

# LXR<sup>AND</sup> CO

LXRandCo, Inc.

December 31, 2017 and 2016

## Independent auditors' report

To the Shareholders of  
**LXRandCo, Inc.**

We have audited the accompanying consolidated financial statements of **LXRandCo, Inc.**, which comprise the consolidated statements of financial position as at December 31, 2017 and 2016, and the consolidated statements of loss and comprehensive loss, changes in shareholders' equity (deficiency) and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

### **Management's responsibility for the consolidated financial statements**

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

### **Auditors' responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of **LXRandCo, Inc.** as at December 31, 2017 and 2016, and its financial performance and its cash flows for the years then ended, in accordance with International Financial Reporting Standards.

*Ernst & Young LLP<sup>1</sup>*

Montréal, Canada  
March 20, 2018

<sup>1</sup> CPA auditor, CA, public accountancy permit no. A129439



LXRandCo, Inc.

Consolidated statements of financial position  
(in Canadian dollars)

As at

	December 31, 2017	December 31, 2016
	\$	\$
<b>Assets (notes 9 and 11)</b>		
<b>Current</b>		
Cash	4,015,025	938,966
Accounts receivable (notes 5 and 19)	4,968,344	2,131,033
Sales tax receivable	280,439	331,180
Income tax receivable	—	31,924
Inventory	15,871,901	6,871,597
Prepaid expenses and deposits	367,079	340,520
<b>Total current assets</b>	<b>25,502,788</b>	<b>10,645,220</b>
Property and equipment, net (note 6)	3,044,726	1,000,913
Intangible assets, net (note 7)	661,808	256,917
Other assets	112,682	112,682
Goodwill (note 8)	5,023,074	—
	<b>34,345,078</b>	<b>12,015,732</b>
<b>Liabilities and shareholders' equity (deficiency)</b>		
<b>Current</b>		
Credit facility and line of credit (note 9)	—	3,399,362
Accounts payable and accrued liabilities (note 10)	5,829,675	4,017,524
Income tax payable	497,811	—
Deferred revenue	149,284	—
Current portion of long-term debt (note 11)	188,810	2,841,026
Preferred shares	—	300,000
<b>Total current liabilities</b>	<b>6,665,580</b>	<b>10,557,912</b>
Long-term debt (note 11)	22,929	187,727
Credit facility and line of credit (note 9)	8,189,476	—
Convertible redeemable preferred shares (note 12)	—	30,226,003
Other liabilities (note 13)	159,097	—
Deferred income taxes (note 14)	216,851	178,243
<b>Total liabilities</b>	<b>15,253,933</b>	<b>41,149,885</b>
<b>Shareholders' equity (deficiency)</b>		
Share capital (note 13)	64,897,185	100
Deficit	(46,913,803)	(28,961,429)
Additional paid-in capital	1,621,168	—
Accumulated other comprehensive loss	(513,405)	(172,824)
<b>Total shareholders' equity (deficiency)</b>	<b>19,091,145</b>	<b>(29,134,153)</b>
	<b>34,345,078</b>	<b>12,015,732</b>

Commitments and contingencies (note 23)

Subsequent events (note 25)

See accompanying notes

On behalf of the Board:

Director

Director

LXRandCo, Inc.

Consolidated statements of loss and comprehensive loss  
(in Canadian dollars)

Years ended December 31

	2017	2016
	\$	\$
<b>Net revenue</b> <i>(note 16)</i>	<b>37,069,137</b>	21,890,810
Cost of sales	<b>26,741,928</b>	14,965,438
<b>Gross profit</b>	<b>10,327,209</b>	6,925,372
Selling, general and administrative expenses <i>(note 15)</i>	<b>16,162,129</b>	6,127,350
Amortization and depreciation expenses	<b>474,777</b>	224,329
<b>Results from operating activities</b>	<b>(6,309,697)</b>	573,693
Finance costs <i>(note 22)</i>	<b>1,010,496</b>	1,473,986
Debt extinguishment costs <i>(notes 9 and 11)</i>	<b>612,939</b>	—
Foreign exchange gain	<b>(104,652)</b>	(193,639)
Share of loss in an associate <i>(note 8)</i>	—	499,007
Non-recurring gain on acquisition of an associate <i>(note 8)</i>	<b>(2,070,422)</b>	—
Non-recurring gain on loss of control of a subsidiary	—	(363,948)
Excess of fair value over net assets acquired <i>(note 1)</i>	<b>14,363,558</b>	—
Non-recurring acquisition costs <i>(note 1)</i>	<b>819,141</b>	—
Gain on expiration of warrants <i>(note 12)</i>	<b>(3,195,459)</b>	—
Change in fair value of convertible redeemable preferred shares <i>(note 12)</i>	—	17,277,928
Convertible redeemable preferred shares dividends <i>(note 12)</i>	<b>61,308</b>	661,442
Change in fair value of warrants <i>(note 12)</i>	—	9,582,300
<b>Loss before income taxes</b>	<b>(17,806,606)</b>	(28,363,383)
Income tax expense (recovery) <i>(note 14)</i>		
Current	<b>106,240</b>	(210,119)
Deferred	<b>39,528</b>	163,754
	<b>145,768</b>	(46,365)
<b>Net loss</b>	<b>(17,952,374)</b>	(28,317,018)
<b>Other comprehensive income (loss)</b>		
Cumulative translation adjustment	<b>(340,581)</b>	11,540
<b>Comprehensive loss</b>	<b>(18,292,955)</b>	(28,305,478)
<b>Loss per share</b> <i>(note 17)</i>		
Basic and fully diluted	<b>(1.97)</b>	(6.17)
Weighted average number of shares outstanding – basic and fully diluted	<b>9,293,676</b>	4,584,080

See accompanying notes

LXRandCo, Inc.

