

*News Release*

## **QuestAir Technologies announces 2005 Results and 2006 Milestones**

**For Immediate Release**

**8 December, 2005**

BURNABY, B.C. - QuestAir Technologies Inc. (“QuestAir” or “the Company”; AIM: QAR; TSX: QAR) reported today its financial and operational results for the fiscal year ended September 30, 2005 (“fiscal 2005”). All amounts are in Canadian dollars unless otherwise noted.

### **2005 Highlights**

- Significant progress in the program with ExxonMobil Research and Engineering Company (“EMRE”) to develop a large capacity hydrogen pressure swing adsorption (“PSA”) system for refinery and petrochemical applications. The program successfully passed an internal ExxonMobil review, authorizing initial funding from EMRE to support the construction of a prototype PSA to be demonstrated at an ExxonMobil refinery in 2006.
- Revenue growth of 110% to \$6.3 million (2004: \$3.0 million), in line with the Company’s revenue target of \$6 million for the fiscal year. QuestAir’s sales order backlog at year end was \$3.0 million, compared to \$3.9 million at September 30, 2004.
- Cash used in operations and capital requirements of \$8.7 million (2004: \$5.7 million), slightly higher than the cash burn target of under \$8.5 million for the fiscal year.
- Net loss of \$9.5 million (\$0.31 per share), unchanged from \$9.5 million (\$1.94 per share) for fiscal 2004.
- Expansion of the distribution channels for QuestAir’s first generation PSA products, including the signing of non-exclusive distribution agreements with Mitsubishi Kakoki Kaisha and Technip KTI S.p.A., and a supply agreement with HyRadix Inc.
- The installation of a hydrogen purification system at a Chevron hydrogen fueling demonstration project in Chino California, as well as the receipt of orders for the Chevron hydrogen station in Oakland California, and a station to be constructed by the Gas Technology Institute in Texas.
- The completion of an initial public offering (“IPO”) on the AIM Market of the London Stock Exchange Plc and the Toronto Stock Exchange, raising net proceeds of approximately \$11.7 million.

Jonathan Wilkinson, President and CEO of QuestAir, said:

“We have made good progress in our first year as a public company. Our revenue more than doubled, year over year, and we were successful in adding value on both the development and commercial sides of our business.

“Our key development program with ExxonMobil passed a critical program review, and remains on track for the planned prototype demonstration at an ExxonMobil refinery in 2006. In the commercial area, our key accomplishments included the distribution agreements signed with MKK and Technip KTI, the agreement to supply H-3200 hydrogen PSA’s to HyRadix, and our continued leadership in the supply of hydrogen purification systems to hydrogen fueling demonstration projects around the world.

“Based on the progress we made in fiscal 2005, we remain confident in our ability to achieve significant growth over the next several years.”

### **Operating Review & 2005 Milestone Update**

QuestAir made significant progress during the year with the program being undertaken with EMRE to develop a large-capacity hydrogen PSA for refinery and petrochemical applications. In September 2005 the program passed an internal ExxonMobil review, authorizing initial funding from EMRE to support QuestAir’s construction of a prototype hydrogen PSA to be demonstrated at an ExxonMobil refinery. As previously announced, the Company expects to receive a series of purchase orders for the prototype plant through the first half of fiscal 2006, rather than a single purchase order that was expected during fiscal 2005. The overall program timing remains on track, and it is expected that the prototype plant will be installed and operational in the second half of calendar 2006.

Strong financial support was received from EMRE through the year, including a \$2.2 million order for test systems to support the development program, and a \$1.3 million engineering service order covering the design of the prototype plant and subsequent commercial systems.

During the year, QuestAir also received a \$0.1 million contract from EMRE to undertake an initial phase of work on the application of the large-capacity PSA product for the processing of contaminated natural gas. This contract is significant in demonstrating the potential application of the large capacity PSA platform to other high-value markets.

