# Naturally Splendid Enterprises Ltd.

**Consolidated Financial Statements**

**December 31, 2015**

**Expressed in Canadian Dollars**

# INDEPENDENT AUDITORS' REPORT

## TO THE SHAREHOLDERS OF NATURALLY SPLENDID ENTERPRISES LTD.

We have audited the accompanying consolidated financial statements of Naturally Splendid Enterprises Ltd., which comprise the consolidated statements of financial position as at December 31, 2015 and 2014, and the consolidated statements of loss and comprehensive loss, changes in equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

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

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the 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 in our audits is sufficient and appropriate to provide a basis for our audit opinion.

*Opinion*
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Naturally Splendid Enterprises Ltd. as at December 31, 2015 and 2014, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

*Emphasis of Matter*
Without qualifying our opinion, we draw attention to note 1 in the consolidated financial statements, which describes matters and conditions that indicate the existence of material uncertainties that may cast significant doubt about the Company's ability to continue as a going concern.

Smythe LLP

Chartered Professional Accountants

Vancouver, British Columbia
April 29, 2016





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## Naturally Splendid Enterprises Ltd.

Consolidated Statements of Financial Position
As at December 31
(Expressed in Canadian Dollars)

| | Note | 2015<br>$ | 2014<br>$ |
|---|---|---|---|
| **Assets** | | | |
| **Current** | | | |
| Cash | | 34,330 | 25,404 |
| Trade and other receivables | 5 | 264,128 | 58,266 |
| Inventories | 6 | 387,803 | 277,773 |
| Advances and prepaid expenses | 7 | 317,310 | 218,925 |
| Deposit | | 1,260 | 40,000 |
| | | 1,004,831 | 620,368 |
| **Due from related parties** | 14 | 414,326 | |
| **Long-term deposits** | 7 | 36,000 | 11,457 |
| **Restricted cash** | 8 | 57,560 | 17,310 |
| **Property and equipment** | 9 | 445,392 | 99,231 |
| **Technology license** | 9 and 10 | 1,399,976 | - |
| **Website, technology and other intangibles** | 4 and 9 | 259,745 | - |
| **Goodwill** | 4 and 20 | 891,168 | - |
| | | **4,508,998** | **748,366** |
| **Liabilities** | | | |
| **Current** | | | |
| Trade and other payables | 12 and 14 | 1,704,998 | 126,882 |
| Current portion of capital lease obligation | 11 | 4,927 | 4,182 |
| Deferred revenues | | 50,000 | - |
| | | 1,759,925 | 131,064 |
| **Capital lease obligation** | 11 | 2,914 | 8,912 |
| **Long-term debt** | 13 | 476,758 | - |
| | | **2,239,597** | **139,976** |
| **Equity** | | | |
| Share capital | 16 | 12,459,312 | 6,403,221 |
| Subscriptions received | 16 | 52,500 | 106,920 |
| Reserves | 16 | 1,112,772 | 355,498 |
| Deficit | | (13,086,443) | (6,257,249) |
| **Equity attributable to owners of the company** | | 538,141 | 608,390 |
| **Non-controlling interest** | | 1,731,260 | - |
| | | 2,269,401 | 608,390 |
| | | **4,508,998** | **748,366** |

**APPROVED AND AUTHORIZED FOR ISSUE BY THE BOARD ON April 29, 2016:**

| | |
|---|---|
| ***"Craig Goodwin"*** | ***"Peter Hughes"*** |
| Director | Director |

## Naturally Splendid Enterprises Ltd.

Consolidated Statements of Loss and Comprehensive Loss
Years ended December 31
(Expressed in Canadian Dollars)

| | Note | 2015 $ | 2014 $ |
|---|---|---|---|
| **Revenue** | | **301,705** | **234,761** |
| **Cost of sales** | | **244,550** | **193,092** |
| **Gross Profit** | | **57,155** | **41,669** |
| **Selling and distribution expenses** | | | |
| Commissions and direct selling | | 842 | 5,741 |
| Facility | | 169,408 | - |
| Product development, net of grants | | 154,735 | 7,944 |
| Product promotion and trade shows | | 312,106 | 172,948 |
| Salaries and wages | | 143,550 | 68,468 |
| Bad debts | | - | 27,729 |
| | | 780,641 | 282,830 |
| **Administrative expenses** | | | |
| Accounting and audit | | 120,073 | 96,763 |
| Amortization | 9 | 134,661 | 30,371 |
| Bank charges, interest and accretion | 13 | 50,101 | 4,899 |
| Consulting | 14 | 327,766 | 135,172 |
| Directors' fees | 14 | 700 | - |
| Legal | | 211,042 | 97,316 |
| Management fees | 14 | 654,020 | 264,000 |
| Office, rent and salaries | | 464,641 | 244,887 |
| Promotion | | 588,745 | 343,248 |
| Share-based payments | 14 and 16 | 906,900 | 201,351 |
| Transfer agent and filing fees | | 70,276 | 107,461 |
| Travel | | 67,758 | 30,938 |
| | | 3,596,683 | 1,556,406 |
| | | (4,320,169) | (1,797,567) |
| Foreign exchange gain (loss) | | 21,103 | (1,029) |
| Other income | 14 | 100,065 | - |
| Interest income | | 1,732 | 2,839 |
| Impairment of goodwill | 20 | (2,784,017) | - |
| **Net loss and comprehensive loss for the year** | | **(6,981,286)** | **(1,795,757)** |
| **Comprehensive loss attributed to:** | | | |
| Owners of the company | | **(6,872,220)** | **(1,795,757)** |
| Non-controlling interest | | **(109,066)** | **-** |
| | | **(6,981,286)** | **(1,795,757)** |
| Comprehensive income (loss) per share | | | |
| Basic and diluted | | $ (0.14) | $ (0.06) |
| Weighted average number of common shares outstanding | | | |
| Basic and diluted | | 51,610,077 | 30,110,027 |

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

**Naturally Splendid Enterprises Ltd.**
Consolidated Statements of Cash Flows
As at December 31
(Expressed in Canadian Dollars)

| | 2015 | 2014 |
|---|---|---|
| | $ | $ |
| **Operating activities** | | |
| Net loss for the year | (6,981,286) | (1,795,757) |
| Adjustments to reconcile loss to net cash | | |
| Amortization | 134,661 | 30,371 |
| Shares issued for services | 49,375 | - |
| Impairment of goodwill | 2,784,017 | - |
| Shares issued for loans | 82,560 | - |
| Interest and accretion expense on loan | 33,465 | - |
| Share-based payments | 906,900 | 201,351 |
| **Changes in non-cash working capital:** | | |
| Trade and other receivables | (162,993) | 61,038 |
| Inventories | (94,302) | (8,259) |
| Advances and prepaid expenses and deposits | (195,685) | 69,165 |
| Long-term deposits | (24,543) | 58 |
| Restricted cash | (40,250) | - |
| Trade and other payables | 1,227,797 | (69,317) |
| Deferred revenues | 50,000 | - |
| **Cash used in operating activities** | (2,230,284) | (1,511,350) |
| | | |
| **Investing activities** | | |
| Repayment of capital lease | (5,253) | (11,302) |
| Purchase of property and equipment, net | (82,935) | (34,046) |
| Acquisition of technology | (549,000) | (176,000) |
| Acquisition of manufacturing facility | (1,750,000) | - |
| Cash acquired from Chi | 3,505 | - |
| **Cash used in investing activities** | (2,383,683) | (221,348) |
| | | |
| **Financing activities** | | |
| Repayments to related parties | (414,326) | (3,675) |
| Loans payable | 317,441 | - |
| Proceeds from issuance of shares, net | 3,295,272 | 1,259,086 |
| Proceeds from options exercised | 146,038 | 87,500 |
| Proceeds from warrants exercised | 1,225,968 | 118,604 |
| Subscriptions received | 52,500 | 106,920 |
| **Cash provided by financing activities** | 4,622,893 | 1,568,435 |
| | | |
| **Net change in cash and cash equivalents** | 8,926 | (164,263) |
| | | |
| **Cash, beginning of year** | 25,404 | 189,667 |
| | | |
| **Cash, ending of year** | 34,330 | 25,404 |