Consolidated statements of changes in shareholders' equity (deficiency)  
(in Canadian dollars)

Years ended December 31

	Share capital \$	Deficit \$	Additional paid-in capital \$	Cumulative translation adjustment \$	Total shareholders' equity (deficiency) \$
<b>Balance as at December 31, 2016</b>	100	(28,961,429)	—	(172,824)	(29,134,153)
Net loss for the year 2017	—	(17,952,374)	—	—	(17,952,374)
Cumulative translation adjustment	—	—	—	(340,581)	(340,581)
Stock-based compensation expense ( <i>note 13</i> )	—	—	1,621,168	—	1,621,168
Conversion of convertible redeemable preferred shares ( <i>note 12</i> )	31,477,370	—	—	—	31,477,370
Class B common shares issued in Qualifying acquisition ( <i>notes 1 and 13</i> )	33,419,715	—	—	—	33,419,715
<b>Balance as at December 31, 2017</b>	<b>64,897,185</b>	<b>(46,913,803)</b>	<b>1,621,168</b>	<b>(513,405)</b>	<b>19,091,145</b>

See accompanying notes

LXRandCo, Inc.

Consolidated statements of cash flows  
(in Canadian dollars)

Years ended December 31

	2017	2016
	\$	\$
<b>Operating activities</b>		
Net loss for the year	(17,952,374)	(28,317,018)
Non-cash items:		
Depreciation of property and equipment	278,261	114,113
Amortization of intangible assets	196,516	110,216
Amortization of deferred financing costs	671,597	372,429
Stock-based compensation expense	1,780,265	—
Deferred income taxes	39,528	163,754
Unrealized foreign exchange loss (gain) on non-monetary assets	88,540	(86,520)
Non-recurring gain on acquisition of an associate	(2,070,422)	—
Gain on expiration of warrants	(3,195,459)	—
Change in fair value of convertible redeemable preferred shares	—	17,277,928
Convertible redeemable preferred shares dividends	61,308	661,442
Change in fair value of warrants	—	9,582,300
Interest accretion expense on subordinated debt	18,279	473,072
Excess of fair value over net assets acquired	14,363,558	—
Non-recurring gain on loss of control of a subsidiary	—	(363,948)
Share of loss in an associate	—	499,007
	<u>(5,720,403)</u>	486,775
Net change in non-cash working capital balances related to operations	<u>(10,014,343)</u>	<u>(4,137,111)</u>
<b>Cash flows used in operating activities</b>	<u>(15,734,746)</u>	<u>(3,650,336)</u>
<b>Investing activities</b>		
Acquisitions of property and equipment	(2,428,961)	(637,175)
Acquisitions of intangible assets	(515,070)	(170,064)
Cash acquired from a step business combination	803,661	—
Cash acquired from acquisition	19,004,989	—
<b>Cash flows provided by (used in) investing activities</b>	<u>16,864,619</u>	<u>(807,239)</u>
<b>Financing activities</b>		
Net increase (decrease) in credit facility	(3,873,743)	2,390,620
Net increase in line of credit	8,602,491	—
Proceeds from issuance of long-term debt	—	272,574
Repayment of long-term debt	(2,817,014)	(369,499)
Payment of financing costs	(610,231)	(541,715)
Proceeds from issuance of convertible redeemable preferred shares	1,000,000	2,704,332
Preferred shares redemption	(300,000)	—
<b>Cash flows provided by financing activities</b>	<u>2,001,503</u>	<u>4,456,312</u>
<b>Effect of exchange rate changes on cash</b>	<u>(55,317)</u>	<u>30,371</u>
<b>Net increase in cash during the year</b>	<u>3,076,059</u>	<u>29,108</u>
Cash, beginning of year	<u>938,966</u>	<u>909,858</u>
<b>Cash, end of year</b>	<u>4,015,025</u>	<u>938,966</u>
<b>Supplementary information (as reported in operating activities)</b>		
Income taxes received	—	(172,022)
Interest paid	<u>839,866</u>	<u>458,721</u>

See accompanying notes

LXRandCo, Inc.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

### 1. Corporate information

LXRandCo, Inc. (“LXRandCo” or the “Company”) is an international omni-channel retailer of branded vintage luxury handbags and accessories. LXRandCo sources and authenticates high quality pre-owned products and sells them through: a retail network of stores located in major department stores in Canada, the United States and Europe; wholesale operations primarily in the United States; and e-Commerce operations including its own website and through the websites of several of its retail partners. LXRandCo is incorporated and domiciled in Canada. The Company’s legal registered address is at 130 Adelaide Street West, Toronto, Ontario, M5H 3P5 and its operating head office is located at 40 Jean-Talon Street West, Montréal, Québec, Canada, H2R 2W5. The Company also maintains an office in Tokyo, Japan.

As at December 31, 2017, LXRandCo’s retail network consisted of 133 stores located as follows: 96 in the United States, 14 in Germany, 4 in Belgium, 5 in the Netherlands, 5 in the United Kingdom and 9 in Canada.

Retail sales are traditionally higher in the fourth quarter due to the holiday season.

On April 17, 2017, Gibraltar Growth Corporation (“Gibraltar Growth”) filed a non-offering long form preliminary prospectus in respect of the acquisition of LXR Produits de Luxe International Inc. (the “LXR Acquisition”), and on May 12, 2017, Gibraltar Growth obtained its receipt from securities regulators for the public filing of its non-offering long form final prospectus in respect of the LXR Acquisition.

