

Consolidated Financial Statements of

KNIGHTHAWK INC.

October 31, 2019 and 2018

(Expressed in Canadian dollars)

KNIGHTHAWK INC.

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INDEPENDENT AUDITOR'S REPORT

To the shareholders of

KnightHawk Inc.

Opinion

We have audited the consolidated financial statements of KnightHawk Inc. and its subsidiaries, together (the "Company"), which comprise the consolidated statements of financial position as at October 31, 2019 and 2018, the consolidated statements of operations and comprehensive loss, changes in equity, and cash flows for the years then ended, and the notes comprising a summary of significant accounting policies and other explanatory information.

In our opinion, these consolidated financial statements, present fairly, in all material respects, the consolidated financial position of the Company as at October 31, 2019 and 2018, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audits in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the audit of the Consolidated Financial Statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audits of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained in our audit is sufficient and appropriate to provide a basis for our opinion.

Other Information

Management is responsible for the other information. The other information comprises the information included in the Management Discussion and Analysis.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audits of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We obtained Management's Discussion and Analysis prior to the date of this auditors report. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objective is to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decision of users on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion of the effectiveness of the Company's internal control

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of managements use of the going concern basis of accounting and, based on the audit, evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonable be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit in this independent auditor's report is Satpal S. Johl.

Burnaby, BC

February 19, 2020



Kanester Johal LLP

Chartered Professional Accountants

KNIGHTHAWK INC.**Consolidated Statements of Financial Position (Expressed in Canadian dollars)**

	October 31, 2019	October 31, 2018
ASSETS		
CURRENT		
Cash and cash equivalents	\$ 756,261	\$ 826,405
Prepaid expenses	4,358	6,825
	760,619	833,230
Assets of discontinued rail related operations (Note 3)	-	11,000
Assets of discontinued air operations (Note 4)	-	-
	\$ 760,619	\$ 844,230
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	\$ 13,821	\$ 13,863
Liabilities of discontinued rail related operations (Note 3)	50,936	54,265
Liabilities of discontinued air operations (Note 4)	92,694	92,694
	157,451	160,822
Other (Note 8)	-	-
	157,451	160,822
Commitments and contingencies (Note 5, 8 and 12)		
SHAREHOLDERS' EQUITY (DEFICIT)		
Share capital (Note 7)	5,553,666	5,553,666
Contributed surplus	79,371	79,371
Accumulated deficit	(5,029,869)	(4,949,629)
	603,168	683,408
	\$ 760,619	\$ 844,230
See accompanying notes		

ON BEHALF OF THE BOARD

(Signed) Kenneth H. Fitzgerald, Director

(Signed) John Howe, Director

KNIGHTHAWK INC.**Consolidated Statements of Operations and Comprehensive Earnings (Loss)****Years ended October 31 (Expressed in Canadian dollars)**

	<u>2019</u>		<u>2018</u>	
Earnings (loss) from discontinued rail related operations (Note 3)	\$	(80,240)	\$	(113,326)
Earnings (loss) from discontinued air operations (Note 4)		-		-
NET COMPREHENSIVE EARNINGS (LOSS) FOR YEAR	\$	(80,240)	\$	(113,326)
COMPREHENSIVE EARNINGS (LOSS) PER SHARE - BASIC	\$	(0.007)	\$	(0.010)
COMPREHENSIVE EARNINGS (LOSS) PER SHARE - DILUTED	\$	(0.007)	\$	(0.010)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING		11,849,853		11,849,853

See accompanying notes

KNIGHTHAWK INC.**Consolidated Statements of Changes in Equity (Deficit) (Expressed in Canadian dollars)**

	Number of Common Shares	Share Capital	Contributed Surplus	Equity (Deficit)	Total Equity (Deficit)
Balance, October 31, 2017	11,849,853	\$ 5,553,666	\$ 79,371	\$ (4,836,303)	\$ 796,734
Comprehensive Earnings (Loss)	-	-	-	(113,326)	(113,326)
Balance, October 31, 2018	11,849,853	5,553,666	79,371	(4,949,629)	683,408
Comprehensive Earnings (Loss)	-	-	-	(80,240)	(80,240)
Balance, October 31, 2019	11,849,853	\$ 5,553,666	\$ 79,371	\$ (5,029,869)	\$ 603,168

