

Consolidated financial statements

Legend Power Systems Inc.

September 30, 2017



Building a better
working world

Independent auditors' report

To the Shareholders of
Legend Power Systems Inc.

We have audited the accompanying consolidated financial statements of **Legend Power Systems Inc.**, which comprise the consolidated statements of financial position as at September 30, 2017 and 2016, and the consolidated statements of loss and comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of **Legend Power Systems Inc.** as at September 30, 2017 and 2016, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Vancouver, Canada
January 23, 2018

Ernst & Young LLP

Chartered Professional Accountants



Legend Power Systems Inc.

Consolidated statement of financial position

As at September 30

	2017	2016
	\$	\$
Assets		
Current		
Cash	1,160,127	1,132,547
Receivables <i>[note 5]</i>	2,637,092	504,624
Inventory <i>[note 6]</i>	1,010,276	469,666
Prepaid expenses and deposits	84,693	49,416
Total current assets	4,892,188	2,156,253
Property and equipment, net <i>[note 7]</i>	84,405	40,062
Intangibles <i>[note 8]</i>	107,060	122,939
	5,083,653	2,319,254
Liabilities and shareholders' equity		
Current		
Accounts payable	592,760	401,670
Accrued liabilities	184,942	221,779
Total current liabilities	777,702	623,449
Warranty provision <i>[note 9]</i>	215,231	192,000
Total liabilities	992,933	815,449
Shareholders' equity		
Share capital <i>[note 10]</i>	38,421,253	33,458,288
Contributed surplus <i>[note 10]</i>	8,331,942	8,861,305
Deficit	(42,662,475)	(40,815,788)
Total shareholders' equity	4,090,720	1,503,805
	5,083,653	2,319,254

See accompanying notes

On behalf of the Board:

Director

Director

Legend Power Systems Inc.

Consolidated statement of loss and comprehensive loss

Year ended September 30

	2017	2016
	\$	\$
Revenue [note 4]	4,228,756	2,079,126
Cost of sales	2,573,418	1,448,896
Gross profit	1,655,338	630,230
Expenses		
Amortization and depreciation	160,977	187,622
Bad debts	—	2,500
General and overhead	591,722	515,467
Professional fees	124,627	99,610
Product development	249,967	58,556
Salaries and consulting fees	1,968,328	1,698,547
Share-based compensation	366,305	415,127
Warranty	61,021	90,970
	3,522,947	3,068,399
Loss before other items	(1,867,609)	(2,438,169)
Foreign exchange gain (loss)	4,998	(4,082)
Other income	15,924	4,888
	20,922	806
Net loss and comprehensive loss for the year	(1,846,687)	(2,437,363)
Basic and diluted loss per share	(0.02)	(0.04)
Weighted average number of common shares outstanding	78,922,080	66,390,800

See accompanying notes

Legend Power Systems Inc.

Consolidated statement of changes in shareholders' equity

Year ended September 30

	Number of shares issued	Share capital	Contributed surplus	Deficit	Total shareholders' equity
	#	\$	\$	\$	\$
Balance at September 30, 2015	59,397,389	32,008,782	7,640,496	(38,378,425)	1,270,853
Common shares and warrants issued for cash	8,300,000	1,660,000	—	—	1,660,000
Common shares and warrants issued for finder's fees	498,750	99,750	—	—	99,750
Share issue costs for financing	—	(125,404)	—	—	(125,404)
Common shares issued for warrants exercised	2,247,807	620,842	—	—	620,842
Fair value for warrants exercised	—	(879,272)	879,272	—	—
Fair value for warrants exercised for finder's fees	—	(52,835)	52,835	—	—
Fair value reversed for warrants exercised	—	126,425	(126,425)	—	—
Share-based compensation	—	—	415,127	—	415,127
Net loss for the year	—	—	—	(2,437,363)	(2,437,363)
Balance at September 30, 2016	70,443,946	33,458,288	8,861,305	(40,815,788)	1,503,805
Common shares issued for warrants exercised	12,342,312	4,067,297	—	—	4,067,297
Fair value reversed for warrants exercised	—	895,668	(895,668)	—	—
Share-based compensation	—	—	366,305	—	366,305
Net loss for the year	—	—	—	(1,846,687)	(1,846,687)
Balance at September 30, 2017	82,786,258	38,421,253	8,331,942	(42,662,475)	4,090,720

See accompanying notes

Legend Power Systems Inc.

