Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS
For the three months ended December 31, 2018 and 2017
(Unaudited – Prepared by Management)

(Expressed in Canadian Dollars)

Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Three months ended December 31, 2018, and 2017

(Unaudited - Expressed in Canadian Dollars)

NOTICE OF NO AUDITOR REVIEW OF
CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited condensed interim consolidated financial statements of Legend Power Systems Inc. for the three months ended December 31, 2018 have been prepared by and are the responsibility of the Company's management.

The auditor of Legend Power Systems Inc. has not performed a review of the unaudited condensed interim consolidated financial statements for the three-month period ended December 31, 2018.

Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Unaudited - Expressed in Canadian Dollars)

	Notes	December 31, 2018 $	September 30, 2018 (Audited) $
ASSETS			
Current			
Cash and cash equivalents		9,613,434	10,046,366
Trade Receivables	6(i)	1,324,086	1,573,298
Due from customers on contract	6(ii)	465,291	1,361,126
Prepaid expenses and deposits		86,614	192,603
Inventory	7	1,632,112	1,066,592
		13,121,537	14,239,985
Property and equipment	3,8	138,800	144,291
Intangible assets	3,9	239,075	129,610
		13,499,412	**14,513,886**
LIABILITIES			
Current			
Accounts payable	10	500,528	501,138
Accrued liabilities		70,871	79,665
Warranty provision	11	38,630	40,863
		610,029	621,666
Warranty provision	11	262,540	269,134
		872,569	890,800
Shareholders' equity			
Share capital	12(i)	50,409,303	50,409,303
Contributed surplus	12(ii)(iii)	8,530,732	8,435,643
Deficit		(46,313,192)	(45,221,860)
		12,626,843	13,623,086
		13,499,412	**14,513,886**

Summary of Significant Accounting Policies (Note 3)
Segments (Note 4)
Commitments (Note 13)

APPROVED BY THE BOARD OF DIRECTORS AND AUTHORIZED FOR ISSUE ON FEBRUARY 26, 2019

"Michael Atkinson", Director *"Randy Buchamer"*, Director

The accompanying notes are an integral part of these interim consolidated financial statements.

Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS

(Unaudited - Expressed in Canadian Dollars)

		For the three months ended December 31,	
		2018	**2017**
	Notes	**$**	**$**
Revenue	5	403,400	1,282,707
Cost of sales	3,5	76,832	803,923
Gross margin		326,568	478,784
Expenses			
Salaries and consulting		892,959	731,764
General and overhead		300,108	162,453
Selling costs	3	100,621	111,787
Share-based compensation	12(ii)	95,089	97,093
Professional fees		34,607	24,000
Warranty provision	11	35,314	17,409
Product development		11,311	66,908
Foreign exchange (gain) loss		(21,707)	6,415
Amortization and depreciation	3,8,9	36,541	12,039
		1,484,843	1,229,868
Operating loss		(1,158,275)	(751,084)
Other income		66,943	3,756
Net loss and comprehensive for the period		**(1,091,332)**	**(747,328)**
Basic and diluted loss per share		(0.01)	(0.01)
Weighted average number of common shares outstanding		101,462,803	84,928,045

The accompanying notes are an integral part of these interim consolidated financial statements.

Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited - Expressed in Canadian Dollars)

