LED MEDICAL DIAGNOSTICS INC.

# CONSOLIDATED FINANCIAL STATEMENTS

## FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

*(EXPRESSED IN U.S. DOLLARS)*

# Independent Auditor's Report

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To the Shareholders of
LED Medical Diagnostics Inc.

We have audited the accompanying consolidated financial statements of LED Medical Diagnostics Inc. (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2017 and December 31, 2016 and the consolidated statements of operations and comprehensive loss, consolidated statement of changes in equity and consolidated statement of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

### Management's responsibility for the 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.

### Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 auditor's 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 auditor considers 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 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 consolidated financial position of LED Medical Diagnostics Inc. as at December 31, 2017 and December 31, 2016 and its financial performance and its cash flows for the years then ended, in accordance with International Financial Reporting Standards.

## Emphasis of matter

Without modifying our opinion, we draw attention to Note 1 in the consolidated financial statements which indicates that the Company incurred a net and comprehensive loss of $2,495,015 and negative cash flows from operations of $4,432,082 for the year ended December 31, 2017. As at December 31, 2017, the Company had an accumulated deficit of $51,781,389. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern.

Grant Thornton LLP

Vancouver, Canada
April 27, 2018

Chartered Professional Accountants

# LED MEDICAL DIAGNOSTICS INC.

Consolidated Statements of Financial Position

(Expressed in U.S. Dollars)

| | Notes | | **December 31, 2017** | | December 31, 2016 |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| **Current assets** | | | | | |
| Cash | | **$** | **2,425,468** | $ | 874,567 |
| Trade and other receivables | 5 | | **1,578,371** | | 799,339 |
| Inventory | 6 | | **778,939** | | 535,951 |
| Prepaid expenses and deposits | 7 | | **433,272** | | 190,577 |
| Total current assets | | | **5,216,050** | | 2,400,434 |
| **Non-current assets** | | | | | |
| Prepaid expenses and deposits | 7 | | **-** | | 93,100 |
| Property and equipment | 8 | | **152,497** | | 176,374 |
| Intangible assets | 9 | | **7,620,287** | | - |
| Goodwill | 10 | | **1,868,130** | | - |
| | | **$** | **14,856,964** | $ | 2,669,908 |
| **Liabilities and shareholders' equity** | | | | | |
| **Current liabilities** | | | | | |
| Trade payables and accrued liabilities | 11 | **$** | **2,191,815** | $ | 3,534,972 |
| Deferred revenue | | | **892,570** | | 309,531 |
| Debenture | 13 | | **2,152,841** | | 665,373 |
| Deferred consideration on acquisition | 4 | | **1,200,000** | | - |
| Total current liabilities | | | **6,437,226** | | 4,509,876 |
| **Non-current liabilities** | | | | | |
| Debenture | 13 | | **3,718,452** | | 1,958,169 |
| Warrants | 15 | | **1,372,122** | | - |
| Lease liability | | | **61,011** | | 89,855 |
| Deferred consideration on acquisition | 4 | | **450,000** | | - |
| Total liabilities | | | **12,038,811** | | 6,557,900 |
| **Shareholders' equity** | | | | | |
| Share capital | 16 | | **50,944,234** | | 40,933,332 |
| Stock-based payment reserve | 17 | | **2,799,476** | | 2,171,196 |
| Warrants reserve | 15 | | **381,374** | | 1,819,396 |
| Accumulated other comprehensive income | | | **474,458** | | 474,458 |
| Deficit | | | **(51,781,389)** | | (49,286,374) |
| | | | **2,818,153** | | (3,887,992) |
| | | **$** | **14,856,964** | $ | 2,669,908 |

*Nature of Operations and Going Concern (Note 1)*

*Lease Obligations and Commitments (Note 12)*

*Subsequent Events (Note 25)*

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

Approved on behalf of the Board of Directors:

____________________Chief Executive Officer
Dr. David Gane

____________________Director
James Topham



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## LED MEDICAL DIAGNOSTICS INC.

Consolidated Statements of Operations and Comprehensive Loss

(Expressed in U.S. Dollars)

For the years ended December 31, 2017 and 2016

| | Notes | | December 31, 2017 | | December 31, 2016 |
|---|---|---|---|---|---|
| **Revenues** | | **$** | **12,688,752** | $ | 10,168,896 |
| **Cost of goods sold** | | | **5,520,050** | | 7,690,130 |
| | | | **7,168,702** | | 2,478,766 |
| **Expenses** | | | | | |
| Sales and marketing | 24 | | **4,855,988** | | 4,742,093 |
| Research and development | 24 | | **1,039,827** | | 132,097 |
| Administration | 24 | | **2,861,091** | | 2,150,282 |
| Stock-based compensation | 17 | | **628,280** | | 220,148 |
| Depreciation and amortization | 8 | | **841,588** | | 348,612 |
| | | | **10,226,774** | | 7,593,232 |
| **Operating loss** | | | **(3,058,072)** | | (5,114,466) |
| **Other (income)/expenses** | | | | | |
| Change in fair value of Canadian dollar denominated warrants | 15 | | **(1,593,244)** | | - |
| Foreign exchange (gain) loss | | | **439,145** | | (22,353) |
| Interest | | | **591,042** | | 281,160 |
| | | | **(563,057)** | | 258,807 |
| **Net loss before income taxes** | | | **(2,495,015)** | | (5,373,273) |
| **Income tax recovery** | 21 | | - | | |
| **Net loss and comprehensive loss for the year** | | $ | **(2,495,015)** | $ | (5,373,273) |
| **Loss per share – basic and diluted** | 23 | **$** | **(0.08)** | $ | (0.47) |
| **Weighted average number of shares outstanding – basic and diluted** | | | **31,668,318** | | 11,312,962 |

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



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## LED MEDICAL DIAGNOSTICS INC.

Consolidated Statements of Changes in Shareholders' Equity (Deficiency)

(Expressed in U.S. Dollars)

For the years ended December 31, 2017 and 2016

| | Number of Shares | Share Capital | Stock-based Payments Reserves | Warrants Reserve | Deficit | Accumulated Other Comprehensive Income | Total Shareholders' Equity (Deficiency) |
|---|---|---|---|---|---|---|---|
| **Balance, January 1, 2016** | **112,319,063** | **$36,135,128** | **$1,912,668** | **$6,537,724** | **($43,913,101)** | **$474,458** | **$1,146,877** |
| Shares issued with debenture financing | 3,759,453 | 79,876 | - | - | - | - | 79,876 |
| Settlement of share capital upon expiry of unexercised warrants | - | 4,718,328 | - | (4,718,328) | - | - | - |
| Issuance of share on exercise of DSU | 350,000 | - | - | - | - | - | - |
| Stock based compensation | - | - | 220,148 | - | - | - | 220,148 |
| Stock-based compensation classified as consulting expense | - | - | 38,380 | - | - | - | 38,380 |
| Net loss comprehensive loss for the year | - | - | - | - | (5,373,273) | - | (5,373,273) |
| **Balance, December 31, 2016** | **116,428,516** | **$40,933,332** | **$2,171,196** | **$1,819,396** | **($49,286,374)** | **$474,458** | **($3,887,992)** |
| Shares issued pursuant to private placement | 220,711,540 | 10,085,814 | - | - | - | - | 10,085,814 |
| Share issuance costs | - | (724,288) | - | - | - | - | (724,288) |
| Subscriber warrants issued pursuant to private placement | - | (2,965,366) | - | - | - | - | (2,965,366) |
| Finder Warrants issued pursuant to private placement | - | (356,386) | - | 356,386 | - | - | - |
| Shares issued with debenture financing | 8,147,916 | 88,768 | - | - | - | - | 88,768 |
| Finder warrants issued with debenture financing | - | - | - | 24,988 | - | - | 24,988 |
| Shares issued as settlement on the purchase of Apteryx | 33,858,400 | 2,062,964 | - | - | - | - | 2,062,964 |
| Share Consolidation (10 to 1) | (341,231,736) | - | - | - | - | - | - |
| Settlement of share capital upon expiry of unexercised warrants | - | 1,819,396 | - | (1,819,396) | - | - | - |
| Stock based compensation | - | - | 628,280 | - | - | - | 628,280 |
| Net loss comprehensive loss for the year | - | - | - | - | (2,495,015) | - | (2,495,015) |
| **Balance, December 31, 2017** | **$37,914,636** | **$50,944,234** | **$2,799,476** | **$381,374** | **$(51,781,389)** | **$474,458** | **$2,818,153** |

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



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# LED MEDICAL DIAGNOSTICS INC.

