

SHARC INTERNATIONAL SYSTEMS INC.
Condensed Consolidated Interim Financial Statements

For the three months ended March 31, 2020

(Unaudited - Expressed in Canadian dollars)

SHARC INTERNATIONAL SYSTEMS INC.

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the condensed financial statements; the statements must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor. The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of financial information by an entity's auditor.

Management has prepared the information and representations in this interim report. The condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards and, where appropriate, reflect management's best estimates and judgment. The financial information presented throughout this report is consistent with the data presented in the condensed financial statements.

The company maintains adequate systems of internal accounting and administrative controls, consistent with reasonable cost. Such systems are designed to provide reasonable assurance that relevant and reliable financial information is produced.

SHARC International Systems Inc.
Condensed Consolidated Interim Statements of Financial Position
(Expressed in Canadian dollars)

	Note	March 31, 2020 (unaudited) \$	December 31, 2019 (audited) \$
ASSETS			
Current			
Cash		1,202,646	109,510
Receivables	4	35,428	54,053
Prepaid expenses		112,044	18,857
Inventory	5	352,041	319,535
Total current assets		1,702,159	501,955
Restricted cash	6	20,000	20,000
Deposits		1,200	1,200
Property and equipment	7	512,860	547,606
Total assets		2,236,219	1,070,761
LIABILITIES AND SHAREHOLDERS' DEFICIENCY			
Current liabilities			
Accounts payable and accrued liabilities	8	488,440	1,171,785
Loans payable	9	—	422,948
Deferred revenue	10	224,672	39,932
Convertible debentures	11	2,363,556	2,238,334
Lease liabilities	12	104,818	101,735
Total current liabilities		3,181,486	3,974,734
Convertible debentures	11	4,024,786	2,640,179
Lease liabilities	12	382,682	410,072
Total liabilities		7,588,954	7,024,985
SHAREHOLDERS' DEFICIENCY			
Share capital	13	14,024,314	13,212,855
Reserves	13	3,381,610	2,985,374
Convertible debentures – equity component		757,663	497,891
Deficit		(23,516,322)	(22,650,344)
Total shareholders' deficiency		(5,352,735)	(5,954,224)
Total liabilities and shareholders' deficiency		2,236,219	1,070,761

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

Nature of Operations and Going Concern [Note 1]

Commitments and Contingencies [Note 14]

Subsequent Events [Note 20]

Approved on behalf of the Board:

/s/ Lynn Mueller
Director

/s/ Matt Engelhardt
Director

SHARC International Systems Inc.
Condensed Consolidated Interim Statements of Loss
and Comprehensive Loss

(Unaudited - Expressed in Canadian dollars)

	Note	Three months Ended March 31, 2020 \$	Three months Ended March 31, 2019 \$
Revenue		54,675	28,331
Cost of sales		(7,465)	(6,725)
Gross margin		47,210	21,606
Expenses			
Accounting and legal		10,726	35,768
Advertising and promotion		58,482	87,880
Bad debt recovery		(7,311)	—
Consulting	8	82,439	89,906
Depreciation	7	34,746	17,404
Insurance		6,325	5,823
Interest and financing expense	9,11,12	332,169	137,823
Office and miscellaneous		16,639	23,170
Regulatory and filing fees		15,418	10,209
Rent	12	12,000	19,438
Research and development		15,584	9,011
Share-based payments	8,13	196,762	68,105
Telephone and utilities		22,371	18,563
Travel		22,738	21,487
Wages and benefits	8	306,843	272,364
Warranty expense		—	6,431
		(1,125,931)	(823,382)
		(1,078,721)	(801,776)
Foreign exchange		(759)	(6,085)
Loss from continuing operations before income taxes		(1,079,480)	(807,861)
Deferred tax recovery		208,204	54,336
Loss from continuing operations		(871,276)	(753,525)
Loss on discontinued operations	15	—	(195,472)
Loss for the period		(871,276)	(948,997)
Other comprehensive gain (loss)			
Foreign currency translation on discontinued operations		—	670
Loss and comprehensive loss for the period		(871,276)	(948,327)
Continuing operations - Basic and diluted loss per common share		(0.02)	(0.02)
Discontinued operations - Basic and diluted loss per common share		—	(0.01)
Weighted average number of common shares outstanding		45,562,358	34,790,471

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

SHARC International Systems Inc.

Condensed Consolidated Interim Statements of Changes in Shareholders' Deficiency

(Unaudited - Expressed in Canadian dollars)

	Common Shares		Reserves	Currency translation reserve	Convertible debenture	Deficit	Total
	Number	\$	\$	\$	\$	\$	\$
Balance, December 31, 2018	38,720,176	13,201,868	3,360,162	(90,540)	125,042	(18,889,188)	(2,292,656)
Issuance of convertible debt	–	–	77,840	–	38,617	–	116,457
Share-based payments	–	–	68,105	–	–	–	68,105
Reversal of expired options	–	–	(60,259)	–	–	60,259	–
Currency translation adjustment	–	–	–	670	–	–	670
Loss for the period	–	–	–	–	–	(948,997)	(948,997)
Balance, March 31, 2019	38,720,176	13,201,868	3,445,848	(89,870)	163,659	(19,777,926)	(3,056,421)
Issuance of convertible debt	–	–	116,155	–	334,232	–	450,387
Warrants issued for loan	–	–	9,111	–	–	–	9,111
Share-based payments	–	–	135,511	–	–	–	135,511
Reversal of expired options	–	–	(721,251)	–	–	721,251	–
Shares for debt	156,950	10,987	–	–	–	–	10,987
Currency translation adjustment	–	–	–	47,149	–	–	47,149
Reclass of currency translation reserve on loss of foreign operations	–	–	–	42,721	–	(42,721)	–
Loss for the period	–	–	–	–	–	(3,550,948)	(3,550,948)
Balance, December 31, 2019	38,877,126	13,212,855	2,985,374	–	497,891	(22,650,344)	(5,954,224)
Common shares issued	10,000,000	650,000	–	–	–	–	650,000
Issuance of convertible debt	–	–	259,772	–	259,772	–	519,544
Share-based payments	–	–	141,762	–	–	–	141,762
Shares for services	1,824,308	161,459	–	–	–	–	161,459
Reversal of expired options	–	–	(5,298)	–	–	5,298	–
Loss for the period	–	–	–	–	–	(871,276)	(871,276)
Balance, March 31, 2020	50,701,434	14,024,314	3,381,610	–	757,663	(23,516,322)	(5,352,735)

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

SHARC International Systems Inc.

