

Management in accordance with International Financial Reporting Standards prepared the accompanying consolidated financial statements of LeoNovus Inc.. Management acknowledges responsibility for the preparation and presentation of the financial statements, including the responsibility for significant accounting judgments and estimates and the choice of accounting principles and methods that are appropriate to the Company's circumstances.

Management has established processes, which are in place to provide them sufficient knowledge to support management representations that they have exercised reasonable diligence that (i) the consolidated financial statements do not contain any untrue statement of material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it is made, as of the date of and for the periods presented by the consolidated financial statements and (ii) the consolidated financial statements fairly present in all material respects the financial condition, results of operations and cash flows of the Company, as of the date of and for the periods presented by the consolidated financial statements. Management is not; however, required to certify the design and evaluation of these processes and has not completed such an evaluation. This may result in additional risks to the quality, reliability, transparency and timeliness of the presentation.

The Board of Directors is responsible for reviewing and approving the consolidated financial statements together with other financial information of the Company and for ensuring that management fulfills its financial reporting responsibilities. An Audit Committee assists the Board of Directors in fulfilling this responsibility. The Audit Committee meets with management to review the financial reporting process and the consolidated financial statements together with other financial information of the Company. The Audit Committee reports its findings to the Board of Directors for its consideration in approving the consolidated financial statements together with other financial information of the Company for issuance to the shareholders.

Management recognizes its responsibility for conducting the Company's affairs in compliance with established financial standards, and applicable laws and regulations, and for maintaining proper standards of conduct for its activities.

Date: August 29, 2017

"Michael Gaffney"

Michael Gaffney
Chairman & CEO

"Daniel Hilton"

Daniel Hilton
CFO

**LeoNovus Inc.,
(the “Company” or “LeoNovus”)
Management’s Discussion and Analysis (MD&A)
For the period April 1, 2017 to June 30, 2017**

The following MD&A was prepared by management and should be read in conjunction with the Company's Consolidated Financial Statements for the year ended December 31, 2016, including all notes, risk factors and information contained therein. The following discussion and analysis provides information that management believes is relevant to the assessment and understanding of the Company's results of operations and financial condition.

We wish to caution readers that this report includes certain forward-looking information and statements. These forward-looking statements contain information that is generally stated to be anticipated, expected or projected by LeoNovus and involve known and unknown risks, uncertainties and other factors which may cause the actual results and performance of Company to be materially different from any future results and performance expressed or implied by such forward-looking information. Potential risks and uncertainties include, without limitation, the uncertainties inherent in the development of LeoNovus' software defined storage solution, LeoNovus' need for significant additional funding to continue as a going concern and rapid developments in technology, including developments by competitors. Forward-looking statements are not guarantees of future performance. They involve risks, uncertainties and assumptions, and actual results may differ materially from those anticipated in these forward-looking statements. Forward-looking information will be updated as required pursuant to National Instrument 51-102 – *Continuous Disclosure Obligations* (“NI 51-102”) and except as required by applicable laws, the Company assumes no obligation to update forward-looking statements should circumstances or management's estimates or opinions change. Additional information relating to the Company and its operations is available on SEDAR at www.sedar.com.

This MD&A includes a discussion of the results of operations and cash flows for the period ended June 30, 2017 and 2016. The unaudited interim condensed consolidated financial statements have been prepared in US dollars and in accordance with International Financial Reporting Standards (“IFRS”) using the accounting policies described in Note 2 to the Company's Consolidated Financial Statements.

Management is responsible for ensuring that processes are in place to provide sufficient knowledge to support the representations made in the financial filings. Management is not; however, required to certify the design and evaluation of these processes and has not completed such an evaluation. Our Audit Committee and Board of Directors provide an oversight role with respect to all public financial disclosures by the Company, and have reviewed this MD&A and the accompanying consolidated financial statements.

Date

This MD&A is dated August 29, 2017 and is in respect of the quarter ended June 30, 2017 and 2016.

History, Nature of Business and Overall Performance

Work Horse Capital & Strategic Acquisitions Ltd., ("Work Horse") incorporated under the Canada Business Corporations Act on December 30, 2008, as a Capital Pool Company ("CPC"), as defined in Policy 2.4 of the TSX Venture Exchange (the "Exchange"). Work Horse became a "reporting issuer" on March 24, 2009 and has been listed on the Exchange since June 10, 2009.