**Supplemental cash flow information (note 21)**

**Naturally Splendid Enterprises Ltd.**

Consolidated Statements of Changes in Equity

(Expressed in Canadian Dollars)

| | Common Shares | Share capital $ | Subscriptions received $ | Reserves $ | Deficit $ | Equity attributable to the owners of the company $ | Non-controlling interest $ | Total equity (deficit) $ |
|---|---|---|---|---|---|---|---|---|
| **Balance at December 31, 2013** | 28,731,105 | 4,853,214 | - | 238,964 | (4,461,492) | 630,686 | - | 630,686 |
| Private placement, net of share issuance costs | 6,843,500 | 1,259,086 | - | - | - | 1,259,086 | - | 1,259,086 |
| Private placement subscriptions received | - | - | 106,920 | - | - | 106,920 | - | 106,920 |
| Warrants exercised | 584,394 | 118,604 | - | - | - | 118,604 | - | 118,604 |
| Reclassify options exercised | 500,000 | 87,500 | - | - | - | 87,500 | - | 87,500 |
| Reclassify warrants exercised | - | 84,817 | - | (84,817) | - | - | - | - |
| Share-based payments | - | - | - | 201,351 | - | 201,351 | - | 201,351 |
| Net loss for the year | - | - | - | - | (1,795,757) | (1,795,757) | - | (1,795,757) |
| **Balance at December 31, 2014** | 36,658,999 | 6,403,221 | 106,920 | 355,498 | (6,257,249) | 608,390 | - | 608,390 |
| | | | | | | | | |
| **Balance at December 31, 2014** | 36,658,999 | 6,403,221 | 106,920 | 355,498 | (6,257,249) | 608,390 | - | 608,390 |
| Private placement, net of share issuance costs | 10,781,882 | 3,364,399 | (106,920) | 37,793 | - | 3,295,272 | - | 3,295,272 |
| Technology license acquisition (note 10) | 2,928,571 | 761,428 | - | - | - | 761,428 | - | 761,428 |
| BPC acquisition (note 4) | 367,647 | 165,441 | - | - | - | 165,441 | - | 165,441 |
| Chi acquisition (note 4) | 319,148 | 116,489 | - | - | - | 116,489 | - | 116,489 |
| Shares issued for services (note 16) | 125,000 | 49,375 | - | - | - | 49,375 | - | 49,375 |
| Shares issued for loans (note 13) | 356,107 | 82,560 | - | - | - | 82,560 | - | 82,560 |
| Warrants exercised | 4,478,669 | 1,225,968 | - | - | - | 1,225,968 | - | 1,225,968 |
| Options exercised | 764,500 | 146,038 | - | - | - | 146,038 | - | 146,038 |
| Option subscriptions received | - | - | 52,500 | - | - | 52,500 | - | 52,500 |
| Reclassify warrants and options exercised | - | 144,393 | - | (144,393) | - | - | - | - |
| Reclassify cancelled options | - | - | - | (43,026) | 43,026 | - | - | - |
| Share-based payments | - | - | - | 906,900 | - | 906,900 | - | 906,900 |
| Net loss for the year | - | - | - | - | (6,872,220) | (6,872,220) | (109,066) | (6,981,286) |
| Non-controlling interest | - | - | - | - | - | - | 1,840,326 | 1,840,326 |
| **Balance at December 31, 2015** | 56,780,523 | 12,459,312 | 52,500 | 1,112,772 | (13,086,443) | 538,141 | 1,731,260 | 2,269,401 |

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

## 1. Nature of Operations and Going Concern

Naturally Splendid Enterprises Ltd. (formerly Race Capital Corp.) ("Naturally Splendid" or the "Company") was incorporated under the laws of the province of British Columbia on December 21, 2010.

The Company is in the natural food industry and provides food supplements packaged for distribution through grocery stores, health and nutrition stores, and other outlets where consumers purchase health-related products. Materials are sourced in bulk and repackaged at the Company's facility with its unique branding under the Company's name. Current products are hemp-based food items that are both conventional and organic, including whole grains and protein powders. Product sales are supported through a combination of direct and online sales and distribution channels.

The head office, principal address, and registered and records office is located at 605 - 1166 Alberni Street, Vancouver, British Columbia, Canada V6E 3Z3.

The Company's consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. For the year ended December 31, 2015, the Company had a net loss of $6,981,286 (2014 - $1,795,757) and a working capital deficit of $755,094 (2014 – working capital of $489,304) as at December 31, 2015.

Management cannot provide assurance that the Company will ultimately achieve profitable operations or positive cash flow. The Company's continuation as a going concern is dependent on its ability to attain profitable operations and raise additional capital. These matters indicate the existence of material uncertainties that may cast significant doubt about the Company's ability to continue as a going concern. These consolidated financial statements do not reflect the adjustments to the carrying values of assets and liabilities, the reported revenues and expenses and consolidated statement of financial position classifications that would be necessary if the going concern assumption was inappropriate. Such adjustments could be material.

## 2. Basis of Presentation

### a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

The consolidated financial statements were authorized for issue by the Board of Directors on the date noted on the consolidated statements of financial position.

**b) Basis of presentation**

These consolidated financial statements have been prepared on the historical cost basis, except for certain financial instruments, which are measured at fair value, as explained in note 15. These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. These consolidated financial statements include the accounts of the following entities:

| | Relationship | Percentage |
|---|---|---|
| Naturally Splendid Enterprises Ltd. | Parent | 100% |
| Naturally Splendid Enterprises 2013 Ltd. | Subsidiary | 100% |
| Naturally Splendid USA Ltd. | Subsidiary | 100% |
| Chi Hemp Industries Inc. ("Chi") (note 4(b)) | Subsidiary | 100% |
| POS BPC Manufacturing Corp. ("BPC") (note 4(a)) | Subsidiary | 51% |

All intercompany balances and transactions are eliminated on consolidation. Control is based on whether an investor has power over the investee, exposure or rights to variable returns from its involvement with the investee, and the ability to use its power over the investee to affect the amount of returns.

## 3. Significant Accounting Policies

**a) Cash equivalents**

Cash equivalents include short-term liquid investments with maturities of 90 days or less, are readily convertible into known amounts of cash and which are subject to insignificant changes in value.

**b) Inventories**

Inventories are stated at the lower of production cost and net realizable value. Production costs include direct and indirect labour, operating materials and supplies, transportation costs, and an appropriate portion of fixed and variable overhead expenses. Inventories are accounted for on a first-in, first-out basis. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Supplies used in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost.

**c) Equipment**

Property and equipment are stated at cost less accumulated amortization and accumulated impairment losses. The cost of an item of property and equipment consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Amortization is provided at rates calculated to write-off the cost of property and equipment, less their estimated residual value, using the declining-balance or straight-line method over the following annual rates:

| | |
|---|---|
| Computer equipment | 55% declining-balance |
| Furniture and equipment | 20% declining-balance |
| Leasehold improvements | Straight line over 5 years |
| Building | Straight line over 40 years |
| Equipment | 15% diminishing balance |

Property and equipment are derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in profit or loss.

**d) Revenue recognition**

The Company generates its revenue from sales to retailers, online web sales, and bulk sales. Sales revenues are recognized when the risks and rewards of ownership pass to the buyer, collection is reasonably assured and the price is reasonably determinable. The Company recognizes revenue from customer orders upon shipment of the order when risks and rewards have been transferred.

**e) Related party transactions**

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control. Related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

**f) Share-based payments**

Share-based payments to employees are measured at the fair value of the instruments issued and recognized over the vesting periods using the graded vesting method. Share-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. Share-based payments to employees are measured at the fair value of the instruments issued and amortized over the vesting periods.

