

**SEA BREEZE POWER CORP.**

**CONSOLIDATED FINANCIAL STATEMENTS**

**DECEMBER 31, 2007 AND 2006**  
**(Stated In Canadian Dollars)**



## AUDITORS' REPORT

To the Shareholders of  
Sea Breeze Power Corp.

We have audited the consolidated balance sheets of Sea Breeze Power Corp. as at December 31, 2007 and 2006, and the consolidated statements of net loss and comprehensive loss, cash flows and shareholders' (deficiency) equity for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Vancouver, Canada

April 25, 2008

"Morgan & Company"

Chartered Accountants

**SEA BREEZE POWER CORP.****Consolidated Balance Sheets**

(Stated in Canadian Dollars)

	<b>DECEMBER 31</b>	
	<b>2007</b>	<b>2006</b>
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 170,035	\$ 230,189
Accounts receivable	115,965	86,148
Marketable securities (Note 4)	750	2,560
Prepaid expenses and deposits	61,335	73,070
	<u>348,085</u>	<u>391,967</u>
<b>Security Deposits</b> (Note 5)	76,975	63,325
<b>Investments</b> (Note 6)	1	1
<b>Property And Equipment</b> (Note 8)	205,455	206,080
	<u>\$ 630,516</u>	<u>\$ 661,373</u>
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	\$ 361,099	\$ 420,693
Loans payable to related parties (Note 9)	1,024,412	844,958
	<u>1,385,511</u>	<u>1,265,651</u>
<b>Convertible Debentures</b> (Note 11)	2,346,659	860,648
	<u>3,732,170</u>	<u>2,126,299</u>
<b>SHAREHOLDERS' DEFICIENCY</b>		
<b>Equity Portion Of Convertible Debentures</b> (Note 11)	1,309,918	199,408
<b>Commitment To Issue Shares</b> (Note 11)	1,814,868	395,606
<b>Share Capital</b> (Note 12)	18,916,167	18,314,592
<b>Contributed Surplus</b>	9,362,015	7,648,191
<b>Special Warrants</b> (Note 13)	245,048	352,849
<b>Accumulated Other Comprehensive Loss</b>	(1,810)	-
<b>Deficit</b>	(34,747,860)	(28,375,572)
	<u>(3,101,654)</u>	<u>(1,464,926)</u>
	<u>\$ 630,516</u>	<u>\$ 661,373</u>

Approved on Behalf of the Board of Directors:

\_\_\_\_\_  
"Paul B. Manson"  
Director

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"Henry P. Anderson, III"  
Director

See accompanying notes to consolidated financial statements

**SEA BREEZE POWER CORP.****Consolidated Statements of Net Loss and Comprehensive Loss**

(Stated in Canadian Dollars)

	YEAR ENDED DECEMBER 31	
	2007	2006
<b>Service Income</b>	\$ -	\$ 83,873
<b>Cost Of Service Income</b>	-	(44,853)
<b>Income On Service Activity</b>	-	39,020
<b>Project Related Costs (Note 14)</b>	<b>2,668,405</b>	<b>2,003,735</b>
<b>Administration Expenses</b>		
Accounting and audit	169,650	183,055
Amortization	25,128	26,293
Bank charges and interest	53,882	48,897
Consulting	39,918	149,597
Filing fees	17,726	21,576
Foreign exchange (gain) loss	(105,347)	33,381
Interest on convertible debentures	493,801	151,234
Legal fees	14,529	79,921
Office and rent	536,484	526,876
Public relations and travel	85,691	102,821
Shareholder's information	29,404	1,976
Stock based compensation	1,812,124	1,396,123
Salaries and benefits	530,299	472,975
Transfer agent	11,986	16,487
<b>Total Administration Expenses</b>	<b>3,715,275</b>	<b>3,211,212</b>
<b>Loss Before The Following</b>	<b>(6,383,680)</b>	<b>(5,175,927)</b>
<b>Interest Income</b>	<b>11,392</b>	<b>10,622</b>
<b>Net Loss For The Year</b>	<b>(6,372,288)</b>	<b>(5,165,305)</b>
<b>Other Comprehensive Loss</b>		
Unrealized loss arising on available for sale investments during the year	(1,810)	-
<b>Comprehensive Loss For The Year</b>	<b>\$ (6,374,098)</b>	<b>\$ (5,165,305)</b>
<b>Loss Per Share - Basic and diluted</b>	<b>\$ (0.09)</b>	<b>\$ (0.08)</b>
<b>Weighted Average Common Shares Outstanding</b>	<b>71,762,147</b>	<b>66,543,033</b>

See accompanying notes to consolidated financial statements

## SEA BREEZE POWER CORP.

### Consolidated Statements of Cash Flows

(Stated in Canadian Dollars)

	YEAR ENDED DECEMBER 31	
	2007	2006
<b>Cash Provided By (Used In):</b>		
<b>Cash Flows From Operating Activities</b>		
Net loss for the year	\$ (6,372,288)	\$ (5,165,305)
Items not affecting cash:		
Interest to be paid in common shares	320,590	110,787
Amortization	25,128	26,293
Interest on loans payable	46,478	40,365
Stock based compensation	1,812,124	1,396,123
Project development costs	-	429,944
Accretion of interest on convertible debentures	162,151	40,365
Changes in non-cash operating working capital items:		
Accounts receivable	(29,817)	(53,439)
Accounts payable and accrued liabilities	(59,594)	7,178
Prepaid expenses	11,735	12,839
Related party receivable	-	336,828
	<u>(4,083,493)</u>	<u>(2,798,811)</u>
<b>Cash Flows From Financing Activities</b>		
Loans payable to related parties	3,666,018	490,289
Common shares issued for cash	395,474	2,121,789
Due from co-venture partner	-	137,738
	<u>4,061,492</u>	<u>2,749,816</u>
<b>Cash Flows From Investing Activities</b>		
Purchase of equipment	(24,503)	(17,916)
Security deposits	(13,650)	10,000
	<u>(38,153)</u>	<u>(7,916)</u>
<b>Decrease In Cash</b>	<b>(60,154)</b>	<b>(56,911)</b>
<b>Cash, Beginning Of The Year</b>	<b>230,189</b>	<b>287,100</b>
<b>Cash, End Of The Year</b>	<b>\$ 170,035</b>	<b>\$ 230,189</b>