See accompanying notes

KNIGHTHAWK INC.**Consolidated Statements of Cash Flows****Years ended October 31 (Expressed in Canadian dollars)**

	<u>2019</u>	<u>2018</u>
NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING ACTIVITIES		
Cash flows from discontinued rail related operations (Note 3)	\$ (70,144)	\$ (96,101)
Cash flows from discontinued air operations (Note 4)	-	-
DECREASE IN CASH DURING YEAR	(70,144)	(96,101)
CASH, BEGINNING OF YEAR	826,405	922,506
CASH, END OF YEAR	\$ 756,261	\$ 826,405

See accompanying notes

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1. NATURE OF OPERATIONS

The Company operated a short line railroad carrying freight within British Columbia, Canada. Its head office and registered office is located at #211 – 1015 Austin Avenue, Coquitlam, British Columbia, Canada, V3K 3N9. It was incorporated under the laws of Canada. However, on July 5, 2013, KnightHawk announced that it had ceased operating its rail and rail related operations. Toward that end, KnightHawk's indirectly wholly owned subsidiary company, Kelowna Pacific Railway Ltd. ("KPR"), made an Assignment into Bankruptcy (the "Filing"). Boale, Wood & Company Ltd. was named Trustee under the Filing. Further information about the Filing is available at www.boalewood.ca.

As a result of the above decision, KPR, and KnightHawk's remaining subsidiaries, discontinued operations and commenced the process toward an orderly disposition of its rail and rail related assets. Net proceeds were used in part to repay any secured debt which was outstanding. The assets and liabilities of discontinued rail and rail related operations, and rail and rail related operating results, have been reclassified in the consolidated financial statements as Discontinued Rail Related Operations.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared using accounting principles generally accepted in Canada, the more significant of which are as follows:

a) Statement of Compliance

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

These consolidated financial statements were authorized for issuance by the Board of Directors of the Company on February 19, 2020.

b) Basis of measurement

These consolidated financial statements have been prepared on a historical cost basis except for financial instruments and assets held for sale from discontinued operations that have been measured at fair value. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting.

These consolidated financial statements, including comparatives, have been prepared on the basis of IFRS that are published at the time of preparation and that are effective or available for adoption on October 31, 2019.

c) Principles of consolidation

The consolidated financial statements include the accounts of KnightHawk Inc. and its wholly-owned subsidiaries, KnightHawk Rail Ltd., 2734141 Canada Inc., 4090187 Canada Inc., and Kelowna Pacific Railway Ltd., with the accounts of Kelowna Pacific Railway Ltd. only included to the date of the above noted Filing. All applicable inter-company transactions and balances have been eliminated.

d) Assets held for sale from discontinued operations

Non current assets included in assets of discontinued operations have been valued at the lower of their carrying amount and fair value less cost to sell.

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In the statement of operations and comprehensive earnings (loss), income and expenses from discontinued operations are reported separately from income and expenses from continuing operations, down to the level of profit (loss) after taxes. Property, plant and equipment and intangible assets, once classified as held for sale, are not depreciated.

e) Functional and presentational currency

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates of exchange in effect at the date of the balance sheet. Items affecting income are converted at rates of exchange in effect at the date of the transaction. Exchange gains and losses are included in income and expenses.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when fair value is determined.

f) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with banks, and short-term highly liquid investments with original maturities of three months or less.

g) Revenue

Interest on cash balances since rail related operations were discontinued is recognized as revenue during and for the period it is earned.

h) Income taxes

Income tax expense comprises current tax and deferred tax. Current tax and deferred tax are recognized in the consolidated statements of operations and comprehensive income (loss), except to the extent that they relate to a business combination, or items recognized directly in equity or in other comprehensive income (loss).

Current tax is the expected tax payable or receivable based on the taxable income or loss for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to taxes payable in respect of prior years.