If it is determined that the fair value of goods and services received cannot be reliably measured, the share-based expense is measured at the fair value of the equity instruments issued using the Black-Scholes option pricing model. For both employees and non-employees, the fair value of share-based expense is recognized in profit or loss, with a corresponding increase in reserves.

**g) Loss per share**

Loss per share is calculated using the weighted average number of common shares outstanding. The calculation of diluted earnings per share assumes that outstanding options and warrants are exercised and the proceeds are used to repurchase shares of the Company at the average market price of the shares for the period. Diluted loss per share is not presented if the effects are anti-dilutive.

**h) Warrants**

Proceeds received on issuance of units, consisting of common shares and warrants, are allocated first to common shares based on the market trading price of the common shares, and any excess is allocated to warrants.

**i) Research and development**

Research costs are expensed as incurred. Product development expenditures are expensed as incurred until such time they meet certain specific criteria for deferral and amortization. Management assesses whether it has met such criteria at each reporting date. In making the assessment, management considers status of the product development, regulatory submissions, marketing and finance plans. The Company has not deferred any product development expenditures to date.

**j) Intangible Assets and Technology License**

The Company's intangible assets include Exclusive License IP ("License IP") acquired with the acquisition of BPC (note 4), website, technology and non-compete clause acquired with the acquisition of Chi (note 4), and technology license agreements acquired from Full Spectrum Laboratories Limited ("FSL") (the "License Technology") (note 10). Intangible assets are recorded at cost less accumulated amortization and any impairment losses. Amortization for intangible assets with finite lives is calculated over the useful lives. The Company's amortization policy for intangible assets with finite lives is as follows:

Technology License – 15 years
Non-compete clause – 1 year
Website and Technology – 1 year

The Company's Licensed IP is not amortized, as it has an indefinite life.

**k) Significant accounting judgments, estimates and assumptions**

The preparation of these consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets, liabilities and contingent liabilities at the date of the consolidated financial statements, and reported amounts of revenue and expenses during the reporting period. Estimates and assumptions are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and further periods if the review affects both current and future periods.

Significant assumptions about the future and other sources of estimation uncertainty that management has made that could result in a material adjustment to the carrying amounts of assets and liabilities in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

*Critical accounting estimates*

Critical accounting estimates are estimates and assumptions made by management that may result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year and include, but are not limited to, the following:

Recoverability of accounts receivable

Provisions are made against accounts that, in the estimation of management, may be uncollectible. The recoverability assessment of accounts receivable is based on a range of factors, including the age of the receivable and the creditworthiness of the customer. The provision is assessed monthly with a detailed formal review of balances and security being conducted quarterly. Determining the recoverability of an account involves estimation as to the likely financial condition of the customer and their ability to subsequently make payments. To the extent that future events impact the financial condition of the customers these provisions could vary significantly.

Share-based payments

The fair value of share-based payments is subject to the limitations of the Black-Scholes option pricing model that incorporates market data and involves uncertainty in estimates used by management in the assumptions. Because the Black-Scholes option pricing model requires the input of highly subjective assumptions, including the volatility of share prices, changes in subjective input assumptions can materially affect the fair value estimate.

Income taxes

In assessing the probability of realizing income tax assets, management makes estimates related to expectations of future taxable income, applicable tax opportunities, expected timing of reversals of existing temporary differences and likelihood that tax positions taken will be sustained upon examination by applicable tax authorities. In making its assessments, management gives additional weight to positive and negative evidence that can be objectively verified.

Interest rates

The Company estimates a fair value interest rate in determining the fair value of the loans payable.

Recovery of deferred tax assets

The Company estimates the expected manner and timing of the realization or settlement of the carrying value of its assets and liabilities and applies the tax rates that are enacted or substantively enacted on the estimated dates of realization or settlement.

*Critical accounting judgments*

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements include, but are not limited to, the following:

Valuation of inventory

Management makes estimates of future customer demand for products when establishing appropriate provisions for inventory obsolescence. In making these estimates management considers the life of inventory and profitability of recent sales.

Useful lives of intangible assets and equipment

Depreciation and amortization of the Company's equipment and intangible assets incorporate estimates of useful lives and residual values. These estimates may change as market conditions change and the future economic benefits from the use of the asset changes, thereby impacting the useful life and residual value of the equipment or intangible asset. Any revisions to useful life are accounted for prospectively.

Impairment of goodwill and Licensed IP

Determining the impairment of goodwill and Licensed IP requires an estimation of the recoverable amount, which is defined as the higher of fair value less cost of disposal or value in use. Many factors used in assessing recoverable amounts are outside of the control of management and it is reasonably likely that assumptions and estimates will change from period to period. These changes may result in future impairments.

The allocation of fair value of assets acquired

The determination of fair value of assets acquired requires management to make assumptions and estimates about future events. The assumptions and estimates with respect to determining the fair value of the assets and liabilities acquired require judgment and include estimates of future cash flows.

The assessment of the transactions as an asset acquisition or business combination

Management has had to apply judgments relating to the Transaction with respect to whether the acquisition was a business combination or an asset acquisition. Management applied a three-element process to determine whether a business or an asset was purchased, considering inputs, processes and outputs of each acquisition in order to reach a conclusion.

Going concern

The assessment of the Company's ability to continue as a going concern and to raise sufficient funds to pay for its ongoing operating expenditures and meet its liabilities for the ensuing year involves significant judgment based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

**l) Income taxes**

Deferred tax is calculated, using the financial position method, on all temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such deferred tax assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred 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 the tax rates that have been enacted or substantively enacted at the reporting date.

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.

**m) Impairment of non-financial assets**

The carrying amount of the Company’s assets is reviewed for an indication that the carrying amount is not recoverable. If an indication of impairment exists, the Company makes an estimate of the asset’s recoverable amount. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. The recoverable amount of an asset group is the higher of its fair value less costs to sell and its value in use. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. The Company tests for impairment on its non-current assets annually.

Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount. Impairment losses are recognized in profit or loss.

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset’s recoverable amount. An impairment loss is reversed only to the extent that the asset’s carrying amount does not exceed the carrying amount that would have been determined, net of amortization, if no impairment loss had been recognized.

**n) Goodwill**

The Company measures goodwill as the fair value of the consideration transferred less the fair value of the identifiable assets acquired and the liabilities assumed, all measured as of the acquisition date. Since goodwill results from the application of the acquisition method of accounting for a business combination, it requires judgment in the determination of the fair value of assets and liabilities.

Goodwill is allocated as of the date of the business combination to the Company’s cash-generating units (“CGU”). Goodwill is not amortized, but is tested for impairment at least annually. An impairment loss in respect of goodwill is not reversed. On the disposal or termination of a previously acquired business, any remaining balance of associated goodwill is included in the determination of the gain or loss on disposal.

**o) Provisions**

Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources that can be reliably estimated will be required to settle the obligation. Where a provision is measured using the cash flows estimated to settle the obligation, its carrying amount is the present value of those cash flows.

**p) Financial instruments**

**Financial assets**

Financial assets are classified as financial assets at fair value through profit or loss ("FVTPL"), held-to-maturity ("HTM"), loans and receivables, available-for-sale ("AFS") or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Company determines the classification of its financial assets at initial recognition. Financial assets are recognized initially at fair value. The subsequent measurement of financial assets depends on their classification as follows:

*Financial assets at fair value through profit or loss*

Financial assets are classified as held-for-trading and are included in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives, other than those designated as effective hedging instruments are also categorized as held-for-trading. These assets are carried at fair value with gains or losses recognized in profit or loss. Transaction costs associated with financial assets at FVTPL are expensed as incurred. Cash is included in this category of financial assets.