#### Supplemental Disclosure For Non-Cash Financing And Investing Activities (Note 15)

See accompanying notes to consolidated financial statements

# SEA BREEZE POWER CORP.

## Consolidated Statements of Shareholders' (Deficiency) Equity Years ended December 31, 2007 and 2006

	COMMON SHARES		EQUITY PORTION OF CONVERTIBLE DEBENTURES	CONTRIBUTED SURPLUS	SPECIAL WARRANTS	COMMITMENT TO ISSUE SHARES	OTHER COMPREHENSIVE LOSS	DEFICIT	TOTAL
	NUMBER	AMOUNT							
Balance, December 31, 2005	63,972,476	\$ 16,007,489	\$ 205,478	\$ 6,311,255	\$ 437,844	\$ 294,367	\$ -	\$ (23,210,267)	\$ 46,166
Issued for cash pursuant to:									
Private placement at \$.30 USD	4,333,334	1,471,080	-	-	-	-	-	-	1,471,080
Private placement at \$.30 USD	333,333	111,053	-	-	-	-	-	-	111,053
Private placement at \$.30 USD	1,119,204	381,659	-	-	-	-	-	-	381,659
Exercise of special warrants at \$0.15	631,000	94,650	-	-	-	-	-	-	94,650
Exercise of warrants at \$0.33	70,000	23,100	-	-	-	-	-	-	23,100
Exercise of stock options at \$0.15	400,000	60,000	-	-	-	-	-	-	60,000
Exercise of stock options at \$0.35	6,000	2,100	-	-	-	-	-	-	2,100
Exercise of stock options at \$0.60	1,000	600	-	-	-	-	-	-	600
Conversion of convertible debenture	85,362	41,132	(6,070)	-	-	-	-	-	35,062
Special warrants valuation	-	84,995	-	-	(84,995)	-	-	-	-
Stock options valuation	-	59,186	-	(59,186)	-	-	-	-	-
Share issue costs	-	(22,452)	-	-	-	-	-	-	(22,452)
Interest payable in shares	-	-	-	-	-	101,239	-	-	101,239
Stock based compensation	-	-	-	1,396,122	-	-	-	-	1,396,122
Net loss for the year	-	-	-	-	-	-	-	(5,165,305)	(5,165,305)
Balance, December 31, 2006	70,951,709	18,314,592	199,408	7,648,191	352,849	395,606	-	(28,375,572)	(1,464,926)
Issued for cash pursuant to:									
Private placement at \$0.34 USD	441,176	166,515	-	-	-	-	-	-	166,515
Exercise of special warrants at \$0.15	803,333	120,500	-	-	-	-	-	-	120,500
Exercise of stock options at \$0.15	523,742	78,561	-	-	-	-	-	-	78,561
Exercise of stock options at \$0.35	49,000	17,150	-	-	-	-	-	-	17,150
Exercise of stock options at \$0.30 USD	40,000	12,748	-	-	-	-	-	-	12,748
Special warrants valuation	-	107,801	-	-	(107,801)	-	-	-	-
Stock options valuation	-	98,300	-	(98,300)	-	-	-	-	-
Equity portion of convertible debentures	-	-	1,309,918	-	-	-	-	-	1,309,918
Conversion of convertible debenture	-	-	(199,408)	-	-	1,098,672	-	-	899,264
Interest payable in shares	-	-	-	-	-	320,590	-	-	320,590
Unrealized loss on marketable securities	-	-	-	-	-	-	(1,810)	-	(1,810)
Stock based compensation	-	-	-	1,812,124	-	-	-	-	1,812,124
Net loss for the year	-	-	-	-	-	-	-	(6,372,288)	(6,372,288)
Balance, December 31, 2007	72,808,960	\$ 18,916,167	\$ 1,309,918	\$ 9,362,015	\$ 245,048	\$ 1,814,868	\$ (1,810)	\$ (34,747,860)	\$ (3,101,654)

# SEA BREEZE POWER CORP.

## Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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### 1. NATURE OF OPERATIONS AND GOING CONCERN

Sea Breeze Power Corp. (the "Company") is a public company incorporated under the Business Corporations Act of British Columbia, Canada. The Company's principal business activity is the development of hydro-electric projects, wind power generation projects and transmission projects in British Columbia, Canada.

These consolidated financial statements have been prepared on a going-concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business.

The Company reported net losses of \$6,372,288 and \$5,165,305 for the year ended December 31, 2007 and 2006, respectively, and has an accumulated deficit of \$34,747,860 at December 31, 2007. These recurring losses and the need for continued funding, discussed below, raise substantial doubt about the Company's ability to continue as a going concern. These consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The Company is in the development stage and currently derives no revenues from its projects. To date, the Company has financed its operations principally through equity financing and loans. The application of the going concern concept is dependent upon continuing rights to the areas, the obtaining of necessary regulatory approvals, the ability to obtain the necessary financing to complete development, and the successful development and sale of electricity.

The Company's ability to meet its obligations in the ordinary course of business is dependent upon its ability to establish profitable operations and to obtain additional funding through public or private equity financing, collaborative or other arrangements with corporate or other sources. Management plans to continue raising capital through private placement equity financing.

Management is working to obtain sufficient working capital from external sources in order to continue operations, as well as further developing the Company's business model to obtain revenues from its wind, hydro-electric power generating and transmission projects. There is, however, no assurance that the aforementioned events, including the receipt of additional funding, will occur or be successful.

# SEA BREEZE POWER CORP.

## Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### a) Principles of Consolidation

These consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada, and include the accounts of the Company and its wholly-owned subsidiaries, Powerhouse Developments Inc., Powerhouse Electric Corp., Sea Breeze Energy Inc., Sea Breeze Management Services Inc., Sea Breeze Power Projects Inc., SBJF Holding Corp. and the Company's proportionate interest (80%) in the assets of the Slollicum Joint Venture, and the Company's proportionate interest (50%) in the assets, liabilities and expenses of Sea Breeze Pacific Regional Transmission Systems, Inc., and the Company's proportionate interest (47.5%) in Sea Breeze High Desert Conversion LP. All significant inter-company balances and transactions have been eliminated upon consolidation. The Company uses the equity method to account for investments over which the Company exerts significant influence. The Company uses the proportionate consolidation method of accounting to account for the Company's interest in jointly controlled entities.