Consolidated statement of cash flows

Year ended September 30

	2017	2016
	\$	\$
Operating activities		
Net loss for the year	(1,846,687)	(2,437,363)
Add (deduct) items not involving cash		
Allowance for doubtful debts	—	2,500
Amortization and depreciation	160,977	187,622
Inventory write-down	15,162	179,081
Share-based compensation	366,305	415,127
Warranty provision	23,231	68,000
Changes in non-cash working capital balances related to operations		
Increase in inventory	(555,772)	(6,608)
Increase in receivables, prepaids and deposits	(2,167,745)	(308,491)
Increase in accounts payable and accrued liabilities	154,253	282,306
Cash used in operating activities	(3,850,276)	(1,617,826)
Investing activities		
Purchase of property, equipment and intangibles	(189,441)	(40,931)
Cash used in investing activities	(189,441)	(40,931)
Financing activities		
Issue of common shares	—	1,660,000
Warrant exercise proceeds	4,067,297	620,842
Share issue costs	—	(25,654)
Cash provided by financing activities	4,067,297	2,255,188
Net increase in cash during the year	27,580	596,431
Cash, beginning of year	1,132,547	536,116
Cash, end of year	1,160,127	1,132,547

See accompanying notes

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

1. Nature of business

Legend Power Systems Inc. [hereafter referred to as the “Company” or “Legend”] is incorporated under the laws of the Province of British Columbia and was established as a legal entity on May 31, 2001. The Company’s principal business activities are the marketing of a patented device, the Electrical Harmonizer, designed to provide energy savings through voltage optimization to commercial and industrial customers. The Company’s common shares are listed on the TSX Venture Exchange.

The Company’s principal office is located at 1480 Frances Street, Vancouver, B.C., V5L 1Y9, Canada.

2. Basis of preparation, statement of compliance and going concern

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards [“IFRS”]. These consolidated financial statements have been prepared on a going concern basis, under the historical cost convention.

These consolidated financial statements have been approved for issuance by the Board of Directors on January 23, 2018. The going concern basis of accounting assumes the Company will continue to realize the value of its assets and discharge its liabilities and other obligations in the ordinary course of business. Should the Company be required to realize the value of its assets in other than the ordinary course of business, the net realizable value of its assets may be materially less than the amounts shown in the consolidated financial statements. These consolidated financial statements do not include any adjustments to the amounts and classifications of assets and liabilities that may be necessary should the Company be unable to repay its liabilities and meet its other obligations in the ordinary course of business or to continue operations.

As at September 30, 2017, the Company had working capital of \$4,122,399 [2016 – \$1,532,804] and an accumulated deficit of \$42,662,475 [2016 – \$40,815,788]. During the year ended September 30, 2017, the Company incurred a net loss of \$1,846,687 [2016 – \$2,437,363]. Based on the working capital as at September 30, 2017, cash proceeds from subsequent exercise of warrants [note 14], estimated cash requirements and projected sales and gross margins for fiscal 2018, management believes the Company has sufficient capital to continue business operations over the next twelve months from the consolidated balance sheet date. In the long term, the continued business operations of the Company are dependent upon economic and market factors which involve uncertainties including profitable commercialization of its products and/or the Company’s ability to obtain adequate financing. There can be no assurance that the Company can achieve profitable commercialization of its products and/or obtain additional capital.

3. Summary of significant accounting policies

Basis of consolidation

The consolidated financial statements include the accounts of the Company and all of its subsidiaries. Subsidiaries are all corporations over which the Company is able, directly or indirectly, to control financial and operating policies, which is the authority usually connected with holding majority voting rights. Subsidiaries are fully consolidated from the date on which control is acquired by the Company. They are deconsolidated from the date that control by the Company ceases.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

The subsidiaries of the Company were all inactive during fiscal 2017. They are as follows:

0809882 B.C. Ltd. – (Canada)	100%
Legend Power Systems Corp. – (USA)	100%
LPSI (Barbados) Limited – (Barbados)	100%

Assets, liabilities, revenue and expenses of the subsidiaries are recognized in accordance with the Company's accounting policies. Inter-company transactions and balances are eliminated upon consolidation.