Consolidated Statements of Cash Flow

(Expressed in U.S. Dollars)

For the years ended December 31, 2017 and 2016

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Net loss for the year | **$ (2,495,015)** | $ (5,373,273) |
| **Adjustments to net loss for items not involving cash**: | | |
| Depreciation and amortization | **841,588** | 315,500 |
| Change in fair value of Canadian dollar denominated warrants | **(1,593,244)** | - |
| Lease liability | **(28,843)** | 2,444 |
| Stock-based compensation | **628,280** | 258,528 |
| Unrealized foreign exchange loss | **260,680** | 2,690 |
| Amortization of intellectual property | **-** | 10,751 |
| Fair value accretion | **39,742** | - |
| Bad debt reserve | **102,898** | 38,905 |
| | **(2,243,914)** | (4,744,455) |
| **Changes in working capital assets and liabilities:** | | |
| Trade and other receivables | **(397,297)** | 727,610 |
| Inventory | **(242,988)** | 4,866,236 |
| Prepaid expenses and deposits | **(146,023)** | 288,504 |
| Trade payables and accrued liabilities | **(1,564,445)** | (3,150,747) |
| Deferred revenue | **230,857** | (436,711) |
| Changes in working capital assets and liabilities | **(2,119,896)** | 2,294,892 |
| Interest paid | **(68,272)** | - |
| Cash flows used in operating activities | **(4,432,082)** | (2,449,563) |
| **Cash flows from investing activities** | | |
| Purchase of Apteryx, net of cash acquired | **(6,521,800)** | **-** |
| Purchase of equipment | **(25,842)** | (117,668) |
| Cash flows used in investing activities | **(6,547,642)** | (117,668) |
| **Cash flows from financing activities** | | |
| Issuance of units, net of issuance costs | **9,450,294** | 79,876 |
| Proceeds from debenture issuance | **3,341,011** | 1,377,203 |
| Cash flows provided by financing activities | **12,791,305** | 1,457,079 |
| **Increase (Decrease) in cash** | **1,811,581** | (1,110,152) |
| **Foreign exchange effect on cash** | **(260,680)** | (2,690) |
| **Cash, beginning of year** | **874,567** | 1,987,409 |
| **Cash, end of year** | **$ 2,425,468** | $ 874,567 |

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



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## 1. NATURE OF OPERATIONS AND GOING CONCERN

LED Medical Diagnostics Inc. ("LED" or the "Company") was incorporated under the British Columbia Business Corporations Act on July 17, 2002 as 651192 B.C. Ltd. and changed its name to LED Medical Diagnostics Inc. on August 20, 2003. The Company's head office, principal address and records office are located at 810 – 580 Hornby Street, British Columbia, Canada, V6C 3B6. The registered and records office is located at 2500 – 700 West Georgia Street, Vancouver, B.C. V7Y 1B3.

The Company has developed, and markets, a medical device under the trade name VELscope®. The device is used in the dental industry to help identify oral soft tissue abnormalities including those which may be cancerous or precancerous and to help define appropriate margins for surgical excision. The Company also features its Digital division that provides dentists and oral health specialists with advanced diagnostic imaging products and software.

On February 10, 2017, the Company acquired 100% of the common shares of Apteryx, Inc. ("Apteryx"). Apteryx is a custom software development company located in Akron, Ohio specializing in medical and dental image processing, data encryption and security, database, data conversion and distributed systems.

These consolidated financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

The Company incurred a net and comprehensive loss of $2,495,015 and has negative cash flow from operations of $4,432,082 for the year ended December 31, 2017. As at December 31, 2017, the Company had an accumulated deficit of $51,781,389. Management assesses the Company's ability to continue as a going concern at each reporting date, using all quantitative and qualitative information available. Material uncertainties have been identified which may cast significant doubt upon the Company's ability to continue as a going concern. This assessment, by its nature, relies on estimates of future cash flows and other future events, whose subsequent changes would materially impact the validity of such an assessment.

In assessing whether the going concern assumption was appropriate, management considered all relevant information available about the future, which was at least, but not limited to, the 12-month period from the date of this report. The following is considered in evaluating the going concern of the entity pertaining to the financial statements as at December 31, 2017:

- The Company has US$5.9 million of debentures and unpaid interest outstanding at December 31, 2017 of which US$2.2 million is payable over the next 12 months and another US$1.2 million due in early 2019.
- The Company also has US$1.65 million in deferred cash consideration for the Apteryx acquisition outstanding at December 31, 2017 of which US$1.2 million is due within the next 12 months. The final payment of $450,000 is due February 10, 2019 and can be either cash or share consideration at the Company's discretion.
- The Company has a history of operating losses since inception and not achieving its revenue and cash flow objectives for its annual fiscal plans approved by the board of directors.
- The Company's forecasted future cash flows are not adequate to meet its debenture, deferred consideration and interest payment obligation over the next 12 months.
- The Company has relied on equity and debt financings to fund its operating losses. Although the Company has a good track record for raising financing there is no guarantee it will be successful in its efforts to raise additional financing or if financing is available, that it will be on terms that are acceptable to the Company.

The Company's ability to continue as a going concern is dependent upon its ability to renegotiate debt repayment terms, raise adequate financing and achieve significant improvements in operating results in the future.

The assessment of the Company's ability to execute its strategy and fund future working capital requirements involves significant judgement. Estimates and assumptions regarding future operating costs, revenue and profitability levels and general business and customer conditions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. As at December 31, 2017 and as at the date of approval of these consolidated financial statements, the outcome of these activities is unknown and subject to considerable uncertainty. These consolidated financial statements do not include any adjustments that might result from the outcome of these uncertainties or if such adjustments would be material.

## 2. BASIS OF PRESENTATION

These consolidated financial statements of the Company, approved by the Board of Directors on April 27, 2018, have been prepared in accordance with International Financial Reporting Standards ("IFRS"). These consolidated financial statements have been prepared on the historical cost basis unless otherwise specified in the accounting policies (Note 3). The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Revenue recognition

The Company generates revenue from the sale of goods as well as professional service contracts, subscriptions to cloud based software, perpetual software license fees, and related maintenance and service fees.

The Company recognizes revenue from sales of goods when it has transferred to the buyer the significant risks and rewards of ownership, it has no longer retained continuing managerial involvement to the degree usually associated with ownership nor has effective control over the goods sold, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Company, and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

The Company recognizes revenue from the sale of software licenses upon the transfer of title to the customer, so long as persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is reasonably assured. Delivery of software licenses, is generally determined to have occurred when the customer downloads the software from the store and is provided the software product key code. The Company uses the residual method to recognize revenue on delivered elements when a license agreement includes one or more elements to be delivered at a future date if evidence of the fair value of all undelivered elements exists. If an undelivered element for the arrangement exists under the license arrangement, revenue related to the undelivered element is deferred based on vendor-specific objective evidence ("VSOE") of the fair value of the undelivered element. If VSOE of fair value does not exist for all undelivered elements, all revenue is deferred until sufficient evidence exists or as elements are delivered.

The Company's multiple-element sales arrangements include arrangements where software licenses and the associated support and maintenance are sold together. The Company has established VSOE of the fair value of the undelivered support and maintenance element based on the contracted price for renewal as listed for sale on the Company's website. The Company's multiple-element sales arrangements generally include rights for the customer to renew support after the bundled term ends. These rights are irrevocable to the customer's benefit, are for specified prices, are consistent with the initial price in the original multiple-element sales arrangement, and the customer is not subject to any economic or other penalty for failure to renew. When the Company's contract with customers include multiple deliverables, consideration received is applied to separate components based on the applicable revenue recognition criteria.

Subscription and support revenues are recognized ratably over the contract terms beginning on the commencement date of each contract, which is the date our service is made available to customers. Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met.

Business combinations

The Company applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interest issued. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. Acquisition related costs are expensed as incurred.

Goodwill is initially measured as the excess of the aggregate of the consideration transferred over the net identifiable assets acquired and liabilities assumed.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Principles of consolidation

Subsidiaries are entities controlled by LED. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. Control is achieved when the Company is exposed to, or has the rights to variable returns from its involvement with an entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is obtained and continue to be consolidated until the date that control ceases. Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries listed in the following table:

| Name of Subsidiary | Country of Incorporation | Ownership Interest | |
|---|---|---|---|
| | | December 31, 2017 | December 31, 2016 |
| LED Dental Inc. | Canada | 100% | 100% |
| LED Dental (U.S.) Ltd. | USA | 100% | 100% |
| Apteryx, Inc. | USA | 100% | - |
| Essentia Genetics Corp.(inactive) | Canada | 100% | 100% |

Determination of functional currency

The consolidated financial statements are presented in U.S. dollars. The functional currency of each of the Company's operating entities is determined using the currency of the primary economic environment in which that entity operates. The consolidated financial statements are presented in U.S. dollars which is the functional and presentation currency of the parent. The functional currencies of the subsidiaries are as follows:

| Name of Subsidiary | Functional Currency ($) |
|---|---|
| LED Dental Inc. | U.S. |
| LED Dental (U.S.) Ltd. | U.S. |
| Apteryx, Inc. | U.S. |
| Essentia Genetics Corp. (inactive) | U.S. |

Foreign currency translation

Foreign currency denominated transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the period-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined. Exchange differences arising on the translation of monetary items or on settlement of monetary items are recognized in profit or loss in the statement of operations in the period in which they arise, except where deferred in equity as a qualifying cash flow or net investment hedge.

Financial instruments

The Company classifies its financial instruments in the following categories: at fair value through profit or loss, loans and receivables, held-to-maturity investments or available-for-sale financial assets and financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition. All of the Company's financial assets are classified as loans and receivables.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Financial assets are classified at fair value through profit or loss when they are either held for trading for the purpose of short-term profit taking, derivatives not held for hedging purposes, or when they are designated as such to avoid an accounting mismatch or to enable performance evaluation where a group of financial assets is managed by key management personnel on a fair value basis in accordance with a documented risk management or investment strategy. Such assets are subsequently measured at fair value with changes in carrying value being included in profit or loss. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are subsequently measured at amortized cost. They are included in current assets, except for maturities greater than twelve months after the end of the reporting period. These are classified as non-current asset

Held-to-maturity investments are non-derivative financial assets that have fixed maturities and fixed or determinable payments, and it is the Company's intention to hold these investments to maturity. They are subsequently measured at amortized cost.