#### b) Financial Instruments – Change in Accounting Policies

Effective January 1, 2007, the Company has adopted three new accounting standards related to financial instruments that were issued by the Canadian Institute of Chartered Accountants ("CICA") in 2005. These accounting policy changes were adopted on a prospective basis with no restatement of prior period financial statements. The new standards and accounting policy changes are as follows:

##### Financial Instruments – Recognition and Measurement (CICA Handbook Section 3855)

In accordance with this new standard the Company now classifies all financial instruments as either held-to-maturity, available-for-sale, held for trading or loans and receivables. Financial assets held to maturity, loans and receivables and financial liabilities other than those held for trading, are measured at amortized cost. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in other comprehensive income. Instruments classified as held for trading are measured at fair value with unrealized gains and losses recognized on the statement of loss.

##### Comprehensive Income (CICA Handbook Section 1530)

Comprehensive income is the change in shareholders' equity during a period from transactions and other events and circumstances from non-owner sources. In accordance with this new standard, when applicable, the Company's financial statements will include, a consolidated statement of comprehensive income/loss and accumulated other comprehensive income/loss will be added to the shareholders' equity section of the consolidated balance sheet. The components of this new category will include unrealized gains and losses on financial assets classified as available-for-sale and the effective portion of cash flow hedges, if any.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

##### Hedges (CICA Handbook Section 3865)

The new standard specifies the criteria under which hedge accounting can be applied and how hedge accounting can be executed. The Company has not designated any hedging relationships.

##### c) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses for the reporting period. Actual results could differ from these estimates.

##### d) Foreign Currency

Monetary items denominated in a foreign currency are translated to Canadian dollars at exchange rates in effect at the balance sheet date. The resulting foreign exchange gains and losses are included in the statement of loss and deficit.

##### e) Cash and Cash Equivalents

Cash and cash equivalents consist of cash and short-term deposits with maturities of 90 days or less when acquired. The Company did not have cash equivalents as of December 31, 2007 and 2006.

##### f) Marketable Securities

The marketable securities were recorded at lower of cost and market on and before December 31, 2006. On January 1, 2007, the Company adopted the new financial instrument standards (CICA Section 3855 and Section 1530) and classifies its marketable securities as "available for sale" and records the marketable securities at their fair values.

##### g) Property and Equipment

Equipment is carried at cost and being amortized as follows:

Computer and automotive equipment	30% declining balance basis
Office and field equipment	20% declining balance basis

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

##### h) Stock Based Compensation

The Company follows the recommendations of CICA Handbook Section 3870 – “Stock Based Compensation and Other Stock Based Payments” to account for stock based transactions with officers, directors, employees, and outside consultants. Accordingly, the fair value of stock options is charged to operations with an offsetting credit to contributed surplus. The fair value of stock options which vest immediately is recorded at the date of grant; the fair value of options which vest in the future is recognized on a straight-line basis over the vesting period. Any consideration received on exercise of stock options together with the related portion of contributed surplus is credited to share capital.

##### i) Loss Per Share

Basic loss per share is calculated using the weighted average number of shares outstanding during the year. The Company uses the treasury stock method to determine the dilutive effect of stock options and other dilutive instruments on loss per share. Under the treasury stock method, only instruments with exercise amounts less than market prices impact the diluted calculations. In computing diluted loss per share, no shares were added to the weighted average number of common shares outstanding during the period ended December 31, 2007 for the dilutive effect of employee stock options and warrants as they were all anti-dilutive. No adjustments were required to reported loss from operations in computing diluted per share amounts.

##### j) Income Taxes

The Company uses the asset and liability method of accounting for income taxes whereby future income tax assets are recognized for deductible temporary differences and operating loss carry forwards, and future income tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the amounts of assets and liabilities recorded for income tax and financial reporting purposes. Future income tax assets are recognized only to the extent that management determines that it is more likely than not that the future income tax assets will be realized. Future income tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment or substantive enactment. The income tax expense or benefit is the income tax payable or refundable for the year plus or minus the change in future income tax assets and liabilities during the year.

##### k) Asset Impairment

On an annual basis or when impairment indicators arise, the Company evaluates the future recoverability of capital assets and project related development costs. Impairment losses or write downs are recorded in the event the net book value of such assets exceeds the estimated indicated future cash flows attributable to such assets.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

l) Service Revenues

The Company provides wind generation research and consulting services to third parties. Revenues from consulting services are recognized over the contract period, which is the period during which the services are provided and the related expenses are incurred.

m) Variable Interest Entities

The Company follows the Canadian Institute of Chartered Accountants (CICA) Accounting Guideline 15 – “Consolidation of Variable Interest Entities” (VIE). The guideline establishes that a VIE is to be consolidated by the primary beneficiary based upon the determination of who will receive the majority of a VIE’s expected losses, expected residual returns, or both, defined as a variable interest, rather than solely based on the voting interests. Variable interests are ownership interests or contractual relationships that enable the holder to share in the financial risks and rewards resulting from the activities of a VIE.

The accounting guideline specifies that an entity is a VIE if either of the following criteria are met:

1. total equity invested is insufficient to finance the entity without additional subordinated financial support; or
2. the holders of the equity investment, as a group:
  - i) do not have the right to make decisions about an entity’s activities that have a significant effect on the success of the entity; or
  - ii) are protected either directly or indirectly from variability in cash flows from the entity; or
  - iii) do not have the right to all of the residual returns of the entity.

The Company has considered the provisions of the guideline for all subsidiaries and their related investments.

As a result of this review, the Company determined that the wholly-owned subsidiary that holds the Company’s interest in the Juan de Fuca partnership is considered a VIE as the equity invested was not sufficient to finance the entity without additional subordinated financial support. The Company then determined that the subsidiary is not the primary beneficiary of the VIE and does not consolidate the entity. Accordingly, the Company’s general and limited partner interests in the partnership are presented as an equity investment and the results from operations are presented as equity income (loss) on the consolidated statement of loss. There was no impact to net earnings as a result of adoption of this accounting guideline.

n) Project Development Costs

The Company expenses project related development costs until such time as final development decisions with respect to each specific project are made. After a final positive development production decision is made on a project, the project related development costs will be capitalized and amortized over the expected life of the project.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

o) Comparative Figures

Certain of the comparative figures have been reclassified to conform with the current year's presentation.