On October 29, 2010, Personal Web Systems Inc. (PWS) completed a reverse takeover transaction with Work Horse, resulting in Work Horse owning all of the issued and outstanding securities of PWS. The acquisition of PWS by Work Horse constituted Work Horse's Qualifying Transaction as defined by the Exchange. Although the transaction resulted in PWS becoming a wholly-owned subsidiary of Work Horse, the transaction constituted a reverse take-over of Work Horse in as much as the former shareholders of PWS and new shareholders from a simultaneous private placement offering own a majority of the outstanding shares of the Company and three of the six members of the Board of Directors are former board members of PWS.

In March 2011, Work Horse's name was changed to LeoNovus Inc. (using a new stock symbol "LTV").

Since January 2013, the Company has completed the following equity transactions:

In January and March 2013, the Company completed a non-brokered private placement offering of 12,735,666 Units at CDN \$0.15 for gross proceeds of CDN \$1,910,000 (US \$1,872,000). Each Unit consisted of one share of stock and a two year warrant for one common share exercisable at CDN \$0.24. In the first close in January, 2,866,000 Units were purchased at a price of CDN \$0.15 per Unit for gross proceeds of CDN \$430,000 (US \$431,000). In the second close, 9,869,666 Units were purchased at a price of CDN \$0.15 per Unit for gross proceeds of CDN \$1,480,000 (US \$1,440,000).

In August 2013, the Company completed a concurrent brokered and non-brokered private placement offering of an aggregate amount of 14,134,116 units at CDN \$0.17 per unit for gross proceeds of CDN \$2,403,000 (US \$2,323,000). Each Unit consisted of one common share of stock and a two year warrant for one common share exercisable at CDN \$0.30.

In October 2013, holders of 2,602,690 purchase price warrants exercised their warrants at CDN \$0.20 per warrant for a total of CDN \$521,000 (US \$536,000). The remaining 979,521 purchase price warrants were not exercised and have expired.

In December 2013, holders of 7,375,000 exchangeable warrants exercised their warrants into common shares in accordance with the warrant agreements dated October 2010.

In January 2014, the Company completed a non-brokered private placement offering of an aggregate amount of 9,700,000 units at CDN \$0.23 per unit for gross proceeds of CDN \$2,231,000 (US \$2,031,000). Each Unit consisted of one share of common stock and a two year warrant for one share exercisable at CDN \$0.40.

In 2014, 8,739,645 warrants from private placements have been exercised for net proceeds of \$1,967,000 CDN.

In February, 2016, the Company completed a non-brokered private placement offering of 2,852,000 common shares at \$0.05 for gross proceeds of \$103,000 (\$CAD 143). 1,426,000 warrants were issued with the units and each warrant is exercisable for one common share at \$CAD 0.10 per share for a period of eighteen months from the date of issuance. The common shares and warrants are subject to a four (4) month and one (1) day hold period from the date of issuance.

In March 2016 the Company completed a non-brokered private placement offering of 5,655,000 common shares at \$0.05 for gross proceeds of \$206,000 (\$CAD 283,000). 2,827,500 warrants were issued with the unit and each warrant is exercisable for one common share at \$CAD 0.10 per share for a period of eighteen months from the date of issuance. The common shares and warrants are subject to a four (4) month and (1) day hold period from the date of issuance.

In February 2017 the Company issued 3,000,000 common shares at \$0.05 in repayment of a Secured Promissory Note of \$113,000 (\$CAD 150). 3,000,000 warrants were issued with the units and each warrant is exercisable for one common share at \$CAD 0.05 for twelve (12) months from the date of issuance, and at \$CAD 0.10 for the thirteenth (13th) month to the twenty-fourth (24th) month from the date of issuance.

On March 10, 2017 the Company completed a non-brokered private placement offering of 26,000,000 common shares at \$0.05 for gross proceeds of \$982,000 (\$CAD 1,300,000). 26,000,000 warrants were issued with the unit and each warrant is exercisable for one common share at \$CAD 0.10 per share for a period of twenty-four (24) months from the date of issuance. The common shares and warrants are subject to a four (4) month and (1) day hold period from the date of issuance.