Held-to-maturity investments are included in non-current assets, except for those which are expected to mature within twelve months after the end of the reporting period.

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or are not suitable to be classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments and are subsequently measured at fair value. Unrealized gains and losses are recognized in other comprehensive income, except for foreign exchange gains and losses associated with monetary available-for-sale financial assets and impairment losses which are recorded in profit or loss.


Held-to-maturity investments are non-derivative financial assets that have fixed maturities and fixed or determinable payments, and it is the Company's intention to hold these investments to maturity. They are subsequently measured at amortized cost.

Held-to-maturity investments are included in non-current assets, except for those which are expected to mature within twelve months after the end of the reporting period.

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or are not suitable to be classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments and are subsequently measured at fair value. Unrealized gains and losses are recognized in other comprehensive income, except for foreign exchange gains and losses associated with monetary available-for-sale financial assets and impairment losses which are recorded in profit or loss.


Non-derivative financial liabilities (excluding financial guarantees) are subsequently measured at amortized cost.

Regular purchases and sales of financial assets are recognized on the trade-date – the date on which the Company commits to purchase the asset.

Financial assets are derecognized when the rights to receive cash flows from the instruments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

At each reporting date, the Company assesses whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a significant and prolonged decline in the value of the instrument is considered to determine whether impairment has arisen.

<u>Cash and cash equivalents</u>

Cash equivalents include highly liquid Canadian dollar denominated guaranteed investment certificates which are readily convertible to contracted amounts of cash without penalty.

<u>Property and equipment</u>

Property and equipment is stated at historical cost less accumulated depreciation and accumulated impairment losses.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to the statement of operations and comprehensive loss during the financial period in which they are incurred. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized in profit or loss.

Depreciation is calculated on a straight-line method to write off the cost of the assets over their estimated useful lives. The depreciation rates applicable to each category of equipment are as follows:

| | | |
|---|---|---|
| Office equipment | 5 years | straight-line method |
| Computer equipment | 3 years | straight-line method |
| Manufacturing tooling | 2 years | straight-line method |
| Leasehold improvements | term of lease | straight-line method |
| Demo equipment | 1-3 years | straight-line method |

Intangible assets

Intangible assets, whether purchased or self-created, are recognized if it is probable that the future economic benefits that are attributable to the asset will flow to the Company and the cost of the asset can be measured reliably.

Amortization of intangible assets is calculated on a straight-line method to write off the cost of the assets over their estimated useful lives. The amortization rates applicable to each category of equipment are as follows:

| | | |
|---|---|---|
| Acquired software technology | 10 years | straight-line method |
| Customer base | 10 years | straight-line method |
| Patents & patent applications | 10 years | straight-line method |
| Trademarks, copy right, brand | 10 years | straight-line method |

The depreciation method and estimates of useful lives ascribed to these other identifiable intangible assets are reviewed at least each financial year end and if necessary, adjusted on a prospective basis.

Goodwill

Goodwill represents the future economic benefits arising from a business combination that are not individually identified and separately recognized. Goodwill is carried at cost less accumulated impairment losses. Refer to note 10 for a description of impairment testing procedures.

Research and development costs

Research costs are expensed as incurred. Development costs are expensed as incurred unless the specific criteria for deferral and amortization have been met. To date, the Company has not capitalized any development costs.

Impairment of non-financial assets, goodwill and intangible assets

The carrying amount of the Company's non-financial assets (which include property and equipment and patents, intellectual property and intangibles with definite life) is reviewed at each reporting date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. An impairment loss is recognized whenever the carrying amount of an asset or its cash-generating unit ("CGU") exceeds its recoverable amount. Impairment losses are recognized in the statement of operations.

The carrying amount of the Company's indefinite life assets (which include Brand and Goodwill) is tested for impairment annually or more frequently if events or changes in circumstances indicate that the assets may be impaired. The assessment of indefinite life is reviewed each period to determine whether the indefinite life assumption continues to be supportable. If deemed unsupportable, the change in the useful life from indefinite to finite life is made and amortization recognized on a prospective basis. An impairment loss is recognized when the carrying amount of an asset or its CGU exceeds its recoverable amount.
Impairment losses are recognized in profit or loss for the period.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

The recoverable amount of assets is the greater of an asset's fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Impairment losses for each CGU reduce first the carrying amount of any goodwill allocated to that CGU. Any remaining impairment loss is charged pro rata to the other assets in the CGU. With the exception of goodwill, all assets are subsequently reassessed for indications that an impairment loss previously recognized may no longer exist.

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount, however, not to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized in previous years. An impairment loss with respect to goodwill is never reversed.

Equity

Share capital represents the value of the shares that have been issued. Any transaction costs associated with the issuing of shares are deducted from share capital.

From time to time the Company issues units consisting of common shares and common share purchase warrants. The Company estimates the fair value of the warrants based on the Black-Scholes valuation model. The residual difference, if any, between the unit price and the fair value of each warrant represents the fair value attributable to each common share. Share issue costs, which includes commissions, facilitation payments, professional fees and regulatory fees, are charged directly to share capital.

Reversal of impairment loss

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount, however, not to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized in previous years. Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment.

Deferred revenue

The Company defers revenue and costs relating to sales if there is a right to return or if transfer of ownership has not occurred as of the reporting date. In these cases, revenue is recognized upon the maturation of the right to return or ownership has been completed. Additionally, the Company has an annual support program and the revenue is recognized over the term of the support agreement.

Leases

Leases of equipment where substantially all the risks and benefits incidental to the ownership of the asset are transferred to the Company are classified as finance leases.

Finance leases are capitalized by recording an asset and a liability at the lower of the fair value of the leased equipment or the present value of the minimum lease payments, including any guaranteed residual values. Lease payments are allocated between the reduction of the lease liability and the lease interest expense for the period.

Leased assets are depreciated on a straight-line basis over the shorter of their estimated useful lives and the lease term.

Lease payments for operating leases, where substantially all the risks and benefits remain with the lessor, are charged as expenses in the periods in which they are incurred.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Income taxes

*Current income tax*

Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date, in the countries where the Company operates and generates taxable income.

Current income tax relating to items recognized directly in other comprehensive income or equity is recognized in other comprehensive income or equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

*Deferred income tax*

Deferred income tax is provided using the liability method on temporary differences at the reporting date between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilized. The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and is reduced only to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period.

Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority, or if relate to different taxable entities, the entities intend either to settle current tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Changes in the expected operating results, enacted tax rates, legislation or regulations, and the Company's interpretations of income tax legislation will result in adjustments to the expectations of future timing difference reversals and may require material deferred tax adjustments.

Stock-based payments

The Company operates an employee stock option plan. Historically, stock-based payments to employees have been measured at the fair value of the instruments issued and amortized over the vesting periods. Stock-based payments to non-employees are measured at the fair value of goods or services received or the fair value of the equity instruments issued, if it is determined the fair value of the goods or services cannot be reliably measured, and are recorded at the date the goods or services are received. The corresponding amount is recorded to the stock-based payment reserve. The fair value of options is determined using the Black–Scholes option pricing model which incorporates all market vesting conditions. The number of shares and options expected to vest is reviewed and adjusted at the end of each reporting period such that the amount recognized for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest.

The Black-Scholes option pricing model was developed for use in estimating the fair value of stock options and compensatory warrants that have no vesting provisions and are fully transferable. Also, option-pricing models require the use of estimates and assumptions including the expected volatility. Changes in the underlying assumptions can materially affect the fair value estimates.

The Company has a Deferred Share Unit Plan ("DSU Plan") for the company's directors, executive officers and service providers. The Company recognizes compensation expense for Deferred Share Units ("DSUs") based on the market price of the Company's stock. A DSU is convertible to shares only, and are valued by reference to the fair value of the equity instruments granted. All of the Company DSUs are equity-settled instruments (See Note 18).

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Warrants

All warrants granted are valued using the fair value method which is determined by the Black-Scholes option pricing model with assumptions for risk free interest rates, dividend yields, volatility factors and an expected life of the warrants. Warrants issued in other than functional currency are accounted for as derivatives liabilities at fair value and revalued every period with the change being recorded as income or expense.

Warrants issued to brokers as a finders' fee are treated as stock-based payment and netted against equity or debt depending on the financing arranged by the broker and are not revalued every period.

Changes in the underlying assumptions can materially affect the fair value estimates.

Research and development tax credits

Research and development tax credits are accounted for using the cost reduction method. Accordingly, tax credits are recorded as a reduction of the related expenses or the capitalized costs when recoverability is reasonably assured.

Earnings per share

The Company presents basic and diluted earnings per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period, adjusted for its own shares held. Diluted EPS is determined by adjusting the profit attributable to common shareholders and the weighted average number of common shares outstanding, adjusted for its own shares held, for the effects of all dilutive potential common shares. Dilutive EPS has not been calculated as the Company is in a net loss position for the periods resulting in an anti-dilutive quantification.

Significant accounting judgments, estimates and assumptions

The preparation of financial statements in conformity with IFRS requires management to make estimates and judgments 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 during the reporting period. Actual results may differ from those estimates.