Deferred tax assets and liabilities are recognized for the future income tax consequences attributable to differences between the consolidated financial statements' carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted or substantially enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized.

i) Earning per share

Basic earnings (loss) per share is calculated using the weighted average number of shares issued and outstanding during the year. The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on earnings per share is calculated presuming the exercise of outstanding options to be issued. It assumes that the proceeds of such exercise would be used to repurchase common shares at the

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average market price during the period. However, the calculation of diluted earnings (loss) per share excludes the effects of various conversions and exercise of options, warrants and, contingent shares to be issued that would be anti-dilutive.

j) Significant accounting judgements and estimates

The preparation of the consolidated financial statements requires management to make judgements and estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the reporting period. Actual outcomes could differ from these judgements and estimates. The consolidated financial statements include judgements and estimates which, by their nature, are uncertain. The impacts of such judgements and estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods.

Significant areas requiring the use of management estimates includes the valuation of amounts receivable, assets held for sale, accrued liabilities, and the ability to realize the benefit of tax loss carry-forwards.

Significant areas requiring the use of management judgements includes the classification of financial instruments and decisions in respect of assets and liabilities of discontinued operations.

k) Impairment

The carrying amount of property and equipment and other financial assets are reviewed for impairment at each reporting period and whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. If any such indication is present, the recoverable amount of the asset is estimated in order to determine whether impairment exists. Where the asset does not generate cash flows that are independent from other Company assets, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

An asset's recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value, using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset or cash generating unit is estimated to be less than its carrying amount, the carrying amount is reduced to the recoverable amount and the impairment is recognized immediately as additional depreciation or other applicable operating expense. Where an impairment subsequently reverses, the carrying amount is increased to the revised estimate of recoverable amount but only to the extent that this does not exceed the carrying value that would have been determined if no impairment had previously been recognized. A reversal is recognized as a reduction in the depreciation charge or other applicable operating expense for the period.

l) Share-based payments

The Company offers equity-settled share-based payment plans for eligible directors, officers and employees. The plan is accounted for using the fair value method. Under the fair value method, compensation expense for these share-based payments is determined based on the fair value at the grant date using the Black-Scholes option pricing model and is charged to income over the vesting period. For equity-settled share-based payments that vest over more than a single period, each tranche of the award is considered to be a separate grant and the fair value of each is calculated on

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the grant date. Management estimates a forfeiture rate for the purpose of determining the compensation expense over the vesting period.

Equity-settled awards relate to stock options. When stock options are exercised, any consideration paid, as well as the related share-based compensation are credited to capital stock. Equity-settled awards are not re-measured subsequent to the initial grant. Equity-settled awards are re-measured for changes in terms and conditions subsequent to their initial grant.

m) Financial instruments

The Company adopted all of the requirements of IFRS 9 Financial Instruments on November 1, 2018. IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 utilizes a revised model for recognition and measurement of financial instruments in a single, forward-looking “expected loss” impairment model. The change did not impact the carrying value of any of the Company’s financial instruments on the transition date.

The Company has assessed the classification and measurement of its financial assets and financial liabilities under IFRS 9. Additional disclosure for financial instruments is set out in Note 10.

The following is the Company’s accounting policy for financial instruments under IFRS 9:

(i) Classification

The Company classifies its financial instruments into the following categories: at fair value through profit and loss (“FVTPL”), at fair value through other comprehensive income (loss) (“FVTOCI”) or at amortized cost. The Company determines the classification of financial assets at initial recognition. The classification of debt instruments is driven by the Company’s business model for managing the financial assets and their contractual cash flow characteristics. Equity instruments that are held for trading are classified as FVTPL. For other equity instruments, on the day of acquisition the Company can make an irrevocable election (on an instrument-by-instrument basis) to designate them as at FVTOCI. Financial liabilities are measured at amortized cost, unless they are required to be measured at FVTPL (such as instruments held for trading or derivatives) or if the Company has opted to measure them at FVTPL.

(ii) Measurement

Financial assets and liabilities at amortized cost

Financial assets and liabilities at amortized cost are initially recognized at fair value plus or minus transaction costs, respectively, and subsequently carried at amortized cost using effective interest method less any impairment.

Financial assets and liabilities at FVTPL

Financial assets and liabilities carried at FVTPL are initially recorded at fair value and transaction costs are expensed in the statements of operations and comprehensive earnings (loss). Realized and unrealized gains and losses arising from changes in the fair value of the financial assets and liabilities held at FVTPL are included in the statements of operations and comprehensive earnings (loss) in the period in which they arise.

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Debt investments at FVTOCI

These assets are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses, and impairment, are recognized in profit or loss. Other net gains and losses are recognized in other comprehensive income ("OCI"). On derecognition, gains and losses accumulated in OCI are reclassified to profit or loss.