Progress was also made with the sale of QuestAir’s first generation gas purification products. During the year, QuestAir signed distribution agreements with Technip KTI S.p.A. and Mitsubishi Kakoki Kaisha (“MKK”), leading suppliers of industrial hydrogen plants. These distribution agreements strengthen QuestAir’s market presence in Japan, Asia and Europe. QuestAir also signed a supply agreement and received an initial US\$263,000 order from HyRadix Inc., a leading developer of hydrogen generators for industrial and hydrogen fueling markets.

In the landfill gas processing market, several project proposals are in active negotiation, and QuestAir is working with the City of Vancouver on a demonstration of a methane purification system at the Vancouver Landfill. This demonstration is expected to be operational in the first half of fiscal 2006, and should provide a valuable reference site to assist in QuestAir’s marketing efforts in the biogas market.

In the emerging hydrogen infrastructure market, QuestAir received orders for three H-3200 hydrogen PSA's to be included in the AC Transit hydrogen fueling station in Oakland, California (two systems) and a hydrogen station to be constructed in Texas by GTI (one system). A H-3200 hydrogen PSA was also included in the Chino hydrogen fueling demonstration station unveiled by Chevron in California in March 2005.

The Company also signed a memorandum of understanding ("MOU") with FuelCell Energy Inc. to evaluate the use of QuestAir's hydrogen purification technology to produce a hydrogen by-product from FuelCell Energy's Direct FuelCell® power plants. As part of this agreement, the parties are working to secure a funded demonstration of this 'hydrogen export' technology.

In summary, progress made towards the achievement of QuestAir's 2005 milestones was as follows:

<b>Milestone</b>	<b>Progress</b>
1. Receive a purchase order for a prototype large capacity hydrogen PSA.	Initial funding from EMRE was approved in September 2005 to support QuestAir's construction of a prototype, and multiple purchase orders are expected in first half of fiscal 2006. A single purchase order was not received during fiscal 2005 due to a revision in the project approval procedures.
2. Increase revenue by at least 100% over 2004 levels.	Revenue of \$6.3 million represented growth of 110% over fiscal 2004 revenue, and exceeded our revenue target of \$6 million for the year.
3. Manage average cash used in operating activities and CAPEX to under \$8.5 million.	Cash burn was slightly (\$0.2 million or 2%) higher than expected due to a delay in the receipt of a \$0.7 million progress payment from EMRE. This payment was received shortly after year end.
4. Sign an additional distribution agreement with a leading hydrogen plant vendor	Distribution agreements were signed with MKK and KTI Technip, exceeding our expectations.
5. Receive the first purchase order for a methane purification system for landfill gas processing.	Several project proposals remain under negotiation, and a demonstration at the Vancouver landfill is expected to be operational in the first half of fiscal 2006. However a formal purchase order was not received during fiscal 2005.
6. Enter into an agreement to demonstrate hydrogen recovery from molten carbonate fuel cell systems.	QuestAir signed a MOU with FuelCell Energy in March 2005 to evaluate the use of QuestAir's technology in FuelCell Energy's fuel cell power plants. As part of this agreement, the parties are working to identify demonstration projects.

### **2006 Outlook and Milestones**

Looking forward, 2006 represents a pivotal year in the development and commercialization of QuestAir's large capacity PSA product for the refinery market. Key highlights expected for the year include the fabrication and shipment of the prototype plant to an ExxonMobil refinery, and the signing of an agreement to extend the large

capacity PSA platform into a new market. A key milestone in the commercial area is the signing of an additional distribution agreement with a leading hydrogen plant vendor, which has the potential to drive additional revenue growth over the coming years.

“We believe that macroeconomic drivers in the oil refining industry create compelling opportunities for our large capacity PSA product currently under development. Our relationship with ExxonMobil remains strong, and we remain very optimistic regarding the growth prospects for the company,” said Wilkinson.

QuestAir’s operational milestones for the remainder of fiscal 2006 are:

**1. Pass final ExxonMobil program review and receive purchase orders for prototype large capacity hydrogen PSA.**

The development program will undergo a final ExxonMobil program review in early calendar 2006, triggering the final purchase orders from EMRE for the prototype plant to be demonstrated at an ExxonMobil refinery.