	Notes	Number of Shares Issued	Capital Stock	Contributed Surplus	Deficit	Total Shareholders' Equity
		#	$	$	$	$
Balance at September 30, 2017 (Audited)		**82,786,258**	**38,421,253**	**8,331,942**	**(42,662,475)**	**4,090,720**
Warrants exercise	12(iii)	4,464,382	2,258,693	(472,940)	-	1,785,753
Option exercise	12(ii)	47,830	12,432	-	-	12,432
Share-based compensation	12(ii)	-	-	97,093	-	97,093
Net loss for the period		-	-	-	(747,328)	(747,328)
Balance at December 31, 2017		**87,298,470**	**40,692,378**	**7,956,095**	**(43,409,803)**	**5,238,670**
Common shares issued with public offering	12(i)	13,156,000	10,524,800	-	-	10,524,800
Share issue costs	12(i)	-	(1,171,307)	225,388	-	(945,919)
Option exercise	12(ii)	1,008,333	363,432	(76,280)	-	287,152
Share-based compensation	12(ii)	-	-	330,440	-	330,440
Net loss for the period		-	-	-	(1,812,057)	(1,812,057)
Balance at September 30, 2018 (Audited)		**101,462,803**	**50,409,303**	**8,435,643**	**(45,221,860)**	**13,623,086**
Share-based compensation	12(ii)	-	-	95,089	-	95,089
Net loss for the period		-	-	-	(1,091,332)	(1,091,332)
Balance at December 31, 2018		**101,462,803**	**50,409,303**	**8,530,732**	**(46,313,192)**	**12,626,843**

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

Legend Power Systems Inc.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited - Expressed in Canadian Dollars)

	Notes	For the three months ended December 31, 2018 $	2017 $
Cash flows used in operating activities			
Loss for the period		(1,091,332)	(747,328)
Items not affecting cash:			
Amortization and depreciation	8,9	36,541	12,039
Share-based compensation	12(ii)	95,089	97,093
Warranty provision	11	35,314	(141)
Foreign exchange (gain) loss		(21,707)	6,415
Inventory write-down (reversal)	7	(138,891)	5,249
Changes in non-cash working capital items:			
Receivables, prepaids and deposits		334,888	(752,236)
Due from customers on contract		895,837	517,099
Inventory		(378,907)	(311,131)
Accounts payable and accrued liabilities		(105,760)	271,194
		(338,928)	(901,747)
Cash flows used in investing activities			
Purchase of property and equipment	3,8	(12,602)	(27,869)
Product development costs	3,9	(125,490)	-
Interest income received		25,835	3,756
		(112,257)	(24,113)
Cash flows from financing activities			
Warrants exercise proceeds	12(iii)	-	1,785,753
Options exercise proceeds	12(ii)	-	12,432
		-	1,798,185
Effect of foreign exchange translation in cash		18,253	-
Net change in cash and cash equivalents for the period		(451,185)	872,325
Cash and cash equivalents, beginning of period		10,046,366	1,160,127
Cash and cash equivalents, end of period		**9,613,434**	**2,032,452**
Non-cash transactions			
Purchase of property and equipment net of trade payables		1,140	-
Purchase of intangible assets net of trade payables		1,283	-

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

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 June 4, 1987. The Company's principal business activities are the marketing of a patented device, the "SmartGATE™", 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, BC, V5L 1Y9, Canada

2. BASIS OF PREPARATION AND STATEMENT OF COMPLIANCE

These condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – *Interim financial reporting* (International Account Standard) which is in accordance with International Financial Reporting Standards ("IFRS"). They do not include all of the information required for full annual financial statements and should be read in conjunction with the consolidated financial statements of the Company for the year ended September 30, 2018. These condensed interim consolidated financial statements have been prepared on a going concern basis, under the historical cost convention, except for certain financial assets and financial liabilities which are measured at fair value.

As at December 31, 2018, the Company had working capital of $12,511,508 (September 30, 2018 - $13,618,319) and an accumulated deficit of $46,313,192 (September 30, 2018 - $45,221,860). During the three months ended December 31, 2018 the Company incurred a net loss of $1,091,332 (2017 - $747,328).

Based on working capital as at December 31, 2018 and estimated cash requirements, projected sales and gross margins for fiscal 2019, management believes the Company has sufficient capital to continue business operations over the next twelve months. 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

The significant changes to the Company's accounting policies, judgements or estimates from those disclosed in the consolidated financial statements for the year ended September 30, 2018, have been disclosed below.