On June 9, 2017, Gibraltar Growth, the predecessor of the Company, completed the acquisition of LXR Produits de Luxe International Inc. (“LXR International”) and closed a private placement (the “Private Placement”) of Class B shares (“Class B Share”) for gross proceeds of \$25 million. Gibraltar Growth, a special purpose acquisition corporation (“SPAC”) whose Class A restricted voting shares (each, a “Class A Restricted Voting Share”) and warrants (each, a “Warrant”) were listed on the Toronto Stock Exchange (the “TSX”), was incorporated under the *Business Corporations Act* (Ontario) for the purpose of effecting an acquisition of one or more businesses or assets, by way of merger, amalgamation, share exchange, asset acquisition, share purchase, reorganization, or other similar business combination involving Gibraltar Growth, referred to as its “qualifying acquisition”. The LXR Acquisition constituted Gibraltar Growth’s qualifying acquisition (the “Qualifying Acquisition”). In connection with the closing of the Qualifying Acquisition, Gibraltar Growth was renamed to LXRandCo, Inc.

## LXRandCo, Inc.

### Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

While Gibraltar Growth was the legal acquirer of LXR International, LXR International was identified as the acquirer for accounting purposes. The LXR Acquisition is outside the scope of IFRS 3, “*Business Combinations*” (“IFRS 3”), and it is accounted for as an equity-settled, share-based payment transaction in accordance with IFRS 2, “*Share-based Payments*” (“IFRS 2”). LXRandCo is considered to be a continuation of LXR International with the net identifiable assets of Gibraltar Growth deemed to have been acquired by LXR International in exchange for shares of LXR International. Under IFRS 2, the transaction is measured at the fair value of the shares deemed to have been issued by LXR International in order for the ownership interest in the combined entity to be the same as if the transaction had taken the legal form of LXR International acquiring 100% of Gibraltar Growth. Any difference in the fair value of the shares deemed to have been issued by LXR International and the fair value of Gibraltar Growth’s identifiable net assets represents a service received by LXR International, recorded through profit and loss. LXR International’s historical financial statements as of and for the periods ended prior to the completion of the Qualifying Acquisition are presented as the historical financial statements of LXRandCo prior to the date of the completion of the Qualifying Acquisition.

Details of the LXR Acquisition are summarized as follows:

	\$
<b>Assets acquired</b>	
Cash	19,004,989
Accounts receivable and other receivable	460,486
	<u>19,465,475</u>
<b>Liabilities assumed</b>	
Accounts payable and income taxes payable	409,318
Net assets acquired	<u>19,056,157</u>
Fair value of shares deemed to have been issued by LXR International ( <i>note 13</i> )	<u>33,419,715</u>
<b>Excess of LXR fair value over net assets acquired</b>	<u>14,363,558</u>

During the year ended on December 31, 2017, the Company incurred legal and other costs of \$819,141 in connection with the LXR Acquisition that were recorded in net loss.

The consolidated financial statements of the Company for the year ended December 31, 2017 were approved by the Company’s Board of Directors on March 20, 2018.

## 2. Summary of significant accounting policies

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

## LXRandCo, Inc.

### Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

The consolidated financial statements have been prepared on a historical cost basis, except for convertible redeemable preferred shares.

#### Basis of consolidation

The consolidated financial statements include the accounts of the Company, and the following wholly owned subsidiaries:

Name	Ownership
LXR Produits de Luxe International Inc. <i>(note 1)</i>	100%
LXR Canada Inc.	100%
LXR Luxe, Inc.	100%
Groupe Global LXR Inc. and its wholly owned subsidiary LXR & Co Inc. <i>(note 8)</i>	100%
LXR&Co Germany GmbH	100%
LXR&Co UK Limited	100%
LXRandCo Netherlands B.V.	100%

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. All intercompany transactions, balances and unrealized gains or losses have been eliminated upon consolidation. The Company has no interests in special purpose entities.

Control is achieved when the Company is exposed, or has rights, to variable returns from its involvement with an investee and has the ability to affect those returns through its power over the investee. Specifically, the Company controls an investee if, and only if, the Company has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns.

The Company assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary.

Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Company gains control until the date the Company ceases to control the subsidiary.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

Profit or loss and each component of other comprehensive income (“OCI”) are attributed to the equity holders of the parent of the Company and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Company loses control over a subsidiary, it:

- Derecognizes the assets and liabilities of the subsidiary
- Derecognizes the cumulative translation differences, recorded in equity
- Recognizes the fair value of any consideration received
- Recognizes the fair value of any investment retained
- Recognizes any surplus or deficit through profit or loss
- Reclassifies the parent’s share of the components previously recognized in OCI through profit or loss or retained earnings (deficit), as appropriate, as would be required if the Company had directly disposed of the related assets or liabilities

### Functional and presentation currency

The consolidated financial statements are presented in Canadian dollars, which is also the functional currency of the parent Company and the primary economic environment in which the Company operates.

For each entity, the Company determines the functional currency and items included in the financial statements of each entity are measured using that functional currency. The Company uses the direct method of consolidation and on disposal of a foreign operation, the gain or loss that is reclassified to profit or loss reflects the amount that arises from using this method.

### Foreign currency translation

Revenue, expenses and non-monetary assets and liabilities denominated in foreign currencies are recorded at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated at exchange rates prevailing at the financial position date. Unrealized and realized translation gains and losses are reflected in net loss.

The assets and liabilities of the Company’s foreign wholly owned subsidiaries are translated into Canadian dollars at the exchange rates in effect at the financial position date. Revenue and expenses are translated at average exchange rates for the period. Differences arising from the exchange rate changes are included in OCI in the cumulative translation adjustment account.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which in substance is considered to form part of the net investment in the foreign operation, are recognized in OCI in the cumulative translation account and reclassified from equity to net loss on disposal of the net investment.