Condensed Consolidated Interim Statements of Cash Flows

(Unaudited - Expressed in Canadian dollars)

	Note	Three months Ended March 31, 2020 \$	Three months Ended March 31, 2019 \$
OPERATING ACTIVITIES			
Loss for the period		(871,276)	(948,997)
Add items not affecting cash:			
Depreciation	7	34,746	17,404
Bad debt recovery		(7,311)	—
Loss on discontinued operations	15	—	195,472
Unrealized foreign exchange		—	6,085
Share-based payments	13[d]	141,762	68,105
Shares for services	13[b]	99,542	—
Accrued interest expense	9,11,12	332,514	132,695
Deferred tax recovery		(208,204)	(54,336)
Changes in non-cash working capital items:			
Receivables		25,936	98,519
Prepaid expenses		12,730	44,340
Inventory		(32,506)	(157,870)
Accounts payable and accrued liabilities		(213,685)	172,279
Deferred revenue		184,740	393
Warranty provisions		—	(13,757)
Cash used in continuing operating activities		(501,012)	(439,668)
Cash used in discontinued operating activities		—	(732,322)
Cash used in operating activities		(501,012)	(1,171,989)
INVESTING ACTIVITY			
Purchase of property and equipment		—	(26,884)
Cash used in continued investing activity		—	(26,884)
Cash used in discontinued investing activity		—	(989,360)
Cash used in investing activities		—	(1,016,244)
FINANCING ACTIVITIES			
Repayment of loans payable	9	(428,400)	(350,000)
Repayment of convertible debentures		(19,660)	(141,735)
Payment of lease liabilities		(39,029)	(5,986)
Proceeds on private placement, net of costs	13[b]	156,000	—
Proceeds on convertible debentures, net of costs	11	1,925,237	568,795
Cash provided by continued financing activities		1,594,148	71,074
Cash provided by discontinued financing activities		—	662,172
Cash provided by financing activities		1,594,148	733,246
Increase (decrease) in cash during the period		1,093,136	(1,454,988)
Impact of exchange rate changes on cash		—	4,475
Cash, beginning of the period – continued operations		109,510	587,849
Cash, beginning of the period – discontinued operations		—	1,311,808
		109,510	1,899,657
Less: Cash, end of the period – discontinued operations		—	(276,377)
Cash, end of the period		1,202,646	172,767

Supplemental disclosure with respect to cash flow (Note 18)

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

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

SHARC International Systems Inc. (the “**Company**” or “**SHARC Energy**”) was incorporated under the *Business Corporations Act* (British Columbia) on February 4, 2011. The Company’s shares are listed on the Canadian Securities Exchange (the “**CSE**”) under the trading symbol “**SHRC**”, Frankfurt Stock Exchange (the “**FSE**”) under the trading symbol “**IWIA**” and the OTC under the symbol “**INTWF**”. The Company is engaged in providing wastewater heat exchange expertise and products that service commercial, industrial, public utilities and residential development projects objectives of reducing their carbon footprint while saving on energy costs. The Company’s registered and records office is located at 1443 Spitfire Place, Port Coquitlam, British Columbia, Canada, V3C 6L4.

These condensed consolidated interim financial statements (the “**Financial Statements**”) have been prepared under the assumption that the Company will continue as a going concern. The going concern basis of presentation assumes that the Company will be able to meet its obligations and continue its operations for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. Realization values may be substantially different from the carrying values as shown, and these Financial Statements do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should the Company be unable to continue as a going concern.

The Company has incurred losses and negative operating cash flows since its inception. As of March 31, 2020, the Company has accumulated a deficit of \$23,516,322 and has a working capital deficit of \$1,479,327. The Company has not generated positive cash flows from operations and additional financings will be required to maintain operations for the near term. These material uncertainties may cast significant doubt on the Company’s ability to continue as a going concern.

The Company will continue to pursue opportunities to raise additional capital through equity markets and/or debt to fund its operating activities; however, there is no assurance of the success or sufficiency of these initiatives. The Company’s ability to continue as a going concern is dependent upon it securing the necessary working capital to eventually generate positive cash flows either from operations or additional financing. These Financial Statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial position that would be necessary if the going concern assumption were inappropriate, and these adjustments could be material.

In March 2020, the World Health Organization declared coronavirus COVID-19 a global pandemic. This contagious disease outbreak, which has continued to spread, and any related adverse public health developments, has adversely affected workforces, economies and financial markets globally, potentially leading to an economic downturn. It is not possible for the Company to predict the duration or magnitude of the adverse results of the outbreak and its effect on the Company’s business or ability to raise funds.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION

[a] Statement of compliance

These Financial Statements have been prepared in accordance with International Accounting Standard (“IAS”) 34 “Interim Financial Reporting”. They do not include all of the information required for full annual financial statements and should be read in conjunction with the Company's audited annual financial statements for the fiscal year ended December 31, 2019, which have been prepared with International Financial Reporting Standards (“IFRS”). These Financial Statements were approved by the Company’s Board of Directors on June 12, 2020.

[b] Basis of measurement and consolidation

These Financial Statements have been prepared on a historical cost basis, except for certain financial assets and financial liabilities measured at fair value.

These Financial Statements include the accounts of the Company’s subsidiaries:

Company	Location	March 31, 2020 Ownership %	December 31, 2019 Ownership %
SHARC Energy Systems Inc. (“SES”)	Canada	100	100
SHARC Energy Systems Australasia Pty Ltd. (“SHARC Australasia”) ⁽¹⁾	Australia	80	80
2336882 Ontario Inc. ⁽¹⁾	Canada	100	100

⁽¹⁾The subsidiary was inactive.

The Company includes assets, liabilities and operations of subsidiaries from the date of acquisition to the date of disposal.

All significant intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Certain comparative period balances have been reclassified for comparative purposes.

[c] Presentation currency

These Financial Statements are presented in Canadian dollars.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments

The preparation of these Financial Statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. These Financial Statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the Financial Statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company reviews its estimates and underlying assumptions on an ongoing basis.