Discussion of Operations and Financial Condition

Understanding our Business

LeoNovus has developed a software-defined storage and Intelligent Network that enables efficient, secure, and high-speed on-premise, hybrid or public cloud computing by leveraging advanced storage mediums to bare metal while identifying and leveraging idle storage in existing hardware systems.

With its innovative and proprietary virtualized network infrastructure, or cloud, the Company has created a geo-distributed data centre capability that scales to a potentially unlimited number of remotely located, physical data sites comprised of compute and storage end-points. This allows our customers the ability to offer cloud services by utilizing existing computing resources that have excess capacity.

Additionally, the Company can operate this secure network with its remotely managed intelligent cloud architecture with support for deploying a high performance, SMART PLATFORM providing connected devices with access to features, content, and functionality over the web. This delivers a flexible real-time, value-added service model to multiple markets including residential, hospitality, commercial businesses and health care. It enables ongoing just-in-time services and includes support, updates, metrics and transaction capabilities while providing a secure network.

LeoNovus is able to offer geo-distributed cloud services as well as enabling a secure app platform that adds new and recurring revenue streams for data centers and colocation providers while avoiding substantial operating costs that single-site data centers incur.

This geo-distributed data centre and network operates securely through LeoNovus' focus on protecting the data and services - not the hardware. LeoNovus takes an encrypted data file, segments it, and re-encrypts the pieces and replicates them across multiple endpoints. This approach provides built in redundancy, delivering higher disaster recovery than a conventional data center leading to better business continuity. If there is a loss of a STB, server or PC or if a device is hacked, the exposure is a useless segment of an encrypted data record. The LeoNovus cloud architecture provides redundancy and geo-distribution, which allows for a business to continue operating without loss or exposure of their data. If a conventional data center is hit by a hurricane or other catastrophe, the data may be lost. While an enterprise may back up its data in multiple data centers, this comes with additional cost and does not solve the risk of their data being hacked or corrupted by a computer virus based on the data being in a single location. In addition, LeoNovus sets a high fault tolerance, which means that the company can lose up to 70% of its endpoints and not lose its client's data.

Management believes that the Company is positioned extremely well in high growth markets to offer a petabyte class, low cost software designed storage product for data to meet the high growth needs coming from the massive growth in data storage driven primarily by the growth in video and analytics.

Industry Outlook

The growth in object based storage and software designed storage systems over the last several years has been phenomenal. Cleversafe, a software defined storage company recently purchased by IBM forecasts that the 100 petabyte customer market has a compounded growth rate of 60% and estimate that there are over 300 of these customers globally in 2016. Potential revenues from each of these customers are in the seven-figure range.

Growth in stored data, however, has presented opportunities for specific cloud offerings based on the continuing high growth of connected devices. In terms of deployment architectures, cloud services are currently undergoing a major paradigm shift including such things as the Internet of Everything (IoE) from centralized cloud computing toward distributed edge computing. This shift is opening up edge-based data to meaningful analysis, by distributing the analytic workloads across the network. It is also shoring up the cloud-level capabilities by making the transmitted data more actionable, and by enriching and contextualizing the payloads. LeoNovus will announce a product later in the year to address this market.

LeoNovus is well positioned with its technology to capitalize on the growth trends in cloud computing by having "best in class" security with its intelligent network including a low cost edge-computing network for high performance and lower latency over a multiplicity of connected devices.

Enterprise On-Premise Private Clouds + Hybrid + Public

Despite a significant shift to cloud applications, most companies (especially in Europe) remain conservative about which applications they put in public clouds. According to a Tata Consultancy Services Survey, less than 20% of U.S. and European companies would consider or seriously consider putting their most critical applications in public clouds. But 66% of U.S. and 48% of European companies would consider putting core applications in private clouds. Typically, these companies have large amounts of unused, and underutilized storage and computing resources within their own firewalls. To illustrate this point, an example might be defined as follows: Using a 100,000 employee enterprise, assume 25% of them have a PC at

work, and that the average PC has between 1-2 TB of storage on board and at least 4 CPU processor cores. Most employees don't end up using anywhere near that amount of storage nor does any one application typically use more than one CPU core when running. LeoNovus' technology can effectively use the "idle" resources in these computers to store encrypted data and run compute-intensive jobs, while remaining behind the company firewall including using the intelligent network to set policies which give the employee priority in usage. This drives extremely efficient use of internal resources while lowering the carbon footprint.