Foreign currency translation

Functional and presentation currency

The subsidiaries' functional currency is the Canadian dollar. The consolidated financial statements are presented in Canadian dollars.

Foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing on the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in comprehensive income or loss.

Equipment

Equipment is stated at historical cost less depreciation and, where necessary, write-downs for impairment. Depreciation is calculated using the declining balance method at the following annual rates:

Computer equipment	33%
Computer software	100%
Furniture and fixtures	33%
Leasehold improvements	20%

The useful lives, residual values and method of depreciation are reviewed at each financial year-end and adjusted if appropriate.

Patents

Patents are recorded at cost less accumulated amortization and, where necessary, write-downs for impairment. Amortization is calculated using the straight-line method over ten years based on the estimated useful life of the asset at the time of purchase. Patents are assessed for impairment whenever there is an indication they might be impaired. The amortization period and amortization method are reviewed at the end of each reporting period. Maintenance costs for patents are expensed as incurred.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

Research and development costs

Research costs are expensed as incurred. Development expenditures on an individual project are recognized as an intangible asset when the Company can demonstrate:

- The technical feasibility of completing the intangible asset so that the asset will be available for use or sale
- Its intention to complete and its ability and intention to use or sell the asset
- How the asset will generate future economic benefits
- The availability of resources to complete the asset
- The ability to measure reliably the expenditure during development

Following initial recognition of the development expenditure as an asset, the asset is carried at cost less any accumulated amortization and accumulated impairment losses. Amortization of the asset begins when development is complete and the asset is available for use. It is amortized over the period of expected future benefit. Amortization is recorded in cost of sales. During the period of development, the asset is tested for impairment annually.

Warranty provision

Warranty provisions for the expected cost of warranty obligations are recorded as an expense at the date of the sale of Electrical Harmonizers. The provision is for estimated costs of product replacement and replacement due to product malfunction after installation. The provision is based on management's best estimates incorporating a number of factors including historical warranty claims and cost experience and the type and duration of warranty coverage. The Company reviews its recorded product warranty provisions quarterly and any adjustment is recorded as an expense.

Current and deferred income taxes

The tax expense is comprised of current and deferred income taxes. Tax is recognized separately in the statement of loss and comprehensive loss, except to the extent that it relates to items recognized in other comprehensive income (loss) or directly in equity. In this case the income tax is also recognized in other comprehensive income (loss) or directly in equity, respectively.

Current tax

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the consolidated statement of financial position date. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred tax

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates [and laws] that have been enacted or substantively

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

enacted at the consolidated statement of financial position date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

Share-based payments

The fair value, at the grant date, of equity-settled share awards is charged to the consolidated statement of loss and comprehensive loss over the period for which the benefits of employee and others providing similar services are expected to be received. The corresponding accrued entitlement is recorded in contributed surplus. The fair value of awards is calculated using the Black-Scholes option pricing model which considers the following factors:

- Exercise price
- Life of the award
- Expected forfeitures
- Expected volatility
- Risk-free interest rate
- Current market price of the underlying shares

Warrants issued in equity financing transactions

The Company engages in equity financing transactions to obtain the funds necessary to continue operations. These equity financing transactions may involve issuance of common shares or units. Units typically comprise a certain number of common shares and share purchase warrants. Depending on the terms and conditions of each equity financing transaction, the warrants are exercisable into additional common shares at a price prior to expiry as stipulated by the terms of the transaction.

The Company has adopted a residual value method with respect to the measurement of common shares and share purchase warrants issued as private placement units. The fair value of the share purchase warrants issued in the private placements is determined by the Black-Scholes option pricing method on the announcement date. The balance is allocated to the common shares.

Financial instruments

All financial assets are initially recorded at fair value and designated upon inception into one of the following four categories: held to maturity, available for sale, loans and receivables or at fair value through profit or loss.

Financial assets classified as fair value through profit or loss are measured at fair value with unrealized gains and losses recognized through comprehensive income or loss. Cash is classified as fair value through profit or loss.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

Financial assets classified as loans and receivables and held to maturity are measured at amortized cost. Receivables are classified as loans and receivables.

Financial assets classified as available for sale are measured at fair value with unrealized gains and losses recognized in other comprehensive loss, except for losses in value that are considered other than temporary. At September 30, 2017, the Company has not classified any financial assets as available for sale or held to maturity.