Critical Judgments

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

- i. Research costs are recognized as an expense when incurred but development costs may be capitalized as intangible assets if certain conditions are met as described in IAS 38, *Intangible Assets*. Management has determined that development costs do not meet the conditions for capitalization under IAS 38 and all research and development costs have been expensed.
- ii. Management is required to assess the functional currency of the Company. The determination of functional currency often requires significant judgment where the primary economic environment in which they operate may not be clear. This can have a significant impact on the consolidated results of the Company based on the foreign currency translation method.
- iii. The Company recognizes the deferred tax benefit related to deferred income and resource tax assets to the extent recovery is probable. Assessing the recoverability of deferred tax assets requires management to make significant estimates of future taxable profit. In addition, future changes in tax laws could limit the ability of the Company to obtain tax deductions from deferred income and resource tax assets.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

Estimation Uncertainty

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

- i. Provisions for income taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxation authorities. Where the final outcome of these tax-related matters is different from the amounts that were originally recorded, such differences will affect the tax provisions in the period in which such determination is made.
- ii. Warranty provisions are recognized for the future obligations to provide services for the repairs and maintenance of products sold to its customers. The Company assesses its warranty provision based on experience. Actual costs incurred may differ from those amounts estimated.
- iii. The Company estimates the net realizable values of inventories, taking into account the most reliable evidence available at each reporting date. The future realization of these inventories may be affected by future technology or other market drive changes that may reduce future selling prices.
- iv. The Company has service agreements with regards to some of its product sales which requires management to make judgments regarding the timing and allocation of revenue. Specifically, installation is generally not assumed to have standalone value and is often recognized on the same basis as the remainder of the services fees. However, the Company defers the recognition of revenue associated with fees for services agreements or warranty costs that are built in to the original sales price and recognizes the associated revenue evenly over the term of the service or warranty is provided.

3. SIGNIFICANT ACCOUNTING POLICIES

These Financial Statements have been prepared on the basis of accounting policies and methods of computation consistent with those applied in the Company's audited annual financial statement for the fiscal year ended December 31, 2019.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

4. RECEIVABLES

	As at March 31, 2020 \$	As at December 31, 2019 \$
GST recoverable (Canada)	14,044	37,785
Trade receivables	21,384	16,268
Total	35,428	54,053

5. INVENTORY

	As at March 31, 2020 \$	As at December 31, 2019 \$
Materials and supplies	9,950	9,950
Work-in-progress	285,635	253,129
Finished goods	56,456	56,456
Total	352,041	319,535

6. RESTRICTED CASH

The restricted cash balance is comprised of a bank lien on funds held as collateral for the Company's corporate credit card limits. The Company reduced the credit card limits by \$30,000 during the year ended December 31, 2019.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

7. PROPERTY AND EQUIPMENT

	Equipment, furniture and fixtures \$	Demo units \$	Computer hardware \$	Leasehold improvements \$	Right of use asset \$	Building under construction \$	Total \$
Cost:							
Balance, December 31, 2018	65,813	303,413	27,926	19,025	—	2,179,312	2,595,489
Addition	9,059	34,134	—	—	604,569	2,394,931	3,042,693
Government grant (Note 14)	—	—	—	—	—	(285,386)	(285,386)
Disposition	—	—	—	—	(20,867)	—	(20,867)
Foreign currency translation	35	—	—	—	(531)	(119,058)	(119,554)
Discontinued operations (Note 15)	(28,827)	—	—	—	(34,491)	(4,169,799)	(4,233,117)
Balance, December 31, 2019 and March 31, 2020	46,080	337,547	27,926	19,025	548,680	—	979,258
Accumulated depreciation:							
Balance, December 31, 2018	34,386	275,589	26,834	16,888	—	—	353,697
Depreciation	8,506	31,959	601	2,137	56,763	—	99,966
Disposition	—	—	—	—	(2,256)	—	(2,256)
Foreign currency translation	20	—	—	—	473	—	493
Discontinued operations (Note 15)	(10,548)	—	—	—	(9,700)	—	(20,248)
Balance, December 31, 2019	32,364	307,548	27,435	19,025	45,280	—	431,652
Depreciation	686	3,723	68	—	30,269	—	34,746
Balance, March 31, 2020	33,050	311,271	27,503	—	75,549	—	466,398
Net book value:							
As of December 31, 2019	13,716	29,999	491	—	503,400	—	547,606
As of March 31, 2020	13,030	26,276	423	—	473,131	—	512,860

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited - Expressed in Canadian dollars)

8. RELATED PARTY DISCLOSURE

Transactions with related parties

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly. Key management personnel include officers and directors.

The Company incurred the following charges with key management personnel:

	Three months Ended March 31, 2020 \$	Three months Ended March 31, 2019 \$
Consulting fees ^[i]	39,500	15,000
Wages and benefits ^[ii]	98,733	167,588
Share-based payments ^[iii]	85,499	27,607
Inventory/cost of sales ^[iv]	—	4,939
	223,732	187,527

- [i] The Company paid consulting fees to a company controlled by the Chief Financial Officer and to a company controlled by the former Senior Vice President of Finance.
- [ii] The Company paid wages and benefits to the Chief Executive Officer and Director, a Director, the former Chief Operating Officer and former Senior Vice President of Finance.
- [iii] Share-based payments was recognized in connection with the vesting of options granted to directors and officers of the Company in the amount of \$97,420. Furthermore, options were terminated and cancelled during the period which resulted in reversal of \$11,921.
- [iv] The Company paid consulting fees to companies controlled by the former Chief Operating Officer and a former Director of SHARC Energy Ltd. (“SHARC UK”) that were capitalized to inventory costs and expensed to cost of sales.

Included in accounts payable is \$216,512 (December 31, 2019 – \$672,587) due to related parties.

Other transactions

On February 11, 2020, the Chief Financial Officer and a Director of the Company settled \$326,794 of accounts payable for equity units in a financing (Note 13 [b]).