The estimates used in determining the recorded amounts in these consolidated financial statements include the following:

*Allowance for doubtful accounts*

Management uses its best estimate of expected returns to estimate a sales return provision. If a reasonable estimate cannot be made, the Company defers revenue and costs relating to the sales at the time the goods are shipped.

*Impairment of long-lived assets, goodwill, patents and intellectual property*

The determination of intellectual property impairment requires significant estimates and assumptions to determine the recoverable amount of an asset and/or CGU, wherein the recoverable amount is the higher of fair value less costs of disposal and value in use. The value in use method involves estimating the net present value of future cash flows derived from the use of the asset and/or CGU, discounted at an appropriate rate.

The estimates of future cash flows require a number of key assumptions about future business performance. These assumptions and estimates are primarily based on the relevant business' historical experience and economic trends. These key estimates include the future revenue levels and operating expenses. The estimates are subject to a number of factors and it is possible that actual results could vary materially from management's estimates. Significant changes in the key assumptions utilized in the estimate of future cash flows could result in an impairment loss or reversal of an impairment loss.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

*Estimated useful lives of long-lived assets*

Judgment is used to determine the components of an asset and the component's useful life and is based on an analysis of all pertinent factors including, but not limited to, the expected use of the asset and in the case of an intangible asset, contractual provisions that enable renewal or extension of the asset's legal or contractual life without substantial cost, and renewal history. If the estimated useful lives were incorrect, this could result in an increase or decrease in the annual amortization expense, and future impairment charges or recoveries.

*Equity-settled stock-based compensation*

The Company estimates the cost of equity-settled stock-based compensation using the Black-Scholes option pricing model. The model takes into account an estimate of the expected life of the option, the current price of the underlying common share, the expected volatility, an estimate of future dividends on the underlying common share, the risk-free rate of return expected for an instrument with a term equal to the expected life of the option, and the expected forfeiture rate.

*Warranty provision*

The Company estimates warranty expense based on historical records, taking into account the likelihood of a warranty issue, estimated costs of warranty repair and total units in the market. The Company records a liability in respect of estimated future warranty costs. The actual cost that the Company may incur and the timing of the repairs to be carried out may differ significantly from the estimated accrual.

*Provisions and Contingencies*

Provisions are liabilities with uncertain timing or amounts, if, in the opinion of management, it is both likely that a future event will confirm that a liability had been incurred at the date of the financial statements and the amount can be reasonably estimated. Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Provisions are discounted to their present values, where the time value of money is material. In cases where it is not possible to determine whether such a liability has occurred, or to reasonably estimate the amount of loss until the performance of some future event, no accrual is made until that time. In the ordinary course of business, the Company may be party to legal proceedings which include claims for monetary damages asserted against the Company and its subsidiaries. The adequacy of provisions is regularly assessed as new information becomes available.

Any reimbursement that the Company is virtually certain to collect from a third party with respect to the obligation is recognized as a separate asset. However, this asset may not exceed the amount of the related provision.

The judgments used in applying the Company's significant accounting policies include the following:

*Determination of cash-generating units ("CGUs")*

The Company's assets are grouped into cash-generating units ("CGUs") based on their ability to generate separate identifiable cash flows. The determination of CGUs involves an assessment regarding the interdependency of cash inflows, and the Company's organizational structure.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont'd)

### New Standards and Interpretations Not Yet Effective

Standards issued but not yet effective up to the date of issuance of the Company's consolidated financial statements are listed below. This listing is of standards and interpretations issued, which the Company reasonably expects to be applicable at a future date. The Company is currently assessing the impact of the following standards on the consolidated financial statements and intends to adopt these standards when they become effective.

### IFRS 9 – Financial Instruments

IFRS 9 - Financial Instruments replaces the current IAS 39 Financial Instruments Recognition and Measurement. The standard introduces new requirements for classifying and measuring financial assets and liabilities. The Company will start the application of IFRS 9 in the financial statements effective from January 1, 2018. The Company has not yet evaluated the impact on the financial statements.

### IFRS 15 – Revenue from Contracts with Customers

IFRS 15 – Revenue from Contracts with Customers replaces all existing revenue requirements in IFRS and applies to all revenue arising from contracts with customers. The standard outlines the principles an entity must apply to measure and recognize revenue. The core principle is that an entity will recognize revenue at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer. The principles in IFRS 15 will be applied using a five-step model:

1) Identify the contract(s) with a customer;
2) Identify the performance obligations in the contract;
3) Determine the transaction price;
4) Allocate the transaction price to the performance obligations in the contract; and
5) Recognize revenue when (or as) the entity satisfies a performance obligation

The standard also specifies how to account for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract. The Company will start the application of IFRS 15 in the financial statements effective from January 1, 2018.

### IFRS 16 – Leases

IFRS 16 – Leases will replace IAS 17 Leases. The new standard specifies how to recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring the recognition of assets and liabilities for all leases, unless the lease term is 12 months or less or the underlying asset has a low value. The standard was issued in January 2016 and is effective for annual periods beginning on or after January 1, 2019. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements.

(Expressed in U.S. Dollars)

## 4. ACQUISITION OF APTERYX

On February 10, 2017, the Company acquired 100% of the common shares of Apteryx, Inc ("Apteryx") for aggregate consideration of US$10,700,326. The fair value of the total consideration paid was US$10,660,584.

The Company accounted for the acquisition using the acquisition method and the results of Apteryx's operations have been included in the consolidated financial statement from the date of the acquisition.

Goodwill acquired with Apteryx primarily comprises the expertise and reputation of the assembled workforce.

The allocation of the purchase price of the net identifiable assets based on their estimated fair values at the date of acquisition is as follows:

| | | |
|---|---|---|
| **ASSETS** | | |
| Cash | $ | 465,562 |
| Accounts receivable | | 484,633 |
| Prepaid expenses | | 3,571 |
| Property & equipment | | 61,156 |
| Acquired software technology | | 6,780,000 |
| Customer base | | 960,000 |
| Patents | | 470,000 |
| Brand | | 141,000 |
| | $ | 9,365,922 |
| **LIABILITIES** | | |
| Accounts payable & accrued liabilities | | 221,286 |
| Deferred Revenue | | 352,182 |
| | $ | 573,468 |
| Total identifiable net assets | $ | 8,792,454 |
| Goodwill on acquisition | | 1,868,130 |
| **Purchase consideration** | **$** | **10,660,584** |

The accounts receivable and prepaid expense fair value was equal to its contractual value, and all amounts were expected to be collected, as applicable.

The Company acquired the following in property, plant and equipment:

| | | |
|---|---|---|
| Furniture and fixtures | $ | 11,064 |
| Equipment | | 50,092 |
| | **$** | **61,156** |

The Company incurred acquisition costs of $365,125, which were expensed through the statement of income under professional fees expense in the year they occurred. This amount was comprised of due diligence, filing, legal and accounting costs.

(Expressed in U.S. Dollars)

### 4. ACQUISITION OF APTERYX (cont'd)

The fair value of the purchase consideration is comprised of the following:

| | | |
|---|---|---|
| Cash | $ | 6,987,362 |
| Deferred Consideration | | 1,610,258 |
| Common shares<br>3,385,840 with a value of $0.80 CND per share ( $2,708,672 CND) | | 2,062,964 |
| **Total consideration paid** | **$** | **10,660,584** |

The Company paid US$6,987,362 in cash and issued 3,385,840 common shares of the Company to the seller at CDN$0.80, representing US$2,062,964 of value. An additional US$1.2 million of the purchase price will be paid in cash tranches over 18 months. The final payment of US$450,000 will be paid in common shares of the Company or in cash at the Company's option, 24 months from closing. Deferred consideration is recorded at fair market value by calculating the present value of the cash flow.

The Company closed a series of financings related to the acquisition for gross proceeds of approximately CDN$14.4 million. The Company completed a private placement of 22,071,154 equity units of the Company (the "Equity Units") for gross proceeds of approximately CDN$13.3 million. (refer to Note 16). The Company also issued senior secured debentures with a principal amount of CDN$1,150,000 maturing 24 months from the closing date. The debenture is attached with a 12% coupon and 2,443,750 common shares of the Company. (refer to Note 13).

### 5. TRADE AND OTHER RECEIVABLES

| | | **December 31, 2017** | | December 31, 2016 |
|---|---|---|---|---|
| Trade accounts receivable | **$** | **1,557,714** | $ | 764,601 |
| Goods and services tax receivable | | **20,657** | | 34,738 |
| | **$** | **1,578,371** | $ | 799,339 |

During the year ended December 31, 2017, the Company has written off accounts receivable of $Nil (December 31, 2016 - $38,904).

### 6. INVENTORY

| | | **December 31, 2017** | | December 31, 2016 |
|---|---|---|---|---|
| VELscope | **$** | **142,822** | $ | 309,278 |
| Digital products | | **636,117** | | 226,673 |
| | **$** | **778,939** | $ | 535,951 |

Inventory is valued at the lower of cost and net realizable value. Cost includes the costs of purchases net of vendor allowances. The Company estimates net realizable value as the amount at which inventories are expected to be sold. Inventories are carried at lower of cost or net realizable value. When the cost of inventories is estimated to be unrecoverable due to obsolescence, damage or declining selling prices, the write-down of inventories is recognized as an expense. Storage and shipping costs, indirect administrative overhead and certain selling costs related to inventories are expensed in the period that these costs are incurred.