Equity investments at FVTOCI

These assets are subsequently measured at fair value. Dividends are recognized as income in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. Other net gains and losses are recognized in OCI and are never reclassified to profit or loss.

(iii) Impairment of financial assets at amortized cost

The Company recognizes a loss allowance for expected credit losses on financial assets that are measured at amortized cost. At each reporting date, the Company measures the loss allowance for the financial asset at an amount equal to the lifetime expected credit losses if the credit risk on the financial asset has increased significantly since initial recognition. If at the reporting date, the credit risk on the financial asset has not increased significantly since initial recognition, the Company measures the loss allowance for the financial asset at an amount equal to the twelve month expected credit losses. The Company shall recognize in the statements of operations and comprehensive earnings (loss), as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognized.

(iv) Derecognition

Financial assets

The Company derecognizes financial assets only when the contractual rights to cash flows from the financial assets expire, or when it transfers the financial assets and substantially all of the associated risks and rewards of ownership to another entity.

Financial liabilities

The Company derecognizes a financial liability when its contractual obligations are discharged or cancelled, or expire. The Company also derecognizes a financial liability when the terms of the liability are modified such that the terms and or cash flows of the modified instrument are substantially different, in which case a new financial liability based on the modified terms is recognized at fair value.

Gains and losses on derecognition are generally recognized in profit or loss.

n) Provisions

Provisions represent liabilities of the Company for which the amount or timing is uncertain. A provision is recognized when, as a result of a past event, the Company has a present obligation (legal or constructive) that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

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o) Recent accounting pronouncements

Certain new standards, interpretations and amendments to existing standards, as noted below, are not yet effective and have not been applied in preparing these financial statements. The Company is in the process of assessing the impacts of the standards and amendments on its consolidated financial statements.

Leases

The new standard was issued with the objective to recognize all leases on the balance sheet. IFRS 16 requires lessees to recognize a “right of use” asset and a lease liability calculated using a prescribed methodology. The mandatory effective date of IFRS 16 is for annual periods beginning on or after January 1, 2019. Early adoption is permitted provided that IFRS 15, Revenue from Contracts with Customers, is also adopted.

3. DISCONTINUED RAIL RELATED OPERATIONS

On July 5, 2013, KnightHawk announced that it had ceased operating its rail and rail related operations. Toward that end, KnightHawk’s indirectly wholly owned subsidiary company, Kelowna Pacific Railway Ltd. (“KPR”), made an Assignment into Bankruptcy (the “Filing”). Boale, Wood & Company Ltd. was named Trustee under the Filing. Further information about the Filing is available at www.boalewood.ca.

As a result of the above decision, KPR, and KnightHawk’s remaining subsidiaries, discontinued operations and commenced the process toward an orderly disposition of its rail and rail related assets. Net proceeds were used in part to repay any secured debt which was outstanding. The assets and liabilities of discontinued rail and rail related operations, and rail and rail related operating results, have been reclassified in the consolidated financial statements as Discontinued Rail Related Operations. All assets and liabilities of KPR were removed from the consolidated financial statements effective the date of the Filing. All remaining assets and liabilities of discontinued rail related operations, being KnightHawk’s remaining subsidiaries, have been written down to their estimated fair values as at October 31, 2019 and 2018. The resulting gain (loss) on write-downs from the removal of KPR from the consolidated financial statements, and the write-downs of the assets and liabilities of KnightHawk’s remaining subsidiaries to their net realizable value, has been noted in the table below and years prior consolidated financial statements.

Included in assets of discontinued rail related operations as at October 31, 2019 were assets of KPR totalling \$Nil (2018 - \$Nil) and assets of KnightHawk’s remaining subsidiaries totalling \$Nil (2018 - \$11,000).

Included in liabilities of discontinued rail related operations as at October 31, 2019 were liabilities of KPR totalling \$Nil (2018 - \$Nil) and liabilities of KnightHawk and its remaining subsidiaries totalling \$50,936 (2018 - \$54,265).