### Cash

Cash on the financial position date comprises cash at banks and on hand.

### Inventory valuation

Inventory is measured at the lower of cost and net realizable value. Cost is determined using the historical unit cost of goods purchased. Costs include the cost of purchase and transportation costs that are directly incurred to bring the inventory to its present location and duty. Net realizable value is the estimated selling price of inventory in the ordinary course of business, less any estimated selling costs.

### Property and equipment

Property and equipment are initially recorded at cost and are depreciated over their useful economic life. Cost includes expenditures that are directly attributable to the acquisition of the asset, including any costs directly related to bringing the asset to a working condition for its intended use. The residual values, useful lives and methods of depreciation of property and equipment are reviewed at each financial year-end and adjusted prospectively, if appropriate. All repair and maintenance costs are recognized in net loss as incurred.

Depreciation of an asset begins once it becomes available for use and is calculated using the straight-line method and the following durations:

Furniture and equipment	5 years
Computer equipment	3 years
Rolling stock	3 years

Leasehold improvements are depreciated on a straight-line basis over the lesser of the useful economic life and the initial term of the leases, plus one renewal option period, not to exceed three years.

Prior to January 1, 2017, the Company depreciated its furniture and equipment, computer equipment and rolling stock using the declining balance method at rates of 20%, 33% and 30%, respectively. The Company did not adjust retrospectively its December 31, 2016 property and equipment carrying amount as this change in depreciation did not result in a significant variance requiring restatement of prior period balances.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

Any gain or loss arising on the disposal or derecognition of an asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in net loss when the asset is derecognized.

### Intangible assets

Intangible assets consist of computer software and website costs. The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets are initially recorded at cost. Intangible assets with finite lives are amortized over their useful economic lives. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life are considered to modify the amortization period and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in net loss.

Amortization of an asset begins once it becomes available for use and is calculated using the straight-line method and the following durations:

Software	2 to 3 years
Website	3 years

Prior to January 1, 2017, the Company amortized its software and website using the declining balance method at the rate of 33%. The Company did not adjust retrospectively its December 31, 2016 intangible assets' carrying amount as this change in amortization did not result in a significant variance requiring restatement of prior period balances.

Any gain or loss arising on the disposal or derecognition of an intangible asset (calculated as the difference between the net disposal proceeds and the carrying amount of the intangible asset) is included in net loss when the intangible asset is derecognized.

Expenditures incurred in connection with the ongoing development of the Company's website are capitalized as intangible assets when they meet the following criteria: the technical feasibility of completing the intangible asset has been demonstrated, the Company has the intention to use the asset, adequate technical, financial and other resources are available to complete the development, the ability to measure reliably the expenditure attributable to the intangible asset during its development exists and commercialization of the asset that will generate future economic benefits for the Company. When the aforementioned criteria are not met, expenditures incurred in connection with the Company's website are expensed as incurred.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

### Leases

Leases are classified as either operating or finance, based on the substance of the transaction at inception of the lease. Classification is re-assessed if the terms of the lease are changed.

Leases in which a significant portion of the risks and rewards of ownership are not assumed by the Company are classified as operating leases. The Company carries on its operations in premises under leases of varying terms and renewal options, which are accounted for as operating leases. Payments under an operating lease are recognized in net loss on a straight-line basis over the term of the lease. When a lease contains a predetermined fixed escalation of the minimum rent, the Company recognizes the related rent expense on a straight-line basis and, consequently, records the difference between the recognized rental expense and the amounts payable under the lease as a deferred lease credit. Contingent (sales-based) rentals are recognized as an expense when incurred through cost of sales.

### Store opening and store closing costs

Store opening costs and store closing costs are expensed as incurred.

### Investment in an associate

An associate is an entity over which the Company has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies. The Company's investment in an associate is accounted for using the equity method.

Under the equity method, the investment in an associate is initially recognized at cost. The carrying amount of the investment is adjusted to recognize changes in the Company's share of net assets of the associate since the acquisition date.

The consolidated statements of loss and comprehensive loss reflects the Company's share of the results of operations of the associate. Any change in OCI of the associate is presented as part of the Company's OCI. Unrealized gains and losses resulting from transactions between the Company and the associate are eliminated to the extent of the interest in the associate or joint venture.

The Company recognizes its share of the loss of an associate until its share of loss equals its interest in the associate. Once the investment is reduced to zero, additional losses are provided for, and a liability is recognized, only to the extent that the Company has incurred legal or constructive obligations or made payments on behalf of the associate. If the associate subsequently reports profit, the Company resumes recognizing its share of the profit only after its share of the profit equals the share of loss not recognized.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

In 2016, the Company's investment in an associate related to its investment in Groupe Global LXR Inc. ("Global"), which was reacquired on January 1, 2017 (*note 8*).

### Impairment

#### *i. Impairment of financial assets*

The Company assesses, at each reporting date, whether there is objective evidence that a financial asset or a group of financial assets is impaired. An impairment exists if one or more events that has occurred since the initial recognition of the asset (an incurred "loss event") has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and observable data indicating that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

#### *ii. Impairment of non-financial assets*

The Company assesses, at each reporting date, whether there is an indication that an item of property and equipment or an intangible asset may be impaired. If any such indication exists, the Company estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or a cash-generating unit's ("CGU") fair value less costs of disposal, and its value in use. When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In determining fair value less costs of disposal, recent market transactions are taken into account. If no such transactions can be identified, an appropriate valuation model is used. 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. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or corporate assets.