#### 3. NEW ACCOUNTING POLICIES NOT YET ADOPTED

The following accounting pronouncements are applicable to future reporting periods. The Company is currently evaluating the effects of adopting these standards:

- i) On January 8, 2008, the CICA issued Section 3064, Goodwill and Intangible Assets. Section 3064, establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. Section 3064 is effective for the Company for annual and interim financial statements commencing January 1, 2009.
- ii) On September 15 2006, the CICA issued three new accounting standards: Handbook Section 1535, Capital Disclosures, Handbook Section 3862, Financial Instruments – Disclosures, and Handbook Section 3863, Financial Instruments – Presentation. Section 1535, Capital Disclosures requires that a company disclose information that enables users of its financial statements to evaluate its objectives, policies and procedures for managing capital including disclosures of any externally imposed capital requirements and the consequences for non-compliance. The new Sections 3862 and 3863 replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. Sections 1535, 3862 and 3863 are effective for the Company for annual and interim financial statements commencing January 1, 2008.

#### 4. MARKETABLE SECURITIES

	Carrying Value	Unrealized losses	Fair Value
Available-for-sale	\$2,560	(\$1,810)	\$750

Upon adoption of the new CICA Handbook Section 3855, the Company designates its marketable securities as available for sale and as such, it is valued at fair value as of December 31, 2007 (2006 – recorded at cost of \$2,560). Unrealized changes to market value are adjusted to Other Comprehensive Income.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 5. SECURITY DEPOSITS

The Company has advanced \$45,825 (2006 - \$45,825) to be held as security on corporate credit card accounts. The funds are held as security for credit advanced to the Company and, as such, may not be used for general corporate purposes. The Company has also posted \$31,150 (2006 - \$17,500) in project related security deposits.

#### 6. INVESTMENTS

##### a) Investment in Juan De Fuca Cable Partnership

During the year ended December 31, 2005, the Company became the holder of a 49.5% limited partnership interest and a 25% equity interest in the general partner, which is also a 1% limited partner, in a newly formed, special purpose (State of Delaware, USA) limited partnership, Sea Breeze Pacific Juan de Fuca Cable, L.P. ("JDFC"). The original purpose of the partnership was to develop the Juan de Fuca Transmission Cable Project ("The Project"). The Project consists of the development of a 550 MW High Voltage Direct Current submarine transmission link spanning the Strait of Juan de Fuca connecting the city of Victoria on the southern tip of Vancouver Island, British Columbia, Canada to Port Angeles, Washington State, U.S.A. The Company and its joint venture partner Boundless Energy, LLC initially developed the Project and assigned their interest in the project to JDFC for a nominal amount. As a result the Company's cost of the investment in the partnership is \$Nil.

On April 6, 2005, JDFC secured a development loan of up to US\$8,000,000 from US Power Fund, LP to advance permitting of the project, and to conduct a bonded bid auction ("Open Season") for capacity on the potential transmission line to be developed jointly by the Company and its partners. The proceeds of the loan are convertible into project equity at US Power Fund's option. Advances of funds under the agreement are subject to certain milestones being met by the Company and its joint venture partner. Loan advances totalling US\$5,791,000 (2006 - US\$5,441,000) have been remitted to the partnership by US Power Fund, LP in tranches through December 31, 2007.

The loan bears 20% interest per annum, compounded annually. As at December 31, 2007, accumulated interest totalled US\$2,728,742 (2006 - US\$1,336,438). The loan balance and accrued interest is repayable by JDFC and matures on the earliest of June 30, 2008 or the day upon which financing for construction of the project is closed (Financial Closing Date).

All proceeds of the loan were used by JDFC to pay costs and expenses incurred in the development of the project and in accordance with the development loan budget.

The loan is secured by a registered security interest in all rights, assets, partners' voting rights, and partners' interests in JDFC and its subsidiaries. The loan agreement further provides for an overrun amount of up to US\$1,000,000 of costs incurred in excess of the amounts budgeted for at each milestone of the development loan agreement to be paid by Boundless and Sea Breeze in the event that Financial Closing has not been achieved upon full advance of the total loan amount. The overrun amount is jointly to be borne by the Company and its joint venture partner Boundless Energy, LLC.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 6. INVESTMENTS (Continued)

##### a) Investment in Juan De Fuca Cable Partnership (Continued)

During the year ended December 31, 2005, an amendment of the original development loan agreement provided for a further transmission project (the "New Project") to be added to the purpose of the partnership. The New Project relates to a submarine transmission cable crossing the Strait of Georgia from Vancouver mainland to Vancouver Island, British Columbia, Canada.

The Company's jointly held subsidiary, Sea Breeze Pacific Regional Transmission System Inc. ("SBPRTS"), sold its right, title and interest in the project to the partnership for costs incurred as at the date of signing the agreement, December 16, 2005.

During the year ended December 31, 2007, JDFC incurred \$1,858,558 of project related costs charged to operations, and \$1,497,099 (US\$1,392,303) of accrued interest related thereto. The Company accounts for its investment under the equity method and, accordingly, as its investment in the partnership is \$Nil as at December 31, 2007, Sea Breeze has not included its 49.75% proportional share of the loss of the partnership in these consolidated financial statements.

A summary of financial data relating to the partnership is as follows:

	<u>2007</u>	<u>2006</u>
<b>Balance Sheets</b>		
Cash	\$ 145,448	\$ 29,244
GST recoverable and deposits	17,521	11,544
<b>Current and Total Assets</b>	<u>\$ 162,969</u>	<u>\$ 40,788</u>
<b>Liabilities</b>	\$ 11,044,000	\$ 8,989,840
<b>Partners' Deficiency</b>	<u>(10,881,031)</u>	<u>(8,949,052)</u>
	<u>\$ 162,969</u>	<u>\$ 40,788</u>
	<u>2007</u>	<u>2006</u>
<b>Statements Of Loss</b>		
Project development costs	\$ 1,858,558	\$ 3,222,149
Interest expense	1,497,121	1,186,865
Foreign exchange	<u>(1,423,701)</u>	<u>117,473</u>
<b>Net Loss For The Year</b>	<u>\$ (1,931,978)</u>	<u>\$ (4,526,487)</u>