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

9. LOANS PAYABLE

- [i] During the year ended December 31, 2015 SHARC UK received a loan of \$102,035 (£50,000) from an unrelated company. The loan accrues interest at a rate of 12.5% per annum and is payable on April 17, 2020. The loan must be repaid in monthly payments of £1,125 with the first payment required on June 17, 2015. An arrangement fee of £1,000 was paid prior to the loan being advanced. The loan is guaranteed by the CEO of SHARC UK. During the year ended December 31, 2019, the Company made payments totaling \$31,840 (£18,790), of which \$2,140 (£1,263) related to interest and \$29,700 (£17,527) related to principal. The balance was repaid in full prior to liquidation and administration of SHARC UK.
- [ii] In March 2018, SHARC Highlands Ltd. (“**Highlands**”) received a £1,000,000 loan facility from a third party lender. This facility is to be used to finance eligible costs incurred in connection with the Clyde Gateway Project. The loan is guaranteed by SHARC UK, bears interest at 3.5%, and is repayable in monthly payments of £7,160 (or pro-rata depending on how much is drawn down) for 180 consecutive payments beginning 4 months from initial draw down. As of October 11, 2019, the facility is fully drawn. The Company has made pro-rata payments of \$80,538 (£47,529), of which \$32,794 (£19,353) related to interest and \$47,744 (£28,176), related to principal. The balance of the loan as at October 11, 2019 was \$1,669,011 (£971,824) and it was derecognized during the deconsolidation of subsidiaries (Note 15).
- [iii] In June 2018, Highlands received a £450,000 loan facility from a third party lender. This facility is to be used to pay costs incurred in connection with the Clyde Gateway Project. The loan provides the lender a bond and floating charge on Highlands, bears interest at 4.73% and interest is capitalized and added to the term loan to be repaid on June 25, 2024 or at such other times and in such amounts as the the Company and the lender may agree. As of October 11, 2019, the facility had \$772,830 (£450,000) drawn. The loan has capitalized interest of \$28,899 (£16,827) bringing the balance of the loan to \$801,729 (£466,827). This loan was derecognized during the deconsolidation of subsidiaries (Note 15).
- [iv] In November 2018, the Company received a \$150,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 12% and was repayable on January 13, 2019. The loan repayment date was extended for 270 days to September 13, 2019. The loan was repaid in May 2019 for \$158,926 including interest.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the three months ended March 31, 2020
(Unaudited - Expressed in Canadian dollars)

9. LOANS PAYABLE (CONTINUED)

- [v] In December 2018, the Company received a \$490,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 6% and was repayable on March 13, 2019. In the event of a default on repayment, the interest rate rises to 9%. During the year ended December 31, 2019, \$265,418 of the loan was repaid. The balance of the loan as at December 31, 2019 is \$260,570. During the year ended December 31, 2019, the third-party lender received 490,000 common share purchase warrants exercisable at \$1.00 for a period of three years, expiring December 31, 2022. The fair value of the share purchase warrants was \$6,378 estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 115.80% which is based on historical volatility, risk-free rate of return of 1.69% and an expected maturity of 3 years. The warrants have been recorded as a financing expenses. The loan was repaid in full during the three months ended March 31, 2020.
- [vi] In December 2018, the Company received a \$210,000 loan from a third-party lender. The loan was guaranteed by the CEO, bore interest at 6% and was repayable on March 13, 2019. In the event of a default on repayment, the interest rate rises to 9%. On March 13, 2019, the loan was repaid in full for \$213,107. During the year ended December 31, 2019, the third-party lender received 210,000 common share purchase warrants exercisable at \$1.00 for a period of three years, expiring December 31, 2022. The fair value of the share purchase warrants was \$2,733 estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 115.80% which is based on historical volatility, risk-free rate of return of 1.69% and an expected maturity of 3 years.
- [vii] In April 2019, the Company received a \$150,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 12% and is repayable on July 24, 2019. The balance of the loan as at December 31, 2019 is \$162,378, including accrued interest of \$12,378. The loan was repaid during the three months ended March 31, 2020.
- [viii] In July 2019, the Company received a \$100,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 24% and is repayable on October 5, 2019. During the year ended December 31, 2019, the loan was repaid in full.
- [ix] In October 2019, the Company received a \$30,000 from a third party lender. The loan was unsecured, non-interest bearing and was repaid in November 2019.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited - Expressed in Canadian dollars)

9. LOANS PAYABLE (CONTINUED)

	As at March 31, 2020 \$	As at December 31, 2019 \$
Balance, beginning of year	422,948	2,425,486
Proceeds from loans	—	1,239,755
Repayment of loans	(428,400)	(891,195)
Interest expense	5,452	131,212
Foreign exchange	—	(11,570)
Balance, end of year	—	2,893,688
Less: discontinued operations (Note 15)	—	(2,470,740)
Less: non-current portion	—	—
	—	422,948

10. DEFERRED REVENUE

Deferred revenue relates to on-going projects and service agreements at period end. Revenue will be recognized on completion and sale of projects and over the length of term for the service agreements.

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11. CONVERTIBLE DEBENTURES

- [i] On May 30, 2017 and June 29, 2017, the Company issued two tranches of unsecured convertible debenture units with total principal amounts of \$1,320,000 and \$1,023,000, respectively. The debentures mature on May 30, 2020 and June 29, 2020, respectively, and bear interest at an annual rate of 12% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time prior to the maturity date into common shares of the Company at a conversion price of \$1.05 per common share.

Each debenture unit consisted of one \$1,000 principal amount senior unsecured convertible debenture and 714 share purchase warrants, each exercisable into one common share of the Company at \$1.05 per share three years from issuance.

The Company may abridge the exercise period of the warrants at any time after the date that is four months after the closing date, by providing written notice to the warrant holders within 30 days, in the event that the volume weighted average closing price of the Company's common shares is greater than \$2.10 per common share for twenty consecutive trading days. The warrants will, unless exercised, expire on the 30th day after the Company provides such written notice to the warrant holders.

Total finders' fees of \$157,010 in cash and 110,900 finders' warrants valued at \$35,815 were incurred on the issuances. Each finders' warrant is exercisable into one common share of the Company at \$1.40 per share two years from issuance. The fair value of \$35,815 was assigned to the 110,900 finders' warrants using the Black-Scholes valuation model with the following weighted average assumptions: expected dividend yield of 0%, expected volatility of 102.68% which is based on historical volatility, risk-free rate of return of 0.85% and an expected maturity of 2 years.

The convertible debentures are compound financial instruments with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debentures by calculating the present value of the principal and interest payments, discounted at a rate of 20%, being management's best estimate of the rate that a non-convertible debenture with similar terms would bear. The equity component consists of the warrants and the equity conversion feature. The values attributed to each was based on the relative fair value approach.