Included in revenues from discontinued rail related operations for the year ended October 31, 2019 was interest of \$14,809 (2018 - \$11,929) which was earned on cash balances since rail related operations were discontinued. Included in expenses from discontinued rail related operations for the year ended October 31, 2019 in this regard were ongoing audit, compliance and other related costs of \$60,899 (2018 - \$67,210). The earnings (loss) from discontinued rail related operations for the year ended October 31, 2019 also included gains (losses) on the sale of assets of discontinued rail related operations of \$2,228 (2018 - \$16,760).

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Earnings (loss) from discontinued rail related operations are as follows:

	For the year ended October 31	
	2019	2018
Revenues	\$ 14,809	\$ 11,929
Expenses	(97,277)	(142,015)
Loss before exchange gain (loss)	(82,468)	(130,086)
Unrealized foreign exchange gain (loss)	-	-
Loss before gain (loss) on sale	(82,468)	(130,086)
Gain on sale of assets	2,228	16,760
Loss before write-downs	(80,240)	(113,326)
Gain (loss) on write-downs	-	-
Loss from discontinued rail related operations net of \$nil tax (See Note 6)	\$ (80,240)	\$ (113,326)

Cash flows from discontinued rail related operations are as follows:

	For the year ended October 31	
	2019	2018
Net inflow (outflow) of cash related to the following activities:		
Operating	\$ (83,372)	\$ (153,861)
Investing	13,228	57,760
Cash flows from discontinued rail related operations	\$ (70,144)	\$ (96,101)

4. DISCONTINUED AIR OPERATIONS

In 2005 the Company's wholly owned air cargo airline subsidiary, 2734141 Canada Inc. (operating as KnightHawk Air Express) discontinued operations and commenced the process toward an orderly disposition of its air freight assets. During 2006 substantially all of its air freight assets were sold with the net proceeds used to repay all secured debt which was outstanding to its outside lender. The remaining assets and liabilities of discontinued air operations and air freight operating results have been reclassified in the consolidated financial statements as Discontinued Air Operations. All assets and liabilities of discontinued air operations have been written down to their estimated fair values as at October 31, 2019 and 2018, with the resulting gain (loss) on write-downs noted in the table below and years prior consolidated financial statements.

Earnings (loss) from discontinued air operations are as follows:

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	For the year ended October 31	
	2019	2018
Revenues	\$ -	\$ -
Expenses	-	-
Earnings (loss) before exchange gain (loss)	-	-
Unrealized foreign exchange gain (loss)	-	-
Loss before write-downs	-	-
Gain on write-downs (See Note 8)	-	-
Earnings (loss) from discontinued air operations net of \$nil tax (See Note 6)	\$ -	\$ -

There was no inflow (outflow) of cash related to operating, financing or investing activities from discontinued air operations in the years ended October 31, 2019 and 2018.

5. RELATED PARTY TRANSACTIONS

During the year, the Company incurred \$41,100 (2018 - \$55,350) in management and consulting services payable to a private company beneficially owned by Kenneth Fitzgerald, a director and Chief Executive Officer of the Company. These transactions were in the normal course of operations.

The total compensation for the Board of Directors and the executive management team is as follows:

	2019	2018
Short-term employment benefits *	\$ 48,600	\$ 62,850
	\$ 48,600	\$ 62,850

* includes management and consulting services noted above

The Company's Chief Executive Officer, Kenneth Fitzgerald, through a private company beneficially owned by him, (the "Consultant") provides management and consulting services to the Company pursuant to a consulting agreement (the "Consulting Agreement"). During the 2016 fiscal year the Compensation Committee of the Board of Directors of the Company consisting of John Howe and Bill Michealoff commenced a review of the Consulting Agreement. The original agreement was entered into on April 17, 2003 and had not been subject to substantive review or updated since that time. Following its deliberations, the Compensation Committee recommended an addendum to the Consulting Agreement (the "Addendum") at a Board meeting held on June 28, 2016. The Addendum provides for a one-time lump sum payment to the Consultant in the amount of three hundred and fifty thousand Canadian Dollars (CDN\$350,000) in the event of the Company's termination of the Consulting Agreement with or without cause or upon a change of control as defined therein. The recommendation of the Compensation Committee was approved by the Board, with Mr. Fitzgerald abstaining, on July 3, 2016, and the Addendum was made effective July 29, 2016. A further discussion of the Addendum is contained in the Management's Discussion and Analysis for the nine months ended July 31, 2016 and year ended October 31, 2019.