Comparatives

Certain prior period amounts are reclassified to conform with the presentation adopted in the current period. The reclassified amounts in the statement of financial position is an amount of $8,654 from property and equipment to intangible assets from change in presentation of computer software. The reclassified amounts in the consolidated statement of loss and comprehensive loss are: an amount of $45,277 related to commissions and sale distribution costs, previously recorded to costs of sales and an amount of $66,510 previously recorded to general and overhead costs pertaining to costs related to sales were reclassified to selling costs for a total of $111,787.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

Changes in accounting policies

IAS 2 – *Inventories*

Inventory is measured at the lower of cost or net realizable value. Transformer and controller costs are assigned to inventory at actual costs. The Company has historically measured all other inventory components on a first in first out (FIFO) basis, however effective October 1, 2018 the Company elected to change its method of component inventory measurement to a weighted average method. Management believes this change will provide greater efficiency and practicability in inventory measurement. The switch from FIFO to weighted average inventory measurement represents a change in accounting policy which is typically accounted for retrospectively in the Company's financial statements as if the new accounting policy was always in place. The retrospective application of this change of measurement for prior comparative periods is however impracticable due to a lack of sufficient data to enable objective assessment of the effect of the change and it would not be feasible to reconstruct such data. The Company has thus applied the new policy prospectively from the beginning of the earliest period feasible which commenced October 1, 2018. The inventory amount reflected in these statements as of December 31, 2018 was calculated under the new method.

New standards

a) 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. Existing IAS 39 classifies financial assets into four measurement categories. The Company adopted the standard effective October 1, 2018. In the year of adoption, the Company is required to provide additional disclosures relating to the reclassified financial assets and liabilities. The adoption of IFRS 9 – *Financial Instruments* had no impact in the Company's financial statements.

The Company's financial instruments consist of cash and cash equivalents, trade receivables and accounts payable. The carrying values of these financial instruments approximate their fair values because of their short-term nature.

<u>Cash and cash equivalents</u>
Cash and cash equivalents are classified as fair value through profit or loss. Cash and cash equivalents are comprised of checking account of $717,996 (September 30, 2018 - $661,387); cashable GIC investments of $8,854,285 (September 30, 2018 - $9,342,183) with maturities of 12 months or less, and GIC's totaling $41,153 (September 30, 2018 - $41,101) held as collateral against Company's credit cards.

<u>Trade receivables</u>
Trade receivable are measured at fair value through comprehensive profit or loss and are comprised of amounts due from various customers. As at December 31, 2018 trade receivables totaled $1,324,086 (September 30, 2018 - $1,573,298) inclusive of $nil write off (September 30, 2018 - $48,943).

<u>Accounts payable</u>
Accounts payable are measured at fair value through comprehensive profit or loss. At December 31, 2018, accounts payable was $500,528 (September 30, 2018 - $501,138) (see Note 10).

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

b) IFRS 15 - *Revenue from contracts with customers*. IFRS 15 replaces IAS 11 Construction Contracts and IAS 18 Revenue, and requires a more explicit presentation and increase in volume of disclosure requirements. IFRS 15 creates a single source of revenue requirements for all entities in all industries and may be adopted using a full retrospective or modified retrospective approach. IFRS 15 specifies how and when to recognize revenue through a five-step model framework for revenue recognition: i) identifying the contract, ii) identifying the performance obligations (including bill on hold agreements) in the contract to determine which goods or services are distinct and require a separate performance obligation, iii) determining the total transaction price (recognizing and allocating variable consideration), iv) allocating the transaction price to the performance obligations, and v) determining whether revenue should be recognized at a point in time or through stages of completion. The main concept is that revenue should be recognized to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration that the entity expects to receive in exchange for those goods or services. The Company has selected the full retrospective approach of adoption. The effect of adoption in the Company's consolidated financial statements is $nil.