**2. Complete fabrication and shipment of the large capacity hydrogen PSA to ExxonMobil refinery.**

The Company expects to complete the fabrication of the prototype plant during the fiscal year. Shipment of the plant to an ExxonMobil refinery is also expected prior to the end of the fiscal year.

**3. Sign agreement with EMRE for marketing of large capacity hydrogen PSA in the oil refining industry.**

The Company expects to sign an agreement with EMRE covering the joint marketing of the large capacity hydrogen PSA to non-Exxon refineries. Active marketing of the product to select refinery customers is expected to begin once this agreement is signed.

**4. Sign agreement to extend large capacity PSA product platform into new market.**

QuestAir intends to leverage the large capacity PSA product platform by developing extensions of the product into additional markets such as natural gas processing, other applications in the petrochemical industry, or the production of high purity hydrogen from natural gas.

**5. Sign an additional distribution agreement for QuestAir's first generation gas purification products with a leading hydrogen plant vendor.**

Distribution relationships are a key component of QuestAir’s strategy to accelerate the penetration of its commercial PSA systems in specific market segments and

geographies. The Company intends to secure another distribution partnership during the coming year.

In addition to the operational milestones for fiscal 2006, the company has set the following key financial targets for the coming fiscal year:

**Revenues:** Total revenue for the year ended September 30, 2006 is expected to be at least \$7.5 million. Purchase orders for the prototype large capacity PSA to be demonstrated at an ExxonMobil refinery in 2006 are currently under negotiation, and it is expected that the last of these orders will be received in the first quarter of calendar 2006. Given current uncertainty related to certain contract terms which may influence revenue recognition, significant revenue from these prototype purchase orders has not been included in the revenue target for fiscal 2006, and it is assumed that the majority of this revenue will be recognized early in fiscal 2007.

**Cash Burn:** Cash used in operations and capital expenditures is expected to be in the range of \$8.5 to \$9.5 million. It is expected that the level of R&D activities on the EMRE refinery program will continue through fiscal 2006 as the Company completes the development program and prepares for the commercial launch of the large capacity hydrogen PSA.

### **2005 Financial Results**

Revenues increased by 110% to \$6.3 million in fiscal 2005 (2004: \$3.0 million). In addition, gross margin increased to 44% in fiscal 2005 (2004: 30%). The improvement in top line performance was partially offset by an increase in research and development expenditures, which increased from \$4.7 million in fiscal 2004 to \$5.7 million in fiscal 2005, and an increase in general and administrative expenditures, which increased from \$2.5 million in fiscal 2004 to \$3.4 million in fiscal 2005. Consequently, the net loss for fiscal 2005 was \$9.5 million (\$0.31 per share), unchanged from \$9.5 million (\$1.94 per share) for fiscal 2004.

### **Operating Results**

The following table provides a breakdown of the Company's revenues from the sale of gas purification systems and engineering service contracts for the reported periods:

(Unaudited, \$ '000)	September 30, 2005	Years ended September 30, 2004
Gas purification systems	4,158	1,226
Engineering service contracts	2,134	1,776
Total revenue	6,292	3,002

The increase in revenue from gas purification systems for fiscal 2005 resulted from increased revenues from commercial PSA systems, and the delivery of two test systems, with a total value of \$2.2 million, to EMRE in support of the program to develop a large capacity hydrogen PSA for use in oil refineries. Engineering service contract revenue also increased for fiscal 2005 as a result of increased work completed on engineering service

contracts with EMRE, which are recognized on a percentage completion basis. The total recognized revenue of \$6.3 million for fiscal 2005 exceeded the revenue target of \$6.0 million provided by management on January 25, 2005.