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 6. INVESTMENTS (Continued)

##### a) Investment in Juan De Fuca Cable Partnership (Continued)

<u>Statements of Cash Flows</u>	<u>2007</u>	<u>2006</u>
<b>Cash Provided By (Used In):</b>		
Net loss	\$ (1,931,978)	\$ (4,526,487)
Items not affecting cash	1,497,099	1,221,302
Changes of non-cash operating working capital items	(251,695)	336,058
<b>Operating Activities</b>	<u>(686,574)</u>	<u>(2,969,133)</u>
<b>Financing Activities</b>	<u>802,778</u>	<u>1,642,947</u>
<b>Investing Activities</b>	<u>-</u>	<u>-</u>
<b>Increase (Decrease) In Cash</b>	<b>116,204</b>	<b>(1,326,186)</b>
<b>Cash, Beginning Of Year</b>	<b>29,244</b>	<b>1,355,430</b>
<b>Cash, End Of Year</b>	<u><b>\$ 145,448</b></u>	<u><b>\$ 29,244</b></u>

##### b) Investment in Standard Hydrogen

During fiscal 2004, the Company paid \$10,000 for a 33% non-controlling interest in a private start-up Ontario corporation, Standard Hydrogen, which conducts research activities. The \$10,000 equity purchase was paid upon commencement of Standard Hydrogen's operations. The Company considers the investment in Standard Hydrogen no longer an economical asset. As of December 31, 2007, the carrying value is \$1 (December 31, 2006 - \$1).

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 7. JOINT VENTURE

In May 2004, the Company incorporated Sea Breeze Pacific Regional Transmission System, Inc.; a company jointly owned and operated by the Company (50%) and Boundless Energy LLC, of York Harbor, Maine (50%). The parties signed a joint venture agreement and are committed to jointly pursue specific merchant transmission opportunities. Summary financial information of the Company's proportionate interest in the joint venture is as follows:

<b>Proportionate Share (50%) of the Joint Venture</b>	<b>2007</b>	<b>2006</b>
Cash	\$ 2,848	\$ 7,322
Prepaid expenses	19,359	31,165
GST recoverable	1,005	194
Accounts receivables	-	14,568
<b>Current Assets</b>	<b>23,212</b>	<b>73,487</b>
<b>Restricted Cash</b>	<b>20,238</b>	<b>20,238</b>
<b>Capital Assets</b>	<b>1,123</b>	<b>424</b>
<b>Total Assets</b>	<b>\$ 44,573</b>	<b>\$ 73,911</b>
<b>Current Liabilities</b>	<b>16,103</b>	<b>14,818</b>
<b>Due to Affiliated Companies</b>	<b>505,783</b>	<b>457,421</b>
<b>Common Shares</b>	<b>100</b>	<b>100</b>
<b>Deficit</b>	<b>(477,413)</b>	<b>(398,428)</b>
<b>Total Liabilities And Equity</b>	<b>\$ 44,573</b>	<b>\$ 73,911</b>
Project related costs (recoveries)	26,583	(14,030)
Expenses	52,402	61,777
<b>Net Loss</b>	<b>\$ (78,985)</b>	<b>\$ (47,747)</b>

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 7. JOINT VENTURE (Continued)

<b>Proportionate Share (50%) of Cash Flows</b>	<b>2007</b>	<b>2006</b>
Net loss	\$ (78,985)	\$ (47,747)
Items not affecting cash	223	106
Changes of non-cash operating working capital items	(85,723)	111,581
<b>Operating activities</b>	<b>(166,485)</b>	<b>63,940</b>
<b>Financing activities</b>	<b>160,024</b>	<b>(63,776)</b>
<b>Investing activities</b>	<b>-</b>	<b>-</b>
<b>Increase (Decrease) In Cash</b>	<b>(6,461)</b>	<b>164</b>
<b>Cash, Beginning of Period</b>	<b>27,560</b>	<b>27,396</b>
<b>Cash, End of Period</b>	<b>\$ 21,099</b>	<b>\$ 27,560</b>
Cash on hand and balances with banks	\$ 2,848	\$ 7,322
Restricted cash	18,251	20,238
	<b>\$ 21,099</b>	<b>\$ 27,560</b>

The Company funded 100% of the costs incurred up to December 31, 2007. As a result, the Company is entitled to a reimbursement of \$405,163 (2006 - \$355,981), which is Boundless Energy's 50% of the joint venture's costs. The Company has recorded an allowance for this amount as the recoverability is uncertain.

#### 8. PROPERTY AND EQUIPMENT

	<b>2007</b>		
	<b>Cost</b>	<b>Accumulated Amortization</b>	<b>Net Book Value</b>
Computer equipment	\$ 109,082	\$ 72,404	\$ 36,679
Automotive equipment	21,156	9,027	12,129
Office equipment	26,776	12,322	14,454
Field equipment	39,012	22,379	16,633
Land	125,560	-	125,560
	<b>\$ 321,586</b>	<b>\$ 116,131</b>	<b>\$ 205,455</b>

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 8. PROPERTY AND EQUIPMENT (Continued)

	2006		
	Cost	Accumulated Amortization	Net Book Value
Computer equipment	\$ 95,860	\$ 56,438	\$ 39,422
Automotive equipment	12,656	5,650	7,006
Office equipment	27,025	11,920	15,105
Field equipment	35,982	16,995	18,987
Land	125,560	-	125,560
	<u>\$ 297,083</u>	<u>\$ 91,003</u>	<u>\$ 206,080</u>

#### 9. LOANS PAYABLE TO RELATED PARTIES

	2007	2006
Loans payable to directors and companies controlled by directors with interest at 10% per annum, unsecured, due on demand (2007 – US\$933,603; 2006 – US\$682,636).	<b>\$ 925,841</b>	\$ 795,476
Interest on loans payable to directors and companies controlled by directors, unsecured, due on demand (2007 – US\$99,436; 2006 – US\$42,463).	<b>98,571</b>	49,482
	<u><b>\$ 1,024,412</b></u>	<u>\$ 844,958</u>

#### 10. RELATED PARTY TRANSACTIONS

All related party transactions are recorded at the exchange value.