Transaction costs associated with financial assets at fair value through profit or loss are expensed as incurred, while transaction costs associated with all other financial assets are included in the initial carrying amount of the asset.

All financial liabilities are initially recorded at fair value and designated upon inception as fair value through profit or loss or other financial liabilities.

Financial liabilities classified as other financial liabilities are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities.

Financial liabilities classified as fair value through profit or loss are measured at fair value with unrealized gains and losses recognized through comprehensive income or loss. At September 30, 2017, the Company has not classified any financial liabilities as fair value through profit or loss.

Revenue recognition

The Company generates revenue through product sales and product sales with installation services.

The total price of a customer arrangement is expected to vary depending on type of equipment and whether or not installation service is included. For those contracts that include installation services the Company utilizes management's best estimate of fair value for the products based upon normal pricing and discounting practices for the product when sold separately. Fair value of installation services is estimated based on third party contractor pricing. The total contractual consideration is allocated between product and installation services based on their relative fair value. Revenue from products and services is recognized so long as persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is reasonably assured.

Inventory

Inventory is measured at the lower of cost or net realizable value. Transformer and controller costs are assigned to inventory by using specific identification of individual costs. Component inventory is measured at weighted average cost.

Critical judgments and estimation uncertainty

The preparation of these consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and reported amounts of revenue and expenses during the reporting period. Actual outcomes could differ from these estimates. These consolidated financial statements include estimates which, by their nature,

Notes to consolidated financial statements

September 30, 2017

are uncertain. The impacts of such estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Critical judgments

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements:

- [i] Management is required to assess whether to test its patent and property and equipment for impairment in accordance with IAS 36, *Impairment of Assets*. In assessing whether there is any indication that long-lived assets may be impaired, management is required to make judgments about whether there are any internal or external indicators of impairment.

At September 30, 2017, management has determined no impairment indicators were present with respect to the Company's patents.

- [ii] Under IAS 18, *Revenue*, management is required to assess, for each sale of goods, whether it is probable that the Company will be able to collect from the customer on the sale. Management is not aware of any circumstances that would impact the Company's ability to collect the amounts outstanding on the sales made.
- [iii] For those contracts that include installation services the Company utilizes management's best estimate of fair value for the products and revenue from installation services is estimated based on third party contractor pricing which is included in the consolidated statement of loss and comprehensive loss.

Estimation uncertainty

The following are key assumptions concerning the future and other key sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year:

- [i] At September 30, 2017, provisions for impairment of inventory and of development costs included in intangibles were made using the best estimate of the net realizable value.
- [ii] At September 30, 2017, provisions for future warranty expense was forecast by the Company based on recent historical experience and expectations of future warranty claim activity.

Impairment of long-lived assets

Impairment tests for long-lived assets are performed when there is an indication of impairment. At each reporting date, an assessment is made to determine whether there are any indications of impairment. If any indication of impairment exists, an estimate of the long-lived asset's recoverable amount is calculated. The recoverable amount is determined as the higher of fair value less costs of disposal and the asset's value in use. If the carrying value of

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

a long-lived asset exceeds its recoverable amount, the asset is impaired and an impairment loss is charged to comprehensive income or loss so as to reduce the carrying amount of the long-lived asset to its recoverable amount.

Loss per share

Basic and diluted loss per share is determined by dividing the net loss for the year by the weighted average number of common shares outstanding during the reporting period. Diluted loss per share is not separately presented, as the effect of securities exercisable into common shares would reduce the amount presented as loss per share.

New accounting standards

New accounting standards not yet adopted

The following is an overview of new accounting standards that the Company will be required to adopt in future years. The Company does not expect to adopt any of these standards before their effective dates. The Company continues to evaluate the impact of these standards on its consolidated financial statements.