During the third quarter of 2009, a company, or companies, controlled by Kenneth Fitzgerald, a director and Chief Executive Officer of the Company, agreed to provide a loan facility to KnightHawk Inc. and or one or more of its subsidiary companies. The loans are repayable on demand and bear

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interest at 12% per annum, with interest only monthly payments. Security for the loans include, a general security agreement creating a fixed and floating charge over the assets of KnightHawk Inc. and its subsidiary companies. The loan proceeds have been used primarily in support of acquisitions of property and equipment, as well as for general working capital purposes. Loan advances under this facility totalled \$500,000 as at October 31, 2011. Repayments of \$200,000 and \$300,000 were made in the third quarter of 2012 and 2013, respectively, reducing total loan advances under this facility to \$Nil as at October 31, 2019 and 2018. Interest charges on the loan advances for the year ended October 31, 2019 were \$Nil (2018 - \$Nil).

6. INCOME TAXES

Reconciliation to statutory rate

The recovery of income taxes in the statement of operations and comprehensive earnings (loss) reflects an income tax rate which differs from the Canadian Statutory Rate as follows:

	2019	2018
Income before income tax from continuing operations	\$ -	\$ -
Income (loss) before income tax from discontinued operations	(80,240)	(113,326)
Income (loss) before income taxes	\$ (80,240)	\$ (113,326)
Expected income tax (recovery) expense at a combined federal and provincial rate of 27.00% (2018 - 26.833%)	\$ (21,665)	\$ (30,409)
Permanent and other differences	(81,018)	(4,532)
Unrecorded potential benefit of non-capital losses not recognized	102,683	34,941
Income tax expense	\$ -	\$ -

Deferred Income Taxes

Deferred income taxes are provided for temporary differences. Deferred incomes tax assets and liabilities are comprised of the following:

	2019	2018
Property and equipment	\$ 2,000	\$ 82,000
Tax loss carry forwards	1,221,000	1,112,000
Valuation allowance	(1,223,000)	(1,194,000)
Net deferred income tax asset (liability)	\$ -	\$ -

Tax losses

The Company has non-capital losses of \$4,203,000 and capital losses of \$640,000 which are available to offset future income taxes. The benefits of these losses are not recognized in these financial statements as it is probable that they will not be realized. The non-capital losses expire as follows:

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<u>Expiry Date</u>	<u>Amount</u>
2026	\$ 1,325,000
2027	322,000
2028	453,000
2029	423,000
2030	349,000
2032	1,000
2033	298,000
2034	121,000
2035	141,000
2036	128,000
2037	132,000
2038	130,000
2039	<u>380,000</u>
	\$ <u>4,203,000</u>

7. SHARE CAPITAL

a) Authorized:

Unlimited common shares without par value

b) Issued:

	<u>2019</u>		<u>2018</u>	
	<u>Number of Shares</u>	<u>\$ Amount</u>	<u>Number of Shares</u>	<u>\$ Amount</u>
Balance outstanding, beginning of year	11,849,853	5,553,666	11,849,853	5,553,666
Balance outstanding, end of year	11,849,853	5,553,666	11,849,853	5,553,666

c) Stock options

The Company maintains a stock option plan for certain employees, officers, and directors to acquire common shares in the Company. Unless otherwise stated, all stock options granted vest immediately.

Details of stock options outstanding are as follows:

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	2019		2018	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Outstanding and exercisable, beginning of year	Nil	N/A	Nil	N/A
Granted	-		-	
Expired	-		-	
Outstanding and exercisable, end of year	Nil	N/A	Nil	N/A

As at October 31, 2019 and 2018, no stock options remained outstanding.

8. OTHER

Other originally represented an uncollateralized non interest bearing promissory note in the amount of \$969,760 (2018 - \$968,434) (U.S. \$736,900) repayable only if certain predetermined quarterly cash flow thresholds are exceeded by the Company. No repayments were required during the year as the Company did not exceed the predetermined quarterly cash flow thresholds in the year.

As the Company has not exceeded the predetermined quarterly cash flow thresholds since inception of this obligation in 2004, and cash flow was further impaired by discontinued operations, Other was written down in the 2015 fiscal year to its estimated fair value of \$Nil as at October 31, 2015. In the event that the Company exceeds the predetermined quarterly cash flow thresholds in any future period, any required repayment will be recorded as an expense in that future period, until the promissory note is repaid in full.