The Company bases any impairment calculations on detailed budgets and forecast calculations, which are prepared separately for each of the Company's CGUs to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of between three and five years, or the lease term if shorter.

The Company's management has defined each of the commercial premises in which it carries out its activities as a CGU, although where appropriate, these premises are aggregated at a district or regional level to form a CGU.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased and if there has been a change in the assumptions used to determine an asset's recoverable amount. A reversal is limited to the extent that an asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, had no impairment loss been recognized. Such reversal is recognized in net loss.

Goodwill represents the excess of the cost of an acquisition over the fair value of the identifiable net assets acquired at the date of acquisition. Goodwill is carried at cost less accumulated impairment losses and is tested for impairment at least annually and when circumstances indicate that the carrying value may be impaired. For the purposes of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Company's CGUs that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

### Provisions

Provisions are recognized when the Company has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the Company expects some or all of a provision to be reimbursed, the reimbursement is recognized as a separate asset, but only when the reimbursement is virtually certain. The expense relating to a provision is presented in the consolidated statements of loss and comprehensive loss net of any reimbursement. All provisions are reviewed at each reporting date and adjusted to reflect the current best estimates.

If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, when appropriate, the risks specific to the liability. When discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

### Share capital

#### *i. Common shares*

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares are recognized as a deduction from equity, net of any tax effects.

#### *ii. Preferred shares*

Preferred shares are classified as a financial liability if they are redeemable on a specific date or at the option of the shareholders. Dividends thereon are recognized as interest expense in net loss as accrued.

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### *iii. Convertible redeemable preferred shares*

Convertible redeemable preferred shares previously issued by the Company also comprised convertible preferred shares that could be converted to common shares at the option of the holders.

The component parts of a compound financial instrument such as the convertible redeemable preferred shares previously issued by the Company, are usually classified separately as financial liabilities and equity in accordance with the rights and obligations of that security. Usually, the conversion option that will be settled by the exchange of a fixed amount of cash for a fixed number of the Company's own equity instruments is classified as an equity instrument. Since the instrument did not previously meet the fixed-for-fixed criteria for bifurcation, the conversion option was classified as a separate other financial liability.

The Company previously designated the entire compound instrument as a financial liability at fair value through profit or loss.

Transaction costs that related to the issuance of the convertible redeemable preferred shares such as legal fees, that were directly attributable to the incurrence of financial liabilities were recorded as a reduction against the preferred share proceeds.

On June 9, 2017, in connection with the closing of the LXR Acquisition, the convertible redeemable preferred shares were converted into Class B common shares (*note 12*).

### **Stock-based compensation**

#### *i. Employee share purchase plan*

The Company has a stock option plan for employees, non-employees and directors from which options to purchase common shares are issued. Options may not be granted with an exercise price of less than the fair value of the options at the grant date. The awards have no cash settlement alternatives. The vesting requirements are typically service-based and the options normally have a contractual life of 10 years.

The fair value of stock-based compensation awards granted to employees is measured at the grant date using the Black-Scholes option pricing model. Measurement inputs include the share price on the measurement date, the exercise price of the option, the expected volatility (based on weighted average historical volatility adjusted for changes expected based on publicly available information), the weighted average expected life of the option (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds).

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The value of the compensation expense is recognized over the vesting period of the stock options as an expense included in selling, general and administrative expenses, with a corresponding increase to contributed surplus in equity. The amount recognized as an expense is adjusted to reflect the Company's best estimate of the number of awards that will ultimately vest. No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Any consideration paid by plan participants on the exercise of stock options and the previously recognized compensation cost of the options exercised included in contributed surplus are credited to share capital.

### *ii. Non-employee share purchase plan*

When the Company exchanges options or shares for goods and services, the measurement basis is the fair value of the services or goods received, as this value is typically more reliably measurable than the equity instruments themselves. Should this not be the case, the estimated fair value of the equity instruments is used. The measurement date in both cases is generally the earlier of the date at which a commitment to earn the equity instruments by the counterparty is reached, the date the equity instruments are granted and the date at which the counterparty's performance is complete. The cost is recognized in the same manner and in the same period as if the Company had paid cash for the goods or the services.

### *iii. Cash-settled transactions*

For cash-settled share-based compensation (deferred share unit plan), the expense is determined based on the fair value of the liability at the end of the reporting period until the award is settled. The value of the compensation is measured based on the closing price of the shares of the Company on the TSX adjusted to take into account the terms and conditions upon which the units were granted, and is based on the units that are expected to vest. The expense is recognized over the period in which the performance or service conditions are satisfied. At the end of each reporting period, the Company re-assesses its estimates of the number of awards that are expected to vest and recognizes the impact of the revisions through profit or loss.

## **Revenue recognition**

Revenue comprises the fair value of the consideration received or receivable for the sale of goods in the ordinary course of the Company's activities. Revenue is recorded net of discounts, rebates, estimated returns and sales taxes. These are generally recorded at the point of sale for retail and e-Commerce sales. There are no discounts or rebates in the wholesale channel. The Company recognizes revenue when the amount can be reliably measured, it is probable that future economic benefits will flow to the Company and when specific criteria have been met for each of the Company's activities as described below. The Company bases its estimates on historical results, taking into consideration the type of customer, the type of transaction and the specifics of each arrangement. Revenue includes sales through the Company's network of retail stores, sales through the Company's e-Commerce channel, and sales through wholesale operations and hybrid stores.

## Notes to the consolidated financial statements

(in Canadian dollars)

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### *i. Retail Stores and e-Commerce sales*

Revenue from Retail Stores is recognized when the goods are delivered to the customer, which is generally at the point of sale. Revenue from e-Commerce sales is recognized upon receipt of the goods by the customer. The Company provides retail store customers with a minimal right to return within a specified period for store credit only while the Company provides e-Commerce customers a minimal right to return within a specified period for store credit or cash refund. Accumulated experience is used to estimate and provide for such returns.