Strategy and Outlook

In 2016 the Company refined its strategy and focused on implementing a software defined object based storage solution. Leonovus is a software company that offers the leading software-defined object storage solution (SDOSS) and governance, risk management and compliance (GRC) solution for the modern enterprise. Designed with the IT manager in mind, Leonovus' patented algorithms virtualize, transform, slice and disperse data across a network of on-premises, hybrid or multi-cloud storage nodes – allowing for the most secure yet internally accessible form of object-based data storage that provides GRC across the entire solution. The advanced geo-distributed architecture minimizes latency, optimizes geo-availability, reduces remote backup costs and meets data sovereignty requirements. With its software and hardware agnostic design, Leonovus provides Petabyte scalability and allows the enterprise to utilize its existing idle storage resources, extend the useable lifespan of depreciated resources and improve the enterprise's overall ROI.

The company expects revenues to start in Q3 2017 and as of this date has several proof-of-concept installations. Supporting the revenue ramp is a strong prospect list of customers that need the unique security and compliance features provided by the Leonovus software defined object-based storage solution. We anticipate this list growing significantly as early adopter customers begin using our technology and become reference accounts for the company.

The company further expects to raise funds in Q3 and Q4 2017 for operating capital to support the company as it enters a revenue growth phase.

Selected Financial Information

The Company was incorporated on December 30, 2008 and has a December 31st year-end. The following selected financial data is derived from the unaudited interim condensed consolidated financial statements of the Company prepared in accordance with IFRS. To June 30, 2017, the functional currency of the Company is the US dollar.

	Three Months Period Ended		Six Month Period Ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Total Revenue	\$ -	\$ -	\$ -	\$ -
General & Administrative Expense	\$ 234,000	\$ 109,000	\$ 373,000	\$ 387,000
Research & Development Expense	\$ 33,000	\$ 48,000	\$ 216,000	\$ 321,000

	Three Months Period Ended		Six Month Period Ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Sales & Marketing Expense	\$ 58,000	\$ -	\$ 126,000	\$ 3,000
Total Operating Expenses	<u>\$ 325,000</u>	<u>\$ 257,000</u>	<u>\$ 715,000</u>	<u>\$ 711,000</u>
Loss from Operations	<u>\$ (325,000)</u>	<u>\$ (257,000)</u>	<u>\$ (715,000)</u>	<u>\$ (711,000)</u>
Foreign Exchange Gain (Loss)	\$ (20,000)	\$ (7,000)	\$ (36,000)	\$ (60,000)
Finance and Interest Income (Expense)	\$ (6,000)	\$ (17,000)	\$ (26,000)	\$ (28,000)
Change in fair value of outstanding warrants	-	\$ 5,000		\$ 5,000
Net Income (Loss)	<u>\$ (351,000)</u>	<u>\$ (276,000)</u>	<u>\$ (777,000)</u>	<u>\$ (794,000)</u>
Income (loss) per common share				
Weighted average number of outstanding shares	159,440,770	130,061,914	159,440,770	130,061,914

	June 30, 2017	June 30, 2016
Cash	\$ 184,000	\$ 51,000
Total Current Assets	\$ 289,000	\$ 452,000
Total Assets	\$ 302,000	\$ 681,000
Total Current Liabilities	\$ 3,186,000	\$ 3,546,000
Total All Liabilities	\$ 3,395,000	\$ 3,931,000
Total Shareholders' Deficiency	\$ (3,092,000)	\$ (3,250,000)
Total Liabilities and Shareholders' Deficiency	\$ 303,000	\$ 681,000
Total Working Capital	\$ (2,896,000)	\$ (3,094,000)
Warrant Liability *	\$ 18,000	\$ 195,000
Working Capital Adjusted for Warrant Liability	\$ (2,878,000)	\$ (2,899,000)

* Note that warrant liability does not use cash to extinguish the liability.

