)	(5,651,665)
Balance at November 30,	7,231,417	\$ 7,231	260,782	\$ 261	\$ 18,532,803	\$ (15,892,703)	\$ 2,647,592

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2013								
Issuance of common stock units under private placement	1,081,161	1,081	—	—	2,161,240	—	2,162,321	
Issuance of common stock under public offering	2,800,000	2,800	—	—	5,597,200	—	5,600,000	
Issuance cost—common stock units under private placement	—	—	—	—	(949,358)	—	(949,358)	
Issuance of common stock units for cash upon conversion of preferred stock units	148,960	149	(148,960)	(149)	—	—	—	
Issuance of common stock upon conversion of dividends on preferred stock	7,205	7	—	—	16,229	(16,236)	—	
Issuance of common stock units for cash	16,129	16	—	—	99,984	—	100,000	
Issuance of common stock and units for services	108,871	109	—	—	447,141	—	447,250	
Issuance of common stock units for loan settlement	34,688	35	—	—	127,964	—	128,000	
Issuance of common stock upon conversion of placement agent warrants	7,000	7	—	—	13,993	—	14,000	
Stock-based compensation	—	—	—	—	95,749	—	95,749	
Net loss for the period	—	—	—	—	—	(3,048,284)	(3,048,284)	
Balance at May 31, 2014	11,435,431	\$ 11,435	111,822	\$ 112	\$ 26,142,945	\$ (18,957,223)	\$ 7,197,269	

See accompanying notes to unaudited condensed consolidated financial statements



## METHES ENERGIES INTERNATIONAL LTD.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
FOR THE SIX MONTHS ENDED MAY 31, 2013 AND MAY 31, 2014  
(EXPRESSED IN US\$)

	Six Months Ended May 31, 2013	Six Months Ended May 31, 2014
Cash flows from operating activities:		
Net loss for the period	\$ (2,883,143)	\$ (3,048,284)
Adjustments to reconcile net loss to net cash used in operations		
Depreciation and amortization	243,695	222,197
Stock-based compensation	66,633	95,749
Unrealized foreign exchange gain	(76,193)	(40,357)
Deferred financing fees amortization	22,583	42,715
Accrued interest	81,641	90,623
Bad debts	—	35,662
Issuance of common stock/units for consulting services	—	371,854
Changes in operating assets and liabilities:		
Accounts receivable	(113,432)	982,617
Inventories	97,173	551,335
Prepaid expenses and deposits	(15,756)	(240,184)
Accounts payable and accrued liabilities	440,132	(1,012,596)
Customer deposits	—	919
Net cash used in operating activities	(2,136,667)	(1,947,750)
Cash flows from investing activity:		
Additions to property, plant and equipment	(351,828)	(90,027)
Additions to intangible assets	(191)	—
Net cash used in investing activity	(352,019)	(90,027)
Cash flows from financing activities:		
Repayment of credit facility	—	(1,019,513)
Advances from short-term loans	385,800	135,705
Repayments of short-term loans	—	(269,401)
Advances from related parties and others	519,258	172,000
Repayments to related parties and others	—	(33,835)
Issuance of common stock/units under private placement and public offering (net of issuance costs)	1,369,390	6,812,963
Issuance of common stock/units for cash	—	100,000
Issuance of common stock upon conversion of placement agent warrants	—	14,000
Net cash provided by financing activities	2,274,448	5,911,919
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(214,238)	3,874,142
Cash and cash equivalents, beginning of period	402,724	174,084
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 188,486	\$ 4,048,226

Supplemental disclosures of cash flow information			
Interest paid	\$	171,723	\$ 216,674
Common shares issued as repayment of loan	\$	—	\$ 128,000

See accompanying notes to unaudited condensed consolidated financial statements

METHES ENERGIES INTERNATIONAL LTD.  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Unaudited  
As of May 31, 2014  
(Expressed in US\$)

NOTE 1 - NATURE OF THE BUSINESS, FINANCING REQUIREMENTS AND BASIS OF PRESENTATION

Methes Energies International Ltd. ("Methes" or the "Company"), was incorporated on June 27, 2007 in the State of Nevada. Methes, through its operations in Canada and the United States, is a biodiesel processing equipment provider and a biodiesel producer. The Company has developed biodiesel processing equipment to produce biodiesel from recycled oils. The Company, through its wholly-owned subsidiary Methes Energies Canada Inc. ("Methes Canada"), operates two biodiesel manufacturing facilities; one is located in Mississauga, Ontario with a nameplate production capacity of 1.3 million gallons per year (mgy), and the second facility is capable of producing 13.0 mgy of biodiesel located in Sombra, Ontario. In addition to Methes Canada, Methes Energies USA Ltd. ("Methes USA") was incorporated as the wholly-owned subsidiary of the Company on June 27, 2007. All references in this Form 10-Q to "Company," "Methes," "we," "us," or "our" refer to Methes Energies International Ltd. and its wholly owned subsidiaries Methes Canada and Methes USA unless the context otherwise indicates.

As at May 31, 2014, due in large part to the funds spent to develop, build and commission our Sombra facility as well as minimal sales of biodiesel, the Company had a working capital deficiency of \$1,270,469. During the six months ended May 31, 2014, the Company incurred a loss of \$3,048,284 and had negative cash flows from operations of \$1,947,750. The Company anticipates that its Sombra facility will generate positive cash flows from operations and will operate profitably once full-scale commercial operations are achieved in the second half of fiscal year 2014. However, in order to meet its development goals and ongoing operational requirements, the Company will require additional financing in the foreseeable future. It is management's opinion that the anticipated positive cash flows from operations and cash from additional financing completed in May 2014 will be sufficient to meet the Company's cash requirements for at least the next 12 months.

The condensed consolidated financial statements have been prepared by the Company without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted as permitted by such rules and regulations. All adjustments, consisting of normal recurring adjustments, have been included. Management believes that the disclosures are adequate to present fairly the financial position, results of operations and cash flows at the dates and for the periods presented. It is suggested that these interim financial statements be read in conjunction with the consolidated financial statements and the notes thereto appearing in the Company's latest annual report on Form 10-K. Results for interim periods are not necessarily indicative of those to be expected for the full fiscal year.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries Methes Canada and Methes USA. All significant inter-company transactions and balances have been eliminated.

#### Deferred Financing Fees

Financing fees relating to other financing arrangements are deferred and amortized over the term of the respective loan.

#### Shipping and Handling Costs

The Company accounts for shipping and handling fees in accordance with FASB ASC 705 "Cost of Sales and Services". Shipping and handling costs for the three and six months ended May 31, 2014 were \$8,032 and \$23,602, respectively (three and six months ended May 31, 2013 was \$101,561 and \$175,255, respectively). Costs related to raw materials purchased, are included in inventory or cost of goods sold, as appropriate. While amounts charged to customers for shipping product are included in revenues, the related outbound freight costs are included in expenses as incurred.

#### Income Taxes and Uncertain Tax Positions

The Company accounts for income taxes under ASC 740 Accounting for Income Taxes. Under ASC 740, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the periods in which those temporary differences are expected to be recovered or settled. Under ASC 740, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. ASC 740-10-05, Accounting for Uncertainty in Income Taxes, prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return.

For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities.

The amount recognized is measured as the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Potential tax benefits from net operating losses and foreign tax credit carry forwards are not recognized by the Company until their realization is more likely than not. The Company assesses the validity of conclusions regarding uncertain tax positions on a quarterly basis to determine if facts or circumstances have arisen that might cause the Company to change their judgment regarding the likelihood of a tax position's sustainability under audit. The Company has determined that there were no material uncertain tax positions as at November 30, 2013 and May 31, 2014.

#### Per Share Data

Basic earnings per share ("EPS") is determined by dividing net earnings available to common stockholders (numerator) by the weighted average number of shares outstanding (denominator) during the period. In computing diluted EPS, the average number of shares of Common Stock outstanding is increased by Common Stock options and warrants outstanding if the exercise prices were lower than the average market price of Common Stocks using the treasury stock method. Diluted earnings per share exclude all potentially dilutive shares if their effect is anti-dilutive. Potentially dilutive shares include 2,163,764 warrants and 483,310 Common Stock options issued and outstanding as at May 31, 2013 and 3,923,149 warrants, 353,922 Common Stock options and 111,822 shares of Preferred Stock issued and outstanding as at May 31, 2014. All outstanding warrants, preferred shares and options have an anti-dilutive effect on the loss per share and are therefore excluded from the determination of the diluted loss per share calculation for the three and six months ended May 31, 2013 and May 31, 2014.

#### New Accounting Pronouncements

In December 2011, the FASB issued ASU No. 2011-11, Disclosures about Offsetting Assets and Liabilities (Topic 210). The new disclosure requirements mandate that entities disclose both gross and net information about instruments and transactions eligible for offset in the statement of financial position as well as instruments and transactions subject to an agreement similar to a master netting arrangement. In addition, the standard requires disclosure of collateral received and posted in connection with master netting agreements or similar arrangements. The amendments are effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The disclosures required by the amendments are required to be applied retrospectively for all comparative periods presented. The Company adopted this statement effective December 1, 2013. The adoption of this statement did not have a material effect on the Company's unaudited condensed consolidated financial statements.