QuestAir's sales order backlog is defined as future revenue from signed gas purification system sales and engineering service contracts that have not yet been recognized by the Company. The following table provides an analysis of the changes in the Company's sales order backlog for fiscal 2005 and fiscal 2004:

(Unaudited, \$ '000)	For the year ended September 30, 2005			For the year ended September 30, 2004		
	Gas Purification Systems	Eng. Service Contracts	Total	Gas Purification Systems	Eng. Service Contracts	Total
Opening Balance	2,812	1,106	3,918	860	35	895
Bookings	3,897	1,951	5,848	3,165	2,820	5,985
Revenue Recognized	(4,158)	(2,134)	(6,292)	(1,226)	(1,776)	(3,002)
Adjustments <sup>1</sup>	(311)	(155)	(466)	13	27	40
Ending Balance	2,240	768	3,008	2,812	1,106	3,918

It should be noted that fluctuations in recognized revenue and the receipt of new sales orders are to be expected in the industrial markets that the Company currently serves. In addition the timing of receipt of new engineering service contracts can vary from period to period.

The total sales order backlog decreased by \$0.9 million, or 23%, during fiscal 2005, compared to an increase in backlog of \$3.0 million for fiscal 2004. The reduction in backlog during fiscal 2005 resulted from an increase in recognized revenues during the year, combined with a 31% reduction in new bookings of engineering service contracts compared to fiscal 2004. Engineering service contract bookings were higher in fiscal 2004 due to the booking of a US\$1.0 million contract from EMRE for the first phase of development of an on-board hydrogen purifier. No comparable contract was booked in fiscal 2005.

Negative adjustments to the Company's sales order backlog also increased in fiscal 2005 to \$0.5 million. These adjustments reflected the negative impact of the appreciation of the Canadian dollar relative to the US dollar, and the adjustment or cancellation of previously booked customer orders with a total value of \$0.3 million.

The Company expects that the backlog as of September 30, 2005 will be substantially recognized as revenue by the third quarter of fiscal 2006.

<sup>1</sup> Adjustments to backlog include adjustments for fluctuations in foreign currency exchange rates, adjustments made to contract values after signing, and cancelled orders.

The following table provides a calculation of the Company's gross profit for the reported periods:

(Unaudited, \$ '000)	Years ended	
	September 30, 2005	September 30, 2004
Sales	6,292	3,002
Cost of goods sold	3,537	2,097
Gross Profit	2,755	905
Gross Margin (%)	43.8%	30.0%

The increase in percentage gross margin for fiscal 2005 compared to the prior year was largely due to higher margins realized on revenue from engineering service contracts recognized during the year. It is expected that margins will fluctuate from year to year depending on the mix of revenues recognized from engineering service contracts and gas purification systems.

A total warranty expense of \$0.4 million was included in the cost of goods sold for fiscal 2005, compared to \$nil for the prior year. \$0.3 million of this warranty expense remains as a provision against future warranty claims.

Sales and marketing expenses were \$1.8 million for fiscal 2005, an increase of 6% compared to \$1.7 million for the prior period. The slight increase in sales and marketing expenses for the year was attributed to increased salary expenses resulting from the addition of personnel to the commercial sales group.

The gross research and development ("R&D") expenditures, offsetting government funding and the resulting net R&D expenditures for the relevant periods, were as follows:

(Unaudited, \$ '000)	Years ended	
	September 30, 2005	September 30, 2004
Gross R&D Expenditure	7,667	6,252
Government Funding	1,933	1,554
Net R&D Expenditure	5,734	4,698

The 22% increase in net R&D spending for fiscal 2005 compared to the prior period was due to increased gross R&D expenditures related to the program undertaken with EMRE to develop a large capacity PSA for use in oil refineries. Government funding increased by \$0.4 million, or 24%, roughly in line with the percentage increase in gross R&D spending, reflecting the fact that the Company's principal government funding from Technology Partnerships Canada is calculated as a fixed percentage of gross R&D expenditures for certain development programs.

It is expected that the level of R&D activities on the EMRE refinery program will continue through fiscal 2006 as the Company completes the design and construction of the prototype hydrogen PSA to be demonstrated at an ExxonMobil refinery beginning in the second half of calendar 2006.

General and administrative (“G&A”) expenses were \$3.4 million for fiscal 2005, an increase of 36% compared to \$2.5 million for the prior year. The increase in G&A expenses was attributed to incremental costs associated with the public listing of the Company’s common shares, including regulatory filing fees, insurance costs and investor relations expenses.