NON-GAAP FINANCIAL MEASURES

Management reports and analyzes its financial results and performance using a range of financial measures. Some of these measures, such as revenues, net income and cash flow from operating activities are defined by IFRS. Other measures are not defined by IFRS.

One key non-IFRS measure used by management is “Adjusted EBITDA”. The Company discloses Adjusted EBITDA as a supplemental non-GAAP (Generally Accepted Accounting Principles) financial performance measure because the Company believes it is a useful metric by which to compare the performance of our business from period to period. The Company understands that analysts, rating agencies and investors in assessing our performance, broadly use measures similar to Adjusted EBITDA. Accordingly, we believe that the presentation of Adjusted EBITDA provides useful information to investors.

Adjusted EBITDA comprises net income (loss) excluding the following: interest/finance income and expense, research and development (“SRED”) tax credit recovery, depreciation, amortization, foreign exchange gains and losses in earnings, stock-based compensation expense, change in fair value of outstanding warrants. Therefore, it may not be comparable to similar measurements presented by other companies. The reconciliation of Adjusted EBITDA with the IFRS measure of net loss for three month periods is as follows:

<i>Dollars stated in 000's</i>	Mar 31 <u>2015</u>	Jun 30 <u>2015</u>	30-Sep <u>2015</u>	31-Dec <u>2015</u>	31-Mar <u>2016</u>	30-Jun <u>2016</u>	30-Sep <u>2016</u>	31-Dec <u>2016</u>	Mar 31 <u>2017</u>	30-Jun <u>2017</u>
Net Income (loss) for the period	53	(677)	(708)	(546)	(519)	(276)	(22)	(419)	(426)	(351)
Add (deduct):										
Interest expense (income)	(17)	(9)	(7)	12	12	17	3	(5)	19	6
Depreciation and amortization	7	6	6	6	5	1	5	1	1	2
Foreign exchange (gain) loss	(70)	4	(31)	(37)	53	7	(17)	(16)	16	36
Stock-based compensation expense (recovery)	63	51	45	(45)	1	14	7	110	75	8
Expense (recovery) on valuation of stock warrants	(748)	(18)	(16)	(13)	-	(5)	(2)	(61)	-	-
Adjusted EBITDA	(712)	(643)	(711)	(623)	(448)	(242)	(26)	(390)	(315)	(299)

Results of Operations

The Company incurred a net loss of \$351,000 and \$777,000 for the three and six month period ended June 30, 2017 compared to a net loss of \$276,000 and \$794,000 for the three and six months ended June 30, 2016. The six months ended June 30, 2016 loss included a \$18,000 favorable adjustment to the fair value of outstanding warrants in 2016, compared to nil in the six months ended June 30, 2017. The favorable adjustment in the six months ended June 30, 2016 is due to a decline in the number of warrants outstanding at period end. Expenses increased from \$257,000 to \$325,000 for the three-month periods ending June 30, 2017 and 2016, and from \$711,000 to \$777,000 for the 6 month periods, due to a reduction of general and administrative expenses, which reduction offset increased research and development and sales and marketing expenses.

Revenue

(\$NIL for the three months ended June 30, 2017)

(\$NIL for the three months ended March 31, 2017)

(\$NIL for the three months ended March 31, 2016)

The Company has not yet commenced its revenue stream from the new technology. Revenues are expected to begin during the third quarter of 2017.

General and Administrative Expenses

(\$234,000 for the three months ended June 30, 2017)

(\$109,000 for the three months ended June 30, 2016)

General and administrative expenses consist primarily of remuneration paid to the Chief Executive Officer, the Chief Financial Officer and our finance and corporate administrative staff. Other significant items include legal and accounting professional fees, rent, travel and insurance. General and administrative expenses decreased by \$125,000 for the three months ended June 30, 2017.