(Expressed in U.S. Dollars)

## 7. DEPOSIT

In 2014, the Company entered into an eight-year lease agreement for premises in Atlanta, Georgia. A requirement of the agreement was for a letter of credit to be issued to the lessor in the amount of $280,000. If the Company is in breach of the terms and conditions of the agreement, the lessor is entitled to the funds being held. The restricted cash was reduced by $120,000 in March 2016, and $90,000 in September 2016. These funds have been returned to the Company with the remaining balance being held until the duration of the agreement is complete. As of December 31, 2017, the Company has complied with the terms and conditions of the agreement and the letter of credit has been reduced to $70,000.

## 8. PROPERTY AND EQUIPMENT

The following table presents details of movement in the carrying value of property and equipment by asset type:

**Cost**

| | Equipment | Computer Equipment | Leasehold Improvements | Total |
|---|---|---|---|---|
| **Balance, January 1, 2016** | **$ 635,426** | **$ 57,994** | **$ 58,706** | **$ 752,126** |
| Additions | 103,784 | 13,884 | - | 117,668 |
| Disposals | (175,759) | (10,097) | - | (185,856) |
| **Balance, December 31, 2016** | **$ 563,451** | **$ 61,781** | **$ 58,706** | **$ 683,938** |
| Additions | 9,581 | 15,286 | 975 | 25,842 |
| Additions from acquisition | 11,063 | 50,093 | - | 61,156 |
| Disposals | - | - | - | - |
| **Balance, December 31, 2017** | **$ 584,095** | **$ 127,160** | **$ 59,681** | **$ 770,936** |

**Accumulated Depreciation**

| | Equipment | Computer Equipment | Leasehold Improvements | Total |
|---|---|---|---|---|
| **Balance, January 1, 2016** | **$ 343,981** | **$ 27,361** | **$ 6,578** | **$ 377,920** |
| Depreciation | 286,508 | 21,034 | 7,958 | 315,500 |
| Disposals | (175,759) | (10,097) | - | (185,856) |
| **Balance, December 31, 2016** | **$ 454,730** | **$ 38,298** | **$ 14,536** | **$ 507,564** |
| Depreciation | 71,426 | 31,453 | 7,996 | 110,875 |
| Disposals | - | - | - | - |
| **Balance, December 31, 2017** | **$ 526,156** | **$ 69,751** | **$ 22,532** | **$ 618,439** |

**Carrying Value**

| | Equipment | Computer Equipment | Leasehold Improvements | Total |
|---|---|---|---|---|
| **Balance, December 31, 2017** | **$ 57,939** | **$ 57,409** | **$ 37,149** | **$ 152,497** |
| **Balance, December 31, 2016** | **$ 108,721** | **$ 23,483** | **$ 44,170** | **$ 176,374** |

(Expressed in U.S. Dollars)

## 9. INTANGIBLE ASSETS

The following table presents details of movement in the carrying value of property and equipment by asset type:

**Cost**

| | Acquired Software Technology | Customer Base | Patents | Brand | Total |
|---|---|---|---|---|---|
| **Balance, January 1, 2017** | $ - | $ - | $ - | $ - | $ - |
| Additions from acquisition | 6,780,000 | 960,000 | 470,000 | 141,000 | 8,351,000 |
| **Balance, December 31, 2017** | **$ 6,780,000** | **$ 960,000** | **$ 470,000** | **$ 141,000** | **$ 8,351,000** |

**Accumulated Amortization**

| | Acquired Software Technology | Customer Base | Patents | Brand | Total |
|---|---|---|---|---|---|
| **Balance, January 1, 2017** | $ - | $ - | $ - | $ - | $ - |
| Amortization | 593,250 | 84,000 | 41,125 | 12,338 | 730,713 |
| **Balance, December 31, 2017** | **$ 593,250** | **$ 84,000** | **$ 41,125** | **$ 12,338** | **$ 730,713** |

**Carrying Value**

| | Acquired Software Technology | Customer Base | Patents | Brand | Total |
|---|---|---|---|---|---|
| **Balance, December 31, 2017** | **$ 6,186,750** | **$ 876,000** | **$ 428,875** | **$ 128,662** | **$ 7,620,287** |
| **Balance, December 31, 2016** | $ - | $ - | $ - | $ - | $ - |

For the purpose of the annual impairment testing, Brand is allocated to Apteryx, the CGU in which Brand belongs. The Company assesses Brand and Goodwill together as part of the annual impairment test for Apteryx. The impairment test performed resulted in no impairment of intangible assets as at December 31, 2017.

## 10. GOODWILL

| | Goodwill |
|---|---|
| **Balance, December 31, 2016** | $ - |
| Acquired through business combination | 1,868,130 |
| **Balance, December 31, 2017** | **$ 1,868,130** |

Goodwill acquired with Apteryx primarily comprises of the expertise and reputation of the assembled workforce.

The Company performed the annual impairment tests of goodwill and intangible assets Apteryx as at December 31, 2017. The impairment test performed resulted in no impairment of goodwill, or intangible assets as at December 31, 2017.

(Expressed in U.S. Dollars)

### 11. TRADE PAYABLES AND ACCRUED LIABILITIES

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Trade payables | **$ 761,710** | $ 2,564,502 |
| Accrued liabilities | **947,998** | 591,225 |
| State and provincial sales tax payable | **482,107** | 379,245 |
| | **$ 2,191,815** | $ 3,534,972 |

The Company warrants that its products will operate substantially in conformity with product documentation. The Company accrues for known warranty issues if a loss is probable and can be reasonably estimated and accrues for estimated incurred but unidentified warranty issues based on historical activity. To date, the Company has had no material warranty claims.

### 12. LEASE OBLIGATIONS AND COMMITMENTS

a) The Company has operating leases with respect to its operating premises in Vancouver, B.C., and Atlanta, Georgia. Future minimum lease payments as at December 31, 2017 are as follows:

| | |
|---|---|
| 2018 | 262,548 |
| 2019 | 258,040 |
| 2020 | 258,040 |
| 2021 | 258,040 |
| 2022 and thereafter | 23,100 |
| **Total future minimum lease payments** | **$ 1,059,768** |

b) The Company pays royalties at a rate of 0.75% of VELscope sales to the British Columbia Cancer Agency. During the year ended December 31, 2017, the Company accrued royalties of $8,109. (December 31, 2016- $12,717). As at December 31, 2017, total royalties accrued but not paid was $20,840 (December 31, 2016 – $12,731), which are classified as a component of accrued liabilities.

c) On August 1, 2014, the Company entered into a one-year consulting agreement ending July 31, 2015 with the former CEO of the Company whereby the former CEO would be paid CDN$295,000 annually and will receive royalties of 2% of all VELscope sales until January 1, 2018. The Company accrued royalties of $21,452 during the year ended December 31, 2017 (December 31, 2016 - $33,911), made payments of $5,620 and has a total of $50,500 accrued but not paid as of December 31, 2017 (December 31, 2016 - $63,325).

d) The Company may be subject to a variety of claims and suits that arise from time to time in the ordinary course of business. These matters are subject to inherent uncertainties. To date, the Company is aware of one claim for unpaid services plus interest. Subsequent to December 31, 2017, the claim was settled for a sum of CDN$75,000 (US$59,651) which has been accrued at December 31, 2017.

### 13. DEBENTURE

On July 22, 2015 (the "closing date"), the Company issued senior secured debentures with a principal amount of CDN$1,100,000 (US$827,365) maturing 12 months from the closing date. The debenture is attached with a 10% coupon and 65,450 common share purchase warrants of the Company at an exercise price of US$2.80. These warrants are exercisable at any time up to and including one year from the closing date. Transaction costs associated with this issuance were CDN$55,055 (US$38,392) and have been netted against the debenture proceeds received. Subsequent to the expiry of the original term and on October 7, 2016 (the "extension date"), the Company extended the terms by five years and increased the interest from 10% to 13%. The first year of interest totaling US$99,452 has been accrued and is payable at maturity 5 years from the extension date. The Company issued 65,481 common shares of the Company as consideration for the amendments. Accrued interest from the extension date to December 31, 2017 is US$140,588.

(Expressed in U.S. Dollars)

**13. DEBENTURE (cont'd)**

On September 25, 2015 (the "closing date"), the Company issued senior secured debentures with a principal amount of US$500,000 maturing 12 months from the closing date. The debenture is attached with a 10% coupon and 35,715 common share purchase warrants of the Company at an exercise price of US$2.80. These warrants are exercisable at any time up to and including one year from the closing date. Transaction costs associated with this issuance were US$10,020 and have been netted against the debenture proceeds received. Subsequent to the expiry of the original term and on October 7, 2016 (the "extension date"), the Company extended the terms by five years and increased the interest rate from 10% to 13%. The first year of interest totaling US$60,694 has been accrued and is payable at maturity 5 years from the extension date. The Company issued 40,464 common shares of the Company as consideration for the amendments. Accrued interest from the extension date to December 31, 2017 is US$80,347.

On July 6, 2016 (the "closing date"), the Company issued senior secured debentures with a principal amount of CDN$385,000 (US$296,885) maturing 12 months from the closing date. The debenture is attached with a 13% coupon and 25,000 common shares of the Company. Transaction costs associated with this issuance were CDN$28,952 (US$20,556) and have been netted against the debenture proceeds received. Subsequent to the expiry of the original term and on July 7, 2017 (the "extension date"), the Company extended the terms until February 10, 2019 and decreased the interest rate from 13% to 12%. The first year of interest totaling US$39,805 has been accrued and is payable at maturity on February 10, 2019. The Company issued 39,167 common shares of the Company as consideration for the amendments. Accrued interest from the extension date to December 31, 2017 is US$17,443.