Employee stock-based compensation expense was \$0.8 million for fiscal 2005, compared to \$0.3 million for the prior period. The increase was a result of a one-time stock option grant and the repricing of certain options at the time of QuestAir’s IPO.

Net capital expenditures for fiscal 2005 were \$0.9 million, compared to \$0.6 million for the prior year. The increase in capital expenditures for the current fiscal year related mainly to the purchase of R&D equipment for the refinery development program undertaken with EMRE. It is expected that capital expenditures will fluctuate from year to year depending on the requirements of specific product development programs and administrative needs.

### **Liquidity and Capital Resources**

At September 30, 2005 cash and short term investments were \$10.4 million, compared to \$6.7 million at September 30, 2004. Cash used by operations and capital requirements<sup>2</sup> for fiscal 2005 was \$8.7 million, compared to \$5.7 million for fiscal 2004. The increase in operational cash burn for the year resulted mainly from increased R&D and capital expenditures related to the development program with EMRE, as well as the collection of a \$2.3 million government funding receivable which reduced the operational cash burn for fiscal 2004.

Cash used by operations and capital requirements of \$8.7 million was slightly higher than the cash burn target of under \$8.5 million provided by management on January 25, 2005. The principal reason for the higher-than-expected cash burn was an unexpected delay in the receipt of a \$0.7 million progress payment from EMRE related to an existing engineering service contract. The progress payment was received shortly following year-end.

On December 21, 2004, the Company completed an IPO of its securities concurrently on the AIM Market of the London Stock Exchange Plc and the Toronto Stock Exchange, raising gross proceeds of approximately \$15.1 million through the sale of 8.6 million common shares at a price of \$1.75 per share. Upon completion of the IPO, the Company had approximately \$17.6 million in combined cash and cash equivalents.

During the year the Company secured a US\$3 million (\$3.5 million) credit facility from Comerica Bank. The credit facility is comprised of a US\$1 million accounts receivable credit line and a US\$2 million term loan. As at September 30, 2005, the Company had drawn \$0.7 million against the term loan. The Company is in compliance with all of its bank covenants.

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<sup>2</sup> Cash used by operations and capital requirements is defined “cash flows from operating activities” and “cash flows from investing activities” (excluding changes in short term investments and note receivable) reported on the Company’s Statement of Cash Flows.

In June 2003, the Company was awarded a \$9.6 million conditionally repayable loan from Technology Partnerships Canada, a funding program administered by Industry Canada. At September 30, 2005, the Company had claimed \$5.9 million against this loan.

At September 30, 2005 QuestAir had 37,307,621 common shares issued and outstanding. In addition, the Company had 4,826,860 stock options outstanding, of which 3,082,400 were exercisable, and 622,308 warrants outstanding at that date.

Further information on QuestAir's financial results for the year ended September 30, 2005 can be found in the Company's 'Management Discussion and Analysis' ("MD&A") at [www.sedar.com](http://www.sedar.com).

## **Consolidated Balance Sheets**

(expressed in Canadian dollars)	As at September 30, 2005	As at September 30, 2004
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 10,414,219	\$ 6,691,923
Accounts receivable - net of allowance for doubtful accounts of \$nil (September 30, 2004 - \$28,486)	1,075,255	425,628
Grants and funding receivables	493,913	687,692
Inventories	1,945,876	1,676,013
Prepaid expenses	299,757	90,283
	14,229,020	9,571,539
<b>Deferred charges</b>	-	399,742
<b>Property, plant and equipment</b>	1,984,014	2,592,286
	<u>\$ 16,213,034</u>	<u>\$ 12,563,567</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Accounts payable and accruals	\$ 2,210,686	\$ 1,781,512
Deferred revenue	1,602,103	1,980,439
Current portion of bank debt	216,839	-
Current portion of obligations under capital lease	110,357	114,810
	<u>4,139,985</u>	<u>3,876,761</u>
<b>Bank debt</b>	433,678	-
<b>Obligations under capital lease</b>	-	120,776
	<u>4,573,663</u>	<u>3,997,537</u>
<b>Shareholders' Equity:</b>		
<b>Share capital</b>		
Authorized		
Unlimited common shares, voting, no par value		
Unlimited preferred shares, issuable in series, no par value		
Common shares	89,774,802	2,795,830
Preferred shares	-	75,315,007
	<u>89,774,802</u>	<u>78,110,837</u>
<b>Contributed surplus</b>	6,647,129	4,015,802
<b>Deficit</b>	(84,782,560)	(73,560,609)
	<u>11,639,371</u>	<u>8,566,030</u>
	<u>\$ 16,213,034</u>	<u>\$ 12,563,567</u>