The type of changes in the disclosure on adoption of IFRS 15 include but are not limited to: disaggregation within revenue segments/categories, additional quantitative disclosures on changes of all contract balances, disclosure of performance obligation for the amounts included in the transaction price, disclosure of significant judgement used when determining the timing and measurement of revenue recognition, and new disclosures about the balances and amortization of assets recognized from the costs to obtain or fulfill a contract.

The Company generates revenue through; 1) product sales and 2) product sales with installation services.

1) Revenue from product sales contracts is recognized when the following conditions are met:

- Persuasive evidence the contract exists, which occurs when the contract is singed by both the Company and the customer.
- The performance obligation is met, which occurs on delivery to and receipt of the equipment by the customer with the exception of bill-and-hold agreements, where the customer has agreed that upon completion of the equipment and its preparation for shipping (the "Hold Date"), title to the equipment shall have passed to customer.
- The transaction price is clearly specified in the contract. The transaction price is recognized in revenue and allocated to product revenue when the performance obligation described above has been completed.

2) Revenue from product sales with installation services contracts is recognized when the following conditions are met:

- Persuasive evidence the contract exists, which occurs when the contract is singed by both the Company and the customer.
- The two performance obligations are met; 1) delivery of equipment and 2) installation of the equipment at the customer's location.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continued

- The transaction price is clearly specified in the contract. The transaction price is recognized in revenue and allocated to product revenue and installation revenue respectively when the product is delivered and then when installation is complete. Allocation of the total transaction price between equipment and installation services utilizes Management's best estimate of fair value for i) the product based upon normal pricing and discounting practices for the product when it is sold separately; and ii) installation services which is estimated based on third party contractor pricing, which requires management to make certain estimates and critical judgments in the process of measuring contracts that include both a system and its installation. The total contractual consideration is allocated between product and installation services based on their relative fair value.

- Revenue from the product component is recognized as in 1) above and revenue from installation services is recognized when the equipment has been installed.

Generally, revenue is recognized as long as persuasive evidence of an arrangement exists, performance obligations have been met, the fee is fixed or determinable, and collectability is reasonably assured.

New standard not yet adopted

IFRS 16 – *Leases*. In January 2016, IFRS 16, was issued which requires, among other things, lessees to recognize leases traditionally recorded as operating leases in the same manner as financing leases. IFRS 16 now prescribes the accounting policies and disclosures applicable to leases for both lessees and lessors. The standard replaces IAS 17, *Leases*, and is effective for annual periods beginning of after January 1, 2019 with earlier application permitted. The Company will adopt the standard effective October 1, 2019, and it expects its facility leases to be recorded on the balance sheet as a result of the transition and is in the process of quantifying the impact.

4. SEGMENTS

The Company has assessed two operating segments based on geographical location of sales and management decision making: Legend Power Systems Inc. - Canada ("Legend Canada") and the Legend Power Systems Corp. - U.S. ("Legend U.S."). Legend Canada derives all its revenues from Canada and in the three months ended December 31, 2018 all of the Company's revenues were attributable to Legend Canada (2017 – 100%). Each reportable segment derives its revenue from the sale or installation of the SmartGATE™. Transfer prices between operating segments are on non- arm's length basis.

The comparative tables below show assets and liabilities, revenues and expenses and net loss and comprehensive loss for each segment. The Company has restated segmented assets, liabilities, revenues and expense and net loss and comprehensive loss for the prior period following the change in the composition of its reportable segments from prior period. Of the assets presented in the table below an amount of $367,713 for Legend Canada and $4,939 for Legend U.S. are non-current assets.