Product Development Expenses

(\$33,000 for the three months ended June 30, 2017)

(\$148,000 for the three months ended June 30, 2016)

Research and development expenses consist primarily of remuneration paid to engineering personnel both in the U.S. and Canada and independent contractors. Other significant items include license fee expenses, travel, rent and other occupancy costs for our Canadian engineering personnel. For the three months ended June 30, 2017, research and development expense decreased by \$115,000 as a result of new contractors, license fees and share based compensation. Despite the working capital challenges, the company continues to invest in Product Development.

Sales and Marketing Expenses

(\$58,000 for the three months ended June 30, 2017)

(\$Nil for the three months ended June 30, 2016)

Sales and marketing expenses consist primarily of compensation; travel costs, public relations and trade show costs. For the three months ended June 30, 2017, sales and marketing expenses increased by \$58,000, as are a result of an increase in our marketing efforts.

Liquidity and Capital Resources

As at June 30, 2017, the Company had \$184,000 of cash and a working capital deficiency of \$2,878,000. Cash increased by \$133,000 in Q2 2017 compared to the June 30, 2016 balance of \$51,000 and the working capital deficiency decreased by \$21,000 down to \$2,878,000 in Q2 2017 compared to the Q2 2016 balance of \$2,899,000. The improved working capital deficiency at June 30, 2017 is due to a number of factors. Prepayment of licences and loans, along with a reduction of accounts payables, accruals, debentures payable and proceeds from the issuance of share capital all supported the improvement in working capital. The Company will need to continue to rely on fundraising activities until it can generate a positive cash flow from operations.

Operations

Cash used in operating activities for three months ended June 30, 2017 of \$280,000 compares to \$103,000 for the same period in 2016. The increase in the use of cash in operations is due to increased research and development and sales and marketing expenses in the year.

Financing Activities

Cash flow from financing activities for three months ended June 30, 2017 of \$Nil compares to \$116,000 for the same period in 2016. The 2016 cash flows arose from issuance of share capital and repayment of promissory notes, and there was no financing activity in 2017.

Investing Activities

Purchases of property and equipment for the three and six months ended June 30, 2017, totaled \$Nil and \$Nil, respectively, compared to \$Nil and \$Nil for the same periods in 2016

Accounting Policies

Statement of compliance

The consolidated financial statements have been prepared in accordance IFRS using the accounting policies disclosed below.

The consolidated financial statements were approved and authorized for issue by the Board of Directors on August 30, 2017

Critical accounting estimates and judgments

The Company's consolidated financial statements are prepared in accordance with IFRS recognition and measurement principles that often require Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts presented and disclosed in the consolidated financial statements. Management reviews these estimates and assumptions on an ongoing basis based on historical experience, changes in business conditions and other relevant factors as it believes to be reasonable under the circumstances. Changes in facts and circumstances may result in revised estimates, and actual results could differ from those estimates. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Significant management judgment

The following are significant management judgments in applying the accounting policies of the Company that have the most significant effect on the consolidated financial statements.

Recognition of deferred income tax assets

Management continually evaluates the likelihood that its deferred tax assets could be realized. This requires management to assess whether it is probable that sufficient taxable income will exist in the future to utilize these losses within the carry-forward period. By its nature, this assessment requires significant judgment. To date, management has not recognized any

deferred tax assets in excess of existing taxable temporary differences expected to reverse within the carry-forward period.

Functional currency

The functional currency for each entity in the consolidated group is the currency of the primary economic environment in which it operates. Determination of functional currency involves significant judgment. Management considers various factors, including but not limited to whether the activities of the entity are carried out as an extension of the Company and/or whether cash flows from the activities of the entity are sufficient to service existing and normally expected obligations without funds being made available by the Company. The Company reconsiders the functional currency of its entities if there is a change in the underlying transactions, events and conditions which determine their primary economic environment.

Investment tax credits

Investment tax credits are subject to audit by the Canada Revenue Agency and the Company's entitlement to these items is based on management's history of success in past claims and its current understanding of the legislation that governs these matters.

Contingencies

Management uses judgment to assess the existence of contingencies. By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. Management also uses judgment to assess the likelihood of the occurrence of one or more future events.

Going concern risk assessment

The assessment of the Company's ability to continue as a going concern and raising additional debt or equity financing or attaining commercial operations and generating sufficient revenues to achieve and sustain profitability for the ensuing year, and to fund planned research and development activities, involves significant judgment based on historical experience and other factors including expectation of future events that are believed to be reasonable under the circumstances. See Note 1 for more information.