*Held-to-maturity and loans and receivables*

HTM and loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortized cost using the effective interest method if the time value of money is significant. Gains and losses are recognized in profit or loss when the financial assets classified in this category are derecognized or impaired, as well as through the amortization process. Transaction costs are included in the initial carrying amount of the asset. Advances and trade and other receivables are classified as loans and receivables.

*AFS financial assets*

AFS financial assets are those non-derivative financial assets that are not classified as loans and receivables. After initial recognition, AFS financial assets are measured at fair value, with gains or losses recognized within other comprehensive income. Accumulated changes in fair value are recorded as a separate component of equity until the investment is derecognized or impaired. Transaction costs are included in the initial carrying amount of the asset. AFS assets include short-term investments in equities of other entities.

The fair value is determined by reference to bid prices at the close of business on the reporting date. Where there is no active market, fair value is determined using valuation techniques. Where fair value cannot be reliably measured, assets are carried at cost. The Company does not have any assets classified as AFS financial assets.

**Financial liabilities**

Financial liabilities are classified as financial liabilities at FVTPL, derivatives designated as hedging instruments in an effective hedge, or as financial liabilities measured at amortized cost, as appropriate. The Company determines the classification of its financial liabilities at initial recognition. The measurement of financial liabilities depends on their classification, as follows:

*Financial liabilities at fair value through profit or loss*

Financial liabilities at FVTPL have two subcategories, comprised of financial liabilities held-for-trading and those designated by management on initial recognition. Transaction costs on financial liabilities at FVTPL are expensed as incurred. These liabilities are carried at fair value with gains or losses recognized in profit or loss. Trade and other payables are included in this category of financial liabilities.

*Financial liabilities measured at amortized cost*

All other financial liabilities are initially recognized at fair value, net of transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. Amortized cost is calculated by taking into account any issue costs, and any discount or premium on settlement. Gains and losses arising on the repurchase, settlement or cancellation of liabilities are recognized, respectively, in interest, other revenues and finance costs. Loans payable are included in this category of financial liabilities.

**Hierarchy**

Financial instruments measured at fair value are classified into one of the 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.

**q) Future accounting pronouncements**

New accounting standards issued but not yet effective applicable to the Company are as follows:

**IFRS 16 *Leases***

IFRS 16 specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is twelve months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17 *Leases.*

This standard is effective for the Company's annual periods beginning January 1, 2019.

**IFRS 9 *Financial Instruments***

IFRS 9 will replace IAS 39 *Financial Instruments: Recognition and Measurement* and IFRIC 9 *Reassessment of Embedded Derivatives*. The final version of this new standard supersedes the requirements of earlier versions of IFRS 9. However, for annual periods beginning before January 1, 2018, an entity may elect to apply those earlier versions instead of applying the final version of this new standard if its initial application date is before February 1, 2015.

The main features introduced by this new standard compared with predecessor IFRS are as follows:

- *Classification and measurement of financial assets:*
  Debt instruments are classified and measured on the basis of the entity's business model for managing the asset and its contractual cash flow characteristics as either: "amortized cost", "fair value through other comprehensive income", or "fair value through profit or loss" (default). Equity instruments are classified and measured as "fair value through profit or loss" unless upon initial recognition elected to be classified as "fair value through other comprehensive income".
- *Classification and measurement of financial liabilities:*
  When an entity elects to measure a financial liability at fair value, gains or losses due to changes in the entity's own credit risk is recognized in other comprehensive income (as opposed to previously profit or loss). This change may be adopted early in isolation of the remainder of IFRS 9.
- *Impairment of financial assets:*
  An expected credit loss impairment model replaced the incurred loss model and is applied to financial assets at "amortized cost" or "fair value through other comprehensive income", lease receivables, contract assets or loan commitments and financial guarantee contracts. An entity recognizes twelve-month expected credit losses if the credit risk of a financial instrument has not increased significantly since initial recognition and lifetime expected credit losses otherwise.
- *Hedge accounting:*
  Hedge accounting remains a choice, however, is now available for a broader range of hedging strategies. Voluntary termination of a hedging relationship is no longer permitted. Effectiveness testing now needs to be performed prospectively only. Entities may elect to continue to applying IAS 39 hedge accounting on adoption of IFRS 9 (until the IASB has completed its separate project on the accounting for open portfolios and macro hedging).

This standard is effective for the Company's annual periods beginning January 1, 2018.

(Expressed in Canadian Dollars)

**IFRS 15 *Revenue from Contracts with Customers***

This new standard establishes a comprehensive framework for the recognition, measurement and disclosure of revenue replacing IAS 11 *Construction Contracts*, IAS 18 *Revenue*, IFRIC 13 *Customer Loyalty Programmes*, IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfers of Assets from Customers*, and SIC-31 *Revenue — Barter Transactions Involving Advertising Services*.

The main features introduced by this new standard compared with predecessor IFRSs are as follows:

- Revenue is recognized based on a five-step model:
  1. Identify the contract with customer;
  2. Identify the performance obligations;
  3. Determine the transaction price;
  4. Allocate the transaction price to the performance obligations; and
  5. Recognize revenue when (or as) the performance obligations are satisfied.

- New disclosure requirements on information about the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers.

This standard is effective for the Company's annual periods beginning January 1, 2018.

## 4. Acquisitions

### a) Acquisition of POS BPC Manufacturing Corp.

On June 18, 2015, the Company completed the acquisition of 51% of BPC in accordance with the terms of a securities purchase agreement with POS Management Corp. and POS Holdings Corp. (together, "POS"). In consideration of the BPC shares, the Company paid $1.75 million and issued 367,647 common shares of the Company to POS, of which the shares are subject to a trading restriction for a period of twelve months from the date of issue. The Company, POS and BPC entered into a unanimous shareholders' agreement that provides, among other things, equal board representation for the companies. Certain directors and officers of the Company and POS were appointed to serve as directors and officers of BPC. BPC operates a 12,000-square-foot facility containing the equipment required to process a variety of products, including the suite of plant-based omega technologies, such as HempOmega that the Company has licensed from FSL.

The Company also entered into a license agreement with POS whereby the Company has the right to sell and market, on an exclusive basis, five ingredients created using POS technology and sell and market, on a non-exclusive basis, additional ingredients created using POS technologies. In consideration of the license, the Company has agreed to pay POS a 5% net revenue royalty.

The acquisition of BPC was accounted for as a business combination and was recorded in the accounts of the Company at its fair value determined as follows:

| | | | | $ |
|---|---|---|---|---|
| Cash | | | | 1,750,000 |
| Shares - fair value closing price | 367,647 | $ | 0.45 | 165,441 |
| Fair value | | | | 1,915,441 |

(Expressed in Canadian Dollars)

The assets acquired were:

| | $ |
|---|---|
| Receivables | 30,473 |
| Prepaid expenses | 38,700 |
| Property and equipment | 308,837 |
| Technology license | 200,000 |
| Accounts payable | (281,408) |
| Long-term debt | (125,852) |
| | 170,750 |

The $1,915,441 purchase price for the 51% controlling interest in BPC was accordingly allocated as follows:

| | $ |
|---|---|
| Net tangible assets | 170,750 |
| NCI | (1,840,326) |
| Goodwill | 3,585,017 |
| Purchase price | 1,915,441 |

**b) Acquisition of Chi Hemp Industries Inc.**

On November 2, 2015, the Company entered into a Securities Purchase Agreement with Chi and the shareholders of Chi whereby Naturally Splendid agreed to acquire all of the issued and outstanding shares of Chi. The definitive agreement was accepted by the TSX Venture Exchange on November 24, 2015. Under the terms of the agreement, the Chi shareholders sold the Chi shares to Naturally Splendid for consideration of $116,489 of common shares (319,148 shares) of Naturally Splendid to the Chi shareholders and cash of $75,000 plus a working capital adjustment. The cash payment will be made in three separate tranches: $25,000 within three months of closing, $25,000 within six months of closing and $25,000 within nine months of closing. On closing of the transaction, the Chi shareholders entered into a one-year consulting agreement with Naturally Splendid. The Chi shareholders will receive a 12% gross sales commission on any lines of business that are directly benefited from their services.