(Unaudited - Expressed in Canadian Dollars)

4. SEGMENTS – continued

As at:	December 31, 2018			September 30, 2018		
	Legend Canada	Legend U.S.	Total	Legend Canada	Legend U.S.	Total
	$	$	$	$	$	$
Assets	13,143,614	330,544	13,474,158	14,107,955	405,931	14,513,886
Liabilities	822,563	50,006	872,569	852,968	37,832	890,800

Three months ended:	December 31, 2018			December 31, 2017		
	Legend Canada	Legend U.S.	Total	Legend Canada	Legend U.S.	Total
	$	$	$	$	$	$
Revenues	403,400	-	403,400	1,282,707	-	1,282,707
Expenses	(1,084,611)	(410,121)	(1,494,732)	(1,979,472)	(50,563)	(2,030,035)
Net loss and comprehensive loss	**(681,211)**	**(410,121)**	**(1,091,332)**	**(696,765)**	**(50,563)**	**(747,328)**

5. REVENUE

Revenue for the three months ended December 31, 2018 was comprised of $137,527 (2017 - $642,495) of product sales, and $265,873 (2017 - $640,212) of installation revenue.

Pursuant to the results of an inventory count completed on December 31, 2018, an increase in inventory valuation in the amount of $138,891 (2017 - $nil) was recorded which materially reduced cost of goods sold reported during Q1 2019. Gross margin was 81% in the three months ended December 31, 2018 compared to 37% margin in the three months ended December 31, 2017.

Five customers accounted for 25%, 21%, 20%, 18% and 11% respectively of the Company’s revenues for the three months ended December 31, 2018 compared with two customers for 52% and 37% respectively for the three months ended December 31, 2017.

(Unaudited - Expressed in Canadian Dollars)

6. RECEIVABLES

i) Trade Receivables

Aging of trade receivables as follows:

Trade Receivables	Total due	0-30 days	31-90 days	91 to a year	Over a year
	$	$	$	$	$
December 31, 2018	1,324,086	1,087,326	5,650	231,110	6,870
September 30, 2018	1,573,298	1,321,166	219,890	25,372	6,870

At December 31, 2018, receivables from four of our customers accounted for 34%, 17%, 17% and 14% respectively of the Company's trade receivables balance for a total of 82% in aggregate. Receivables from three customers accounted for 60%, 14%, and 14%, respectively of the Company's trade receivables balance for a total of 88% in aggregate at September 30, 2018.

ii) Due from customers on contract

Due from customers on contract amounts of $465,291 at December 31, 2018 and $1,361,126 at September 30, 2018, relates to equipment delivered and/or installation services performed for sales where revenue has been recognized, and customers had not yet been invoiced.

7. INVENTORY

Inventories consist of the following, as at December 31, 2018 and September 30, 2018:

	December 31, 2018	September 30, 2018
	$	$
Finished products ("SmartGATE™")	180,480	148,475
Work in progress inventory	267,996	56,837
Transformers and components	1,183,636	861,280
	1,632,112	**1,066,592**

During the three months ended December 31, 2018, inventories were recognized as cost of sales in the amount of $49,325 (2017 – $295,244). An inventory adjustment in the amount of $138,891 was allocated on reversal of a year-end adjustment (2017 – inventory impairment of $5,249).

(Unaudited - Expressed in Canadian Dollars)

8. PROPERTY AND EQUIPMENT

	Computer equipment	Equipment and furniture	Leasehold Improvements	Total
	$	$	$	$
Cost				
Balance at September 30, 2017	101,945	351,478	20,944	474,367
Additions	31,181	85,652	5,875	122,708
Disposals	(6,519)	-	-	(6,519)
Balance at September 30, 2018	126,607	437,130	26,819	590,556
Additions	4,503	9,239	-	13,742
Balance at December 31, 2018	131,110	446,369	26,819	604,298
Accumulated Depreciation				
Balance at September 30, 2017	77,798	298,468	14,925	391,191
Additions	15,956	37,602	3,041	56,599
Disposals	(1,525)	-	-	(1,525)
Balance at September 30, 2018	92,229	336,070	17,966	446,265
Additions	5,114	13,385	734	19,233
Balance at December 31, 2018	97,343	349,455	18,700	465,498
Net book value				
At September 30, 2018	34,378	101,060	8,853	144,291
At December 31, 2018	**33,767**	**96,914**	**8,119**	**138,800**

(Unaudited - Expressed in Canadian Dollars)

9. INTANGIBLE ASSETS

In 2007, the Company purchased the worldwide patents for the SmartGATE™. These patents are now fully amortized.