On May 28, 2014, the FASB issued a new financial accounting standard on revenue from contracts with customers, Update No. 2014-09, Revenue from Contracts with Customers (Topic 606). The standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance. The accounting standard is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016. Early adoption is not permitted. The Company is currently evaluating the impact of this accounting standard.

All other recent pronouncements issued by the FASB or other authoritative standards groups with future effective dates are either not applicable or are not expected to be significant to the condensed consolidated financial statements of the Company.



## NOTE 3 - INVENTORIES

Inventories consisted of the following:

	As at November 30, 2013	As at May 31, 2014
Raw materials	\$345,049	\$148,748
Finished goods	444,648	89,614
Equipment	11,366	11,366
	\$801,063	\$249,728

## NOTE 4 – PROPERTY, PLANT AND EQUIPMENT

	As at May 31, 2014		As at November 30, 2013	As at November 30, 2013
	Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Sombra site:				
Land	\$ 409,134	\$ —	\$ 409,134	\$ 409,134
Building	2,944,356	278,713	2,665,643	2,702,446
Equipment	775,865	439,032	336,833	390,465
Equipment - Denami 3000	4,254,995	273,939	3,981,056	3,975,441
Computer equipment	11,835	8,827	3,008	5,918
Vehicle	11,622	872	10,750	11,331
Mississauga site:				
Computer equipment	23,464	22,985	479	1,316
Leasehold improvements	102,201	60,805	41,396	46,591
Equipment and fixtures	255,463	191,125	64,338	77,662
Equipment - Denami 600	720,042	176,053	543,989	558,390
	\$ 9,508,977	\$ 1,452,351	\$ 8,056,626	\$ 8,178,694

Total depreciation expense included in selling, general and administrative expenses in the unaudited consolidated statements of operations related to property, plant and equipment for the three and six months ended May 31, 2014 was \$106,317 and \$212,095, respectively (three and six months ended May 31, 2013 was \$117,177 and \$233,593, respectively).

## NOTE 5 - PAYABLE TO RELATED PARTIES AND OTHERS

Payable to related parties is comprised of the following:

	As at November 30, 2013	As at May 31, 2014
Michel G. Laporte (stockholder and Director)	\$ 719,230	\$ 745,750
World Asset Management Inc. (reclassified to short-term loans - Note 6, Promissory note (iii))	1,495,477	—
Other loan	36,695	—
	\$ 2,251,402	\$ 745,750

The payables to related parties and others bear interest at 8% per annum, are unsecured and repayable on demand. The related parties and others have agreed in writing to postpone the repayment of their debts in favor of the credit facility referred to in note 7. Interest expense incurred during the three and six months ended May 31, 2014 was \$13,260 and \$26,250 (three and six months ended May 31, 2013 - \$28,465 and \$60,625).

## NOTE 6 - SHORT-TERM LOANS

	As at November 30, 2013	Advances and Reclassification	Interest Accrued	Repayments	Foreign Exchange Adjustments	As at May 31, 2014
Term loan (July 2013)	\$ 1,506,560	\$ —	\$ —	\$ —	(30,880)	\$ 1,475,680
Term loan (Dec 2013)	—	135,705	2,506	—	2,640	140,851
Promissory note (i)	52,533	—	1,600	—	—	54,133
Promissory note (ii)	402,558	—	4,099	(397,400)	(9,257)	—
Promissory note (iii)	—	1,667,477	55,898	—	—	1,723,375
	\$ 1,961,651	\$ 1,803,182	\$ 64,103	\$ (397,400)	\$ (37,497)	\$ 3,394,039

## Term loan (July 2013)

On July 12, 2013, Methes Canada entered into a term loan facility agreement with a lender (the "Agreement") pursuant to which Methes Canada is able to borrow up to \$1,475,680 (historical amount of \$1,540,640 or CDN\$1,600,000) for a term of 12 months at an interest rate of 12% per annum (the "July 2013 Facility"). Under the terms of the Agreement, interest is payable monthly and outstanding principal is due at maturity. Outstanding principal would be prepayable after six months upon 30 days' notice and payment of a penalty equal to one-month's interest. The July 2013 Facility is collateralized by a security agreement from Methes Canada on certain of its assets except for accounts receivable and inventory and a first collateral mortgage on its real property located at Sombra, Ontario. The July 2013 Facility prohibits payment of debt owed by the Company to certain of its stockholders and a director (see note 5) during the life of the facility and contains other customary debt covenants. As at May 31, 2014, the Company was in compliance with these covenants.

Interest expense incurred during the three and six months ended May 31, 2014 was \$43,850 and \$87,568 (three and six months ended May 31, 2013 - \$nil and \$nil).

Term loan (December 2013)

On December 16, 2013, Methes Canada entered into a one year term Mortgage Loan Agreement for \$1,844,600 (CDN\$2,000,000) bearing interest at 9% per annum for the purposes of discharging the existing July 2013 Facility (CDN\$1,600,000). The difference will be used to upgrade the Mississauga facility for the production of biodiesel. Interest only is to be paid monthly and the term is renewable for an additional year. As at May 31, 2014, monies advanced from this loan totaled \$138,345 (historical amount of \$135,705 or CDN\$150,000).

Interest expense incurred during the three and six months ended May 31, 2014 was \$2,506 and \$2,506 (three and six months ended May 31, 2013 - \$nil and \$nil).

Promissory Notes:

- (i) In January 2010, the Company borrowed \$40,000 from a lender and issued to the lender a demand promissory note in the principal amount of \$40,000 bearing interest at 8% per annum. Repayment of the loan and payment of the accrued interest is due upon demand.

Interest expense incurred during the three and six months ended May 31, 2014 was \$800 and \$1,600 (three and six months ended May 31, 2013 - \$800 and \$1,600).

- (ii) On January 26, 2013, the Company borrowed \$368,920 (historical amount of \$397,400 or CDN \$400,000) from a lender and issued to the lender a demand promissory note in the principal amount of CDN \$400,000 bearing interest at 8% per annum (the "January 2013 Note"). Repayment of the loan and payment of the accrued interest is due upon demand.

During the six months ended May 31, 2014 total principal payments of \$397,400 (CDN\$400,000) and total interest of \$32,571 (CDN\$34,057) were made against the note (now paid in full), as follows:

- On January 17, 2014, the Company converted \$128,000 USD (CDN \$139,845) of the outstanding principal due on the January 2013 Note into 34,688 shares of Common Stock based at the closing market price of \$3.69 per share of Common Stock on January 17, 2014.

- On January 30, 2014, the Company paid \$153,871 USD (CDN \$172,000) against the outstanding principal balance through borrowing a note payable from another lender.

- On May 30, 2014, the Company paid the remaining balance of \$81,305 USD (CDN \$88,155).

Interest expense incurred during the three and six months ended May 31, 2014 was \$1,569 and \$4,099 (three and six months ended May 31, 2013 - \$7,914 and \$10,576).

- (iii) Previously, this loan was classified as a payable to related party as the lender held stocks of the Company. As at May 31, 2014, no stocks are held by the lender and therefore this loan has been re-classified under the short-term loans. A total principal of \$1,280,000 and accrued interest of \$215,477 as at November 30, 2013 were reclassified to short-term loans.

On January 28, 2014, the Company borrowed \$172,000 from this lender and issued to the lender a demand promissory note in the principal amount of \$172,000 bearing interest at 8% per annum. Repayment of the loan and payment of the accrued interest is due upon demand.

As at May 31, 2014, a total principal of \$1,452,000 and accrued interest of \$271,375 were outstanding. This loan bears interest at 8% per annum. Repayment of the loan and payment of the accrued interest is due upon demand.

Interest expense incurred during the three and six months ended May 31, 2014 was \$29,040 and \$55,898 (three and six months ended May 31, 2013 - \$20,800 and \$48,000).

NOTE 7 - CREDIT FACILITY

On August 16, 2013, Methes Canada entered into and closed on a working capital loan facility from a Toronto, Ontario lending firm (the "Working Capital Facility"). Under the Working Capital Facility, Methes Canada may borrow up to \$1,500,000 for its Sombra, Ontario biodiesel manufacturing plant, of which up to \$750,000 may be from cash advances against Methes Canada's accounts receivables through factoring of accounts receivable with full recourse and up to an additional \$750,000 in cash advances for use exclusively to purchase feedstock for the production of biodiesel. The Working Capital Facility is secured by a pledge of the accounts receivable and inventory of Methes Canada and Methes USA.

In connection with all borrowings to purchase feedstock, Methes Canada issued a promissory note to the lender bearing a per annum interest rate equal to the Bank of Montreal Prime Rate plus sixteen percent (16%) and is due and payable upon the earlier of demand or August 13, 2014. The effective interest rate as of May 31, 2014 was 19% (16% plus 3% prime rate). Under the terms of the promissory note, interest only is payable monthly on the last business day of each calendar month.