9. EARNINGS PER SHARE

For the years ended October 31, 2019 and 2018, the effect of potentially dilutive securities was not included in the calculation of diluted earnings per share as the result would have been anti-dilutive.

10. RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

The Corporation's financial instruments consist of cash and cash equivalents, prepaid expenses, and accounts payable and accrued liabilities which are classified as at amortized cost, and assets held for resale and liabilities of discontinued operations which are classified as at FVTPL.

Fair values

CPA Canada establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The three levels of the fair value hierarchy are as follows:

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- 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.

The financial instruments recorded at fair value on the consolidated statement of financial position are assets and liabilities of discontinued rail related operations and assets and liabilities of discontinued air operations, measured using Levels 1, 2 and 3 of the fair value hierarchy. The fair values of all these instruments approximate their carrying values.

Financial risk management

In the normal course, the Company is exposed to various risks such as credit risk, interest rate risk, foreign currency risk, and liquidity risk.

Credit risk

Credit risk is the risk of an unexpected loss if a counterparty to a financial instrument fails to meet its contractual obligations.

Interest rate risk

The Company is exposed to interest rate risk, which is the risk that the fair value of future cash flows of a financial instrument will vary as a result of changes to market interest rates. This includes interest earned on cash balances since rail related operations were discontinued.

To perform sensitivity analysis, the Company assesses the impact of hypothetical changes in interest rates on interest earned on such cash balances. Information provided by the analysis does not represent the Company's view of future market changes, nor does it necessarily represent the actual changes in fair value that would occur under normal market conditions because, of necessity, all variables other than the specific market risk factor are held constant. In reality, changes in one factor may result in a change to another, which may magnify or counteract the sensitivities.

Based on cash balances as at October 31, 2019 of \$756,261, a 1% increase (decrease) in interest rates could increase (decrease) annual net comprehensive earnings by approximately \$8,000.

Currency risk

The unsecured non interest bearing promissory note described in Note 8 of the consolidated financial statements is denominated in U.S. dollars. Foreign currency risks are dependant on the U.S. dollar exchange rate at the time of the payment of this note.

The Company does not trade derivative financial instruments and does not enter into speculative transactions.

To perform sensitivity analysis, the Company assesses the impact of hypothetical changes in foreign currency exchange rates on foreign currency denominated financial instruments. Information provided by the analysis does not represent the Company's view of future market changes, nor does it necessarily represent the actual changes in fair value that would occur under normal market conditions because, of necessity, all variables other than the specific market risk factor are held

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constant. In reality, changes in one factor may result in a change to another, which may magnify or counteract the sensitivities.

Based on the total of the unsecured non interest bearing promissory note described in Note 8 as at October 31, 2019 of \$969,760 (Canadian \$ equivalent), a 1% increase (decrease) in the value of the U.S. dollar relative to the Canadian dollar could decrease (increase) net comprehensive earnings by approximately \$10,000 in a future period where repayment was required (See Note 8).

Liquidity risk

The Company monitors and manages its cash requirements to ensure access to sufficient funds to meet operational or investing requirements. The Company's principal source of liquidity is cash on hand. The Company's primary uses of funds are for working capital requirements, contractual obligations and overhead. As such, the Company sets priorities on its uses of available funds based on short-term requirements and strategic initiatives, while keeping in mind its long-term contractual obligations and returning value to its shareholders.

11. CAPITAL MANAGEMENT

The Company's objective when managing capital is to maximize shareholder value and safeguard the Company's ability to continue as a going concern. This is accomplished by increasing the underlying value of the Company's assets through internal growth and investing the Company's capital profitably, and having that value reflected in the share price. Capital includes funding provided by or through, share capital, loans, and trade creditors.

12. COMMITMENTS AND CONTINGENCIES

The Company has no operating lease commitments.

From time to time, in the ordinary course of operations, the Company may be involved in potential or alleged legal actions. The Company makes an accrual based on its judgement regarding the likelihood of the outcome of the action and information in hand.

See Note 5 and 8 also.

13. SEGMENTED REPORTING

The Company operated from one geographic area, British Columbia, Canada, and had one operating segment, rail freight and related services, which discontinued operations in the year ended October 31, 2013.