During the years ended September 30, 2018 and 2017, activities associated with development of the Company's next generation technology were classified as having progressed from the research phase, into the development stage, thus certain related expenditures during the years were capitalized. During the three months ended December 31, 2018 an amount of $126,773 (2017 - $nil) was capitalized to product development. Certain of the Company's new technologies reached the production phase and started to generate economic benefits thus costs associated with its development are being amortized over the estimated useful economic life of the technology which is 5 years. As at December 31, 2018, remaining useful life of the product development was 5 years (September 30, 2018 – 5 years).

	Patents	Product Development	Computer Software	Total
	$	$	$	$
Cost				
Balance at September 30, 2017	1,638,099	107,060	103,433	1,848,592
Additions	-	27,336	21,985	49,321
Balance at September 30, 2018	1,638,099	134,396	125,418	1,897,913
Additions	-	126,773	-	126,773
Balance at December 31, 2018	1,638,099	261,169	125,418	2,024,686
Amortization				
Balance at September 30, 2017	1,638,099	-	102,203	1,740,302
Additions	-	13,440	14,561	28,001
Balance at September 30, 2018	1,638,099	13,440	116,764	1,768,303
Additions	-	13,058	4,250	17,308
Balance at December 31, 2018	1,638,099	26,498	121,014	1,785,611
Carrying Amount				
At September 30, 2018	-	120,956	8,654	129,610
At December 31, 2018	**-**	**234,671**	**4,404**	**239,075**

10. ACCOUNTS PAYABLE

Accounts payable consist of the following, as at December 31, 2018 and September 30, 2018:

	December 31, 2018	September 30, 2018
	$	$
Trade payables	367,335	363,351
Sales tax payable	100,972	108,872
Trade payable to related parties	32,221	28,915
	500,528	501,138

(Unaudited - Expressed in Canadian Dollars)

11. WARRANTY PROVISION

	Total
	$
Balance at September 30, 2017	215,231
Warranty fulfillments	(127,040)
Additional provision	221,806
Balance at September 30, 2018	309,997
Warranty fulfillments	(44,141)
Additional provision	35,314
Balance at December 31, 2018	**301,170**

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. As at December 31, 2018, the average remaining years of equipment under warranty was 7.80 years (September 30, 2018 – 7.96 years).

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS

i) Share Capital

The Company's authorized share capital is an unlimited number of common shares without par value. At December 31, 2018, the Company had 101,462,803 shares issued and outstanding. 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.

	Common shares	**Share capital**
		$
Balance, September 30, 2017	**82,786,258**	**38,421,253**
Issued with public offering (1)	12,500,000	8,877,683
Over - allotment option (2)	656,000	475,810
Issued with exercise of warrants	4,464,382	2,258,693
Issued with exercise of options	1,056,163	375,864
Balance September 30, 2018 and December 31, 2018	**101,462,803**	**50,409,303**

1) On April 6, 2018, the Company completed a $10 million public offering, issuing 12.5 million common shares at a price of $0.80 per share. The Company paid a cash commission of $531,240 to the underwriters and incurred additional share issue costs of $378,191 in legal and filing fees bringing the net proceeds to $9,090,569. The Company issued 664,050 broker warrants to the underwriters in connection with this public offering. Each broker warrant entitles the holder to purchase one common share of the Company at $0.80 per share until April 6, 2020. An amount of $212,886 was recorded to share issue costs for the fair value of the brokers warrants issued to the underwriters, calculated using Black Scholes Model with the following assumptions: share price $0.80, exercise price $0.80, expected life 2 years, annual volatility 73% and risk-free rate 1.36%.