Cash advances against accounts receivables will be based on the amount of the receivables net of a purchase discount as agreed with the lender with an interest rate of Bank of Montreal Prime Rate plus three percent (3%). Effective interest rate as of May 31, 2014 was 6% (3% plus 3% prime rate). The amounts outstanding under this promissory note must be recorded on the grid schedule provided by the lender. The balance outstanding as at November 30, 2013 of \$1,019,513 was fully repaid during the first quarter of fiscal 2014 through factoring of accounts receivable and cash from operations. Accordingly, as of May 31, 2014 the balance outstanding was \$nil.

Interest expense incurred under this credit facility during the three and six months ended May 31, 2014 was \$nil and \$7,909 (three and six months ended May 31, 2013 - \$nil and \$nil).

Subsequent to the current quarter, the credit facility was discontinued (see Note 14).

## NOTE 8 - STOCKHOLDERS' EQUITY

## COMMON STOCK

The Company is authorized to issue 75,000,000 shares of Common Stock with a par value of \$0.001 and had 7,231,417 and 11,435,431 shares of Common Stock issued and outstanding as of November 30, 2013 and May 31, 2014, respectively.

	No. of Shares	Price per Share
Common Stock		
Balance as at November 30, 2013	7,231,417	
December 2013 Private Placement	1,081,161	\$ 2.00
January 3, 2014 Issuance for services rendered	25,000	\$ 3.49
January 10, 2014 Issuance for cash and services rendered	50,000	\$ 2.50
January 17, 2014 Issuance for loan settlement	34,688	\$ 3.69
January 28, 2014 Issuance for services rendered	25,000	\$ 3.55
March 13, 2014 Series A-2 Preferred Stock conversions and accrued dividends	21,648	\$ 2.27
March 17, 2014 Series A-1 Preferred Stock conversions and accrued dividends	123,528	\$ 2.25
May 1, 2014 Issuance for services rendered	25,000	\$ 2.45
May 9, 2014 Series A-2 Preferred Stock conversion and accrued dividends	10,989	\$ 2.27
May 9 and 19, 2014 Placement Agent Warrant exercises	7,000	\$ 2.00
May 27, 2014 Underwritten public offering issuance	2,500,000	\$ 2.00
May 28, 2014 Underwritten public offering over-allotment issuance	300,000	\$ 2.00
Balance as at May 31, 2014	11,435,431	

#### December 2013 Private Placement

During the month of December 2013 the Company issued a total of 1,081,161 units (each a “Unit”) to accredited investors at a price of \$2.00 per Unit under a private placement and raised net proceeds of approximately \$1.87 million, after deducting the sales commission and fees (the “December 2013 Private Placement”). Each Unit consists of one share of Common Stock and one five year Common Stock Warrant to purchase one share of Common Stock at an exercise price of \$4.00 per share (“Common Stock Warrant”). (see Stock Warrant Table below).

In connection with the December 2013 Private Placement, the Company issued compensatory warrants (the “Placement Agent Warrant”) to the Placement Agents for the offering exercisable for an aggregate of 108,116 Units. Each of these warrants is exercisable to acquire a Unit at an exercise price of \$2.00 per Unit. The fair value of these warrants at the grant date was \$257,553. This amount was estimated using the Black-Scholes option pricing model with an expected life of 5 years, risk free interest rates between 1.66% and 1.74%, a dividend yield of 0%, and an expected volatility of 75%. (see Stock Warrant Table below).

#### January 3, 2014 Issuance for services rendered

On January 3, 2014, the Company issued 25,000 shares of Common Stock in the second installment quarterly payment of consulting fees for services to be rendered by a consultant which were valued at \$87,250, based on the closing market price of \$3.49 per share on the day of issuance.

#### January 10, 2014 Issuance for cash and services rendered

On January 10, 2014, the Company sold 50,000 Units to an accredited investor in a private placement for a purchase price of \$125,000 (or \$2.50 per Unit) of which \$100,000 was paid in cash and \$25,000 was settled through services rendered to the Company, which was included in the selling, general and administrative expenses. The aggregate fair value of the Units sold in this offering was \$310,000 (or \$6.20 per Unit), based on the closing market price of \$3.58 per share of Common Stock on the day of issuance, and the fair value of the Common Stock Warrants of \$2.62 per warrant. The fair value of the Common Stock Warrants was estimated using the Black-Scholes option pricing model with an expected life of 5 years, risk free interest rates of 1.64%, a dividend yield of 0%, and an expected volatility of 100%. The excess of the estimated fair value over the purchase price in the amount of \$185,000 is included in the selling, general and administrative expenses. (see Stock Warrant Table below).

#### January 17, 2014 Issuance for loan payment

On January 17, 2014, the Company issued 34,688 shares of Common Stock to a note holder at \$3.69 per share of Common Stock in conversion of \$128,000 of a note payable by the Company (See Note 6, Promissory - (ii)).

#### January 28, 2014 Issuance for services rendered

On January 28, 2014, the Company issued 25,000 shares of Common Stock in payment of consulting fees for services to be rendered by a consulting corporation for a term of one year. These shares of Common Stock were valued at \$88,750, based on the closing market price of \$3.55 per share on the date of issuance, of which \$29,583 is included in prepaid expenses as at May 31, 2014.

#### March 13, 2014 Series A-2 Preferred Stock Conversions

On March 13, 2014, two holders of our Series A-2 Convertible Preferred Stock (“Series A-2 Preferred”) converted 20,876 shares of outstanding Series A-2 Preferred with an aggregate stated value of approximately \$49,139 (including

accrued dividends of \$1,750) into 21,648 shares of Common Stock at a price of \$2.27 per share.

March 17, 2014 Series A-1 Preferred Stock Conversions

On March 17, 2014, two holders of our Series A-1 Convertible Preferred Stock ("Series A-1 Preferred") converted 117,646 shares of outstanding Series A-1 Preferred with an aggregate stated value of approximately \$293,235 (including accrued dividends of \$13,235) into 123,528 shares of Common Stock at a price of \$2.25 per share.

May 1, 2014 Issuance for services rendered

On May 1, 2014, the Company issued 25,000 shares of Common Stock in the third quarterly installment payment of consulting fees for services to be rendered by a consultant which were valued at \$61,250, based on the closing market price of \$2.45 per share on the date of issuance, of which \$45,813 is included in prepaid expenses as at May 31, 2014.

May 9, 2014 Series A-2 Preferred Stock Conversion

On May 9, 2014, a holder of our Series A-2 Preferred converted 10,438 shares of outstanding Series A-2 Preferred with an aggregate stated value of approximately \$26,250 (including accrued dividends of \$1,250) into 10,989 shares of Common Stock at a price of \$2.27 per share.



May 9 and 19, 2014 Placement Agent Warrants Exercises

On May 9 and 19, 2014, two holders of Placement Agent Warrants exercised their warrants for an aggregate of 7,000 Units at a price of \$2.00 per Unit or an aggregate stated value of \$14,000, which included 7,000 shares of Common Stock and 7,000 Warrants (each at an exercise price of \$4.00).

May 27, 2014 Underwritten Public Offering Issuance

On May 27, 2014, the Company closed an underwritten public offering of 2,500,000 shares of Common Stock and raised net proceeds of \$4.5 million, after deducting Underwriter's fees and estimated offering expenses. Under the terms of the Underwriting Agreement, the Underwriter had an option through June 26, 2014, to purchase up to an additional 375,000 shares of Common Stock under the same terms as the public offering to cover over-allotments (the "Over-Allotment Option"), if any.

May 28, 2014 Underwritten Public Offering Over Allotment Issuance

On May 28, 2014, the Underwriter partially exercised the Over-Allotment Option for 300,000 shares of Common Stock raising approximately \$550,000 of additional net proceeds for the Company.

PREFERRED STOCK

The Company is also authorized to issue up to 10,000,000 shares of preferred stock with a par value of \$0.001 per share, from time to time in one or more series, without shareholder approval, when authorized by its board of directors (the "Board"). As of each of November 30, 2013 and May 31, 2014, the Board has designated 152,519 shares of Series A-1 Preferred and 134,341 shares of Series A-2 Preferred. As of November 30, 2013, 138,654 shares of Series A-1 Preferred and 122,128 shares of Series A-2 Preferred were issued and outstanding (for a total of 260,782 shares outstanding as of November 30, 2013). During the six months ended May 31, 2014, 117,646 shares of Series A-1 Preferred and 31,314 shares of Series A-2 Preferred were converted into shares of Common Stock. As of May 31, 2014, 21,008 shares of Series A-1 Preferred and 90,314 shares of Series A-2 Preferred were issued and outstanding (for a total of 111,822 shares outstanding as of May 31, 2014). Collectively, the Series A-1 Preferred and the Series A-2 Preferred are referred to herein as the "Series A Preferred Stock."

As at May 31, 2014, on the Series A Preferred Stock had total accumulated dividends of \$16,668, none of which have been declared by the Board or accrued (May 31, 2013 - \$nil).