On initial recognition, the liability components were \$1,962,798 (\$1,801,419 net of transaction costs), the warrants were \$190,101 (\$125,042 net of transaction costs and tax effect) and the residual equity components were \$190,101 (\$125,042 net of transaction costs and tax effect).

Accretion charges, included in interest and financing expense on the statement of loss and comprehensive loss, attributable to the debentures for the three months ended March 31, 2020 was \$125,223 of which \$69,327 (March 31, 2019 -\$112,778, of which \$69,327) relates to accrued interest.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

[ii] On March 8, 2019, May 9, 2019 and June 28, 2019, the Company issued three tranches of unsecured convertible debenture units with total principal amounts of \$810,000, \$1,330,000 and \$550,000 respectively. The debentures mature on March 8, 2022, May 9, 2022 and June 28, 2022, respectively, and bear interest at an annual rate of 8% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.32 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 1,563 share purchase warrants, each exercisable into one common share of the Company at \$0.40 per share three years from issuance.

If at any time after the first year anniversary of the closing date the closing price of the common shares of the Company is \$0.64 or greater for 20 consecutive trading days, the Company may, at its option, convert the debenture and any accrued and unpaid interest thereon into common shares by disseminating a press release, in which case the debentures shall be converted into common shares on the second business day after dissemination of such press release. The warrants will not be subject to acceleration.

Total finders' fee of \$161,400 in cash and 162 debenture warrants, with a nominal value, were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as the units in the placement. The Company incurred legal, regulatory and other share issuance costs of \$238,117.

The convertible debentures are compound financial instruments with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debentures by calculating the present value of the principal and interest payments, discounted at a rate of 20%, being management's best estimate of the rate that a non-convertible debenture with similar terms would bear. The equity component consists of the warrants and the equity conversion feature. The values attributed to each was based on the relative fair value approach.

On initial recognition, the liability components were \$2,022,861 (\$1,722,363 net of transaction costs), the warrants were \$333,569 (\$193,995 net of transaction costs and tax effect) and the residual equity components were \$333,569 (\$193,996 net of transaction costs and tax effect).

Accretion charges, included in interest and financing expense on the statement of loss and comprehensive loss, attributable to the debentures for the three months ended March 31, 2020 was \$117,993, of which \$53,800 (March 31, 2019 -\$9,058, of which \$4,083) relates to accrued interest.

Subsequent to quarter end, \$200,000 of principal amount was converted into 625,000 common shares. (Note 20)

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11. CONVERTIBLE DEBENTURES (CONTINUED)

[iii] On December 20, 2019, the Company issued unsecured convertible debenture units with total principal amount of \$1,030,000. The debenture matures on December 20, 2022, and bears interest at an annual rate of 8% due semi-annually. The debenture is convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.10 per common share. Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture

If at any time after May 21, 2020 the closing price of the common shares of the Company is \$0.40 or greater for 20 consecutive trading days, the Company may, at its option, convert the debenture and any accrued and unpaid interest thereon into common shares by disseminating a press release, in which case the debentures shall be converted into common shares on the second business day after dissemination of such press release.

Total finders' fee of \$30,000 in cash and 30 debenture warrants, with a nominal value, were incurred on the issuance. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in this placement. The Company incurred legal, regulatory and other share issuance costs of \$761.

The convertible debenture is a compound financial instrument with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debenture by calculating the present value of the principal and interest payments, discounted at a rate of 20%, being management's best estimate of the rate that a non-convertible debenture with similar terms would bear. The equity component consists of the warrants and the equity conversion feature. The values attributed to each was based on the relative fair value approach.

On initial recognition, the liability component was \$774,544 (\$751,412 net of transaction costs), and the residual equity components were \$255,456 (\$178,853 net of transaction costs and tax effect).

Accretion charges, included in interest and financing expense on the statement of loss and comprehensive loss, attributable to the debenture for the three months ended March 31, 2020 was \$37,659, of which \$22,889 relates to accrued interest.

Subsequent to quarter end, \$450,000 of principal amount was converted into 4,500,000 common shares. (Note 20)

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11. CONVERTIBLE DEBENTURES (CONTINUED)

[iii] On February 13 and February 24, 2020, the Company issued unsecured convertible debenture units with total principal amounts of \$1,764,000 and \$276,000 respectively. The debentures mature on February 13 and February 24, 2023, respectively, and bear interest at an annual rate of 2% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.10 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 5,000 share purchase warrants, each exercisable into one common share of the Company at \$0.20 per share three years from issuance.

Total finders' fee of \$102,000 in cash and 203 debenture warrants were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in the placement. The Company incurred legal, regulatory and other share issuance costs of \$12,763.

The convertible debenture is a compound financial instrument with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debenture by calculating the present value of the principal and interest payments, discounted at a rate of 20%, being management's best estimate of the rate that a non-convertible debenture with similar terms would bear. The equity component consists of the warrants and the equity conversion feature. The values attributed to each was based on the relative fair value approach.

On initial recognition, the liability component was \$1,268,870 (\$1,197,488 net of transaction costs), the warrants were \$385,564 (\$259,772 net of transaction costs and tax effect) and the residual equity components were \$385,564 (\$259,772 net of transaction costs and tax effect).

Accretion charges, included in interest and financing expense on the statement of loss and comprehensive loss, attributable to the debenture for the three months ended March 31, 2020 was \$31,465, of which \$5,158 relates to accrued interest.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Convertible debenture transactions and the amount of convertible debentures outstanding are summarized below:

	May 30, 2017 \$	June 29, 2017 \$	March 8, 2019 \$	May 9, 2019 \$	June 28, 2019 \$	Dec. 20, 2019 \$	Feb. 13, 2023 \$	Feb.24, 2023 \$	Total \$
Balance, December 31, 2018	1,148,000	890,381	—	—	—	—	—	—	2,038,381
Principal	—	—	810,000	1,330,000	550,000	1,030,000	550,000	1,030,000	3,720,000
Equity component	—	—	(68,402)	(152,318)	(63,339)	(247,827)	(63,339)	(247,827)	(531,886)
Warrant component	—	—	(68,402)	(152,318)	(63,339)	—	(63,339)	—	(284,059)
Transaction costs	—	—	(257,652)	(103,405)	(38,460)	(30,761)	(38,460)	(30,761)	(430,278)
Accretion expense	274,498	206,614	124,718	139,204	43,655	4,525	43,655	4,525	793,214
Interest payment	(158,400)	(122,760)	(52,920)	(70,047)	(22,732)	—	(22,732)	—	(426,859)
Balance, December 31, 2019	1,264,098	974,235	487,342	991,116	405,785	755,937	405,785	755,937	4,878,513
Principal	—	—	—	—	—	—	1,764,000	276,000	2,040,000
Equity component	—	—	—	—	—	—	(314,694)	(49,180)	(363,874)
Warrant component	—	—	—	—	—	—	(314,694)	(49,180)	(363,874)
Transaction costs	—	—	—	—	—	—	(98,994)	(15,769)	(114,763)
Accretion expense	71,569	53,654	41,678	54,413	21,902	37,659	28,095	3,370	312,340
Balance, March 31, 2020	1,335,667	1,027,889	529,020	1,045,529	427,687	793,596	1,063,713	165,241	6,388,342