The acquisition of Chi was recorded in the accounts of the Company at its fair value determined as follows:

| | | |
|---|---|---|
| Cash - payable in three equal installments | $ | 75,000 |
| Shares - 319,148 at market value of $0.365 | | 116,489 |
| Working capital adjustment | | 15,476 |
| Payment allocated to shareholder loans | | (45,115) |
| | $ | 161,850 |

(Expressed in Canadian Dollars)

The assets acquired and the purchase price allocation was:

| | | |
|---|---|---|
| Cash | $ | 3,505 |
| Accounts receivable | | 12,396 |
| Inventory | | 15,728 |
| Security deposit | | 1,260 |
| Non-competition clause | | 30,926 |
| Technology and website | | 31,417 |
| Goodwill | | 90,168 |
| Accounts payable | | (23,550) |
| | $ | 161,850 |

## 5. Trade and Other Receivables

The Company's trade and other receivables arise from two main sources: trade receivables due from customers and Goods and Services Tax/Harmonized Sales Tax ("GST/HST") due from the government authorities. These are as follows:

| | **December 31, 2015 $** | **December 31, 2014 $** |
|---|---|---|
| GST/HST receivable | 14,108 | 13,567 |
| Trade receivables * | 250,020 | 44,699 |
| | 264,128 | 58,266 |

* Trade receivables are net of an allowance for bad debts of $27,729 (2014 - $27,729).

## 6. Inventories

| | **December 31, 2015 $** | **December 31, 2014 $** |
|---|---|---|
| Seed and finished products for resale | 182,499 | 137,427 |
| Containers, labels and raw products | 205,304 | 140,346 |
| | 387,803 | 277,773 |

(Expressed in Canadian Dollars)

## 7. Prepaid Expenses

| | December 31, 2015 $ | December 31, 2014 $ |
|---|---|---|
| License technology advance[1] | - | 176,000 |
| Product research and development [2] | 232,590 | - |
| Investor relations advances [3] | 27,000 | - |
| Other | 57,720 | 54,382 |
| | 317,310 | 218,925 |
| Long term deposits | 36,000 | 11,457 |
| | 353,310 | 241,839 |

[1] As at December 31, 2014, the Company had advanced $176,000 for the acquisition of the License Technology from Boreal Technologies Inc. ("Boreal") (note 10).

[2] During the year ended December 31, 2015, the Company advanced $250,000 for services relating to research of hemp and hemp-based technologies to a related entity. The balance remaining at December 31, 2015 is $232,590.

## 8. Restricted Cash

The Company has deposited funds into an interest-bearing term deposit with its principal banker as security against corporate credit lines.

(Expressed in Canadian Dollars)

## 9. Equipment and Intangibles

The changes in the Company's equipment for the years ended December 31, 2015 and 2014 are as follows:

| | Computer equipment | Furniture and equipment | Leasehold Improvements | Manufacturing facility | Total |
|---|---|---|---|---|---|
| | $ | $ | $ | $ | $ |
| **Cost** | | | | | |
| December 31, 2013 | 47,079 | 89,039 | 4,300 | - | 147,918 |
| Additions | 9,393 | 33,381 | 15,668 | - | 58,442 |
| December 31, 2014 | 56,472 | 122,420 | 19,968 | - | 206,360 |
| Additions from acquisition of POS BPC Manufacturing Corp | - | - | - | 332,505 | 332,505 |
| Additions | 13,447 | 33,349 | - | 35,765 | 82,560 |
| **December 31, 2015** | 69,919 | 155,769 | 19,968 | 368,270 | 621,425 |
| **Depreciation** | | | | | |
| December 31, 2013 | 32,228 | 36,600 | 430 | - | 76,758 |
| Additions | 14,593 | 13,177 | 2,601 | - | 30,371 |
| December 31, 2014 | 46,821 | 49,777 | 3,031 | - | 107,129 |
| Acquisition of POS BPC Manufacturing Corp | - | - | - | 23,290 | 23,290 |
| Additions | 13,433 | 17,600 | 4,342 | 10,240 | 45,614 |
| **December 31, 2015** | 60,254 | 67,377 | 7,373 | 33,530 | 176,033 |
| **Net Book Value** | | | | | |
| December 31, 2014 | 9,651 | 72,643 | 16,937 | - | 99,231 |
| December 31, 2015 | 9,665 | 88,392 | 12,595 | 334,740 | 445,392 |

The changes in the Company's website, technology and other intangibles for the years ended December 31, 2015 and 2014 are as follows:

| | Website and Technology (note 4) | Non-compete Clause (note 4) | Licensed IP (note 4) | Total |
|---|---|---|---|---|
| | $ | $ | | $ |
| **Cost** | | | | |
| December 31, 2013 and 2014 | - | - | - | - |
| Additions from acquisition of Chi and BPC (Note 4) | 31,417 | 30,926 | 200,000 | 262,343 |
| Additions | - | - | - | - |
| **December 31, 2015** | 31,417 | 30,926 | 200,000 | 262,343 |

| | Website and Technology (note 4) | Non-compete Clause (note 4) | Licensed IP (note 4) | Total |
|---|---|---|---|---|
| **Depreciation** | | | | |
| December 31, 2013 and 2014 | - | - | - | - |
| Additions | 1,309 | 1,289 | - | 2,598 |
| **December 31, 2015** | 1,309 | 1,289 | - | 2,598 |
| **Net Book Value** | | | | |
| December 31, 2014 | - | - | - | - |
| December 31, 2015 | 30,108 | 29,637 | 200,000 | 259,745 |

(Expressed in Canadian Dollars)

The changes in the Company's licensed technology for the years ended December 31, 2015 and 2014 are as follows:

| | Licensed Technology (note 10) |
|---|---|
| | $ |
| **Cost** | - |
| December 31, 2013 and 2014 | - |
| Additions | 1,486,425 |
| **December 31, 2015** | 1,486,425 |
| **Depreciation** | |
| December 31, 2013 and 2014 | - |
| Additions | 86,449 |
| **December 31, 2015** | 86,449 |
| **Net Book Value** | |
| December 31, 2014 | - |
| December 31, 2015 | 1,399,976 |

## 10. Technology License

During the year ended December 31, 2015, the Company completed the technology acquisition agreement, and subsequently amended that agreement.

Naturally Splendid USA Ltd. entered into a Novation Agreement with FSL, Boreal and the Company whereby Boreal assigned, and Naturally Splendid USA Ltd. assumed, all rights, title and interest in and to a Restated and Amended License Agreement between FSL and Boreal (the "License Agreement"). The License Agreement provides that the licensee has a worldwide license to manufacture, commercialize and sell products based on the following proprietary technology of FSL:

**a)** on an exclusive basis, (i) the terpene, hemp oil and cannabinoid formulation technology, (ii) omega formulation technology, (iii) protein formulation technology, (iv) cannabinoid technology, and (v) the tongkat ali formulations; and

**b)** on a non-exclusive basis, (i) the Supercritical CO2 and plant oil extraction technology, (ii) genetic plant and artificial seed technology, (iii) biosynthesis of cannabinoids, and (iv) microencapsulation of cannabinoid oils.

Under the terms of the Novation Agreement, Naturally Splendid USA Ltd. paid $725,000 to Boreal and the Company issued 2,928,571 common shares of the Company valued at the time of closing at $761,428 for a total acquisition cost of $1,486,425, of which $176,000 was prepaid at December 31, 2014. The License Agreement is amortized over a 15-year period representing the term of the agreement plus one renewal period. Amortization expense recorded for the year ended December 31, 2015 is $86,449 (2014 - $nil).