STOCK WARRANT TABLE:

	Grant Date	Exercise Period	No of Warrants	Exercise Price per share	Fair Value of Broker Warrants
Balance as at November 30, 2013			2,678,872		
Common Stock Warrants issued – Private Placement	Dec. 20, 2013	5 years from grant date	1,081,161	\$ 4.00	
Placement Agent Warrant – Private Placement	Dec. 20 2013	5 years from grant date	108,116	\$ 2.00	\$ 257,553
Placement Agent Warrant – Private Placement (November	Dec. 20 2013	5 years from grant date	5,000	\$ 2.00	\$ 6,403

27, 2013)

Common Stock Warrant issued-accredited investor	Jan. 10, 2014	5 years from grant date	50,000	\$	4.00
Placement Agent Warrant exercise			(7,000)	\$	2.00
Common Stock Warrant issued upon exercise of Placement Agent Warrant	May 9 and 14, 2014	Dec. 20, 2018	7,000	\$	4.00
Balance as at May 31, 2014			3,923,149		

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## NOTE 9 - STOCK-BASED COMPENSATION

The Company's Amended and Restated the 2008 Directors, Officers and Employees Stock Option Plan, which was originally approved by the stockholders at the annual general meeting of the Company held on December 5, 2007, and subsequently amended by the stockholders on July 23, 2008. This plan was established to enable the Company to attract and retain the services of highly qualified and experienced directors, officers, employees and consultants and to give such persons an interest in the success of the Company and its subsidiaries. The total number of shares currently authorized under the plan is 391,134. The options and awards will be granted at the discretion of the Board of Directors. Options issued under the plan that are deemed to be incentive stock options will be priced at not less than 100% of the fair market value of the common shares at the date of the grant, subject to certain limitations for 10 percent stockholders. The fair value of each option granted was estimated at the time of grant using the Black-Scholes option pricing model. There were no options granted during the six months ended May 31, 2013 and 2014.

All the grants vest quarterly over a two year period and expire on the tenth anniversary of the grant date. The following table summarizes the stock option activities of the Company.

	Number of options
Outstanding as of November 30, 2012	383,310
Granted	10,000
Exercised	—
Cancelled/forfeited	(27,379)
Outstanding as of November 30, 2013	365,931
Granted	—
Exercised	—
Cancelled/forfeited	(5,215)
Outstanding as of May 31, 2014	360,716

The stock-based compensation for the three and six months ended May 31, 2014 was \$2,824 and \$7,696 (six months ended May 31, 2013 - \$28,150 and \$66,632). The Company recorded this in selling, general and administrative expenses with the corresponding credit to additional paid-in capital.

As of November 30, 2013 the Company has a total of 365,931 options outstanding to purchase Common Stock held by employees, directors and advisory board members, of which 353,922 are vested and exercisable. All of these outstanding stock options have an exercise price above the average market price. As of November 30, 2013, the total fair value of the options granted to employees at the respective grant dates was \$1,476,973, of which the unrecognized portion of \$13,088 related to the unvested shares associated with these stock option grants will be recognized over a period of two years.

As of May 31, 2014 the Company has a total of 360,716 options outstanding to purchase Common Stock held by employees, directors and advisory board members, of which 354,466 are vested and exercisable. All of these outstanding stock options have an exercise price above the average market price. As of May 31, 2014, the total fair value of the options granted to employees at the respective grant dates was \$1,476,973, of which the unrecognized portion of \$5,392 related to the unvested shares associated with these stock option grants will be recognized over a period of 18 months.

2012 Option Plan:

Under the Company’s 2012 Directors, Officers and Employees Stock Option Plan (the “2012 Plan”), the Company granted a total of 100,000 options to purchase Common Stock to its four independent directors and chief financial officer on April 2, 2013. The total number of shares currently authorized under the plan is 400,000. The options and awards will be granted at the discretion of the Board. Options issued under this plan that are deemed to be incentive stock options will be priced at not less than 100 percent of the fair market value of the shares of Common Stock underlying the options at the date of the grant, subject to certain limitations for 10 percent stockholders. The fair value of each option granted was estimated at the time of grant using the Black-Scholes option pricing model.

All the options granted under the 2012 Plan, vest yearly at the rate of one-third per year, starting on the first year anniversary of the grant date and expire on the fifth anniversary of the grant date. The following table summarizes the stock option activities of the Company.

Outstanding as of November 30, 2012	—
Granted	100,000
Exercised	—
Cancelled/forfeited	—
Outstanding as of November 30, 2013	100,000
Granted	—
Exercised	—
Cancelled/forfeited	—
Outstanding as of May 31, 2014	100,000

The share-based compensation for the three and six months ended May 31, 2014 was \$44,026 and \$88,052 (three and six months ended May 31, 2013 - \$nil and \$nil). The Company recorded this in selling, general and administrative expenses with the corresponding credit to additional paid-in capital.

As of November 30, 2013 the Company has granted options to purchase a total of 100,000 shares of Common Stock at an exercise price of \$3.94 per share, to its four independent directors and chief financial officer, all of which are currently outstanding and of which none are vested and exercisable. All of these outstanding stock options have an exercise price equal to the fair market price on the date of grant. As of November 30, 2013, the total fair value of the options granted to the independent directors and chief financial officer at the respective grant dates was \$292,174, of which the unrecognized portion of \$186,022 related to the unvested shares associated with these stock option grants will be recognized over a period of three years.

As of May 31, 2014 the Company has granted a total of 100,000 options to purchase Common Stock to employees, directors and advisory board members, all of which are currently outstanding and of which none are vested and exercisable. All of these outstanding stock options have an exercise price above the average market price. As of May 31, 2014, the total fair value of the options granted at the respective grant dates was \$292,174, of which the unrecognized portion of \$97,970 related to the unvested shares associated with these stock option grants will be recognized over a period of two years.

#### NOTE 10 - FAIR VALUE MEASUREMENTS, CONCENTRATIONS AND RISK

a) The Company's cash and cash equivalents, which are carried at fair values, are classified as a level 1 financial instrument at November 30, 2013 and May 31, 2014.

b) The Company is exposed to the following concentrations of risk:

##### Major Customers

Two major customers comprised 66% and 68% of total revenue for the three and six months ended May 31, 2014 (three and six months ended May 31, 2013 - two major customers comprised 66% and 22% of total revenue).

As at November 30, 2013, the accounts receivable balance from the two major customers was \$659,902 and \$26,083 respectively. As at May 31, 2014, the accounts receivable balance from two major customers was \$Nil and \$39,740 respectively.

##### Major Vendors

The Company has an exclusive agreement to manufacture biodiesel processor equipment with a third party equipment manufacturer. During the three and six months ended May 31, 2014, the Company made purchases of \$nil and \$nil (three and six months ended May 31, 2013 - \$nil and \$45,893) from this equipment manufacturer. As of November 30, 2013 and May 31, 2014, the Company had accounts payable of \$21,856 and \$6,837 owing to this equipment manufacturer, respectively.

The Company's major purchases of feedstock oil and biodiesel from third parties for the three and six months ended May 31, 2014 were \$nil and \$nil (three and six months ended May 31, 2013 - three major vendors comprising total purchases of \$1,051,843 and \$1,566,918).

As at November 30, 2013, the accounts payable balance to the three major vendors were \$nil, \$1,053,479 and \$575,043.

As at May 31, 2014, the accounts payable balance from the three major vendors was \$1,046,453 (balance includes interest incurred on outstanding balance of \$97,973), \$nil and \$352,670. These balances were paid in full subsequent to quarter end.

#### Economic and Political Risks

The Company faces a number of risks and challenges as a result of having primary operations and marketing in Canada and sales in the United States. Changing political climates in Canada and the United States could have a significant effect on the Company's business.

c) The Company's financial instruments are exposed to certain financial risks, including credit risk, currency risk and liquidity risk.

### Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's cash and cash equivalents and trade accounts receivable. The Company places its cash and cash equivalents with institutions of high creditworthiness. The carrying value of the financial assets represents the maximum credit exposure.

The Company minimizes credit risk by routinely reviewing the credit risk of the counterparty to the arrangement and has maintained an allowance for doubtful accounts of \$65,662 related to credit risk as at May 31, 2014 (as at November 30, 2013 - \$30,000), which is considered adequate.

### Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company's functional currency is U.S. dollars. A significant change in the currency exchange rates between the U.S. dollar relative to the Canadian dollar could have an effect on the Company's results of operations, financial position and cash flows. The Company has not entered into any derivative financial instruments to manage exposures to currency fluctuations.

Included in selling, general and administrative expenses are foreign currency gains (losses) for the three and six months ended May 31, 2014 of \$49,576 and (\$30,210) (three and six months ended May 31, 2013 of \$1,579 and \$75,959).

### Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company has a planning and budgeting process in place to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its expansionary plans. The Company ensures that there are sufficient funds to meet its short-term business requirements, taking into account its anticipated cash flows from operations and its holdings of cash.

As at May 31, 2014, due in large part to the funds spent to develop and build the Sombra facility as well as minimal sales of biodiesel, the Company had a working capital deficiency of \$1,270,469.