- [i] IFRS 9, *Financial Instruments*. This standard partially replaces IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 measures financial assets, after initial recognition, at either amortized cost or fair value. The existing IAS 39 standard classifies financial assets into four measurement categories. The standard is effective for annual periods beginning on or after January 1, 2018. In the year of adoption, the Company is required to provide additional disclosures relating to the reclassified financial assets and liabilities.
- [ii] IFRS 15, *Revenue from Contracts with Customers*. IFRS 15 is effective for annual periods beginning on or after January 1, 2018. IFRS 15 specifies how and when to recognize revenue as well as requires entities to provide users of financial statements with more informative and relevant disclosures. The standard supersedes IAS 18, *Revenue*, IAS 11, *Construction Contracts*, and a number of revenue-related interpretations. The new standard will apply to nearly all contracts with customers; the main exceptions are leases, financial instruments and insurance contracts.

4. Segments

The Company has one operating segment and operates in two geographical areas, Canada and the United States. Substantially all of the Company's sales in 2017 and 2016 were in Canada. Two customers accounted for 11.9% and 15.1% respectively of the Company's sales for the year ended September 30, 2017. One customer accounted for 49.8% of the Company's sales for the year ended September 30, 2016. Product sales and installation services accounted for 79% and 21% of revenue respectively for the years ended September 30, 2017 and 2016.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

5. Receivables

	Total due	0-30 days	31-60 days	61-90 days	91-120 days	Over 120 days
	\$	\$	\$	\$	\$	\$
September 30, 2016	314,051	80,810	16,949	—	114,761	101,531
September 30, 2017	2,637,092	1,935,881	431,620	—	125,610	143,981
					2017	2016
					\$	\$
Accounts receivable					2,637,092	314,051
GST refundable					—	190,573
					2,637,092	504,624

Receivables from three customers account for 10.9%, 13.1%, and 16.4%, respectively of the Company's receivables balance for a total of 40.4% in aggregate at September 30, 2017. Receivables from four customers accounted for 33%, 15%, 16% and 29%, respectively of the Company's receivables balance for a total of 93% in aggregate at September 30, 2016.

6. Inventory

Inventories consist of the following:

	2017	2016
	\$	\$
Finished goods	142,602	108,747
Transformers and components	867,674	360,919
	1,010,276	469,666

During the year ended September 30, 2017, inventories were recognized as cost of sales in the amount of \$1,712,032 [2016 – \$470,744] and inventory impairment was also recognized as cost of sales in the amount of \$15,162 [2016 – \$179,081]. Inventory impairments resulted from the write down of components to their estimated net realizable value due to the expectation that they will not be used in the production of controllers for transformers sold.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

7. Property and equipment

	Computer equipment	Computer software	Furniture and fixtures	Leasehold improvements	Total
	\$	\$	\$	\$	\$
Cost					
Balance at September 30, 2015	72,399	91,973	277,967	12,152	454,491
Additions	3,797	8,874	19,607	8,653	40,931
Balance at September 30, 2016	76,196	100,847	297,574	20,805	495,422
Additions	25,749	2,586	53,904	139	82,378
Balance at September 30, 2017	101,945	103,433	351,478	20,944	577,800
Accumulated depreciation					
Balance at September 30, 2015	64,817	85,039	271,793	9,889	431,538
Additions	3,945	8,502	8,291	3,084	23,822
Balance at September 30, 2016	68,762	93,541	280,084	12,973	455,360
Additions	9,036	8,662	18,385	1,952	38,035
Balance at September 30, 2017	77,798	102,203	298,469	14,925	493,395
Net book value					
At September 30, 2016	7,434	7,306	17,490	7,832	40,062
At September 30, 2017	24,147	1,230	53,009	6,019	84,405

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

8. Intangibles

In 2007, the Company purchased the worldwide patents for the Electrical Harmonizer. The patents are amortized over their estimated remaining lives.

	Patents \$	Development costs \$	Total \$
Cost			
Balance at September 30, 2015	1,638,099	—	1,638,099
Additions	—	—	—
Balance at September 30, 2016	1,638,099	—	1,638,099
Additions	—	107,060	107,060
Balance at September 30, 2017	1,638,099	107,060	1,745,159
Amortization			
Balance at September 30, 2015	1,351,360	—	1,351,360
Additions	163,800	—	163,800
Balance at September 30, 2016	1,515,160	—	1,515,160
Additions	122,939	—	122,939
Balance at September 30, 2017	1,638,099	—	1,638,099
Carrying amount			
At September 30, 2016	122,939	—	122,939
At September 30, 2017	—	107,060	107,060

9. Warranty provision

Included in the amount expensed during the year ended September 30, 2017 is \$23,231 for replacement of controller units [2016 – \$90,970].