## **Consolidated Statements of Operations and Deficit**

(expressed in Canadian dollars)	September 30, 2005	For the year ended September 30, 2004
<b>Revenues</b>	\$ 6,292,309	\$ 3,001,955
<b>Cost of goods sold</b>	3,537,068	2,097,264
<b>Gross Profit</b>	<u>2,755,241</u>	<u>904,691</u>
<b>Operating expenses</b>		
Research and development - net	5,733,846	4,697,897
General and Administration	3,427,315	2,479,387
Sales and marketing	1,779,703	1,677,173
Amortization	1,531,112	1,810,710
	<u>12,471,976</u>	<u>10,665,167</u>
<b>Loss before undernoted</b>	<u>(9,716,735)</u>	<u>(9,760,476)</u>
<b>Other income</b>		
Interest income	226,165	190,834
Other income (expense)	(26,288)	53,743
	<u>199,877</u>	<u>244,577</u>
<b>Loss for the year</b>	(9,516,858)	(9,515,899)
<b>Deficit – Beginning of year</b>	(73,560,609)	(64,044,710)
<b>Preferred share conversion</b>	(1,705,093)	-
<b>Deficit – End of year</b>	<u>\$(84,782,560)</u>	<u>\$ (73,560,609)</u>
<b>Basic and diluted loss per share</b>	\$ (0.31)	\$ (1.94)
<b>Weighted average number of common shares outstanding</b>	30,017,856	4,915,287

## **Consolidated Statements of Cash Flows**

(expressed in Canadian dollars)	September 30, 2005	For the year ended September 30, 2004
<b>Cash flows from operating activities</b>		
Loss for the year	\$ (9,516,858)	\$ (9,515,899)
Items not involving cash		
Amortization	1,531,112	1,810,710
Gain on sale of property, plant and equipment	(7,418)	(2,357)
Non-cash compensation expense	754,759	300,661
Foreign currency gain	(9,661)	(12,772)
	<u>(7,248,066)</u>	<u>(7,419,657)</u>
Changes in non-cash operating working capital		
Accounts, grants and funding receivables	(455,846)	2,288,482
Inventories	(269,864)	(740,527)
Prepaid expenses	(209,474)	29,220
Accounts payable and accrued liabilities	782,382	(614,156)
Deferred revenue	(378,337)	1,395,138
	<u>(531,139)</u>	<u>2,358,157</u>
	<u>(7,779,205)</u>	<u>(5,061,500)</u>
<b>Cash flows from investing activities</b>		
Decrease in short-term investments	-	9,876,040
Purchase of property, plant and equipment	(1,261,919)	(744,282)
Decrease in note receivable	-	150,000
Proceeds on sale of property, plant and equipment	10,895	2,919
Government grants and funding related to property, plant and equipment	335,600	133,402
	<u>(915,424)</u>	<u>9,418,079</u>
<b>Cash flows from financing activities</b>		
Issuance of common shares	15,050,000	-
Share issue costs	(2,835,287)	-
Issuance of common shares on exercise of stock options	20,470	15,480
Repayment of obligations under capital lease	(115,568)	(133,968)
Bank debt	650,518	-
Deferred charges	(353,208)	(46,534)
	<u>12,416,925</u>	<u>(165,022)</u>
<b>Increase (decrease) in cash and equivalents</b>	3,722,296	4,191,557
<b>Cash and equivalents – Beginning of year</b>	6,691,923	2,500,366
<b>Cash and equivalents – End of year</b>	<u>\$ 10,414,219</u>	<u>\$ 6,691,923</u>

## Notes to the financial statements

### 1. United States generally accepted accounting principles

The Company follows generally accepted accounting principles in Canada (Canadian GAAP), which are different in certain respects from those applicable in the United States (U.S. GAAP). The significant differences between Canadian GAAP and U.S. GAAP with respect to the Company's consolidated financial statements are described below, however, disclosures that would otherwise be required under U.S. GAAP have not been provided.