The Company will be required to pay FSL a 4.5% gross revenue royalty. Commencing November 17, 2016 and each year thereafter, the Company will be obligated to pay a minimum gross revenue royalty of

(Expressed in Canadian Dollars)

US$1.6 million. Notwithstanding the foregoing, no royalties will be payable to FSL on the first C$1,750,000 of royalties payable under the License Agreement.

On September 23, 2015, as a result of the closing of a restated and amended licence agreement, Naturally Splendid acquired a 100% interest, without royalty, in FSL's omega technologies, including HempOmega and H2Omega. FSL removed the minimum annual royalty of US$1.6 million noted above. In consideration of owning a 100% interest in the omega technologies and the removal of the minimum royalty, Naturally Splendid extinguished its non-exclusive licence of FSL's bioreactor technology, and changed its exclusive licence on certain analytical testing standard operating procedures ("SOPs") and GC-MS terpene analysis SOPs to a non-exclusive licence.

## 11. Capital Lease Obligation

During the year ended December 31, 2014, the Company entered into a lease contract for equipment used in operations. The Company has accounted for this as a capital lease obligation.

The following table summarizes the outstanding obligation:

| | **December 31, 2015 $** | **December 31, 2014 $** |
|---|---|---|
| Lease payments due within one year | 5,859 | 5,859 |
| Lease payments due within two to five years | 2,988 | 8,848 |
| Total lease payments | 8,847 | 14,707 |
| Lease payment amounts representing interest | (1,006) | (1,613) |
| Present value of net minimum lease payments | 7,841 | 13,094 |
| Current portion | (4,927) | (4,182) |
| | 2,914 | 8,912 |

## 12. Trade and Other Payables

Trade and other payables are non-interest-bearing, unsecured and have settlement dates within one year.

| | **December 31, 2015 $** | **December 31, 2014 $** |
|---|---|---|
| Trade and other payables | 1,704,998 | 126,882 |

(Expressed in Canadian Dollars)

### 13. Long-Term Debt

| | | December 31, 2015 $ | December 31, 2014 $ |
|---|---|---|---|
| Loan payable to Saskatchewan Opportunities Corporation | [1] | 143,500 | - |
| Loan due September 29, 2017 bearing interest at 12.0% | [2] | 79,360 | - |
| Interest and accretion expense for the year | | 4,553 | - |
| Loan due October 2, 2017 bearing interest at 12.0% | [3] | 238,080 | - |
| Interest and accretion expense for the year | | 11,265 | - |
| | | 476,758 | - |

[1] Non-interest bearing loan for $309,000 with monthly payments of $6,438 beginning April 1, 2017. The loan bears no interest; however, if at any time the loan goes in default, interest will accrue at 5%. A general security agreement on BPC assets is pledged as security. The loan is due March 2021. The fair value of the loan was calculated using a market interest rate of 25%. The loan was recorded at fair value at the date of acquisition of POS at $125,852. Interest accretion of $17,647 has been recognized in the consolidated statements of loss and comprehensive loss and the loan has been recorded at $143,500 at December 31, 2015.

[2] On October 2, 2015, the Company entered into a loan agreement with Robert Schulz, whereby the lender agreed to loan the Company $100,000 for a period of two years at an interest rate of 12% per annum. The Company has the right to repay all of the outstanding balance of the loan by paying the lender an amount equal to 124% of the loan less any accrued interest paid by Naturally Splendid, provided that either: (i) Naturally Splendid completes financings totalling at least $1.5 million in the year following the date of acceptance by the TSX Venture Exchange of the loan; or (ii) Naturally Splendid exercises this right one year after the Exchange acceptance date. Further, the lender will also have the right to have Naturally Splendid repay the loan prior to the maturity date at the repayment price, provided that Naturally Splendid completes financings totalling at least $1.5 million in the year following the Exchange acceptance date. As additional consideration of the loan, Naturally Splendid issued 95,238 common shares to the lender, fair valued $22,080.

The loan payable was recognized initially at fair value discounted for the value of the bonus shares issued.

[3] On October 23, 2015, the Company closed on a loan agreement with Coast Mountain Aviation Inc. whereby the lender agreed to loan Naturally Splendid $300,000 for a period of two years at an interest rate of 12% per annum. Prior to the maturity date, Naturally Splendid will have the right to repay all of the outstanding balance of the loan by paying the lender the loan plus any accrued and unpaid interest provided that either Naturally Splendid completes financings totalling at least $1.5 million during the term of the loan, or Naturally Splendid exercises this right one year after the Exchange acceptance date. Further, the lender will also have the right to have Naturally Splendid repay the loan prior to maturity date at the repayment price provided that Naturally Splendid completes financings totalling at least $1.5 million during the term of the loan. As additional consideration of the loan, Naturally Splendid issued 260,869 common shares to the lender, fair valued at $60,480.

The loan payable was recognized initially at fair value discounted for the value of the bonus shares issued.

(Expressed in Canadian Dollars)

## 14. Key Management Compensation and Related Party Transactions

### Key management compensation

The remuneration of directors and other members of key management were as follows:

| | 2015<br>$ | 2014<br>$ |
|---|---|---|
| Management fees | 455,858 | 180,000 |
| Directors' fees | 700 | - |
| Share-based payments (note 16) | 654,880 | 201,351 |
| | 1,111,438 | 381,351 |

Key management personnel were not paid post-employment benefits, termination benefits or other long-term benefits during the period.

### Related party transactions:

Management fees were paid to a company controlled by the Company's Chief Financial Officer and consulting fees were paid to a company controlled by a director. Transactions with related parties were as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2015<br>$ | 2014<br>$ |
| Management fees | 60,000 | 60,000 |
| Consulting fees | 42,000 | 42,000 |
| | 102,000 | 102,000 |

POS Management Corporation is a company subject to common control. During the year ended December 31, 2015, the Company received contract services revenue from POS Management Corporation totaling $100,065 (2014: $nil) and incurred management fees expense of $73,833 (2014: $nil).

The following are amounts due to/from related parties:

- $5,879 (2014: $558) due to management and consultants for fees outstanding included in accounts payable and accrued liabilities.
- $556,966 (2014 - $nil) due to POS Pilot Plant Corp., a company subject to common control, relating to management fees outstanding included in accounts payable and accrued liabilities.
- $414,326 (2014 - $nil) due from POS Management Corp., a company subject to common control, relating to subcontractor fees included in due from related parties.
- $22,600 (2014 - $nil) due to POS Holdings Corp., a company subject to common control, relating to consulting fees outstanding included in accounts payable and accrued liabilities.

(Expressed in Canadian Dollars)

## 15. Financial Instruments

### a) Categories of financial instruments

| | December 31, 2015 $ | December 31, 2014 $ |
|---|---|---|
| **Financial Assets** | | |
| Fair value through profit or loss, at fair value | | |
| Cash | 34,330 | 25,404 |
| Loans and receivables, at amortized cost | | |
| Trade and other receivables | 250,020 | 44,699 |
| Restricted cash | 57,560 | 17,310 |
| Total financial assets | 341,910 | 87,413 |
| **Financial Liabilities** | | |
| Other liabilities, at amortized cost | | |
| Trade and other payables | 1,704,998 | 126,882 |
| Long-term debt, including current portion | 476,758 | - |
| Total financial liabilities | 2,181,756 | 126,882 |

### b) Fair value

The fair value of financial assets and financial liabilities at amortized cost is determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions. The Company considers the carrying amounts of all its financial assets and financial liabilities recognized at amortized cost in these consolidated financial statements to approximate their fair values due to the short-term maturity of these instruments.

### c) Management of financial risks

The Company examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of these risks. These risks arise from the normal course of operations and all transactions undertaken are to support the Company's ability to continue as a going concern. Management manages and monitors these exposures to ensure appropriate measures are implemented in a timely and effective manner. The risks associated with these consolidated financial instruments and the policies on how to mitigate these risks are set out below.