On October 7, 2016 (the "closing date"), the Company issued senior secured debenture with a principal amount of CDN$500,000 (US$380,875) maturing 24 months from the closing date. The debenture is attached with a 12% coupon and 75,000 common shares of the Company. Transaction costs associated with this issuance were CDN$48,340 (US$36,825) and have been netted against the debenture proceeds received. Accrued interest at December 31, 2017 is US$59,651.

On December 22, 2016 (the "closing date"), the Company issued senior secured debenture with a principal amount of CDN$800,000 (US$594,960) maturing 24 months from the closing date. The debenture is attached with a 12% coupon and 170,000 common shares of the Company. Transaction costs associated with this issuance were CDN$81,548 (US$60,647) and have been netted against the debenture proceeds received. Accrued interest at December 31, 2017 is US$78,474.

On February 10, 2017 (the "close date"), the Company issued senior secured debentures with a principal amount of CDN$1,150,000 (US$875,857) maturing 24 months from the closing date. The debenture is attached with a 12% coupon and 244,375 common shares of the Company. The Company issued 35,200 finder's warrants (the "Finder's Warrants") to arm's length finders. Transaction costs associated with this issuance were CDN$35,288 (US$26,876) and have been netted against the debenture proceeds received. Accrued interest at December 31, 2017 is US$27,439.

On October 30, 2017 (the "closing date"), the Company issued second secured debentures with a principal amount of CDN$2,500,000 (US$1,938,690), maturing 24 months from the closing date. The debenture is attached with a 12% coupon and 531,250 common shares of the Company. The Company also issued 88,800 finder's warrants (the "Finder's Warrants") to arm's length brokers. Each Finder's Warrant is non-transferrable and exercisable at an exercise price of CDN$1.00 at any time up to and including the date which is 24 months from the closing date. Transaction costs associated with this issuance were CDN $232,032(US$179,935) and have been netted against the debenture proceeds received. Accrued interest at December 31, 2017 is US$41,093.

**14. RELATED PARTY TRANSACTIONS**

Related parties include key management, the Board of Directors, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.

During the year ended December 31, 2017 and 2016, the Company paid or accrued the following compensation expenses to key personnel of the Company:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Short-term compensation | **$ 915,948** | $ 802,221 |
| Stock-based payments | **$ 297,101** | $ 187,548 |



LED MEDICAL DIAGNOSTICS INC.

(Expressed in U.S. Dollars)

## 15. WARRANTS

On November 30, 2017, the Company completed the consolidation of its common shares on the basis of 10 pre-consolidation common shares for 1 post-consolidation common share. As a result, all outstanding warrant information presented has been retroactively adjusted on a 10 to 1 basis.

On February 10, 2017, the Company completed a private placement of equity units consisting of one common share and one-half of one common share warrant (the "Subscribers' Warrants"). The Company issued 11,035,553 Subscriber's Warrants with each warrant entitling the holder to acquire one common share at an exercise price of CDN$1.00 for a period of 24 months. The Subscriber Warrants were valued at fair market value using the Black-Sholes pricing model at a value of US$2,965,366 and accounted for on the balance sheet as a derivative liability. The Subscriber Warrants are revalued every period with the change being recorded as income or expense. The mark to market adjustment for the Subscriber Warrants for the year ended December 31, 2017 was $1,593,244 (December 31, 2016 - $NIL).

The Company also issued 1,326,286 finder's warrants (the "Finders' Warrants") to an arm's length finder as part of the private placement. Each Finders' Warrants is non-transferable and exercisable into one common share at an exercise price of CDN$1.00 for a period of 24 months. The Finders' Warrants were valued at fair market value using the Black-Scholes pricing model at a value of US$356,386.

On February 10. 2017, the Company issued 35,200 finder's warrants to arm's length finders as part of a debenture financing. Each Finder's Warrant is non-transferrable and exercisable at an exercise price of CDN$1.00 for a period of 24 months from the closing date. The fair value of the Finder's Warrants was calculated using the Black-Scholes pricing model and was valued at US$7,426.

On October 30, 2017, the Company issue issued 88,800 finder's warrants to arm's length brokers a debenture financing. Each Finders' Warrant is non-transferrable and exercisable at an exercise price of CDN$1.00 for a period of 24 months from the closing date. The fair value of the Finder's Warrants was calculated using the Black-Scholes pricing model and was valued at US$17,562.

The Finders' Warrants were treated as stock-based payment and recorded in equity.

The following table summarizes the warrant liability attributable to Canadian dollar denominated warrant transactions that occurred during the periods ended:

| | **December 31, 2017** | | December 31, 2016 | |
|---|---|---|---|---|
| | **Number of Warrants** | **Weighted Average Exercise Price** | Number of Warrants | Weighted Average Exercise Price |
| | | **(CDN$)** | | (CDN$) |
| Warrants outstanding, beginning of year | - | - | - | - |
| Issued | 12,485,839 | 1.00 | - | - |
| Exercised | - | - | - | - |
| Expired | - | - | - | - |
| **Warrants outstanding, end of period** | **12,485,839** | **1.00** | **-** | **-** |
| **Warrants exercisable, end of period** | **12,485,839** | **1.00** | **-** | **-** |

(Expressed in U.S. Dollars)

### 15. WARRANTS (cont'd)

The following table summarizes the US dollar denominated warrant transactions that occurred during the periods ended:

| | **December 31, 2017** | | December 31, 2016 | |
|---|---|---|---|---|
| | **Number of Warrants** | **Weighted Average Exercise Price** | Number of Warrants | Weighted Average Exercise Price |
| | | **(US$)** | | (US$) |
| Warrants outstanding, beginning of period | 1,724,260 | 3.60 | 3,402,613 | 3.60 |
| Issued | - | - | - | - |
| Exercised | - | - | - | - |
| Expired | (1,724,260) | 3.60 | (1,678,353) | 4.90 |
| **Warrants outstanding, end of period** | **-** | **-** | **1,724,260** | **3.60** |
| **Warrants exercisable, end of period** | **-** | **-** | **1,724,260** | **3.60** |

The following table summarizes information about the Company's warrants outstanding at December 31, 2017:

| | **Warrants Outstanding** | | **Warrants Exercisable** | |
|---|---|---|---|---|
| **Exercise Prices** | **Number Outstanding** | **Weighted Average Remaining Term (Years)** | **Number Exercisable** | **Weighted Average Remaining Term (Years)** |
| CDN$1.00 | 12,485,839 | 1.16 | 12,485,839 | 1.16 |
| | **12,485,839** | **1.16** | **12,485,839** | **1.16** |

The following table summarizes information about the Company's warrants outstanding at December 31, 2016:

| | **Warrants Outstanding** | | **Warrants Exercisable** | |
|---|---|---|---|---|
| **Exercise Prices** | **Number Outstanding** | **Weighted Average Remaining Term (Years)** | **Number Exercisable** | **Weighted Average Remaining Term (Years)** |
| US$2.00 | 657,360 | 1.15 | 657,360 | 1.15 |
| US$2.50 | 1,066,900 | 0.40 | 1,066,900 | 0.40 |
| | **1,724,260** | **0.69** | **1,724,260** | **0.69** |

### 16. SHARE CAPITAL

On November 30, 2017, the Company completed the consolidation of its common shares on the basis of 10 pre-consolidation common shares for 1 post-consolidation common share. As a result, all outstanding common share, option and deferred share unit information presented has been retroactively adjusted on a 10 to 1 basis.

(Expressed in U.S. Dollars)

**16. SHARE CAPITAL (cont'd)**

Authorized share capital

Unlimited number of common shares without par value

| | Number of Common Shares (Post Consolidation) | | Amount |
|---|---|---|---|
| **Outstanding, January 1, 2016** | **11,231,906** | **$** | **36,135,128** |
| Shares issued with debenture financing | 375,945 | | 79,876 |
| Settlement of share capital upon expiry of unexercised warrants | - | | 4,718,328 |
| Issuance of shares on exercise of DSU | 35,000 | | - |
| **Outstanding, December 31, 2016** | **11,642,851** | **$** | **40,933,332** |
| Shares issued pursuant to private placement | 22,071,154 | | 10,085,814 |
| Share issuance costs | - | | (724,288) |
| Subscriber warrants issued pursuant to private placement | - | | (2,965,366) |
| Finder warrants issued pursuant to private placement | - | | (356,386) |
| Shares issued as settlement on the purchase of Apteryx | 3,385,840 | | 2,062,964 |
| Shares issued with debenture financing | 814,792 | | 88,768 |
| Settlement of share capital upon expiry of unexercised warrants | - | | 1,819,396 |
| Rounding adjustment due to share consolidation | (1) | | |
| **Outstanding, December 31, 2017** | **37,914,636** | **$** | **50,944,234** |

On February 10, 2017, the Company completed a private placement of 22,071,154 equity units (the "Equity Units') at an issue price of CDN$0.60 per unit for total gross proceeds of approximately CDN$13.2 million (US$10.1 million). The Equity Units comprised of one common share and one-half of one common share purchase warrant (the "Subscribers' Warrants") with each warrant entitling the holder to acquire one common share at an exercise price of CDN$1.00 for a period of 24 months. Additionally, the Company issued 1,326,286 finder's warrants (the "Finders' Warrants") to an arm's length finder. (Refer to note 15). The company paid the issuance costs of CDN$950,988 (US$724,286) relating to legal, finders' and regulatory fees.