#### Consolidated Balance Sheets

	September 30, 2005		September 30, 2004	
	Canadian GAAP	U.S. GAAP	Canadian GAAP	U.S. GAAP
Liabilities				
Class C preferred (a)	-	-	-	5,877,243
Shareholders' equity				
Common shares	89,774,802	81,320,036	2,795,830	2,795,830
Preferred shares (a)	-	-	75,315,007	56,000,436
Contributed surplus	6,647,129	5,326,001	4,015,802	9,418,709

#### Consolidated Statements of Operations and Deficit

	Year ended	
	September 30, 2005	September 30, 2004
Loss for the year under Canadian GAAP	\$(9,516,858)	\$(9,515,899)
Accretion of redeemable preferred shares	(48,780)	(211,885)
Preferred share conversion	1,790,253	-
Loss for the year under U.S. GAAP	<u>(7,775,385)</u>	<u>(9,727,784)</u>
Deficit - Beginning of year under Canadian GAAP	(73,560,609)	(64,044,710)
Add: Accumulated accretion on redeemable preferred shares calculated under U.S. GAAP	(5,388,661)	(5,176,776)
Accumulated stock based compensation under U.S. GAAP	(208,460)	(208,460)
Deduct: Accumulated accretion of redeemable preferred shares calculated under Canadian GAAP	13,631,542	13,631,542
Deficit - Beginning of year under U.S. GAAP	<u>(65,526,188)</u>	<u>(55,798,404)</u>
Preferred share conversion under Canadian and U.S. GAAP	(1,705,093)	-
Deficit - End of year under U.S. GAAP	<u>\$(75,006,666)</u>	<u>\$(65,526,188)</u>
Loss per share - U.S. GAAP	\$ (0.32)	\$ (1.98)

## Consolidated Statements of Cash Flows

	September 30, 2005	Year Ended September 30, 2004
Loss for the year under U.S. GAAP	\$(7,775,385)	\$(9,727,784)
Items not involving cash		
Amortization	1,531,112	1,810,710
Gain on sale of property, plant and equipment	(7,418)	(2,357)
Non-cash compensation expense recorded in contributed surplus	754,759	300,661
Foreign currency gain	(9,661)	(12,772)
Accretion on preferred shares (a)	48,780	211,885
Changes in non-cash operating working capital	(531,139)	2,358,157
Cash flows from operating activities under U.S. and Canadian GAAP	<u>(5,988,952)</u>	<u>(5,061,500)</u>
Cash flows from financing activities under Canadian GAAP	12,416,925	(165,022)
Preferred share conversion	<u>(1,790,253)</u>	<u>-</u>
Cash flows from financing activities under U.S. GAAP	<u>10,626,672</u>	<u>(165,022)</u>
Cash flows from investing activities under U.S. and Canadian GAAP	<u>(915,424)</u>	<u>9,418,079</u>
Increase in cash and cash equivalents under U.S. and Canadian GAAP	<u>\$3,722,296</u>	<u>\$4,191,557</u>

### a) Redeemable preferred shares reorganization

For the period from November 5, 2002 to July 1, 2003, the Class C preferred shares were accounted for as equity under U.S. GAAP. On July 1, 2003, the Company adopted the provisions of Statement of Financial Accounting Standards No. 150 (SFAS 150), which resulted in the Class C preferred shares being classified as a liability. The liability for the Class C preferred shares was reflected at its fair value of \$5,665,358 and the resulting gain of \$5,194,447 from the adoption of SFAS 150 has been recorded in shareholders' equity as contributed surplus. The Class A and B preferred shares are classified as equity for U.S. GAAP purposes.