The Company anticipates that its Sombra facility will generate positive cash flows from operations and will operate profitably once full-scale commercial operations are achieved in the second half of fiscal year 2014. It is management's opinion that the anticipated positive cash flows from operations and cash from additional financing completed in May 2014 will be sufficient to meet the Company's cash requirements for at least the next 12 months.

As at May 31, 2014, the Company received customer deposits of \$9,104 (November 30, 2013 - \$8,185) against equipment to be shipped in the subsequent quarter.

### NOTE 11 - COMMITMENTS

#### Building Leases:

Methes Canada is a party to a lease agreement for the Mississauga facility and to a sublease agreement for a unit adjacent to its Mississauga facility. On September 28, 2012, the Company re-negotiated and renewed a combined five year lease term for both of these facilities starting from January 1, 2013 to December 31, 2017. The renewed lease

term provides for a two month rent free period in 2013.

As at May 31, 2014, Methes Canada must pay, in addition to other amounts such as it's pro rata share of taxes, the following amounts over the term of the lease:

	Annual Minimum Rent
2014	\$ 68,129
2015	\$ 136,259
2016	\$ 136,259
2017	\$ 136,259
2018	\$ 11,355



## Railroad Car Leases:

As at May 31, 2014, the Company is a party to the following lease agreements for railcars at its Sombra facility:

	Start Date	End Date	Term
Four railcars at \$3,100 per month	August 1, 2013	July 31, 2018	60 months
Four railcars at \$3,100 per month	April 1, 2013	March 31, 2018	60 months
Four railcars at \$ 3,600 per month	July 1, 2013	June 30, 2018	60 months
Four railcars at \$3,140 per month	December 1, 2011	November 30, 2016	60 months
One railcar at \$575 per month	January 1, 2012	December 31, 2016	60 months
One railcar at \$575 per month	May 1, 2012	June 30, 2015	36 months
Ten railcars at \$8,460 per month	May 1, 2013	April 30, 2018	60 months
Ten railcars at \$8,510 per month	May 1, 2013	April 30, 2018	60 months
			Annual Minimum Rent
2014			\$ 186,360
2015			\$ 369,845
2016			\$ 365,820
2017			\$ 321,815
2018			\$ 147,250

## NOTE 12 - CONTRIBUTION AGREEMENTS WITH MINISTER OF NATURAL RESOURCES OF CANADA

## Mississauga Facility:

In 2009, the Company entered into a Non-Refundable Contribution Agreement with the Minister of Natural Resources of Canada for the Mississauga facility under the ecoENERGY for Biofuels program. Under this agreement, the Company may receive up to \$4,989,643 (CDN\$5,410,000) in the years from 2009 to 2016 from the Canadian government in biodiesel production incentives when biodiesel is produced and sold. The contribution from the Canadian Government is non-refundable by the Company.

For the three and six months ended May 31, 2014, the Company claimed incentives of \$nil and \$nil (three and six months ended May 31, 2013 - \$8,559 and \$10,170). Since entering into the program to May 31, 2014, the Company has claimed total incentives of \$1,485,285 and has received a total of \$1,458,286.

Included in accounts receivable as at November 30, 2013 and May 31, 2014, is an amount receivable of \$nil and \$nil, respectively, due from the Minister of Natural Resources of Canada.

## Sombra Facility:

In 2010, the Company applied for an incentive under the ecoENERGY for Biofuels program for its Sombra facility and was approved by the Canadian government. The final Contribution Agreement with the Minister of Natural Resources of Canada for the Sombra facility under the ecoENERGY for Biofuels program was signed by the Company and the Canadian Government on December 6, 2011. Under this agreement as amended, the Company may receive up to \$13,636,390 (CDN\$14,785,200) from the years 2012 to 2017 from the Canadian government in biodiesel production incentives when biodiesel is produced and sold. The contribution from the Canadian Government is non-refundable by the Company.

For the three and six months ended May 31, 2014, the Company claimed incentives of \$25,557 and \$38,592 (three and six months ended May 31, 2013 - \$161,565 and \$168,833). Since entering into the program to May 31, 2014, the Company has claimed total incentives of \$575,467 and has received a total of \$549,910.

Included in accounts receivable as at November 30, 2013 and May 31, 2014, is an amount receivable of \$277,573 and \$25,557, respectively, due from the Minister of Natural Resources of Canada.

## NOTE 13 - SEGMENT INFORMATION

The Company reports a single operating segment, being a producer and seller of biodiesel fuel and biodiesel processing equipment.

Geographic segments:

The Company's assets and operating facilities, other than cash balances of \$16,066 at November 30, 2013 and \$822,978 at May 31, 2014, are all located in Canada. The Company services the majority of its customers in the United States. The Company derives its revenue geographically as follows:

	Three Months Ended May 31, 2013	Three Months Ended May 31, 2014	Six Months Ended May 31, 2013	Six Months Ended May 31, 2014
Revenue				
United States	\$2,071,344	\$289,778	\$2,171,133	\$570,972
Canada	257,010	149,627	367,332	246,911
	\$2,328,354	\$439,405	\$2,538,465	\$817,883

## NOTE 14 - SUBSEQUENT EVENTS

In June 2014, the Working Capital Facility of \$1,500,000, described in Note 7 was discontinued, as the Company's management believes it no longer requires this facility.

In June 2014, the Company entered into certain derivative contracts to hedge its exposure to price risk related to feedstock oil.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and related notes included elsewhere in this report. Some of the statements in this discussion and elsewhere in this report constitute forward-looking statements within the meaning of Section 21E of the Securities and Exchange Act of 1934. See "Cautionary Statement Regarding Forward-Looking Information" following the Table of Contents of this report. Because this discussion involves risk and uncertainties, our actual results may differ materially from those anticipated in these forward-looking statements.

### Overview

We are a renewable energy company that offers an array of products and services to a network of biodiesel fuel producers. We also market and sell in the U.S. and Canada biodiesel fuel produced at our small-scale production and demonstration facility in Mississauga, Ontario, Canada, and at our intermediate scale production facility in Sombra, Ontario, Canada. The first of two Denami 3000 processors, designed to produce up to 6.5 million gallons per year, or mgy, of biodiesel, was placed in substantially full time production in the fourth quarter of 2013. In October 2013 we shipped more than 18 railcars (over 485,000 gallons) of biodiesel from our Sombra facility which is significantly higher than our previous highest monthly total of 8 railcars in April 2013. During the quarter ended May 31, 2014, our largest source of revenue was from the sale biodiesel fuel.

Among other services, we sell feedstock to our network of biodiesel producers, sell their output in the U.S. and Canada, provide them with proprietary software used to operate and control their processors, remotely monitor the quality and characteristics of their output, upgrade and repair their processors, and advise them on adjusting their processes to use varying feedstock and improve their output. Through the accumulation of production data from our network, we are equipped to provide consulting services to network members and other producers for operating their facilities, maintaining optimum production and solving production problems. For our network services and the license of our operating and communications software, we receive a royalty from network members based on the gallons of biodiesel produced.

Our revenue sources include the sale of biodiesel produced at our own facility, the sale of biodiesel that we purchase from network members and other third-party producers, the sale of biodiesel equipment, the sale of feedstock to network members and other third-party biodiesel producers, Canadian government incentive payments, royalties from our network members, and revenue from other services we provide related to the production of biodiesel.

As of May 31, 2014, due in large part to our investment of capital to develop, build and commission our Sombra facility as well as minimal sales of biodiesel, we had a working capital deficiency of \$1,270,469. During the six months ended May 31, 2014, we incurred a loss of \$3,048,284 and had negative cash flow from operations of \$1,947,750. Our Sombra facility is approved by the U.S. Environmental Protection Agency ("EPA") as a Foreign Renewable Fuel Producer and as a result the biodiesel produced at this facility is eligible for export to the United States. Obtaining this approval from the EPA enables us to sell our biodiesel into the U.S., and provides our U.S. importers the ability to generate Renewable Identification Numbers ("RINs"). RINs are used in the U.S. to track compliance with Renewable Fuel Standard 2 ("RFS2") and are generated when a gallon of biodiesel is produced or imported into the U.S. We began commercial operation at the Sombra plant in November 2012.

As of May 30, 2014, subsequent to the consummation of our initial public offering ("IPO") on October 30, 2012, we have raised aggregate net proceeds of approximately \$9.5 million from the sale of our equity securities including the following (also see Note 8):

net proceeds of approximately \$1.5 million from our private placement completed in February 2013;  
net proceeds of approximately \$50,000 from our Regulation S private placement completed in August 2013;  
net proceeds of approximately \$473,000 from our private placement of Series A Preferred Stock completed in October 2013;

net proceeds of approximately \$2.24 million from our private placement completed in December 2013;  
net proceeds of approximately \$125,000 (including, \$25,000 of services rendered to us) from our private placement completed in January 2014; and

net proceeds of approximately \$5.05 million from our public offering completed in May 2014.