The Company also issued shares and finder's warrants as part of the debenture financing (refer to Note 13) and as part of the settlement to purchase Apteryx Inc. (refer to Note 4).

**17. STOCK-BASED PAYMENTS**

Commencing in 2005, the Company has granted, by way of directors' resolutions, share options to directors, officers, employees and other service providers at the exercise price set out at the grant date. The Company has a rolling incentive stock option plan. Under the terms of the Company's stock option plan, the Board of Directors may grant options to directors, officers, employees, consultants and service providers equal to 10% of issued and outstanding common shares of the Company from time to time on a rolling basis. The plan provides for the granting of options at the closing price of the Company's stock on the day prior to the grant date. The option plan states that the Board of Directors are the administrators of the plan with defined vesting period for options granted.

(Expressed in U.S. Dollars)

**17. STOCK-BASED PAYMENTS (cont'd)**

A summary of the Company's outstanding share options is presented below:

| | Outstanding options | |
|---|---|---|
| | Number of Common Shares (Post Consolidation) | Weighted Average Exercise Price in (CDN$) |
| **Outstanding, January 1, 2016** | **716,000** | **$ 3.90** |
| Options granted | 377,500 | 1.80 |
| Options forfeited | (218,333) | 2.60 |
| Options expired | (325,100) | 4.60 |
| **Outstanding, December 31, 2016** | **550,067** | **$ 2.50** |
| Options granted | 2,930,000 | 0.91 |
| Options forfeited | (210,565) | 1.36 |
| Options Expired | (32,500) | 3.52 |
| **Outstanding, December 31, 2017** | **3,237,002** | **$ 1.12** |

On April 10, 2017 and May 31, 2017, the Company granted a total of 2,930,000 stock options exercisable at a range of CDN$0.90 to CDN$1.00 per share in accordance with its stock option plan to directors, officers, consultants and employees. The options are for a term of up to 5 years and generally vest over a three-year period.

The options outstanding at December 31, 2017 have an exercises price in the range of CDN$0.90 to $4.90 (2016 – CDN$0.18 to $0.49 pre-consolidation) and a weighted average contractual life of 4.10 years (2016 – 5.53 years). The amount of options exercisable at the end of 2017 was 758,66 (2016 – 387,100).

The following table illustrates the assumptions of the option pricing models:

| Grant Date of Share Options | Share Price in CDN$ | Exercise Price | Annual Dividend Yield of Share Options | Volatility | Risk-Free Interest Rate | Expected Life of the Share Options |
|---|---|---|---|---|---|---|
| January 27, 2015 | $2.70 | $2.80 | Nil | 113.22% | 0.51% | 8 years |
| February 26, 2015 | $2.40 | $2.50 | Nil | 112.22% | 0.51% | 5 years |
| February 5, 2016 | $1.70 | $1.80 | Nil | 108.56% | 0.38% | 8 years |
| May 25, 2016 | $1.30 | $1.80 | Nil | 107.90% | 0.63% | 3 years |
| May 25, 2016 | $1.30 | $1.80 | Nil | 107.90% | 0.63% | 2 years |
| April 10, 2017 | $0.80 | $1.00 | Nil | 108.56% | 0.76% | 2 years |
| April 10, 2017 | $0.80 | $1.00 | Nil | 108.56% | 0.76% | 5 years |
| April 10, 2017 | $0.80 | $0.90 | Nil | 108.56% | 0.76% | 5 years |
| May 31, 2017 | $0.80 | $0.90 | Nil | 108.56% | 0.69% | 5 years |

For the year ended December 31, 2017, the Company recognized $628,280, of stock-based compensation expense (2016 – $258,529). Forfeiture rate is estimated based upon prior year forfeitures as a percentage of the total amount of options issued.

(Expressed in U.S. Dollars)

## 18. DEFERRED SHARE UNITS

The Company has a DSU Plan for the company's directors, executive officers and service providers ("eligible person").

DSU activity is presented below:

| | Number of DSUs | Weighted Average exercised price |
|---|---|---|
| **Outstanding, December 31, 2016** | **36,000** | **2.50** |
| Granted | - | - |
| Exercised | - | - |
| **Outstanding, December 31, 2017** | **36,000** | **2.50** |

All DSUs are exercisable as of December 31, 2017. The contractual life is dependent upon service provided to the Company. Options expire on December 15 of the 1st calendar year after service is terminated. During the year ended December 31, 2017, the Company recorded an expense of $Nil (2016 – $Nil).

## 19. SEGMENTED INFORMATION

The Company operates in a single geographical segment, being North America, and a single reporting segment, the development and commercialization of medical devices based on its proprietary imaging platform to aid in the detection and treatment of disease in human tissues. The North American segment makes up over 98% of the Company's sales. In addition, the Company provides dental and oral health specialists with advanced diagnostic imaging products and software.

The Company's operating segment is reported in a manner consistent with the internal reporting provided to the Chief Executive Officer ("CEO"). The CEO is considered the chief operating decision-maker ("CODM") and has the authority for resource allocation and is responsible for assessing the Company's performance.

## 20. CAPITAL DISCLOSURES

The Company's objectives for managing capital are:

- To maintain financial strength and to protect its ability to meet its on-going liabilities;
- To safeguard the Company's ability to continue as a going concern in order to pursue further development of medical devices so that it can provide adequate returns for shareholders and benefits for other stakeholders;
- To fund capital projects for facilitation of business expansion provided there is sufficient liquidity of capital to enable the internal financing;
- To maximize returns for shareholders over the long-term; and
- To maintain a capital base so as to maintain investor, creditor and market confidence.

The Company considers the items included in shareholders' equity (deficiency) and debt as capital. The Company sets the amount of capital in proportion to risk. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may issue new shares or return capital to shareholders. The Company is not subject to externally imposed capital requirements. There were no changes to the approach to capital management during the year.

(Expressed in U.S. Dollars)

### 20. CAPITAL DISCLOSURES (cont'd)

The capital of the Company consists of the consolidated equity and debentures, net of cash:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Equity/Deficiency | **$ 2,818,153** | $ (3,887,992) |
| Debentures | **5,871,293** | 2,623,542 |
| | **8,689,446** | (1,264,450) |
| Less: Cash | **(2,425,468)** | (874,567) |
| | **$ 6,263,978** | $ (2,139,017) |

### 21. INCOME TAXES

Income tax expense differs from the amount that would be computed by applying the federal and provincial statutory income tax rates of 26% (December 31, 2016 – 26%) to loss before income taxes due to the following:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Net loss before income taxes | **$ (2,495,015)** | $ (5,373,273) |
| Tax recovery at applicable rates | **(877,000)** | (1,397,051) |
| Non-deductible items and other | **142,000** | 68,697 |
| Temporary differences not recognized | **1,318,000** | (564,896) |
| Foreign currency translation | **425,765** | (135,294) |
| Opening deferred income tax adjustment | **(684,765)** | 2,028,544 |
| Share issue costs | **(324,000)** | |
| Income tax recovery | **$ -** | $ - |

The deferred tax assets have not been recognized in these consolidated financial statements, as management does not consider it more likely than not those assets will be realized in the carry forward period.

The composition of the Company's deferred tax assets as at December 31, 2017 and 2016 is as follows

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Deferred tax assets in relation to: | | |
| Non-capital losses carry forward | **$ 10,224,000** | $ 8,482,876 |
| SR&ED pool | **335,052** | 313,760 |
| Patents and intellectual property | **145,000** | 146,147 |
| Property and equipment | **75,000** | 201,543 |
| Reserves | **54,000** | |
| Share issue costs | **340,000** | 85,546 |
| **Deferred tax assets not recognized** | **$ 11,173,052** | $ 9,229,872 |

(Expressed in U.S. Dollars)

### 21. INCOME TAXES (cont'd)

As at December 31, 2017, the Company has net operating loss carry forwards for Canadian purposes aggregating US$25,321,708. These losses may be carried forward to apply against future income for tax purposes and will expire, if not utilized as follows:

| | | |
|---|---|---|
| 2026 | $ | 1,332,573 |
| 2027 | | 1,973,745 |
| 2028 | | 2,229,734 |
| 2029 | | 2,864,934 |
| 2030 | | 3,226,110 |
| 2031 | | 935,506 |
| 2032 | | 1,446,412 |
| 2033 | | 2,078,341 |
| 2034 | | 3,910,255 |
| 2035 | | 1,335,398 |
| 2036 | | 2,310,041 |
| 2036 | | 1,678,659 |
| **Net operating loss carry forwards** | **$** | **25,321,708** |

The Company also has $ 1,288,660 (CDN$1,620,257) of discretionary deductions relating to its research and development activities. These deductions can be carried forward indefinitely.