*Credit risk*

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Financial instruments that potentially subject the Company to credit risk consist of cash and trade receivables. The Company deposits cash with major Canadian commercial banks. In order to reduce its credit risk in relation to trade receivables, the Company has adopted credit policies that include the analysis of the financial position of its customers and the regular review of their respective credit limits.

*Liquidity risk*

Liquidity risk is the risk that the Company will be unable to meet its financial obligations as they become due. The Company is reliant upon equity issuances and loans as its main sources of cash. The Company manages liquidity risk by maintaining an adequate level of cash to meet its ongoing obligations. The Company continuously reviews its actual expenditures, forecasts cash flows and matches the maturity dates of its cash to capital and operating needs. The Company's accounts payable and accrued liabilities are due within 3 months.

The Company has been successful in raising financing in the past; however, there is no assurance that it will be able to do so in the future. As at December 31, 2015, the Company had working capital deficit of $755,094 (2014 - working capital of $489,304).

*Interest rate risk*

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. Interest earned on cash and cash equivalents is at nominal interest rates, and therefore the Company does not consider interest rate risk to be significant.

The interest rate on loans payable as at December 31, 2015 is fixed, as such, the Company is not exposed to interest cash flow risk.

*Other risk*

Unless otherwise noted, it is management's opinion that the Company is not exposed to significant currency or other risk. The Company does not hold or issue financial instruments for trading purposes, nor does it utilize derivative instruments in the management of foreign currency, commodity price or interest rate market risks.

## 16. Share Capital

### a) Authorized

Unlimited number of common shares and preferred shares without par value.

### b) Issued and outstanding

The total issued and outstanding share capital consists of 56,780,523 common shares without par value.

During the year ended December 31, 2015, the Company completed the following transactions:

- 3,393,300 units were issued at a price of $0.50 per unit for gross proceeds of $1,696,650. Each unit comprised one common share of the Company and one-half of one common share purchase warrant (the "Warrant"), with each full Warrant entitling the holder to purchase one additional common share at $0.75 for a period of two years from the date of the issue. The Company paid finder's cash commissions totaling $104,884 and issued a finder 194,664 non-transferable warrants with a fair value of $21,572.
- 7,388,582 units were issued at a price of $0.25 per unit for gross proceeds of $1,847,146. Each unit comprised one common share of the Company and one-half of one common share

purchase warrant (the "Warrant"), with each full Warrant entitling the holder to purchase one additional common share at $0.40 for a period of two years from the date of the issue. The Company will have the right to accelerate the expiry date of the Warrants if, at any time, the volume weighted average price of the Company's common shares is equal to or greater than $0.50 for ten consecutive trading days. In the event of acceleration, the expiry date will be accelerated to a date that is 30 days after the Company issues a news release announcing that it has elected to exercise this acceleration right. The Company paid finder's cash commissions totaling $36,720 and issued a finder 146,880 non-transferable warrants with a fair value of $16,221.

- 2,928,571 common shares of the Company were issued for a fair value of $761,428 to acquire technology (note 10).
- 367,647 common shares of the Company were issued at a fair value of $165,441 to acquire BPC (note 4).
- 319,148 common shares of the Company were issued at a fair value of $116,489 to acquire Chi (note 4).
- 356,107 common shares of the Company were issued at a fair value of $82,560 as bonuses to lenders providing loan financing to the Company (note 13).
- 125,000 shares were issued for services to a related party at a fair value of $49,375.
- 764,500 common shares were issued upon the exercise of 764,500 options at a price of $0.19 and $0.20 per share, for gross proceeds of $146,038.
- 4,478,669 common shares upon the exercise of 4,478,669 warrants at a price of $0.25 and $0.30 per share for gross proceeds of $1,225,968.

During the year ended December 31, 2014, the Company completed the following transactions:

- 6,843,500 units at $0.20 per unit for gross proceeds of $1,368,700. Each unit comprised one common share and one-half of one common share purchase warrant. Each whole warrant will entitle the holder to purchase one additional common share at $0.30 for a period of two years from date of issue. The Company will have the right to accelerate the expiry of the warrants if at any time the average closing price of the Company's shares is equal to or greater than $0.40 per share for ten consecutive trading days. In the event of acceleration, the expiry date shall be accelerated to 30 days after the Company issues a news release announcing its election to exercise the acceleration right. The Company paid $109,614 and issued 382,650 finder's warrants as finders' fees for the private placement. Each finder's warrant is exercisable on the same terms as the warrants attached to the units issued.
- 500,000 common shares upon the exercise of 500,000 options at a price of $0.175 per share for gross proceeds of $87,500.
- 366,394 common shares upon the exercise of 366,394 warrants at a price of $0.175 per share for gross proceeds of $64,119.
- 218,000 common shares upon the exercise of 218,000 warrants at a price of $0.25 per share for gross proceeds of $54,485.

(Expressed in Canadian Dollars)

**c) Stock-based compensation**

The following is a summary of changes in stock options for the years ended December 31, 2015 and 2014:

| | December 31, 2015 | | December 31, 2014 | |
|---|---|---|---|---|
| | Number of options | Weighted average exercise price | Number of options | Weighted average exercise price |
| Options outstanding, beginning of year | 2,409,750 | $ 0.18 | 1,750,000 | $ 0.175 |
| Options granted | 2,445,000 | $ 0.38 | 1,159,750 | $ 0.196 |
| Options exercised | (764,500) | $ 0.19 | (500,000) | $ 0.175 |
| Options cancelled | (300,000) | $ 0.20 | - | - |
| Options outstanding and exercisable, end of year | 3,790,250 | $ 0.31 | 2,409,750 | $ 0.18 |

The following are the outstanding stock options as of December 31, 2015:

| Expiry date | Number of options outstanding | Weighted average exercise price | Weighted average remaining contractual life in years |
|---|---|---|---|
| March 24, 2016 | 345,000 | $ 0.200 | 0.23 |
| April 16, 2017 | 99,750 | $ 0.200 | 1.29 |
| November 3, 2017 | 175,000 | $ 0.300 | 1.84 |
| March 4, 2018 | 925,500 | $ 0.175 | 2.26 |
| March 23, 2020 | 2,025,000 | $ 0.400 | 4.23 |
| November 3, 2020 | 220,000 | $ 0.300 | 4.85 |
| | 3,790,250 | | 3.23 |

The following are the outstanding stock options as of December 31, 2014:

| Expiry date | Number of options outstanding | Weighted average exercise price | Weighted average remaining contractual life in years |
|---|---|---|---|
| March 24, 2016 | 460,000 | $ 0.200 | 1.23 |
| April 16, 2017 | 199,750 | $ 0.200 | 2.29 |
| March 4, 2018 | 1,250,000 | $ 0.175 | 3.26 |
| March 12, 2019 | 500,000 | $ 0.190 | 4.19 |
| | 2,409,750 | | 4.26 |

(Expressed in Canadian Dollars)

During the year ended December 31, 2015, the Company recognized share-based payments expense of $906,900 (2014 - $201,351) in relation to 2,445,000 (2014 - 1,159,750) stock options granted during the year.