## Factors Influencing Our Results of Operations

The principal factors affecting our results of operations are as follows:

### Biodiesel and feedstock price fluctuations

Biodiesel is a low carbon, renewable alternative to petroleum-based diesel fuel and is primarily sold to the end user after it has been blended with petroleum-based diesel fuel. Biodiesel prices have historically been correlated to petroleum-based diesel fuel prices. Accordingly, biodiesel prices have generally been affected by the same factors that affect petroleum prices, such as worldwide economic conditions, wars and other political events, OPEC production quotas, changes in refining capacity and natural disasters. Recently enacted government requirements and incentive programs, such as RFS2 and the blenders' tax credit, which expired on December 31, 2013, have reduced this correlation, although it remains a significant factor in the market price of our product.

Our operating results also generally reflect the relationship between the price of biodiesel and the price of the feedstock used to produce biodiesel. Spot market prices for virgin vegetable oil or used vegetable oil or rendered animal fat may increase, which would adversely affect our gross margins. The price of vegetable oil, as with most other products made from crops, is affected by weather, disease, changes in government incentives, demand and other factors. A significant reduction in the supply of vegetable oil because of weather or disease, or increases in the demand for vegetable oil, could result in higher feedstock prices. The price of vegetable oil and other feedstock has fluctuated significantly in the past and may fluctuate significantly in the future.

### Government programs related to biodiesel production and use

Biodiesel has been more expensive to produce than petroleum-based diesel fuel and as a result the industry depends on Canadian and U.S. federal and, to a lesser extent, provincial and state usage requirements and tax incentives.

On July 1, 2010, RFS2 was implemented, stipulating Renewable Volume Obligations (“RVOs”) requirements for the amount of biomass-based diesel that must be utilized in the United States each year. Under RFS2, obligated parties, including petroleum refiners and fuel importers, must show compliance with these standards. The RFS2 program required the domestic use of 800 million gallons of biodiesel in 2011, one billion gallons in 2012 and 1.28 billion gallons in 2013. The 2014 RVO was set at 1.7 billion gallons under RFS2 but the EPA is considering keeping the 2014 and 2015 RVOs at 1.28 billion gallons. The delay by the EPA in establishing the 2014 RVOs has greatly affected the demand for biodiesel so far this year. According to the National Biodiesel Board (“NBB”), 57% of their biodiesel producing members were not producing as of early June 2014.

### Renewable Identification Numbers (“RINs”)

RINs are used to track compliance with RFS2 and are generated when a gallon of biodiesel is produced or imported into the U.S. In late 2011 and early 2012 the EPA announced that some U.S. producers had generated and sold invalid RINs. The loss of integrity and confidence in the RINs market affected the demand as well as the price of biodiesel. As a result, the demand for RINs from small and medium size biodiesel producers declined dramatically. As a small and medium size producer, we and our existing customers have been directly affected by this situation. A portion of the price of a gallon of biodiesel includes a dollar value attributed to RINs. If a buyer of biodiesel cannot verify the integrity of the RINs attached to the biodiesel the buyer might not want to purchase or might ask for a discount creating a situation for the producer where it is not profitable to produce biodiesel.

In February 2013, the EPA introduced a new Quality Assurance Program (“QAP”) that would allow for buyers of RINs to verify their validity. The QAP provides a clear path and system for independent third parties, approved by the EPA,

to audit and monitor, on an ongoing basis, the production of biodiesel and verify that RINs have been correctly generated. The QAP, once fully in place, will be retroactive to January 1, 2013.

#### Seasonal fluctuations

Our operating results are influenced by seasonal fluctuations in the price of biodiesel. Our sales tend to decrease during the winter season due to perceptions that biodiesel will not perform adequately in colder weather. Colder seasonal temperatures can cause the higher cloud point biodiesel we make from inedible animal fats to become cloudy and eventually gel at a higher temperature than petroleum-based diesel or lower cloud point biodiesel made from soybean, canola or inedible corn oil. Reduced demand in the winter for our higher cloud point biodiesel may result in excess supply of such higher cloud point biodiesel or lower prices for such higher cloud point biodiesel. In addition, our production facilities are located in Canada and our costs of shipping biodiesel to warmer climates generally increase in cold weather months.

#### Dependence on significant customers

A large part of our revenue is generated from a few large customers. The sales to these customers are made at spot market prices, and we have no binding purchase agreements for our biodiesel, which could affect the consistency of our revenues. Potential customers for biodiesel regularly bid for biodiesel in the spot market at prices that are quoted on a daily basis. As a matter of convenience, we prefer to deal with customers with whom we have had a past relationship, although the specific customers to whom we sell have varied over time. The loss of one or more customers who have been among our largest customers historically would not have a material adverse effect on our business because we believe that a customer or customers could be replaced by one or more new customers regularly bidding for biodiesel, and we believe this will continue to be the case. For example, in the six months ended May 31, 2014, 57% of our total revenue was from one major customer who was also our largest customer during the year ended November 30, 2013. This customer accounted for 24% of our total revenue during the same period in fiscal 2013.

#### Lengthy sales cycle

The sale of one of our Denami processors in a particular financial period would have a significant effect on our quarter-to-quarter and year-to-year results. The purchase of our Denami processors involves a significant commitment of capital by customers, with the attendant delays frequently associated with large capital expenditures. For these and other reasons, the sales cycle associated with our Denami processors is typically lengthy, varying from 6 to 18 months. The lengthy sales cycles of our equipment sales, as well as the size and timing of orders, make it difficult to forecast our future results of operations.

## Results of Operations

Three and six months ended May 31, 2013 and May 31, 2014

Set forth below is a summary of certain financial information for the periods indicated:

	Three Months Ended May 31, 2013	Three Months Ended May 31, 2014	Six Months Ended May 31, 2013	Six Months Ended May 31, 2014
Revenue				
Biodiesel sales				
Resales	\$ 415,782	\$ —	\$ 463,496	\$ 124,764
Internal production	1,664,522	316,294	1,747,244	501,067
Feedstock sales	40,802	69,719	84,988	96,341
Glycerin sales	22,635	10,649	36,441	23,847
Government incentives	170,124	25,557	179,004	38,592
Equipment sales	2,657	750	2,657	1,397
Royalties	2,793	11,454	6,775	11,454
Others	9,039	4,982	17,860	20,421
	2,328,354	439,405	2,538,465	817,883
Cost of goods sold	2,221,184	371,921	2,410,713	664,540
Gross profit	107,170	67,484	127,752	153,343
Operating expenses				
Selling, general and administrative expenses	1,476,838	1,442,291	2,767,926	2,907,700
Loss before interest and taxes	(1,369,668)	(1,374,807)	(2,640,174)	(2,754,357)
Other expenses				
Interest expense	(122,143)	(192,035)	(242,969)	(293,927)
Loss before income taxes	(1,491,811)	(1,566,842)	(2,883,143)	(3,048,284)
Income taxes	—	—	—	—
Net loss for the period	\$ (1,491,811)	\$ (1,566,842)	\$ (2,883,143)	\$ (3,048,284)



Three and six months ended May 31, 2013 compared to the three and six months ended May 31, 2014

Revenue. Our total revenues for the three months ended May 31, 2013 and May 31, 2014 were \$2.33 million and \$439,000, respectively, representing a decrease of \$1.89 million or 81%. Our total revenues for the six months ended May 31, 2013 and May 31, 2014 were \$2.54 million and \$818,000, respectively, representing a decrease of \$1.72 million or 68%. The reasons for this decrease are outlined below.

Biodiesel. Biodiesel sales for the three months ended May 31, 2013 and May 31, 2014, excluding government incentives, were \$2.08 million and \$316,000, respectively, a decrease of approximately \$1.76 million or 85%. For the three months ended May 31, 2013 and May 31, 2014, our resales of biodiesel purchased from third party producers were \$416,000 and \$125,000, respectively, a decrease of approximately \$291,000 or 70%. Revenue from our internal production, excluding government incentives, for the three months ended May 31, 2013 and May 31, 2014 was \$1.66 million and \$316,000, respectively, a decrease of \$1.34 million or 81%. For the three months ended May 31, 2013 and May 31, 2014, our average sales price per gallon for 100 percent biodiesel ("B100") was \$4.11 and \$4.08, respectively, a decrease of \$0.03 per gallon, or 0.73%. Gallons sold for the three months ended May 31, 2013 and 2014 were 506,000 and 77,600 gallons, respectively, a decrease of 428,400 gallons, or 85%.

Biodiesel sales for the six months ended May 31, 2013 and May 31, 2014, excluding government incentives, were \$2.21 million and \$625,800, respectively, a decrease of approximately \$1.6 million or 72%. For the six months ended May 31, 2013 and May 31, 2014, our resales of biodiesel purchased from third party producers were \$463,000 and \$125,000, respectively, a decrease of approximately \$338,000, or 73%. Revenue from our internal production, excluding government incentives, for the six months ended May 31, 2013 and May 31, 2014 was \$1.75 million and \$501,000, respectively, a decrease of \$1.2 million, or 71%. For the six months ended May 31, 2013 and May 31, 2014, our average sales price per gallon for B100 was \$4.13 and \$4.52, respectively, an increase of \$0.39 per gallon, or 9%. Gallons sold for the six months ended May 31, 2013 and 2014 were 535,447 and 138,529 gallons, respectively, a decrease of 396,918 gallons, or 74%.