At December 31, 2017, the Company also has loss carry forwards for U.S. income tax purposes totalling $11,668,354. These losses may be carried forward to apply against future income for tax purposes and will expire, if not utilized as follows:

| | |
|---|---|
| 2034 | $ 1,118,138 |
| 2035 | 3,560,990 |
| 2036 | 4,325,720 |
| 2037 | 2,663,506 |
| **Net operating loss carry forwards** | **$ 11,668,354** |

### 22. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board of Directors approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures. The type of risk exposure and the way in which such exposure is managed is provided as follows:

<u>Classification of financial instruments</u>

Financial assets included in the statement of financial position are as follows:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Loans and receivables | | |
| Cash | $ 2,425,468 | $ 874,567 |
| Trade and receivables | 1,578,371 | 799,339 |
| | **$ 4,003,839** | $ 1,673,906 |

(Expressed in U.S. Dollars)

**22. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)**

Financial liabilities included in the statement of financial position are as follows:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Derivative liability at fair value through profit or loss: | | |
| Warrants | $ 1,372,122 | - |
| | **$ 1,372,122** | - |

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Other financial liabilities: | | |
| Trades payable and accrued liabilities | $ 2,191,815 | $ 3,534,972 |
| Deferred revenues | 892,570 | 309,531 |
| Debenture | 5,871,293 | 2,623,542 |
| Deferred consideration on acquisition | 1,650,000 | - |
| | **$ 10,605,678** | $ 6,468,045 |

Fair value

Due to the short-term nature of cash, trade and other receivables, trade payables and accrued liabilities and deferred revenue, their fair values approximate their carrying amounts.

The fair value of the Company's debenture and accrued interest payable is estimated by a discounted cash flow model based on market rate of interest existing at the end of the reporting period. Management believes that there has been no significant change in market interest rate since the inception of the debenture and as such the fair value of the debenture approximates the carrying value given that an immaterial amount of transaction cost was allocated to the debenture at inception.

Financial instruments measured at fair value are classified into one of three levels in the fair value hierarchy according to the relative reliability of the inputs used to estimate the fair values. The three levels of the fair value hierarchy are:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

Details of the Company's debentures and information about the fair value hierarchy as at December 31, 2017 are as follows:

| | **Quoted prices in active markets (Level 1)** | **Significant other observable inputs (Level 2)** | **Significant unobservable inputs (Level 3)** | **Fair value at December 31, 2017** |
|---|---|---|---|---|
| Debenture | - | $ 4,129,245 | $ 1,742,048 | $ 5,871,293 |
| **Total** | - | **$ 4,129,245** | **$ 1,742,048** | **$ 5,871,293** |

(Expressed in U.S. Dollars)

**22. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)**

Details of the Company's warrants and information about the fair value hierarchy as at December 31, 2016 are as follows:

| | Quoted prices in active markets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Fair value at December 31, 2016 |
|---|---|---|---|---|
| Debenture | - | $ 2,623,542 | - | $ 2,623,542 |
| **Total** | **-** | **$ 2,623,542** | **-** | **$ 2,623,542** |

The Company measures warrants using the Black-Scholes method, which utilizes the risk-free rate and the stock price volatility to estimate the fair value of warrants. The effects of non-observable inputs are not significant for CDN denominated warrants. There were no transfers between Level 1 and 2 in 2017 or 2016.

Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is exposed to credit risks arising from its cash and receivables. The Company manages credit risk by placing cash with major Canadian and U.S. financial institutions. With respect to receivables, the Company performs ongoing credit evaluations of its customers' financial condition.

The Company monitors collectability of receivables on an on-going basis to determine credit risk. In order to mitigate credit risk, the Company offers credit terms to established customers. Other customers are required to pay in advance or by credit card, prior to shipping of the product. At December 31, 2017, any accounts receivable due beyond one year have been provided for in the allowance for doubtful accounts.

As at December 31, 2017 and December 31, 2016, the Company's exposure to credit risk for these financial instruments was as follows:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Cash | $ 2,425,468 | $ 874,567 |
| Trade and Other Receivables | 1,578,371 | 799,339 |
| | **$ 4,003,839** | $ 1,673,906 |

Trade and other receivable balances of $1,578,371 as at December 31, 2017 (December 31, 2016 - $799,339) were aged as follows in the below table. It does not include goods and services tax receivable of $20,657 as at December 31, 2017 (December 31, 2016 – $34,738).

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Current | $ 1,075,602 | $ 540,537 |
| 31-60 days | 184,460 | 72,646 |
| Over 60 days | 297,652 | 142,075 |
| | **$ 1,557,714** | $ 755,258 |

(Expressed in U.S. Dollars)

### 22. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company has a planning and budgeting process in place to help determine the funds required to support the Company's normal operating requirements on an ongoing basis. The Company manages its liquidity risk associated with its financial liabilities through the use of cash flow generated from operations, and the issuance of additional equity primarily through private placements, as required to meet the payment requirements of maturing financial liabilities.

The contractual maturities of the Company's trade payables as at December 31, 2017 are listed below. Refer to the Note 12 for other contractual maturities, lease obligations and commitments that are not included in the table below.

Trade payables were aged as follows as at December 31, 2017 and December 31, 2016, respectively and do not include accrued liabilities, warranty provision and state and provincial sales tax payable. All trade payables are current liabilities:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Current | $ 440,118 | $ 221,101 |
| 31-60 days | 34,752 | 164,082 |
| Over 60 days | 286,840 | 2,179,319 |
| | **$ 761,710** | $ 2,564,502 |

The following is an analysis of the contractual maturities of the Company's non-derivative accrued liabilities at December 31, 2017:

| | **Within One Year** | **Between One and Five years** |
|---|---|---|
| Trade payables and accrued liabilities | $ 2,191,815 | $ - |
| Deferred revenue | 892,570 | - |
| Debenture | 2,152,841 | 3,718,452 |
| Deferred consideration on acquisition | 1,200,000 | 450,000 |
| | **$ 6,437,226** | $ 4,168,452 |

The following is an analysis of the contractual maturities of the Company's non-derivative liabilities at December 31, 2016:

| | **Within One Year** | **Between One and Five Years** |
|---|---|---|
| Trade payables and accrued liabilities | $ 3,534,972 | $ - |
| Deferred revenue | 309,531 | - |
| Debenture | 665,373 | 1,958,169 |
| | **$ 4,509,876** | $ 1,958,169 |

(Expressed in U.S. Dollars)

## 22. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)

The ability of the Company to make the aforementioned payment requirements related to maturing financial liabilities in the near term is dependent on the ability to obtain a line of credit and other debt instruments and the timing of cash flows from operations. The ability to obtain additional financing is dependent on continued access to debt and/or equity markets which may not be available on acceptable terms. In the event that debt or equity capital is not available on acceptable terms, the Company may need to explore other strategic alternatives.

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Interest rate risk is limited to the portion of the Company's cash held in bank accounts that earn interest and debentures that pay interest. There is no interest rate risk associated with the debentures as they carry a fixed rate of interest.

Due to the limited and short-term nature of these financial instruments, fluctuations in the interest rates will not have a significant impact on their fair value. As at December 31, 2017, the Company had not entered into any derivative contracts to manage this risk.

Currency risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada and the United States. The Company's functional currency is the U.S. dollar. The Company has not hedged its exposure to currency fluctuations.

The following is a summary of the Company's exposure to currency risk:

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| | **CDN$** | CDN$ |
| Cash | $ 345,952 | $ 461,801 |
| Trade receivables | 28,133 | 30,703 |
| Trade payable and accrued liabilities | (24,386) | (799,414) |
| **Net statement of financial position exposure** | **$ 349,699** | **$ (306,910)** |

Assuming that all other variables remain constant, a 10% change in the value of the Canadian dollar against the U.S. dollar would not materially affect the loss from operations.

## 23. EARNINGS PER SHARE

Profit attributable to ordinary shareholders (basic and diluted)

Earnings per share is calculated using Net Income (Loss)/Average Shares Outstanding.

| | **December 31, 2017** | December 31, 2016 |
|---|---|---|
| Loss for the year attributable to shareholders | $ 2,495,015 | $ 5,373,273 |
| Loss attributable to ordinary shareholders (basic and diluted) | **$ 2,495,015** | $ 5,373,273 |
| Loss per share – basic and diluted | **$(0.08)** | $(0.47) |
| Weighted average number of shares outstanding (basic and diluted) | **31,668,318** | 11,312,962 |

## 24. EMPLOYEE BENEFITS AND DEPRECIATION

The Company has incurred $ 5,355,362 (2016 – $ 4,693,901) of employee benefits and depreciation and amortization of $841,588 (2016 – $326,252). Employee benefits include wages, commissions, payroll taxes, stock-based payments and employee benefits.

## 25. SUBSEQUENT EVENTS

On April 24, 2018, the Company entered into an amending agreement (the "Amending Agreement") which extends the terms of the February 10, 2017 Apteryx purchase agreement (the "Purchase Agreement"). In the Purchase Agreement, a holdback payment of $500,000 was due on February 10, 2018 and a deferred cash payment of $300,000 was due on March 10, 2018. The Amending Agreement states the Company will pay $450,000 of the holdback payment which consists of $277,778 already paid plus an additional payment of $172,222 on May 17, 2018. The remaining $50,000 on the holdback payment and the $300,000 deferred cash payment have been extended to November 10, 2019 and will bear interest at 12% per annum paid in arrears quarterly commencing May 17, 2018. The remaining deferred payments of $400,000 on August 10, 2018 and $450,000, payable in shares or cash at the Company's option, on February 10, 2019 are unchanged from the Purchase Agreement. As of April 27, 2018, the Company is compliant with the payment terms of the Amending Agreement.