Estimation uncertainty

Information about estimates and assumptions that have the most significant effect on recognition and measurement of assets, liabilities, income and expenses is provided below. Actual results may be substantially different.

Share based payments and warrants

The estimation of share based compensation and warrants requires the selection of an appropriate valuation model and consideration as to the inputs necessary for the valuation model chosen. The Company has made estimates as to the volatility of its own shares, the probable life of share options and warrants granted, the time of exercise of those share options and warrants, as well as forfeiture rates. The valuation model used by the Company is the Black-Scholes model.

Valuation adjustments for inventory

The Company records valuation adjustments for inventory by comparing the inventory cost to its net realizable value. This process requires the use of estimates and assumptions related to future market demand, costs and prices. These adjustments are reviewed on an ongoing basis and may have a significant impact on any valuation adjustment for inventory.

Review of carrying value of assets and impairment charges

In the determination of carrying values and impairment charges, management of the Company reviews the recoverable amount (the higher of the fair value less costs to sell or the value in use) in the case of non-financial assets. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period. Changes in these assumptions may alter the results of non-financial asset, impairment charges recognized in loss and the resulting carrying amounts of assets. (Note 4)

Contingencies

When contingencies exist, Management estimates the related financial impact to the Company based on the possible outcomes of one or more future events.

Contractual Obligations and Off-Balance Sheet Arrangements

The Company is not yet party to any industry contracts or arrangements. There are no off balance sheet arrangements.

Transactions with Related Parties

In October 2013, two Directors and a shareholder of the Company were provided loans totalling \$349,000 to finance the exercise of 1,696,600 warrants to purchase common shares of the Company ("Share Purchase Loans"). The Share Purchase Loans matured in October 2016. One of the three loans was repaid to the Company in October 2016. At December 31, 2016 the Company determined that the remaining Share Purchase Loans were impaired. The remaining 1,317,744 common shares acquired under the loans are pledged as security against the Share Purchase Loans and are held as security by the Company. The former Chairman and CEO, Gordon Campbell is the Director that has defaulted on the loan held by him personally and by a company controlled by Mr. Campbell. The Company is reviewing it's legal options to recover the approximately \$275,000 owed by Campbell and his company. As a result the loans have been written down to \$39,000, which was the fair value of the commons shares as at December 31, 2016. The impairment has resulted in a write-down of the loan of \$232,000.

Outstanding Share Data

As at June 30, 2017 (note all dollar amounts in this section are in CDN Dollars):

There were 159,440,770 common shares of the Company outstanding, excluding 1,317,744 shares that were issued with Share Purchase Loans in 2013 to shareholders of the Company. These shares are pledged as security against these loans and are not considered outstanding.

There were a total of 14,936,000 options outstanding on the following terms: 12,016,000 at \$0.05 per option exercisable through 2020; 600,000 at \$0.06 per option exercisable through 2022; 1,215,000 at \$0.10 per option exercisable through 2020; 455,000 at \$0.19 per option exercisable through 2018; 90,000 at \$0.23 per option exercisable through 2019; 250,000 at \$0.24 per option exercisable through 2018; 260,000 at \$0.35 per option exercisable through 2019; 50,000 at \$0.39 per option exercisable through 2019.

There were 185,380 broker warrants outstanding at \$0.10 per warrant exercisable through August 2019. There were 367,575 broker unit warrants at \$0.10 exercisable through September 2017.

There were 1,560,000 finder warrants outstanding at \$0.10 exercisable through March 2019.

There were 3,000,000 debenture warrants outstanding at \$0.05 exercisable through January 2018, and at \$0.10 through January 2019. There were 3,000,000 debenture warrants outstanding at \$0.10 exercisable through September 2018, and there were \$2,000,000 debenture warrants outstanding at \$0.05 exercisable through December 2017.

There were 28,827,500 private placement warrants outstanding on the following terms: 2,827,500 at \$0.10 per warrant exercisable through September 2017 and 26,000,000 at \$0.10 exercisable through March 2019.