At September 30, 2004, the liability for the Class C preferred shares was recorded at its estimated fair value of \$5,877,243, with the increase of \$211,885 being recorded as an accretion charge in the consolidated statement of operations and deficit. Immediately prior to the conversion of the Class C preferred shares (see below), a further \$48,780 was recorded as an accretion charge for that part of fiscal 2005 for which the Class C preferred shares were outstanding. This increased the estimated fair value of the liability to \$5,926,023 immediately prior to conversion.

In December of 2004, the Company completed an initial public offering of its securities on the Toronto Stock Exchange and on the AIM Market of the London Stock Exchange Plc., consisting of a new issue of 8,600,000 Common Shares, for gross proceeds of \$15,050,000.

Immediately prior to closing the initial public offering, the Company completed a reorganization of its share capital whereby the existing share classes were converted into

a single class of common shares. To complete the share capital reorganization, certain terms of the Class A, B and C preferred shares relating to automatic conversion rights were modified to convert these shares into common shares. The modification of the share rights is accounted for on a fair value basis. The difference between the fair value of the preferred share rights prior to and subsequent to the modification is accounted for as an adjustment to shareholders' equity and to operations for U.S. GAAP purposes. The modification to the Class A and B preferred share rights resulted in an increase in deficit of \$1,705,093 for both Canadian and U.S. GAAP purposes as these shares are classified as equity. However, the modification of the Class C preferred share rights resulted in a gain of \$1,790,253 for U.S. GAAP purposes, as the Class C preferred shares were classified as a liability. Under Canadian GAAP, the modification of the Class C preferred shares was treated as contributed surplus. With respect to calculating loss per share for U.S. GAAP purposes, both the gain on the conversion of the Class C preferred shares and the charge related to the conversion of the Class A and B preferred shares were included in the computation of loss per share.

b) Stock-based compensation

Under Canadian GAAP, the Company adopted the fair value based method of accounting for stock based compensation, on a prospective basis, to account for all its awards of shares and share options that are granted, modified or settled on or after October 1, 2002. The Company also adopted, on a prospective basis, the fair value based method of accounting for stock-based compensation for U.S. GAAP purposes effective October 1, 2002. Prior to October 1, 2002, the Company used the intrinsic value based method to account for the above awards for U.S. GAAP.

Had the Company adopted the fair value based method under U.S. GAAP for the period prior to October 1, 2002, the Company's net loss and loss per share under U.S. GAAP would have been presented as follows:

(expressed in Canadian dollars)	September 30, 2005	Year ended September 30, 2004
Loss for the year	\$(7,775,385)	\$(9,727,784)
Additional compensation expense under fair value based method	(65,118)	(336,842)
Loss for the year - pro forma	\$(7,840,503)	\$(10,064,626)
Loss per share - pro forma		
Basic and diluted	\$ (0.32)	\$ (2.05)

In the calculation of the additional compensation expense above, the fair value of each share option grant was estimated on the date of the grant using the Black-Scholes option valuation model with the following assumptions:

Expected dividend yield	0%
Expected stock price volatility	0%
Risk-free interest rate	2.5%
Expected life of options	5 years

**About QuestAir Technologies Inc.**

QuestAir Technologies, Inc. is a developer and supplier of proprietary gas purification systems for several large international markets, including existing markets such as oil refining, biogas production and natural gas processing, and emerging markets such as fuel cell power plants and fuel cell vehicle refueling stations. QuestAir is based in Burnaby, British Columbia and its shares trade on the AIM Market of the London Stock Exchange Plc. and on the Toronto Stock Exchange under the symbol “QAR”.

**Forward-looking statements**

Certain statements in this press release may constitute “forward-looking” statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this press release, such statements use such words as “anticipate”, “believe”, “plan”, “estimate”, “expect”, “intend”, “may”, “will” and other similar terminology. These statements reflect current expectations regarding future events and operating performance and speak only as of the date of this press release. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements.

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