Related party transactions not disclosed elsewhere in these consolidated financial statements are as follows:

a) Consulting Fees

During the year ended December 31, 2007, the Company incurred \$74,400 (2006 - \$72,000) in consulting fees to a company controlled by a director of the Company. Further, the Company incurred \$109,320 (2006 - \$176,130) for consulting services to officers of the Company. Included in accounts payable and accrued liabilities is \$18,344 (2006 - \$56,224) owing to such officers of the Company.

b) Public Relation Fees and Governmental Advisory Services

The Company paid \$6,000 (2006 - \$72,000) to a company controlled by an officer for public relations and governmental advisory services.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 10. RELATED PARTY TRANSACTIONS (Continued)

##### c) Interest Payable

As at December 31, 2007, accrued convertible debenture interest payable in shares included \$590,886 (2006 - \$294,380) owing to directors or companies controlled by directors.

##### d) Fees Charged to Partnership

During the year ended December 31, 2007, the Company charged the JDFC partnership \$376,676 (2006 - \$655,904) for travel, wages and consulting fees related to the JDF transmission project.

#### 11. CONVERTIBLE DEBENTURES

	<u>2007</u>	<u>2006</u>
Convertible debentures	\$ 4,446,879	\$ 941,655
Conversions during the year	(913,837)	(27,818)
Equity portion of convertible debentures	<u>(1,309,918)</u>	<u>(199,408)</u>
	2,223,124	714,429
Interest accretion	<u>123,535</u>	<u>146,219</u>
Debt portion of convertible debenture	<u>\$ 2,346,659</u>	<u>\$ 860,648</u>

- a) On March 9, 2007 the Company issued convertible debentures to directors of the Company in the amount of \$1,207,403 (US\$1,218,000), which are due and payable on March 9, 2012. The debentures are convertible into units of the Company at US\$0.34 per unit in years one and two, and increasing by 10% per unit in each subsequent year for five years (year 1 to year 5: US\$0.34, US\$0.34, US\$0.37, US\$0.41, and US\$0.45). Each unit consists of one common share and one share purchase warrant. Each share purchase warrant has a term of two years from the date of conversion and entitles the holder to purchase one common share at the conversion price. Interest on the debenture is calculated at 12% per annum. The interest payments are payable in shares and calculated semi-annually at the market price of the shares on the semi-annual calculation dates. The interest shares are to be issued on March 9, 2012 or upon conversion of the debenture, whichever is sooner.

As of December 31, 2007, accumulated interest payable was \$124,501 (2006 - \$nil) resulting in a possible 321,212 (2006 - nil) common shares issuable in payment thereof. The amount has been recorded as a commitment to issue shares within the shareholders' equity section of the balance sheet. The debentures are secured by a floating charge over all assets of the Company.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 11. CONVERTIBLE DEBENTURES (Continued)

- b) On August 28, 2007 the Company issued convertible debentures to directors of the Company in the amount of \$2,250,000, which are due and payable on August 28, 2012. The debentures are convertible into units of the Company at \$0.42 per unit in years one and two, and increasing by 10% per unit in year three to five years (year 1 to year 5: \$0.42, \$0.42, \$0.46, \$0.51, and \$0.56). Each unit consists of one common share and one share purchase warrant. Each share purchase warrant has a term of two years from the date of conversion and entitles the holder to purchase one common share at the conversion price. Interest on the debenture is calculated at 12% per annum. The interest payments are payable in shares and calculated semi-annually at the market price of the shares on the semi-annual calculation dates. The interest shares are to be issued on August 28, 2012 or upon conversion of the debenture, whichever is sooner.

As of December 31, 2007, accumulated interest payable was \$93,205 (2006 - \$nil) resulting in a possible 233,014 (2006 - nil) common shares issuable in payment thereof. The amount has been recorded as a commitment to issue shares within the shareholders' equity section of the balance sheet. The debentures are secured by a floating charge over all assets of the Company.

- c) On May 7, 2003 the Company issued convertible debentures in the amount of \$1,000,000, which are due and payable on May 7, 2008. The debentures are convertible into units of the Company at USD\$0.34 per unit. Each unit consists of one common share and one purchase warrant. Each share purchase warrant has a term of two years from the date of conversion and entitles the holder to purchase one common share at the conversion price. Interest on the debenture is calculated at 12% per annum.

On December 19, 2007, the debentures were converted into units of the Company at US\$0.34 per unit. Upon conversion, the Company is committed to issue 2,702,889 shares as at December 31, 2007.

As of December 19, 2007, interest payable was \$501,961 (2006 - \$395,606) resulting in 1,024,655 (2006 - 785,766) common shares issuable in payment thereof. The amount has been recorded as a commitment to issue shares within the shareholders' equity section of the balance sheet. Of the total debentures converted on December 19, 2007, \$677,379, with interest payable of \$373,216, was issued to directors or companies controlled by directors.

- d) The liability component of the convertible debenture is calculated as the present value of the principal, discounted at a rate approximating the interest rate that was estimated would have been applicable to non-convertible debt at the time the debenture was issued. This portion of the convertible debenture is accreted over its term to the full face value by charges to interest expense. The accretion is a non-cash transaction and has been excluded from the statement of cash flows.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 11. CONVERTIBLE DEBENTURES (Continued)

The equity element of the convertible debt comprises the value of the conversion option, being the difference between the face value of the convertible debenture and the liability component.

#### 12. SHARE CAPITAL AND SHAREHOLDERS' EQUITY

a) Authorized

Unlimited common shares without par value and 20,000,000 preferred shares without par value

b) Private Placements

During the year ended December 31, 2007, the Company completed a private placement of 441,176 units at a price of US\$0.34 per unit for gross proceeds of \$166,515 (US\$150,000). Each unit consists of one common share and one half share purchase warrant with one full share purchase warrant exercisable into one common share at a price of US\$0.50 in the first year and US\$0.75 in the second year.