Of the total convertible debentures payable, the current amount is \$2,363,556 (December 31, 2019 - \$2,238,334).

Debenture warrant transactions and the number of debenture warrants outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2018	—	—
Issued	192	1,000
Balance, December 31, 2019	192	1,000
Issued	203	1,000
Balance, March 31, 2020	305	1,000

Date of Expiry	Exercise Price \$	Number of Warrants Outstanding
March 8, 2022	1,000	48
May 9, 2022	1,000	80
June 28, 2022	1,000	30
December 20, 2022	1,000	33
February 13, 2023	1,000	176
February 24, 2023	1,000	27
Balance, March 31, 2020	1,000	305

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Payments required over the next five years are as follows:

	May 30, 2017 \$	June 29, 2017 \$	March 8, 2019 \$	May 9, 2019 \$	June 28, 2019 \$	Dec. 20, 2019 \$	Feb. 13, 2023 \$	Feb.24, 2023 \$	Total \$
2020	1,385,530*	1,083,876*	64,800	106,400	44,000	84,689	31,066	4,692	2,805,053
2021	—	—	64,800	106,400	44,000	84,689	35,280	5,520	338,400
2022	—	—	821,895	1,366,353	571,269	1,110,111	35,280	5,520	3,910,428
2023	—	—	—	—	—	—	1,768,214	276,828	2,045,042
2024	—	—	—	—	—	—	—	—	—
	1,385,530	1,083,876	951,495	1,579,153	659,269	1,277,200	1,869,840	292,560	9,098,923

* Subsequent to year end, the Company settled the principal balances of these convertible debentures (Note 20) and paid the remaining interest for the May 30, 2017 and June 29, 2017 issuance.

12. LEASE LIABILITIES

Lease liabilities

The Company leases vehicles and office space in Canada. The lease liabilities were measured at the present value of the remaining lease payments as of January 1, 2019, discounted using an incremental borrowing rate at that date of 12%. The Company recorded a ROU asset of the same amount (Note 7).

At adoption, the value of the lease liabilities and ROU asset was \$604,569.

For the three months ended March 31, 2020, the Company recognized interest expense on the lease liability of \$14,374 (March 31, 2019 - \$1,585).

Lease liabilities

Lease liabilities	487,500
Less: non-current portion	(104,818)
March 31, 2020	382,682

Undiscounted lease payments

Not later than one year	156,116
Later than one year and not later than 5 years	463,093
March 31, 2020	619,209

The Company elected not to apply the new lease standard to short term leases with an initial term of 12 months or less but rather to recognise the lease expense on a straight line basis. For the three months ended March 31, 2020, \$Nil related to a short-term office lease and \$12,000 of variable lease payments (March 31, 2019 - \$19,438 and \$Nil, respectively) were included in rent expense on the statement of loss and comprehensive loss.

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13. SHARE CAPITAL

[a] Authorized Share Capital

The authorized share capital consisted of unlimited number of common shares. The common shares do not have a par value. All issued shares are fully paid.

[b] Common shares

The Company had the following share capital transactions during the year ended December 31, 2019:

- [i] During the year ended December 31, 2019, the Company issued 156,950 common shares valued at \$10,987 to settle an outstanding debt of \$15,695. As a result, the Company recognized a gain on debt settlement of \$4,708 on the consolidated statement of loss and comprehensive loss

The Company had the following share capital transactions during the three months ended March 31, 2020:

- [i] On January 13, 2020, the Company issued 1,093,750 common shares pursuant to a consulting agreement. The valuation was based on the fair value of the shares issued.
- [ii] On February 11, 2020, the Company issued 10,000,000 units at a price of \$0.065 for cash proceeds of \$156,000 and the settlement of debt of \$494,000 owed to officers, directors and consultants (the “**Financing**”). Debt settlement of officers and directors of the Company account for \$326,794 of the total settlements (Note 8).

Each unit consists of one common share and one common share purchase warrant. Each common share purchase warrant is exercisable into one common share at a price of \$0.10 for a period of two years from closing. In the event that the Company’s shares trade above \$0.25 for a period of 10 consecutive trading days at any time after June 12, 2020, the Company may accelerate the expiry date of the warrants by giving notice to the holders thereof and in such case, the warrants will expire on the 30th day after the date of giving such notice.

On March 5, 2020, related parties and consultants agreed to amend the exercise price of 7,027,596 out of 10,000,000 common share purchase warrants originally granted in the Financing to \$0.25 from \$0.10.

- [iii] On February 17, 2020 the Company issued 550,000 common shares in connection with the termination of the former Chief Operating Officer and an employee. The valuation was based on the fair value of the shares issued.
- [iv] On March 16, 2020 the Company issued 180,558 common shares pursuant to an employment agreement. The valuation was based on the fair value of the shares issued.