	Total \$
Balance at September 30, 2015	124,000
Warranty fulfillments	(22,970)
Additional provision, net	90,970
Balance at September 30, 2016	192,000
Warranty fulfillments	(37,790)
Additional provision, net	61,021
Balance at September 30, 2017	215,231

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

The Company provides a warranty on its equipment for a period of 10 years. The warranty provision will be used to fulfill warranty claims, should they arise, over the 10-year warranty period provided to customers.

10. Share capital and contributed surplus

The Company's authorized share capital is an unlimited number of common shares without par value. All issued common shares are fully paid. Contributed surplus consists of the accumulated fair value of common share options recognized as share-based compensation, fair value of warrants and fair value of broker warrants.

Issued share capital

[a] During the year ended September 30, 2017, the following transactions occurred:

[i] During the year, 12,342,312 warrants were exercised at between \$0.15 and \$0.40 each for total proceeds of \$4,067,297. The fair value reversal for these warrants was \$895,668.

[b] During the year ended September 30, 2016, the following transactions occurred:

[i] During September 2016, 356,665 warrants were exercised at \$0.15 each for total proceeds of \$53,500.

[ii] During July 2016, 1,780,031 warrants were exercised at \$0.30 each for total proceeds of \$534,009 and 254,302 warrants with an exercise price of \$0.30 expired unexercised.

[iii] On May 9, 2016, the Company received \$33,333 from the exercise of 111,111 warrants at \$0.30 each.

[iv] On December 30, 2015, the Company completed a private placement in which it issued a total of 8,300,000 units at \$0.20 per unit for aggregate gross proceeds of \$1,660,000. Each unit consisted of one common share and one common share purchase warrant. Each warrant entitled the holder to purchase one share at a price of \$0.40 per share until December 30, 2017. The Company paid finder's fees on the funds raised, satisfied by the issuance of 498,750 units.

The fair value of the unit warrants, estimated using the Black-Scholes option pricing model, is \$932,107. The assumptions used were: a risk-free interest rate of 0.48%; an estimated volatility of 107.98%; an expected life of two years; an expected dividend yield of 0%. The residual value of \$780,728 was attributed to the common shares.

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

Stock options

The Company has an incentive share option plan [the "Plan"]. Under the Plan a total of 10% of the Company's outstanding common shares are reserved for the issuance of share options to directors, officers, employees and consultants. The terms of each option award are fixed by the directors at the time of grant. Share options awarded have a maximum term of five years. Share options vest over various time periods from the grant date to five years at the discretion of the Board of Directors.

A summary of the Company's share options at September 30, 2017, including the changes during the year, is as follows:

	Share options	Weighted average
	#	exercise price
		\$
Balance, September 30, 2015	4,856,160	0.41
Granted	1,941,666	0.25
Forfeited	(166,666)	0.42
Expired	(566,664)	0.63
Balance, September 30, 2016	6,064,496	0.34
Granted	2,825,000	0.30
Forfeited	(446,667)	0.31
Expired	(183,333)	0.42
Balance, September 30, 2017	8,259,496	0.32

The following table summarizes share options outstanding and exercisable at September 30, 2017:

Options outstanding	Options exercisable	Exercise price	Expiry date
		\$	
541,667	541,667	0.30	May 21, 2018
557,830	557,830	0.30	August 20, 2018
910,000	910,000	0.20	February 23, 2019
1,480,000	1,233,332	0.55	September 30, 2019
170,000	80,000	0.35	May 31, 2018
1,599,999	801,666	0.25	January 26, 2021
175,000	87,501	0.25	February 9, 2021
250,000	187,500	0.30	October 10, 2019
2,300,000	—	0.27	May 2, 2022
275,000	—	0.56	September 18, 2022
8,259,496	4,399,496		

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

The fair value of share options awarded to employees, directors and consultants was estimated on the respective date of award using the Black-Scholes option pricing model with the following assumptions:

	<u>2017</u>	<u>2016</u>
Risk-free interest rate	1.38%	1.50%
Estimated volatility	108.55%	112.84%
Expected life [years]	3.57	3.63

The Black-Scholes option pricing model was developed for use in estimating the fair value of share options that have no vesting provisions and are fully transferable. Also, option pricing models require the use of estimates and assumptions including the expected volatility. The Company uses expected volatility rates which are based upon historical volatility rates. Changes in the underlying assumptions can materially affect the fair value estimates.