(Unaudited - Expressed in Canadian Dollars)

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS - continued

2) On April 30, 2018, the Company completed an over-allotment option exercised by the underwriters in connection with the April 6, 2018 Offering. As a result, the Company issued an additional 656,000 common shares at a price $0.80 per share for additional gross proceeds of $524,800. The Company paid cash commission of $31,488 to the underwriters and incurred additional cash share issue costs of $5,000, bringing the net proceeds to $488,312. The Company issued 39,360 brokers warrants to the underwriters at a price of $0.80 expiring April 30, 2020. An additional amount of $12,502 was recorded to share issue costs for the fair value of the broker warrants issued to the underwriters in connection with the over-allotment. Fair value of the 39,360 broker warrants was calculated using the Black Scholes pricing model using the following assumptions: share price $0.80, exercise price $0.80, expected term 2 years, annual volatility 71.78% and risk-free rate of 1.43%.

ii) 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 outstanding at December 31, 2018 and September 30, 2018, including the changes during the period, is as follows:

	Share options	Weighted average exercise price
		$
Balance, September 30, 2017	**8,259,496**	**0.32**
Granted	875,000	0.74
Exercised	(1,056,163)	0.28
Expired	(275,000)	0.30
Forfeited	(690,000)	0.41
Balance, September 30, 2018	**7,113,333**	**0.37**
Forfeited	(42,500)	0.72
Balance, December 31, 2018	**7,070,833**	**0.37**

During the three months ended December 31, 2018, the Company did not grant any stock options (2017 – 200,000). The weighted average fair value of options granted during the three months ended December 31, 2018 was $nil per option (2017 - $0.35).

An amount of $95,089 was recorded to share-based compensation expense for 408,752 options vested during the three months ended December 31, 2018 (2017 - $97,093 for 712,501 options vested).

During the three months ended December 31, 2018 no options were exercised (2017 – 47,830 for total proceeds of $12,432).

(Unaudited - Expressed in Canadian Dollars)

12. SHARE CAPITAL AND CONTRIBUTED SURPLUS - continued

The fair value of share options awarded to employees, directors and consultants was estimated on the dates of award using the Black-Scholes option-pricing model with the following weighted average assumptions during the three months ended December 31, 2017:

	2018	2017
Risk-free interest rate	n/a	1.42%
Estimated volatility	n/a	108.33%
Expected life (years)	n/a	3.58
Forfeiture rate	n/a	17.61%
Dividend rate	n/a	0.00%

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.

The following table summarizes share options outstanding and exercisable at December 31, 2018:

Options outstanding	Options exercisable	Exercise price	Year of Expiry
		$	
2,245,000	2,245,000	0.20 - 0.55	2019
170,000	120,000	0.35	2020
1,951,666	1,668,055	0.25 - 0.30	2021
2,105,000	1,090,836	0.27 - 0.75	2022
599,167	77,502	0.55 - 0.92	2023
7,070,833	**5,201,393**		

iii) Warrants

The continuity of share purchase warrants during the years ended September 30, 2018 and 2017 is as follows:

	Number of warrants	Weighted average exercise price
		$
Balance, September 30, 2017	4,464,382	0.40
Exercised	(4,464,382)	0.40
Issued, broker warrants	703,410	0.80
Balance, September 30, 2018 and December 31, 2018	**703,410**	**0.80**

During the three months ended December 31, 2018, no investors warrants were exercised (2017 – 4,464,382 for an average price $0.40) for total proceeds of $nil (2017 - $1,785,753). An amount of $nil (2017 - $472,940) was transferred to share capital from contributed surplus in connection with this exercise.

In April 2018, the Company issued 703,410 broker warrants to the underwriters in connection with the Offering and overallotment option. Each broker warrant entitles the holder to purchase one common share of the Company at $0.80 per share until April 2020.