Assuming all of these options and warrants were exercised, 213,317,225 common shares would be issued and outstanding on a fully diluted basis.

Risks and Uncertainties

The preparation of financial statements in accordance with IFRS contemplate the continuation of the Company as a going concern. During the year ended December 31, 2016, the Company had a net loss of \$1,236,000, a deficit of \$22,923,000 and negative working capital of \$3,024,000. In the absence of raising additional debt not yet achieved commercial operations and had a net loss or equity financing or attaining commercial operations and generating sufficient revenues to achieve and sustain profitability, there is significant doubt regarding the Company's ability to continue as a going concern. The Company believes that financing initiatives will provide sufficient cash flow for it to continue as a going concern in its present form; however, there can be no assurance that the Company will achieve such results. The financial statements do not include any adjustments related to the recoverability and classification of recorded asset amounts, or the amounts and classification of liabilities that might be necessary should the Company be unable to continue its operations. The Company's ability to realize its assets and discharge its liabilities is dependent on its ability to obtain additional financing.

Quarterly Information

	Three months ended				
	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016
Service Revenue	\$ -	\$ -	\$ -	\$ -	\$ -
General & Administrative Expense	\$ 234,000	\$ 138,000	\$ 233,000	\$ 120,000	\$ 109,000
Research & Development Expense	\$ 33,000	\$ 184,000	\$ 156,000	\$ (85,000)	\$ 148,000
Sales & Marketing Expense	\$ 58,000	\$ 69,000	\$ 90,000	\$ 3,000	\$ -
Total Operating Expenses	\$ 325,000	\$ 391,000	\$ 479,000	\$ 38,000	\$ 257,000
Loss from Operations	\$ (325,000)	\$ (391,000)	\$ (479,000)	\$ (38,000)	\$ (257,000)
Foreign Exchange Gain (Loss)	\$ (20,000)	\$ (16,000)	\$ 16,000	\$ 17,000	\$ (7,000)
Finance and Interest Income (Expense)	\$ (6,000)	\$ (19,000)	\$ (17,000)	\$ (3,000)	\$ (17,000)
Change in fair value of outstanding warrants	\$ -	\$ -	\$ 61,000	\$ 2,000	\$ 5,000
Net Income (Loss)	\$ (351,000)	\$ (426,000)	\$ (419,000)	\$ (22,000)	\$ (276,000)
Weighted average outstanding shares	159,440,770	159,440,770	130,440,770	130,061,914	130,061,914
Income (loss) per share	\$ -	\$ -	\$ -	\$ -	\$ -
	Three months ended				
	June 30, 2016	March 31, 2016	December 31, 2015	September 30, 2015	June 30, 2015
Service Revenue	\$ -	\$ -	\$ -	\$ 6,000	\$ 47,000
General & Administrative Expense	\$ 109,000	\$ 278,000	\$ 398,000	\$ 388,000	\$ 358,000
Research & Development Expense	\$ 148,000	\$ 173,000	\$ 213,000	\$ 304,000	\$ 245,000
Sales & Marketing Expense	\$ -	\$ 3,000	\$ (27,000)	\$ 76,000	\$ 144,000
Total Operating Expenses	\$ 257,000	\$ 454,000	\$ 584,000	\$ 768,000	\$ 747,000
Loss from Operations	\$ (257,000)	\$ (454,000)	\$ (584,000)	\$ (762,000)	\$ (700,000)
Foreign Exchange Gain (Loss)	\$ (7,000)	\$ (53,000)	\$ 37,000	\$ 31,000	\$ (4,000)
Finance and Interest Expense	\$ (17,000)	\$ (12,000)	\$ (12,000)	\$ 7,000	\$ 9,000
Change in fair value of outstanding warrants	\$ 5,000	\$ -	\$ 13,000	\$ 16,000	\$ 18,000
Net Loss	\$ (276,000)	\$ (519,000)	\$ (546,000)	\$ (708,000)	\$ (677,000)
Weighted average outstanding shares	130,061,914	130,061,914	121,554,914	121,554,914	121,554,914
Loss per share	\$ -	\$ -	\$ -	\$ (0.01)	\$ (0.01)