The overall decrease in revenue from the sales of our biodiesel and the resales of biodiesel purchased from others was primarily due to a very low demand as a result of the expiration of the blender's tax credit ("BTC") on December 31, 2013 which, combined with an extremely cold winter, reduced the demand for biodiesel in the first half of 2014. Furthermore, the delay, by the EPA, in establishing the 2014 RVOs has greatly affected the demand for biodiesel so far this year. According to the National Biodiesel Board ("NBB"), 57% of their biodiesel producing members were not producing as of early June 2014.

Feedstock. For the three months ended May 31, 2013 and May 31, 2014, feedstock sales were \$41,000 and \$70,000, respectively, an increase of \$29,000, or 71%. For the six months ended May 31, 2013 and May 31, 2014, feedstock sales were \$85,000 and \$96,300, respectively, an increase of \$11,350, or 13%. In the more recent period, with some variations in quantities, we were able to source additional feedstock as well as other products related to the production of biodiesel on the spot market that we resold immediately to our customers in Canada at a profit. We intend to continue with this strategy as opportunities arise to generate additional profit.

Glycerin. For the three months ended May 31, 2013 and May 31, 2014, Glycerin sales were \$22,600 and \$10,600, respectively, a decrease of \$12,000. For the six months ended May 31, 2013 and May 31, 2014, Glycerin sales were \$36,000 and \$24,000, respectively, a decrease of \$12,000.

Government incentives. For the three months ended May 31, 2013 and May 31, 2014 we received \$170,000 and \$25,000, respectively, a decrease of \$145,000, or 85%. For the six months ended May 31, 2013 and May 31, 2014 we received \$179,000 and \$39,000, respectively, a decrease of \$140,000, or 78%. This decrease was due to the decrease in the sales volume of biodiesel.

Equipment sales. For the three months ended May 31, 2013 and May 31, 2014 we generated \$2,600 and \$750, respectively, from equipment sales. For six months ended May 31 2013 and May 31, 2014 we generated \$2,700 and \$1,400, respectively, from equipment sales. Effective January 30, 2014, we entered into a sale and licensing agreement with an Aruba company pursuant to which they agreed to the purchase of a Denami 600 processor and license our software and monitoring system. We believe that the Denami 600 will be used for the local production of biodiesel in Aruba and is expected to be built and delivered to Aruba by about November 2014.

Royalties. For the three months ended May 31, 2013 and May 31, 2014 we received royalties of \$2,800 and \$11,000, respectively. For six months ended May 31, 2013 and May 31, 2014 we received royalties of \$6,700 and \$11,000, respectively. Our customers own the Denami 600 processors, but license the software and monitoring system from us in exchange for an ongoing royalty payment \$0.11 per gallon of biodiesel produced by their Denami 600 processors.

Other. Other revenue for the six months ended May 31, 2013 and May 31, 2014 was \$9,000 and \$5,000, respectively, a decrease of \$4,000, or 44%. Other revenue for the six months ended May 31, 2013 and May 31, 2014, was \$18,000 and \$20,000, respectively, an increase of \$2,000, or 11%, primarily due to recovery of accounts receivable previously written-off. Other revenue includes recovery of prior year sales and other miscellaneous sales.

Cost of goods sold. Our cost of goods sold for the three months ended May 31, 2013 and May 31, 2014 were \$2.22 million and \$372,000, respectively, a decrease of \$1.8 million, or 83%. Our cost of goods sold for the six months ended May 31, 2013 and May 31, 2014 were \$2.41 million and \$665,000, respectively, a decrease of \$1.7 million, or 71%. This decrease was primarily due to minimum sales of biodiesel in the six months ended May 31, 2014 as a result of very low demand.

Biodiesel cost of goods sold decreased by \$1.7 million to \$285,000, or 86%, for the three months ended May 31, 2014 compared to cost of goods sold of \$1.98 million for the three months ended May 31, 2013. If the average feedstock price and the price paid for biodiesel purchased from other biodiesel producers in Canada remained constant for the three months ended May 31, 2014 compared to the same fiscal period in 2013, the decrease in gallons of biodiesel sold would have resulted in \$1.68 million decrease in the related biodiesel cost of goods sold. For the three months ended May 31, 2014, the decrease in cost of goods sold was lower because of a \$19,000 decrease in average feedstock prices.

Biodiesel cost of goods sold decreased by \$1.53 million to \$515,000, or 75%, for the six months ended May 31, 2014 compared to cost of goods sold of \$2.05 million for the six months ended May 31, 2013. If the average feedstock price and the price paid for biodiesel purchased from other biodiesel producers in Canada remained constant for the six months ended May 31, 2014 compared to the same fiscal period in 2013, the decrease in gallons of biodiesel sold would have resulted in \$1.52 million decrease in the related biodiesel cost of goods sold. For the six months ended May 31, 2014, the decrease in cost of goods sold was lower because of a \$22,000 decrease in average feedstock prices, which was offset by an \$8,600 increase in the price paid for biodiesel purchased from others.

All other costs of goods sold, excluding biodiesel cost of goods sold, for the three months ended May 31, 2013 and May 31, 2014 were \$241,000 and \$87,000, respectively, and for the six months ended May 31, 2013 and May 31, 2014 were \$363,000 and \$149,000, respectively. The decrease was mainly due to lower sales of feedstock as a result of lower feedstock demand.

Selling, general and administrative expenses. Our selling, general and administrative expenses for the three months ended May 31, 2013 and May 31, 2014, were \$1.48 million and \$1.44 million, respectively, a decrease of \$40,000, or 2%. This decrease was mainly related to a decrease in salaries and wages of \$171,000 as a result of layoffs which was offset by an increase in professional fees of \$150,000 as a result of an increase in consulting services and audit fees.

Our selling, general and administrative expenses for the six months ended May 31, 2013 and May 31, 2014, were \$2.77 million and \$2.9 million, respectively, an increase of \$130,000, or 5%. This increase was mainly related to an increase in professional fees of \$490,000 as a result of an increase in consulting services and audit fees which was offset by a decrease in operating expenses including, but not limited to, a decrease in salaries and wages of \$172,000, decrease in utilities of \$94,000, a decrease in shop supplies of \$62,000 and a decrease in travel expenses of \$40,000.

Other expenses and income. For the three months ended May 31, 2013 and May 31, 2014, we incurred interest expenses of \$122,000 and \$192,000, respectively. These amounts relate to accruals for interest expense associated with our outstanding loans. The increase in interest expense in the second quarter of 2014 was mainly due to the interest of \$97,000 on feedstock oil payable to a vendor which was offset by a decrease in interest rate on our term loan from 23% in 2013 to 12% in the same period in 2014. For the three months ended May 31, 2013 and May 31, 2014, we paid term loan interest of \$84,900 and \$43,900, respectively.

For the six months ended May 31, 2013 and May 31, 2014, we incurred interest expenses of \$243,000 and \$294,000, respectively. These amounts relate to accruals for interest expense associated with our outstanding loans. The increase in interest expense in the second quarter of 2014 was mainly due to the interest of \$97,000 on feedstock oil payable to a vendor which was offset by a decrease in the interest rate on our term loan from 23% in fiscal 2013 to 12% in fiscal 2014. For the six months ended May 31, 2013 and May 31, 2014, we paid term loan interest of \$169,000 and \$88,000, respectively.

Income taxes. No income tax expense or benefit was recorded during the three and six months ended May 31, 2013 and May 31, 2014 due to ongoing taxable losses. As of May 31, 2014, we were not subject to any uncertain tax exposures.

Net loss. For the three months ended May 31, 2014, our net loss increased by \$75,000 to \$1.56 million from \$1.49 million for the three months ended May 31, 2013. The increase in net loss for the three months ended May 31, 2014 was primarily due to the decrease of \$40,000 of gross profit and an increase of \$70,000 of interest expense, which was offset by a decrease of \$34,000 in selling, general and administrative expenses. For the six months ended May 31, 2014, our net loss increased by approximately \$165,000 to \$3.05 million from \$2.88 million for the six months ended May 31, 2013. The increase in net loss for the six months ended May 31, 2014 was primarily due to the \$140,000 increase in selling, general and administrative expenses and \$50,000 increase in interest expense offset by a \$26,000 increase in gross profit.

## Liquidity and Capital Resources

Sources of liquidity. Since inception, a significant portion of our operations was financed through the sale of our capital stock. At November 30, 2013 and May 31, 2014, we had cash and cash equivalents of \$174,084 and \$4.048 million respectively.

As of May 30, 2014, subsequent to the consummation of our IPO on October 30, 2012, we have raised aggregate net proceeds of approximately \$9.5 million from the sale of our equity securities including the following (also, see Note 8 of the unaudited condensed consolidated financial statements elsewhere in this report):

- net proceeds of approximately \$1.5 million from our private placement completed in February 2013;
- net proceeds of approximately \$50,000 from our Regulation S private placement completed in August 2013;
- net proceeds of approximately \$473,000 from our private placement of Series A Preferred Stock completed in October 2013;
- net proceeds of approximately \$2.24 million from our private placement completed in December 2013;
- net proceeds of approximately \$125,000 (including, \$25,000 of services rendered to us) from our private placement completed in January 2014; and
- net proceeds of approximately \$5.05 million from our public offering completed in May 2014.