### *ii. Wholesale and Hybrid Store sales*

Revenue from wholesale operations and hybrid stores is recognized upon shipment of the merchandise. The Company does not generally grant right of returns to wholesale customers.

### **Income taxes**

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in net loss except to the extent that they relate to items recognized directly in equity or in OCI.

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered or paid. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the financial position date. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

The Company uses the liability method of accounting for deferred income taxes, which requires the establishment of deferred income tax assets and liabilities for all temporary differences caused when the tax bases of assets and liabilities differ from their carrying amounts reported in the consolidated financial statements. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the temporary differences when they reverse, based on tax rates that have been enacted or substantively enacted at the end of the reporting period. The Company recognizes deferred income tax assets for unused tax losses and deductible temporary differences only to the extent that, in management's opinion, it is probable that future taxable income will be available against which they can be utilized. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority and the Company intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Deferred income tax assets and liabilities are recognized on the consolidated statements of financial position under non-current assets or liabilities irrespective of the expected dates of realization or settlement.

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### Earnings (loss) per share

Basic earnings (loss) per share are calculated using the weighted average number of shares outstanding during the year.

The diluted earnings (loss) per share are calculated by adjusting the weighted average number of shares outstanding to include additional shares issued from the assumed conversion of preferred shares and the exercise of stock options, if dilutive. For stock options, the number of additional shares is calculated by assuming that the proceeds from such exercises, as well as the amount of unrecognized stock-based compensation which is considered to be assumed proceeds, are used to purchase common shares at the average market price during the reporting period.

### Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial instruments are recognized depending on their classification with changes in subsequent measurements being recognized in income or loss or in OCI.

The Company has made the following classifications:

- Cash and convertible redeemable preferred shares, including warrants, are classified as “fair value through profit or loss”, and measured at fair value. Changes in fair value are recorded in net loss.
- Accounts receivable are classified as “Loans and Receivables”. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method.
- Accounts payable and accrued liabilities, credit facility and long-term debt are classified as “Other Financial Liabilities”. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method.

Transaction costs related to financial instruments classified as financial liabilities at fair value through profit or loss are expensed as incurred. Transaction costs related to financial liabilities classified as Other Financial Liabilities are reflected in the carrying amount of the financial liability and are then amortized over the estimated useful life of the instrument using the effective interest rate method.

### Government grants

Government grants are recognized where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognized as income on a systematic basis over the periods that the costs, which it is intended to compensate, are expensed.

## Notes to the consolidated financial statements

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Where the grant relates to an asset, it is recognized as income in equal amounts over the expected useful life of the related asset.

### 3. Changes in accounting principles

#### Standards issued but not yet effective

IFRS 9, "Financial Instruments" ("IFRS 9"), partially replaces the requirements of IAS 39, "Financial Instruments: Recognition and Measurement". This standard is the first step in the project to replace IAS 39. The IASB intends to expand IFRS 9 to add new requirements for the classification and measurement of financial liabilities, derecognition of financial instruments, impairment and hedge accounting to become a complete replacement of IAS 39. These changes are applicable for annual periods beginning on or after January 1, 2018, with earlier application permitted. The adoption of this new standard will not have a significant impact on the consolidated financial statements of the Company.

IFRS 15, "Revenue from Contracts with Customers" ("IFRS 15") replaces IAS 11, "Construction Contracts", and IAS 18, "Revenue", as well as various interpretations regarding revenue. This standard introduces a single model for recognizing revenue that applies to all contracts with customers, except for contracts that are within the scope of standards on leases, insurance and financial instruments. This standard also requires enhanced disclosures. Adoption of IFRS 15 is mandatory and will be effective for annual periods beginning on or after January 1, 2018. The Company is currently finalizing its assessment of the impacts of adopting this standard on the Company's consolidated financial statements and related note disclosures. The Company's preliminary position is that the adoption of this new standard will not have a significant impact on the consolidated financial statements of the Company.

IFRS 16, "Leases" ("IFRS 16") replaces IAS 17, "Leases". This standard provides a single model for leases abolishing the current distinction between finance and operating leases, with most leases being recognized in the statement of financial position. Certain exemptions will apply for short-term leases and leases of low value assets. The new standard will be effective for annual periods beginning on or after January 1, 2019. Early application is permitted, provided the new revenue standard, IFRS 15, has been applied, or is applied at the same date as IFRS 16. The Company is currently assessing the impact of adopting this standard on its consolidated financial statements and related note disclosures.

Disclosure initiative (amendment to IAS 7) In January 2016, the IASB issued amendments to IAS 7, Statements of Cash Flows which will require specific disclosures for movements in certain liabilities on the statement of cash flows. These amendments will be applicable for the annual period beginning on or after January 1, 2017, with earlier application permitted. The implementation of these amendments is not expected to have a significant impact on the Company.

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IFRS 2, “Share-based payment” (“IFRS 2”) In June 2016, the IASB issued amendments to IFRS 2, clarifying how to account for certain types of share-based payment transactions. The amendments provide requirements on the accounting for: the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; share-based payment transactions with a net settlement feature for withholding tax obligations; and a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled. The amendments apply for annual periods beginning on or after January 1, 2018. As a practical simplification, the amendments can be applied prospectively. Retrospective, or early, application is permitted if information is available without the use of hindsight.