The fair value of each option granted was estimated as at the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

| | **December 31, 2015** | **December 31, 2014** |
|---|---|---|
| Risk-free interest rate | 0.58% | 1.33% |
| Expected life (years) | 4.79 | 3.47 |
| Annualized volatility | 101.25% | 92.26% |
| Expected dividends | - | - |
| Exercise price | $0.38 | $0.20 |

**d) Warrants**

A summary of the Company's warrants for the years ended December 31, 2015 and 2014 is as follows:

| | **December 31, 2015** | | **December 31, 2014** | |
|---|---|---|---|---|
| | **Number of warrants** | **Weighted average exercise price** | **Number of warrants** | **Weighted average exercise price** |
| Outstanding, beginning of period | 6,487,054 | $ 0.279 | 3,372,774 | $ 0.240 |
| Issued | 5,732, 485 | $ 0.521 | 3,804,400 | $ 0.300 |
| Exercised | (4,478,669) | $ 0.273 | (584,394) | $ 0.203 |
| Expired and cancelled | (330,000) | - | (105,726) | $ 0.175 |
| Outstanding, end of period | 7,410,870 | $ 0.459 | 6,487,054 | $ 0.279 |

The following are the outstanding warrants as at December 31, 2015:

| | **Outstanding warrants** | **Exercise price** | **Expiry date** |
|---|---|---|---|
| Common share purchase warrants | | | |
| | 1,489,950 | $ 0.30 | April 26, 2016 |
| | 3,694,291 | $ 0.40 | February 23, 2017 |
| | 1,628,650 | $ 0.75 | May 27, 2017 |
| | 68,000 | $ 0.75 | July 14, 2017 |
| Agent warrants | 188,435 | $ 0.30 | April 26, 2016 |
| | 146,880 | $ 0.40 | February 23, 2017 |
| | 194,664 | $ 0.75 | May 27, 2017 |
| | 7,410,870 | | |

(Expressed in Canadian Dollars)

The following are the outstanding warrants as at December 31, 2014:

| | Outstanding warrants | Exercise price | Expiry date |
|---|---|---|---|
| Common share purchase | | | |
| Warrants | 2,642,654 | $ 0.25 | November 1, 2015 |
| | 3,421,750 | $ 0.30 | April 26, 2016 |
| Agent warrants | 40,000 | $ 0.25 | November 1, 2015 |
| | 382,650 | $ 0.30 | April 26, 2016 |
| | 6,487,054 | | |

**e) Reserves**

As of December 31, 2015 and 2014, the reserves of the Company were as follows:

| | December 31, 2015 $ | December 31, 2014 $ |
|---|---|---|
| Stock option reserves | 1,074,979 | 343,279 |
| Warrant reserves | 37,793 | 12,219 |
| Total reserves | 1,112,772 | 355,498 |

## 17. Commitments

On May 23, 2013, the Company entered into an offer to lease new premises with a lease term commencement date of June 1, 2013, terminating July 31, 2018. The basic rent is payable in advance at a rate of $3,656 per month plus the proportionate share of expenses in respect of operating costs and property taxes amounting to $2,072 per month.

## 18. Capital Disclosure

The capital structure of the Company consists of equity attributable to common shareholders, comprising issued capital and deficit. The Company’s objectives when managing capital are to: (i) preserve capital, (ii) obtain the best available net return, and (iii) maintain liquidity. The Company manages the capital structure and makes adjustments to it in light of changes in economic condition and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue new debt, acquire or dispose of assets, or adjust the amounts of cash and investments. The Company’s policy is to invest its excess cash in highly-liquid, guaranteed, bank-sponsored instruments.

There were no significant changes in the Company’s approach or objectives and policies for managing its capital during the year ended December 31, 2015. The Company is not subject to externally imposed capital restrictions.

(Expressed in Canadian Dollars)

## 19. Income Taxes

The Company's combined statutory tax rate is currently at 26%, reflecting a combined federal corporate tax rate of 15% and BC corporate tax rate of 11%.

A reconciliation of income tax provisions computed at Canadian statutory rates to the reported income tax provision is provided as follows:

| | **2015** | **2014** |
|---|---|---|
| | **$** | **$** |
| Loss before income taxes | (6,981,286) | (1,795,757) |
| Expected income tax recovery | (1,815,134) | (466,897) |
| Adjustment resulting from | | |
| Differences between Canadian and foreign tax rates | (40,929) | (103) |
| Non-deductible items | 960,150 | 68,509 |
| Other | (11,184) | (28,231) |
| Over provided in prior years | (47,777) | (97,209) |
| Unused tax losses | 954,874 | 523,931 |
| Income tax recovery | - | - |

The Company recognizes tax benefits on losses or other deductible amounts generated where the probable criteria for the recognition of deferred tax assets has been met. The Company's unrecognized deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

| | **2015** | **2014** |
|---|---|---|
| | **$** | **$** |
| Deferred tax assets | | |
| Non-capital losses | 9,436,410 | 6,047,176 |
| Share issue costs | 302,814 | 227,984 |
| Property and equipment | 119,537 | 99,631 |
| Unrecognized deferred tax | 9,858,761 | 6,374,791 |

As at December 31, 2015, the Company has non-capital losses carried forward for Canadian purposes aggregating approximately $9,436,000 available to reduce taxable income otherwise calculated in future years.

(Expressed in Canadian Dollars)

These losses expire as follows:

| Year | Amount $ |
|---|---|
| 2028 | 452,201 |
| 2029 | 228,860 |
| 2030 | 172,798 |
| 2031 | 672,019 |
| 2032 | 228,387 |
| 2033 | 2,723,602 |
| 2034 | 1,569,560 |
| | 3,388,983 |
| | 9,436,410 |

## 20. Goodwill

Goodwill acquired through business combinations has been allocated to two Cash Generating Units (“CGU”):

The breakdown of goodwill for December 31, 2015 and 2014 is as follows:

BPC

| | 2015 | 2014 |
|---|---|---|
| Balance, beginning of the year | $ - | $ - |
| Additions | 3,585,017 | - |
| Impairment | (2,784,017) | - |
| Balance, end of the year | $ 801,000 | $ - |

Chi

| | 2015 | 2014 |
|---|---|---|
| Balance, beginning of the year | $ - | $ - |
| Additions | 90,168 | - |
| Balance, end of the year | $ 90,168 | $ - |

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired. Impairment is determined by assessing the recoverable amount of the CGU to which goodwill relates. Where the recoverable amount of the CGU is less than the carrying amount, an impairment loss is recognized. For the purposes of impairment testing, the aggregate amount of acquired goodwill has been assigned to the BPC and Chi CGUs. These CGUs represent the lowest level within the Company for which the information about goodwill is available and monitored for internal management purposes.

(Expressed in Canadian Dollars)

The Company performed the annual impairment tests of goodwill at December 31, 2015. The recoverable amounts have been determined using Level 3 inputs, based on value-in-use calculation using pre-tax cash flow projections from financial budgets approved by senior management for 2016, forecasts over a five year period based on management's best estimates, and uses a pre-tax discount rate of 22.5%.

The most significant assumptions used in the impairment calculation are the discount rate and the estimates used in determining future expected cash flows. The Corporation performed a sensitivity analysis by changing the post-tax discount rates by +/- 1% and noted no material impact on the recoverable amount.

Following the impairment tests, it was determined that the carrying value of the Company's goodwill exceeded their recoverable amount. Accordingly, the Company recorded an impairment charge of $2,784,017 on the goodwill recognized on acquisition of BPC.

## 21. Supplemental Cash Flow Information

| | 2015 | 2014 |
|---|---|---|
| Non-cash items: | | |
| Bonus shares | 82,560 | - |
| Shares issued for services | 49,375 | - |
| Shares issued for technology license | 761,428 | - |
| Consideration for acquisition of Chi included in accounts payable and accrued liabilities | 75,000 | - |
| | 893,363 | - |
| **Interest and taxes paid** | | |
| Interest | - | - |
| Taxes | - | - |

## 22. Events After the Reporting Period

The Company has evaluated the events occurring subsequent to December 31, 2015 and determined that the following were reportable events:

1) On February 1, 2016, the Company signed a Memorandum of Understanding with Korea Beauty Healthcare. Co., Ltd. ("KBH") to distribute the Company's hemp-based food products in South Korea.

2) 282,000 warrants with an exercise price of $0.30 were exercised for gross proceeds of $84,600.

3) 1,237,450 warrants with an expiration date of April 26, 2016 were extended by one year and 158,935 agent warrants expired unexercised. 310,000 options with an expiration date of March 24, 2016 were repriced from $0.200 to $0.285and extended by three years.