During the year ended September 30, 2017, the Company granted 2,825,000 [2016 – 1,774,999] incentive stock options with a weighted average fair value of \$0.20 each [2016 – \$0.17] using the Black-Scholes option pricing model.

Warrants

A summary of the number of common shares reserved pursuant to the Company's outstanding warrants is as follows:

	<u>Number of warrants</u>	<u>Weighted average exercise price</u> \$
Balance, September 30, 2015	10,510,053	0.29
Issued	8,798,750	0.40
Exercised	(2,247,807)	0.28
Expired	(254,302)	0.30
Balance, September 30, 2016	16,806,694	0.35
Exercised	(12,342,312)	0.33
Balance, September 30, 2017	4,464,382	0.40

The following table summarizes information of the number of common shares reserved pursuant to the warrants outstanding and exercisable at September 30, 2017:

<u>Number of warrants</u>	<u>Exercise price</u> \$	<u>Expiry date</u>
4,464,382	0.40	December 30, 2017

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

11. Commitments

On February 9, 2016, the Company entered into an agreement to lease premises in Vancouver, B.C. which requires the following payments in each of the following fiscal years:

	\$
2018	125,240
2019	128,580
2020	131,920
	<u>385,740</u>

The lease payments are subject to changes or increases in additional rent, generally described as the Company's portion of the landlord's common area charges and property taxes.

The Company has an employment agreement with the President and CEO of the Company that contains severance provisions whereby termination without cause could result in additional costs to the Company unless renegotiated or settled otherwise.

12. Related party disclosures

The Company entered into the following related party transactions during the years ended September 30, 2017 and 2016.

During the years ended September 30, 2017 and 2016, the following amounts were incurred with respect to key management personnel; being the Company's CEO and the CFO:

[i] Transactions with key management personnel

	2017	2016
	\$	\$
Salaries and fees to key management employees	339,090	291,535
Share-based compensation	162,269	230,740

[ii] Transactions with directors

The following amounts were incurred with respect to non-executive directors of the Company:

	2017	2016
	\$	\$
Share-based compensation	72,569	75,296

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

13. Income taxes

Unrecognized deferred tax assets of the Company as at September 30, 2017 and 2016 are as follows:

	2017	2016
	\$	\$
Operating loss carryforwards	6,081,000	5,715,000
Property and equipment	380,000	370,000
Other	187,000	226,000
	<u>6,648,000</u>	<u>6,311,000</u>
Assets not recognized	(6,648,000)	(6,311,000)
Net deferred income tax assets	<u>—</u>	<u>—</u>

The following temporary differences have not been set up as deferred tax assets:

	2017	Expiry	2016	Expiry
	\$		\$	
Operating loss carryforwards	22,964,000	2022 to 2037	21,546,000	2022 to 2036
Property and equipment	1,445,000	none	1,407,000	none
Share issuance cost	243,000	2038 to 2040	414,000	2037 to 2040
Patent	1,638,000	none	1,515,000	none
Taxable capital losses	240,000	none	240,000	none
Warranty provision	215,000	none	192,000	none

There are approximately \$22,300,000 Canadian operating losses and \$600,000 US operating losses.

The recovery of income taxes shown in the statements of loss and comprehensive loss and deficit differs from the amounts obtained by applying statutory rates to the loss before provision for income taxes as follows:

	2017	2016
	\$	\$
Net income (loss) before taxes	(1,846,687)	(2,437,363)
Combined federal and provincial income tax rate	26.25%	26.25%
Expected income tax recovery	(485,000)	(640,000)
Non-deductible expenses	99,000	109,000
Share issue costs incurred during the year	—	(33,000)
Unrecognized benefit of tax attributes	337,000	515,000
Other including differences in foreign tax rates and foreign exchange	49,000	49,000
Actual income tax recovery	<u>—</u>	<u>—</u>

Legend Power Systems Inc.

Notes to consolidated financial statements

September 30, 2017

14. Subsequent events

Subsequent to September 30, 2017, 4,464,382 common share purchase warrants were exercised at \$0.40 each for total proceeds of \$1,785,753.