### 4. Significant accounting judgments, estimates and assumptions

The preparation of the consolidated financial statements in conformity with IFRS requires the Company to make judgments, apart from those involving estimation, in applying accounting policies that affect the recognition and measurement of assets, liabilities, revenue and expenses. Actual results may differ from the judgments made by the Company. Information about judgments that have the most significant effect on recognition and measurement of assets, liabilities, revenue and expenses are discussed below. Information about significant estimates is discussed in the following section.

#### Key sources of estimation uncertainty

##### *i. Inventory valuation*

The Company records a write-down to reflect management’s best estimate of the net realizable value of inventory which includes assumptions and estimates for future sell-through of units, selling prices as well as disposal costs, where appropriate, based on historical experience. Management continually reviews the carrying value of its inventory, to assess whether the write-down is adequate, based on current economic conditions and an assessment of sales trends.

As at December 31, 2017, the provision for inventory obsolescence is \$120,137 (nil as at December 31, 2016). The net change of the provision for inventory obsolescence was charged to the cost of sales in the consolidated statements of loss and comprehensive loss.

##### *ii. Sales returns*

Sales returns are estimated on the basis of historical returns and are recorded so as to allocate them to the same period as the original revenue is recorded. Accumulated experience is used to estimate and provide for such returns.

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### Critical judgements in applying accounting policies

#### *i. Determining the achievement of control*

Management used judgment in determining the effective date on which the Company obtained control of Global (note 8). Management determined the Company effectively obtained control of Global on January 7, 2017, which is a date earlier than the closing date of June 10, 2017, since the reacquisition was approved by common shareholders and only pending on legal documentation finalization.

#### *ii. Income taxes*

The Company may be subject to audits related to tax risks, and uncertainties exist with respect to the interpretation of tax regulations, changes in tax laws, and the amount and timing of future taxable income. Differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to taxable income and income tax expense already recorded.

The Company establishes provisions if required, based on reasonable estimates, for possible consequences of audits by the tax authorities. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the entity and the responsible tax authority, which may arise on a wide variety of issues.

The Company recognizes deferred income tax assets for unused tax losses and deductible temporary differences only to the extent that, in management's opinion, it is probable that future taxable income will be available against which they can be utilized. Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

### 5. Accounts receivable

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
	\$	\$
Trade	<b>4,904,967</b>	1,683,209
Trade receivable from an associate (Groupe Global LXR Inc.)	—	397,575
Less: allowance for doubtful accounts	<b>(21,868)</b>	(10,890)
	<b>4,883,099</b>	2,069,894
Other trade receivable	<b>85,245</b>	61,139
	<b>4,968,344</b>	2,131,033

Trade receivables are non-interest bearing and are generally due on terms of up to 30 days.

As at December 31, 2017, trade receivables of an initial value of \$1,436,710 (2016 – \$76,440) were past due but not impaired.

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## 6. Property and equipment

	Furniture and equipment	Computer equipment	Rolling stock	Leasehold improvements	Total
	\$	\$	\$	\$	\$
<b>Cost</b>					
Balance, December 31, 2016	910,873	113,937	54,653	256,830	1,336,293
Acquisitions	2,259,438	142,258	—	27,265	2,428,961
Disposals	(4,474)	—	—	—	(4,474)
Cumulative translation adjustment	(66,100)	(3,326)	—	(3,748)	(73,174)
<b>Balance, December 31, 2017</b>	<b>3,099,737</b>	<b>252,869</b>	<b>54,653</b>	<b>280,347</b>	<b>3,687,606</b>

	Furniture and equipment	Computer equipment	Rolling stock	Leasehold improvements	Total
	\$	\$	\$	\$	\$
<b>Accumulated depreciation</b>					
Balance, December 31, 2016	190,420	73,441	30,874	40,645	335,380
Depreciation	136,694	46,064	19,314	76,188	278,260
Cumulative translation adjustment	28,348	281	37	574	29,240
<b>Balance, December 31, 2017</b>	<b>355,462</b>	<b>119,786</b>	<b>50,225</b>	<b>117,407</b>	<b>642,880</b>

	Furniture and equipment	Computer equipment	Rolling stock	Leasehold improvements	Total
	\$	\$	\$	\$	\$
<b>Net carrying value</b>					
Balance, December 31, 2016	720,453	40,496	23,779	216,185	1,000,913
<b>Balance, December 31, 2017</b>	<b>2,744,275</b>	<b>133,083</b>	<b>4,428</b>	<b>162,940</b>	<b>3,044,726</b>

## 7. Intangible assets

	Software	Website	Total
	\$	\$	\$
<b>Cost</b>			
Balance, December 31, 2016	17,700	351,928	369,628
Reacquisition of an associate	103,422	8,064	111,486
Acquisitions	515,070	—	515,070
Cumulative translation adjustment	—	(25,428)	(25,428)
<b>Balance, December 31, 2017</b>	<b>636,192</b>	<b>334,564</b>	<b>970,756</b>

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	<b>Software</b>	<b>Website</b>	<b>Total</b>
	\$	\$	\$
<b>Accumulated amortization</b>			
Balance, December 31, 2016	1,635	111,076	112,711
Amortization	<b>93,954</b>	<b>102,562</b>	<b>196,516</b>
Cumulative translation adjustment	—	<b>(279)</b>	<b>(279)</b>
<b>Balance, December 31, 2017</b>	<b>95,589</b>	<b>213,359</b>	<b>308,948</b>
	<b>Software</b>	<b>Website</b>	<b>Total</b>
	\$	\$	\$
<b>Net carrying value</b>			
Balance, December 31, 2016	16,065	240,852	256,917
<b>Balance, December 31, 2017</b>	<b>540,603</b>	<b>121,205</b>	<b>661,808</b>

The Company recorded \$34,518 (2016 – nil) of government assistance against website cost for eligible expenses claimed for investment tax credits.