During the year ended December 31, 2006, the Company completed three private placements totalling \$1,963,792 (US\$1,758,261) and issued 5,785,871 units at US\$0.30 per unit, resulting in a net consideration of \$1,941,339. Each unit consists of one common share and one-half of a share purchase warrant. Each full warrant entitles the holder to purchase one additional common share at a price of US\$0.50 per share in the first year and US\$0.75 per share in the second year following the closing date. A finder's fee was capitalized against share capital in the amount of \$22,453 (US\$20,000).

c) As at December 31, 2007, the Company had the following warrants to purchase common shares of the Company outstanding:

<u>NUMBER OF WARRANTS</u>		<u>EXERCISE PRICE</u>	<u>EXPIRY DATE</u>
1,815,667	*1)	\$0.15	April 16, 2008
500,000	*2)	\$0.15	April 16, 2008
69,546		\$0.40	June 6, 2008
2,166,666	*3)	\$0.74	June 29, 2008
166,666	*3)	\$0.74	August 30, 2008
559,600	*3)	\$0.74	October 13, 2008
220,588	*3)	\$0.74	April 23, 2009
<u>5,498,733</u>			

\*1) see Note 13

\*2) contingently issuable – see Note 13

\*3) exercisable at US\$0.75

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 12. SHARE CAPITAL AND SHAREHOLDERS' EQUITY (Continued)

A summary of changes in the Company's warrants for the year ended December 31, 2007 is as follows:

	NUMBER OF WARRANTS	WEIGHTED AVERAGE EXERCISE PRICE
Balance, December 31, 2005	5,355,625	\$ 0.36
Granted	3,002,478	0.58
Exercised	(701,000)	(0.17)
Expired	(255,625)	(0.70)
Balance, December 31, 2006	7,401,478	0.46
Granted	220,588	(0.53)
Exercised	(803,333)	(0.15)
Expired	(1,320,000)	(0.33)
<b>Balance, December 31, 2007</b>	<b>5,498,733</b>	<b>\$ 0.46</b>

- d) At December 31, 2007, the Company has a fixed stock option plan. Under the policies of the TSX Venture Exchange ("TSXV"), the Company may grant incentive stock options up to a total of 20% of the Company's issued and outstanding common shares of 71,612,885 issued as of the record day of May 13, 2007.

On August 29, 2007, the Company granted 3,962,902 options exercisable at \$0.42 for a period of three years to officers, directors, employees and consultants of the Company. One third of the stock options vested immediately, one third vest after six months and one third vest after eighteen months from the date of grant.

On June 29, 2006, the Company granted 2,691,754 options exercisable at \$0.30 for a period of three years to officers, directors, employees and consultants of the Company. One third of the stock options vested immediately, one third vest after six months and one third vest after eighteen months from the date of grant.

During the year ended December 31, 2007, the Company charged \$1,812,124 in stock based compensation expense to operations as follows:

A stock based compensation expense of \$1,041,926 (2006 - \$1,396,123) was charged to operations, relating to vested options, which were granted during the years 2005 and 2006. The remaining stock based compensation expense of \$770,198 relates to options granted during the year 2007.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 12. SHARE CAPITAL AND SHAREHOLDERS' EQUITY (Continued)

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	<u>2007</u>	2006
Risk free interest rate	<b>4.19%</b>	4.42%
Expected life	<b>5 years</b>	3 years
Expected volatility	<b>126%</b>	101%
Expected dividend yield	-	-
Weighted average of fair value of options granted	<b>\$0.36</b>	\$ 0.20

The following table summarizes information about fixed stock options outstanding at December 31, 2007:

RANGE OF EXERCISE PRICES	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE	WEIGHTED AVERAGE EXERCISE PRICE
\$ 0.30–1.00	12,539,095	2.02 years	\$ 0.51	10,013,827	\$ 0.48

A summary of changes in the Company's fixed stock option plan for the period ended December 31, 2007 is as follows:

	OPTIONS OUTSTANDING	
	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE
Balance, December 31, 2005	12,141,841	0.62
Granted	2,691,754	0.33
Exercised	(407,000)	(0.15)
Forfeited	(4,757,660)	(0.71)
Balance December 31, 2006	9,668,935	\$ 0.53
Granted	3,962,902	0.42
Exercised	(612,742)	0.18
Forfeited	(480,000)	0.43
Balance December 31, 2007	<u>12,539,095</u>	<u>\$ 0.51</u>

- e) Of the Company's issued and outstanding shares, 100,000 are held in escrow, their release being subject to future company earnings and regulatory approval.

## **SEA BREEZE POWER CORP.**

### **Notes to Consolidated Financial Statements December 31, 2007 and 2006**

(Stated in Canadian Dollars)

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#### **13. SPECIAL WARRANTS**

On April 16, 2003 the Company acquired 100% of the shares of Sea Breeze Energy Inc. ("Sea Breeze"), a company developing projects to generate energy from wind power and incorporated under the British Columbia Business Corporations Act.

As consideration for the shares the Company is to pay 5% net profit royalties from proceeds of the sale of energy generated from the Sea Breeze wind power locations under development at the time of closing of the agreement and 5% of the net proceeds of any sale of such wind power properties, as well as to issue special warrants which allow the holder to acquire 4,000,000 common shares of the Company, of which 2,500,000 were exercisable upon closing of the transaction valued at their fair value of \$336,819 using the Black-Scholes option pricing model. The exercise price of the special warrants is \$0.15 per share. Any unexercised warrants expire on April 16, 2008.

Of the remaining special warrants 1,000,000 were exercisable upon receipt of the first project approval certificate from the British Columbia Environmental Assessment Office, and 500,000 warrants are exercisable upon commencement of commercial wind generated power production.

On June 28, 2004 the Company received an approval certificate from British Columbia Environmental Assessment Office for the Knob Hill wind farm project and issued 1,000,000 special warrants. The warrants were valued at their fair value of \$134,700 using the Black-Scholes option pricing model.

The value of the consideration of the remaining 500,000 special warrants and the net profit royalties will be recorded when the amounts become due and payable.

As the acquired company was in the development stage and had not commenced business operations, the acquisition has been accounted for as a purchase of assets and net liabilities of Sea Breeze Energy Inc., with fair value of the consideration given being allocated to fair value of the identifiable assets and liabilities acquired on April 16, 2003. The consideration given in excess of the net liabilities assumed has been expensed as project related costs. The fair value of \$471,519 was calculated using a Black-Scholes pricing model with the following weighted average assumptions: risk free rate of 5.25%; dividend yield of \$Nil, volatility factor of 184% and an average expected life of the warrants in each year of 3 years.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

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#### 14. PROJECT DEVELOPMENT COSTS

- a) The project development costs incurred and expensed relating to the hydroelectric, wind farm, and transmission projects are as follows:

	<u>2007</u>	<u>2006</u>
Hydroelectric projects	\$ 336,701	\$ 193,146
Wind farm projects	1,423,401	613,338
Transmission projects	<u>908,304</u>	<u>1,197,251</u>
Total project related expenses for the year	<u>\$ 2,668,406</u>	<u>\$ 2,003,735</u>

Cumulative project costs incurred since the projects' inception amounted to \$13,751,892 (2006 - \$11,083,486).