(Unaudited - Expressed in Canadian Dollars)

13. COMMITMENTS

On December 4, 2017 the Company entered into an agreement to lease premises in Toronto, Ontario and on March 22, 2018 the Company entered into an agreement to lease premises in Vancouver, B.C. When taken together the lease agreements require the following minimum lease payments in each of the below fiscal years:

2019	$151,117
2020	$143,399
2021	$70,775

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.

During the three months ended December 31, 2018 an amount of $49,531 (2017 - $23,338) was recorded to rent expense for the monthly lease payments.

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 re-negotiated or settled otherwise.

The Company has a management services agreement with the CFO of the Company that contains severance provisions whereby termination without cause could result in additional costs to the Company unless re-negotiated or settled otherwise.

14. RELATED PARTY DISCLOSURES

The Company entered into the following related party transactions during the three months ended December 31, 2018 and 2017.

(i) Transactions with Key Management Personnel:

The following amounts were incurred with respect to Key Management Personnel; being the Company's CEO and the CFO:

	2018	**2017**
	$	**$**
Salaries and consulting fees to key management personnel	108,437	88,812
Share-based compensation	24,661	162,269
	133,098	251,081

(ii) Transactions with Directors:

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

	2018	**2017**
	$	**$**
Share-based compensation	36,905	19,622

At December 31, 2018, a total of $32,221 (September 30, 2018 - $28,915) was due to related parties for consulting fees and expenses reimbursement.

15. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Financial instruments

The Company's financial instruments consist of cash and cash equivalents, trade receivables, accounts payable and amounts due to related parties. The carrying values of these financial instruments approximate their fair values because of their short-term nature.

Risk management

The risks associated with these financial instruments and the policies regarding their management are discussed below. Management monitors these risk exposures to ensure appropriate measures are implemented in a timely and effective manner.

Foreign currency risk

The Company is exposed to the US dollar versus Canadian dollar exchange rate fluctuation risks through operations of its US subsidiary and expenses incurred in US dollars. As at December 31, 2018 all of Company's liquid assets and liabilities were held in Canadian dollars and US dollars. A significant change in the USD exchange rate relative to the Canadian dollar could affect the Company's results of operations. A change in the value of US dollar by 10% relative to the value of the Canadian dollar would have affected the Company's results of operations for the three months ended December 31, 2018 by approximately $26,000 (2017 - $5,000).

Interest rate risk

Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. The Company is exposed to interest rate risk due to its potential impact on cash and cash equivalents. The Company earns interest on deposits based on current market interest rates, which during the three months ended December 31, 2018 ranged from 0.5% to 1.6% (2017 – 0.5% to 1.6%). A 1% change in interest rates would have affected the Company's results of operations for the three months ended December 31, 2018 by approximately $94,000 (2017 - $20,000). The Company does not have any interest-bearing liabilities.

Credit risk

Credit risk is the risk of an unexpected loss if the counterparty to a financial instrument fails to meet its contractual obligations. The credit risk associated with cash is believed to be minimal as cash is on deposit with Canadian and foreign banks that are deemed to be creditworthy. Receivables are comprised primarily of amounts due from various customers. The Company is exposed to credit risk through accounts receivable from customers. At December 31, 2018, receivables from four customers accounted for 34%, 17%, 17% and 14% respectively of the Company's receivable balance for a total of 82% in aggregate. Receivables from three customers accounted for 60%, 14%, and 14%, respectively of the Company's receivable balance for a total of 88% in aggregate at September 30, 2018.

Liquidity risk

Liquidity risk is managed by ensuring sufficient financial resources are available to meet obligations associated with financial liabilities. As at December 31, 2018 the Company had cash and cash equivalents of $9,613,434 to settle its current liabilities of $610,029.

16. SUBSEQUENT EVENTS

Subsequent to December 31, 2018, 380,000 stock options were exercised for total proceeds of $76,000 and 385,000 options expired.