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13. SHARE CAPITAL (CONTINUED)

[c] Common share purchase warrants

Common share purchase warrant transactions and the number of common share purchase warrants outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2018	17,209,791	0.67
Issued	4,904,470	0.49
Expired	(1,676,789)	(1.38)
Balance, December 31, 2019	20,437,472	0.56
Issued	20,200,000	0.20
Expired	—	—
Balance, March 31, 2020	40,637,472	0.38

Date of Expiry	Exercise Price \$	Number of Warrants Outstanding
May 11, 2020	0.60	5,964,495*
May 30, 2020	1.05	942,857**
June 7, 2020	0.60	4,180,650*
June 29, 2020	1.05	730,714**
November 22, 2021	0.35	3,714,286
March 8, 2022	0.40	1,266,030
May 3, 2022	0.40	2,078,790
June 28, 2022	0.40	859,650
December 31, 2022	1.00	700,000
February 11, 2022	0.10	2,972,404
February 11, 2022	0.25	7,027,596
February 13, 2023	0.20	8,820,000
February 24, 2023	0.20	1,380,000
Balance, March 31, 2020	0.38	40,637,472

*Expired unexercised subsequent to period end (Note 20) **Amended subsequent to period end (Note 20)

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13. SHARE CAPITAL (CONTINUED)

[d] Stock options

During the three months ended March 31, 2020, the Company recorded share-based payments of \$141,762 (March 31, 2019 - \$68,105). During the three months ended March 31, 2020, the Company recorded a reversal of reserves on expired and forfeited options of \$5,298 (March 31, 2019 - \$60,259). The fair values of share options granted during the three months ended March 31, 2020 and 2019 are estimated using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2020	2019
Risk-free interest rate	1.42%	—
Estimated annualized volatility	114.79%	—
Expected life	5.0 years	—
Expected dividend yield	0%	—
Exercise price	\$0.09	—
Fair value per option	\$0.0736	—
Share price	\$0.09	—

Stock option transactions and the number of stock options outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2018	3,181,858	0.45
Issued	1,208,000	0.20
Expired	(3,781,858)	(0.40)
Balance, December 31, 2019	608,000	0.28
Issued	4,400,000	0.09
Expired	(100,000)	(0.26)
Balance, March 31, 2020	4,908,000	0.11

Date of Expiry	Exercise Price \$	Number of Options Outstanding	Number of Options Exercisable
July 12, 2021	1.05	100,000	100,000
October, 29, 2024	0.09	408,000	68,000
January 19, 2025	0.075	2,900,000	966,667
February 26, 2025	0.125	950,000	316,667
March 1, 2025	0.14	200,000	50,000
March 16, 2025	0.105	350,000	87,500
Balance, March 31, 2020	0.11	4,908,000	1,588,834

As of March 31, 2020, the weighted average remaining life for outstanding options was 4.75 years (December 31, 2019 – 3.52 years).

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14. COMMITMENTS AND CONTINGENCIES

[a]Low Carbon Infrastructure Transition Programme (“LCITP”) Grant for Clyde Gateway

SHARC UK has received grant funding of £1,684,188 for 50% of eligible capital costs associated with the Clyde Gateway Project. During the year ended December 31, 2019, \$285,386 (£168,419) was received for a total of \$2,928,736 (£1,684,188) grant received to date.

Per the underlying funding agreements, the parties jointly forecasted the expected revenue that would be generated from the projects for the first five years after completion. Under the terms of the grant, should the projects actual revenue exceed 10% or more of the forecasted revenue, the Scottish government reserves the right to require the Company to repay part of the grant.

This contingent liability is no longer applicable as of October 29, 2019 when SHARC UK entered into liquidation (Note 15).

[b]Parent Company Guarantee to Scottish Water Horizon Ltd. (“SWH”) for the Finance Facility to Bandwidth Energy Ltd. (“Bandwidth”)

During the year ended December 31, 2018, the Company entered into a joint arrangement and held a 50% interest in Bandwidth for £10,000 (\$17,357) with the other 50% held by SWH. As the Company held joint control of the arrangement but the legal form of the arrangement and the contractual terms of the arrangement did not give or specify that the parties had rights to the assets, and obligations for the liabilities and therefore, the investment was treated as a joint venture and accounted for as an equity investment.

The Company provided a guarantee to SWH for the finance facility provided to Bandwidth for the execution of certain works, namely the design, installation, testing and commissioning of a new sewage heat recovery system (“**Aqualibrium**”) totalling £604,726. The guarantee is limited to 50% of the finance facility provided, excluding any interest accrued per the original loan facility.

On September 17, 2019, the Company agreed to sell its 50% interest in Bandwidth for £10,000 cash to SWH, the other 50% shareholder, and terminated the agreement (“**Termination Agreement**”) for Aqualibrium with Bandwidth for £15,000. The Company continues to work with Bandwidth to bring Aqualibrium to commissioning.

[c]Parent Company Guarantee for Bandwidth for Installation and Operations and Maintenance of Aqualibrium

The Company provided certain guarantees over the installation and operations and maintenance of Aqualibrium (the “**Performance Guarantees**”). During the year ended December 31, 2019, on sale of the Company’s interest in Bandwidth to SWH, the parties entered into a Termination Agreement (Note 15). The Company however continues to work with Bandwidth to ensure these Performance Guarantees are achieved.

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15. DISCONTINUED OPERATIONS

On October 7, 2019, the Company signed an engagement letter with a liquidator for the liquidation and wind-up of SHARC UK. The liquidator was officially appointed October 29, 2019. Furthermore, on October 11, 2019, the Company appointed an administrator for Highlands. Both the liquidator and administrator for SHARC UK and Highlands, respectively, have taken possession of the subsidiaries and all of their assets and liabilities. The liquidator and administrator are also responsible for all ongoing costs of the subsidiaries until the administrator for Highlands is able to sell Clyde Gateway. Any profits obtained or losses incurred by the liquidator and administrator in the insolvency processes have no impact on the Company since all financial assets and obligations were transferred to the liquidator and administrator.

The Company established that following the appointments of the liquidator and administrator, it effectively lost control of the operations of SHARC UK and Highlands. The operating results and cash flow of SHARC UK and Highlands have been classified as discontinued operations on the statement of loss and comprehensive loss and as cash flow from discontinued operations respectively, for each of the year ended December 31, 2019. The consolidated statement of financial position as at December 31, 2019 does not include any balances of Highlands and SHARC UK as these have been deconsolidated as at October 11, 2019 and October 29, 2019 respectively.

As a result of the insolvency and the appointment of the administrator and liquidator, the Company has derecognized the assets and liabilities of Highlands and SHARC UK. The Company has received no consideration in the deconsolidation of Highlands and SHARC UK.