- b) The project development expenses relating to hydroelectric projects in British Columbia are as follows:

	<u>2007</u>	<u>2006</u>
<b>Cascade</b>	<u>\$ 336,701</u>	<u>\$ 171,119</u>
<b>Slollicum</b>	<u>-</u>	<u>17,995</u>
<b>Great Central Lake</b>	<u>-</u>	<u>4,032</u>
	<u>\$ 336,701</u>	<u>\$ 193,146</u>
<b>Cumulative Hydro Project Costs</b>	<u>\$ 5,843,853</u>	<u>\$ 5,507,152</u>

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 14. PROJECT DEVELOPMENT COSTS (Continued)

- c) The project related development expenses relating to wind farm projects in British Columbia are as follows:

	<u>2007</u>	<u>2006</u>
Knob Hill	\$ 583,303	\$ 434,278
God's Pocket	51,383	2,013
Shushartie Mountain	217,513	4,454
Hushamu	59,791	16,665
Windy Ridge	61,402	1,034
Nimpkish	69,009	6,649
Other projects under preparation	<u>381,000</u>	<u>148,245</u>
Total project related expenses for the year	<u>\$ 1,423,401</u>	<u>\$ 613,338</u>
<b>Cumulative Wind Farm Project Costs</b>	<u>\$ 5,450,778</u>	<u>\$ 4,027,377</u>

- d) The project related development expenses relating to transmission projects in Canada and the United States are as follows:

	<u>2007</u>	<u>2006</u>
Transmission projects	<u>\$ 908,304</u>	<u>\$ 1,197,251</u>
<b>Cumulative Transmission Project Costs</b>	<u>\$ 2,457,261</u>	<u>\$ 1,548,957</u>

#### 15. SUPPLEMENTAL DISCLOSURE FOR NON-CASH INVESTING AND FINANCING ACTIVITIES

During the years ended December 31, 2007 and 2006 the Company had the following non-cash financing and investing activities:

- i) committed to issuing 2,702,889 (2006 – 85,362) common shares pursuant to the conversion of \$913,837 (2006 - \$27,818) of principal and \$184,835 (2006 - \$9,548) of accrued interest thereto of convertible debentures;
- ii) allocated \$98,300 (2006- \$59,186) to common shares pursuant to the exercise of options;
- iii) allocated \$107,801 (2006 - \$84,995) to common shares pursuant to the exercise of special warrants;
- iv) issued \$1,207,403 (\$1,218,000 USD) convertible debenture in exchange for loans payable to related parties;
- v) issued \$2,250,000 convertible debenture in exchange for loans payable to related parties.

## SEA BREEZE POWER CORP.

### Notes to Consolidated Financial Statements December 31, 2007 and 2006

(Stated in Canadian Dollars)

#### 16. INCOME TAXES

A reconciliation of income taxes at statutory rates to the Company's effective income tax expense is as follows:

	<u>2007</u>	<u>2006</u>
Statutory tax rate	34%	34%
Expected income tax recovery	\$ (2,167,000)	\$ (1,756,000)
Non-deductible differences	1,533,000	1,170,000
Future income tax expense (benefit) resulting from change in tax rate	1,672,000	-
Unrecognized tax losses and change in valuation allowance	<u>(1,038,000)</u>	<u>586,000</u>
Income tax provision	<u>\$ -</u>	<u>\$ -</u>

Future tax assets (liabilities) of the Company are as follows:

	<u>2007</u>	<u>2006</u>
Project development costs	\$ 4,309,000	\$ 4,815,000
Operating losses	2,541,000	2,623,000
	<u>6,850,000</u>	<u>7,438,000</u>
Less: Valuation allowance	<u>(6,850,000)</u>	<u>(7,438,000)</u>
Future tax asset (liability) recognized	<u>\$ -</u>	<u>\$ -</u>

As at December 31, 2007, the Company has incurred operating income tax losses totalling \$9,421,000 which expire from 2008 to 2027 as follows:

2008	\$ 776,000
2009	\$ 462,000
2010	\$ 1,274,000
2014	\$ 1,479,000
2015	\$ 1,985,000
2026	\$ 1,687,000
2027	\$ 1,758,000

A valuation allowance has been recorded to reduce the net benefit recorded in the financial statements related to these future tax assets. The valuation allowance is deemed necessary as a result of the uncertainty associated with the ultimate realization of these tax assets.

## **SEA BREEZE POWER CORP.**

### **Notes to Consolidated Financial Statements December 31, 2007 and 2006**

(Stated in Canadian Dollars)

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#### **17. FINANCIAL INSTRUMENTS**

a) Fair Value of Short Term Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, deposits, accounts payable and accrued liabilities, and loans payable to related parties. Unless otherwise stated, the fair value of the financial instruments approximates their carrying value, due to their short term to maturity.

b) Convertible Debenture and Interest Rate Risk

The Company's debentures detailed in Note 12 are all convertible at the option of the holders into common shares of the Company and are issued with interest payable at rates less than normal market rates under similar conditions without the conversion feature.

Therefore, should the holder of such debentures not elect to exercise their conversion rights, replacement funds would not likely be available to repay the debentures on their respective maturity dates at equivalent rates. No reliable estimate can be made as to the financial amount of such risk.

#### **18. COMMITMENT**

The Company leases its office premises in Vancouver, Canada. The office lease commenced on October 1, 2006 and ends September 30, 2008. The future minimum lease payment for 2008 is \$105,183.

#### **19. SEGMENTED INFORMATION**

The Company's activities are in the power generation and transmission industry. As at December 31, 2007, all of the Company's assets were in Canada.

#### **20. SUBSEQUENT EVENTS**

Subsequent to December 31, 2007, the Company:

- a) Issued 1,815,668 common shares for proceeds of \$272,350 pursuant to the exercise of special warrants.
- b) Granted 3,578,542 stock options at an exercise price of \$0.31 to employees, consultants and directors of the Company.