On December 16, 2013, Methes Canada entered into a one year term Mortgage Loan Agreement for \$1,806,000 (\$2,000,000 CDN) bearing interest at 9% per annum (the "December 2013 Loan") for the purposes of discharging the July 2013 Facility (\$1,600,000 (CDN)), described in Note 6 of the unaudited condensed consolidated financial statements elsewhere in this report. The difference will be used to upgrade the Mississauga facility for the production of biodiesel.

On August 16, 2013, Methes Canada entered into and closed on a working capital loan facility from a Toronto, Ontario lending firm (the "Working Capital Facility"). Under the Working Capital Facility, Methes Canada may borrow up to \$1,500,000 for its Sombra, Ontario biodiesel manufacturing plant, of which up to \$750,000 may be from cash advances against Methes Canada's accounts receivables through factoring of accounts receivable with full recourse and up to an additional \$750,000 in cash advances for use exclusively to purchase feedstock for the production of biodiesel. The Working Capital Facility is secured by a pledge of the accounts receivable and inventory of Methes Canada and Methes USA. The balance outstanding as of November 30, 2013 of \$1,019,513 was fully repaid during the first quarter of fiscal 2014 through factoring of accounts receivable and cash from operations. Accordingly, as of May 31, 2014 the balance outstanding was \$nil.

Cash flow. The following table presents information regarding our cash flows and cash and cash equivalents for the six months ended May 31, 2013 and May 31, 2014:

	(Amounts rounded to nearest thousands)	
	Six Months Ended	
	May 31, 2013	May 31, 2014
Net cash flows used in operating activities	\$ (2,137)	\$ (1,948)
Net cash flows used in investing activities	(352)	(90)
Net cash flows provided by financing activities	2,275	5,912
Net change in cash and cash equivalents	(214)	3,874
Cash and cash equivalents, end of period	\$ 188	\$ 4,048

Operating activities. Net cash used in operating activities was \$2.137 million for the six months ended May 31, 2013. For the six months ended May 31, 2013, the net loss was \$2.88 million, which includes total non-cash items for depreciation, amortization, stock compensation expense and unrealized foreign exchange gain of \$338,000. The net cash used in operating activities included a net working capital decrease of \$408,000. Working capital decreases were a result of an increase in accounts payable and accrued liabilities of \$440,000, a decrease in inventories of \$97,000 offset by an increase in accounts receivable of \$113,000 and an increase in prepaid expenses and deposits of \$16,000. The net result was cash used in operations of \$2.14 million.

Net cash used in operating activities was \$1.948 million for the six months ended May 31, 2014. For the six months ended May 31, 2014, the net loss was \$3.05 million, which includes total non-cash items for depreciation, amortization, stock compensation expense, unrealized foreign exchange gain, deferred financing fees amortization, accrued interest and issuance of common stock for services of \$818,000. The net cash used in operating activities included a net working capital increase of \$282,000. Working capital increases were a result of a decrease in customer deposits of \$900, a decrease in inventories of \$551,000, a decrease in accounts receivable of \$983,000 offset by a decrease in accounts payable and accrued liabilities of \$1.013 million, and an increase of prepaid expenses and deposits of \$240,000. The net result was cash used in operations of \$1.948 million. Our current operating cash requirement is approximately \$314,000 per month. However, once our Sombra facility commences full-scale production, we expect to generate positive cash flow from operations.

Investing activities. Net cash used in investing activities for the six months ended May 31, 2013 was \$352,000, consisting of additions to property, plant and equipment, mainly representing costs related to our Sombra facility. Net cash used in investing activities for the six months ended May 31, 2014 was \$90,000, consisting of additions to property, plant and equipment, mainly representing costs related to our Sombra facility.

Financing activities. Net cash provided from financing activities for the six months ended May 31, 2013 was \$2.27 million, which mainly included cash proceeds received from private placements of our equity securities of \$1.37 million, financing from related parties of \$519,000 and short-term loan of \$386,000. Net cash provided by financing activities for the six months ended May 31, 2014 was \$5.91 million, which mainly included cash proceeds from the private and public offering of our equity securities of \$6.8 million offset by payment of financing from credit facility of \$1.02 million.

As of May 31, 2014, due in large part to the funds spent to develop, build and commission our Sombra facility as well as minimal sales of biodiesel, we had a working capital deficiency of \$1,270,469.

During the six months ended May 31, 2014, we took steps to improve our cash and working capital positions by: (i) obtaining the December 2013 Loan; (ii) raising net cash proceeds of approximately \$1.97 million from the private placements of our equity securities; and (iii) converting \$128,000 USD (CDN \$139,845) of the outstanding principal due on the January 2013 Note, described in Note 6 of the unaudited consolidated financial statements elsewhere in this report, into 34,688 shares of Common Stock based on the closing market price of \$3.69 per share of Common Stock on January 17, 2014.

We anticipate that our Sombra facility will generate positive cash flow from operations and will operate profitably once sufficient level of commercial operation is achieved in the second half of the current fiscal year. It is management's opinion that our cash and cash equivalents and the anticipated positive cash flow from operations will be sufficient to meet our cash requirements for at least the next 12 months.

Capital Expenditures. We have expended \$8.48 million to purchase our Sombra facility, retrofit that facility and equip it so it can begin full scale production of biodiesel. These funds were expended as follows: \$2.03 million for the original purchase price of the facility; \$1.56 million for the costs of retrofitting and \$4.89 million for Denami 3000 processors, storage tanks and other production equipment. The funds used to purchase and complete the Sombra facility were provided by the cash proceeds from sale of our equity securities, monies borrowed from a stockholder and a term loan.

Future commitments. We otherwise have no material commitments for future capital expenditures.

#### Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements.

#### Recent Accounting Pronouncements

For a discussion of new accounting pronouncements affecting the Company, refer to “Note 2 - Summary of Significant Accounting Policies” to our unaudited condensed consolidated financial statements included elsewhere in this report.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a smaller reporting company we are not required to provide the information required by this Item.

### ITEM 4. CONTROLS AND PROCEDURES

#### (a) Evaluation of Disclosure Controls and Procedures

Our management, with the participation of both of our chief executive officer and chief financial officer, carried out an evaluation of the effectiveness of our “disclosure controls and procedures” (as defined in the Securities Exchange Act of 1934 (the “Exchange Act”) Rules 13a-15(e) and 15-d-15(e)) as of the end of the period covered by this report (the “Evaluation Date”). Based upon that evaluation, our chief executive officer and chief financial officer each concluded that as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported, within the time periods specified in the U.S. Securities and Exchange Commission’s (SEC) rules and forms and (ii) is accumulated and communicated to our management, including our chief executive officer and our chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

#### (b) Changes in Internal Control over Financial Reporting

There were no changes in our internal controls over financial reporting that occurred during the quarter covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## PART II. OTHER INFORMATION

## ITEM 5. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Recent Sales of Unregistered Securities

Unless otherwise stated, the sales of the securities described below were deemed to be exempt from registration under the Securities Act in reliance upon Section 4(a)(2) and 4(a)(5) of the Securities Act (or Regulation D or Regulation S promulgated thereunder), or Rule 701 promulgated under Section 3(b) of the Securities Act as transactions by an issuer not involving any public offering or pursuant to benefit plans and contracts relating to compensation as provided under Rule 701. The purchasers of the securities in each of these transactions represented their intentions to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof, and, other than with respect to the non-transferable options, appropriate legends were placed on the securities issued in these transactions. All purchasers had adequate access, through their relationships with us, to information about our company. The sales of these securities were made without any general solicitation or advertising.

## Private Placements

On May 1, 2014, we issued 25,000 shares of Common Stock in the third quarterly installment payment of consulting fees for services to be rendered by a consultant, which were valued at \$61,250, based on the closing market price of \$2.45 per share on the date of issuance, of which \$45,813 is included in prepaid expenses as at May 31, 2014.

## ITEM 6. EXHIBITS

## Exhibit

Number	Description
<u>31.1</u>	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
<u>31.2</u>	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
<u>32.1</u>	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
<u>32.2</u>	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
101.INS	XBRL Instance Document**
101.SCH	XBRL Taxonomy Extension Schema Document**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document**

\* Filed herewith.

\*\* Furnished with this report. In accordance with Rule 406T of Regulation S-T, the information in these exhibits shall not be deemed to be "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to liability under that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act of 1933, as amended, except as expressly set forth by specific reference in such filing.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Methes Energies International Ltd.

Dated: July 14, 2014

/s/ Michel G. Laporte  
Michel G. Laporte, Chief Executive  
Officer  
(Principal Executive Officer)

Dated: July 14, 2014

/s/ Edward A. Stoltenberg  
Edward A. Stoltenberg, Chief  
Financial Officer  
(Principal Financial Officer)