Loss on insolvency of Net Assets

Carrying value of Net Assets	\$
Current Assets	
Cash	113,776
Receivables	253,384
Prepaid expenses	8,352
Inventory	17,868
Deposits	8,799
Property and equipment	4,212,869
Current Liabilities	
Accounts payable and accrued liabilities	(1,520,087)
Loans payable	(91,492)
Lease liability	(12,760)
Loans payable	(2,379,248)
Lease liability	(13,112)
Loss on insolvency of Net Assets	598,349

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15. DISCONTINUED OPERATIONS (CONTINUED)

Net Loss from Discontinued Operations

	Note	Three months Ended March 31, 2020 \$	Three Months Ended March 31, 2019 \$
Revenue		—	421,393
Cost of Sales	8	—	(235,463)
Gross Margin		—	185,930
Expenses			
Accounting and legal		—	17,250
Advertising and promotion		—	31,574
Consulting	8	—	34,675
Depreciation	7	—	4,168
Insurance		—	9,129
Office and miscellaneous		—	11,173
Rent		—	12,315
Research and development		—	29,152
Telephone and utilities		—	7,749
Travel		—	56,098
Wages and benefits	8	—	150,670
		—	(363,953)
Other income (expense)			
Gain (loss) on equity investment		—	(888)
Interest and financing expense	9,14	—	(16,561)
Loss on discontinued operations		—	(195,472)

As at March 31, 2020, the total insolvency of net assets and loss on discontinued operations was \$Nil (December 31, 2019- \$1,205,159).

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16. CAPITAL MANAGEMENT

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern in order to support the development of its business and maintain the necessary corporate and administration functions to facilitate these activities. The capital of the Company consists of items included in shareholders' deficiency.

The Company manages and adjusts its capital structure when changes to the risk characteristics of the underlying assets or changes in economic conditions occur. To maintain or adjust the capital structure, the Company may attempt to raise new funds.

There were no changes to the Company's approach to capital management during the period other than disclosed in Note 15. The Company is not subject to externally imposed capital requirements.

17. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value

IFRS 13 establishes a fair value hierarchy for financial instruments measured at fair value that reflects the significance of inputs used in making fair value measurements as follows:

Level 1 – quoted prices in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liabilities, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and

Level 3 – inputs for the asset or liability that are not based upon observable market data.

The fair value of cash is based on Level 1 inputs. The fair value of the Company's cash, receivables, accounts payable and accrued liabilities and loans payable approximate their carrying values due to the short-term to maturity. The fair value of long-term liabilities are initially recorded at fair value and subsequently carried at amortized cost using rates comparable to market interest rates.

[a] Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's cash and receivables are exposed to credit risk. The Company reduces its credit risk on cash by placing these instruments with institutions of high credit worthiness. Receivables are primarily from sales or loans. The Company believes these parties to be of sound creditworthiness, and to date, all receivables have been settled in accordance with agreed upon terms and conditions. As at March 31, 2020 and December 31, 2019, the Company is exposed to credit risk arising from receivables.

[b] Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company manages liquidity risk by maintaining sufficient cash balances to enable settlement of transactions on the due date. The Company addresses its liquidity through debt financing. While the Company has been successful in securing financings in the past, there is no assurance that it will be able to do so in the future. The Company is exposed to liquidity risk.

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17. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

[c] Market risk

[i] Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. As at March 31, 2020 the Company is not exposed to any significant interest rate risk.

[ii] Currency risk

Foreign exchange risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. As at March 31, 2020 and December 31, 2019, the Company is not exposed to currency risk.

18. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

The following is the non-cash operating, investing and financing activities:

	Three months ended March 31, 2020 \$	Three months ended March 31, 2019 \$
ROU asset recognized upon accounting policy change	—	91,281
Additions to property and equipment in accounts payable and accrued liabilities	—	1,788,826
Reversal of share-based payments	5,298	60,259
Issuance of convertible debt – equity component	363,874	65,785
Issuance of convertible debt – warrant component	363,874	65,785
Inventory transferred to property and equipment	91,923	—
Private placement units issued for debt	494,000	—
Additions to prepaid expenses by common share issuance	87,500	—
Discontinued operations (Note 15)		

19. SEGMENTED INFORMATION

The Company has a single operating segment, the sales and marketing of sewage heat recovery systems. As at March 31, 2020 and December 31, 2019, all of the Company's continuing operations, assets and employees are in Canada.

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20. SUBSEQUENT EVENTS

[a] On May 7, 2020, the Company issued 45,455 common shares to settle an outstanding debt of \$8,925.

[b] On May 29, 2020, the Company issued unsecured convertible debenture units with a principal amount of \$2,000,000. The debenture matures on May 29, 2023 and bears interest at an annual rate of 2% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.15 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 3,333 share purchase warrants, each exercisable into one common share of the Company at \$0.25 per share for three years from issuance.

Total finders' fee of \$100,000 in cash and 200 debenture warrants were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in the placement.

[c] On May 29, 2020, the Company settled with all holders ("**Debentureholders**") of the Company's \$1,320,000 and \$1,023,000 12% unsecured, convertible debentures which were set to mature on May 30, 2020 and June 29, 2020 (the "**Maturing Debentures**").

The Debentureholders have entered into settlement agreements with the Company (the "**Settlement Agreements**") pursuant to which the Debentureholders accepted 75% cash payout of the outstanding principal amount of the Maturing Debentures, the payout of any accrued and unpaid interest up to the date of maturity and the amendment of 1,673,571 common share purchase warrants (the "**Warrants**") in consideration for the cancellation of the Maturing Debentures and a release of the Company's obligations under the Maturing Debentures. The expiry date of the Warrants will be extended by two years from May 30, 2020 and June 29, 2020 to May 30, 2022 and June 29, 2022, respectively, and the exercise price of the Warrants will be repriced to \$0.25 from \$1.05 (collectively, the "**Warrant Amendments**"). The Warrant Amendments are subject to the approval of the CSE.

[d] On June 12, 2020, the Company issued unsecured convertible debenture units with a principal amount of \$700,000. The debenture matures on June 12, 2023 and bears interest at an annual rate of 2% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.15 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 3,333 share purchase warrants, each exercisable into one common share of the Company at \$0.25 per share for three years from issuance.

Total finders' fee of \$34,475 in cash and 69 debenture warrants were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in the placement.

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20. SUBSEQUENT EVENTS (CONTINUED)

- [e] Subsequent to March 31, 2020, 10,145,145 common share purchase warrants expired unexercised.

- [f] Subsequent to March 31, 2020, holders of convertible debentures converted \$650,000 of principal into 5,125,000 common shares.