## 8. Business combination

On January 7, 2017, as part of a strategic decision to better integrate the Company's omni-channel strategy and improve the reporting of its entire operations, the Company reacquired control of an associate, Groupe Global LXR Inc. by repurchasing the interest of Global that it did not own for total consideration of \$3,384,086 through the issuance of 59,558 convertible redeemable preferred shares of the Company. Global is the subsidiary of the Company that is responsible for the LXR's Canadian and U.S. e-Commerce operations through its website, www.lxrco.com.

The assets acquired, liabilities assumed and results of operations have been consolidated as of the effective date of January 1, 2017. The excess of the purchase price over tangible assets, identifiable intangible assets acquired and liabilities assumed was recorded as goodwill. The purchase price of the business combination entered into has been allocated to assets acquired and liabilities assumed based on their estimated fair values at the acquisition date, using management's best estimates of the fair values using the data available at the acquisition date.

The Company recognized a gain resulting from a business acquisition of \$2,070,422 arising from the fair value of its existing ownership interest in Global.

# LXRandCo, Inc.

## Notes to the consolidated financial statements

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Details of the business combination, accounted for by using the acquisition method, are summarized as follows:

	\$
<b>Assets acquired</b>	
Cash	803,661
Accounts receivable and other receivable	30,228
Inventory	54,933
Prepaid expenses	2,907
Tangible and intangible assets	184,064
Goodwill	2,952,652
	<u>4,028,445</u>
<b>Liabilities assumed</b>	
Accounts payable and accrued liabilities	341,254
Loan payable to related parties	303,105
	<u>644,359</u>
Net assets acquired	<u>3,384,086</u>
Purchase price consideration	
Issuance of 59,558 convertible redeemable preferred shares	<u>3,384,086</u>

### 9. Credit facility and line of credit

On June 9, 2017, concurrent with the closing of the LXR Acquisition, the Company repaid a revolving term loan and a capital expenditure term loan that it had with Sterling National Bank. The Company incurred \$142,480 of termination fees that were recorded as debt extinguishment costs. Unamortized deferred financing fees were expensed in 2017.

On June 14, 2017, the Company entered into a credit agreement with a Canadian chartered bank that provides the Company with a new credit facility to finance its growth (the "Line of Credit"). The Line of Credit consists of a revolving credit facility for an authorized amount of up to \$25,000,000, subject to a maximum draw based on a borrowing base calculated as a percentage of eligible accounts receivable and eligible inventory as defined in the credit agreement.

The Line of Credit bears interest at (a) the bank's prime rate (3.2% as at December 31, 2017) or U.S. base rate if denominated in U.S. dollars (4.5% as at December 31, 2017) plus an applicable margin of 0.50%, or (b) the banker's acceptance rate (1.37% as at December 31, 2017), plus an applicable margin of 2.00% or LIBOR (1.56% as at December 31, 2017) plus an applicable margin of 2.00%, at the Company's option. A commitment fee of 0.25% of the unused portion of the Line of Credit is also due. The Line of Credit matures on June 14, 2019 and accordingly, it is presented as a long-term liability. As at December 31, 2017, the Company had drawn \$8,602,491 on the available balance. The Company incurred \$610,231 of financing costs attributable to the issuance of the Line of Credit. As at December 31, 2017, unamortized financing costs recorded as reduction of the Line of Credit amount to \$413,015.

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The Line of Credit can be used to enter into foreign exchange contracts not exceeding a maximum amount of \$1,000,000, secured by forward exchange contracts entered into by the Company. The Line of Credit can also be used to issue letters of credit not exceeding a maximum amount of \$2,000,000.

The Line of Credit is collateralized by substantially all assets of the Company and its subsidiaries. The Line of Credit requires the Company to meet certain financial covenants, which were all met as at December 31, 2017.

10. Accounts payable and accrued liabilities

	December 31, 2017 \$	December 31, 2016 \$
Accounts payable and accrued liabilities	5,828,511	3,941,708
Government remittances	1,164	75,816
	<b>5,829,675</b>	<b>4,017,524</b>

11. Long-term debt

	December, 31 2017 \$	December, 31 2016 \$
Subordinated debt of \$1,500,000 from the Business Development Bank of Canada ("BDC") (i)	—	1,495,644
Bonus payment (i)	—	637,375
	—	2,133,019
Term loans from Investissement Québec ("IQ") (ii)	180,000	369,944
Term loans from BDC	—	106,508
Term capital expenditure loan (iii)	—	228,778
Other term loans	31,739	190,504
Total long-term debt	211,739	3,028,753
Current portion	188,810	2,841,026
	<b>22,929</b>	<b>187,727</b>

(i) Subordinated debt with BDC

On August 15, 2013, the Company, through its wholly owned subsidiary LXR Canada Inc., obtained financing of \$1,500,000 from BDC in the form of an unsecured debt maturing on August 15, 2018, bearing interest at an annual rate of 8.75%. Upon maturity, the Company was required to remit an additional compensation in the form of a bonus payment representing 1.2% of the Company's consolidated value as defined in a formula in the agreement. Under the terms of the agreement, the Company was also required to remit monthly a royalty of 0.30% of consolidated annual sales.

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The subordinated debt required that certain financial covenants be maintained on a consolidated basis, which were not all met for the year ended December 31, 2016. On April 12, 2017, the Company obtained a confirmation from BDC, waiving its rights, arising from the breach of the covenants as at December 31, 2016, to demand repayment for a period of more than one year from the financial position date. Through issuance of the waiver, the Company and BDC amended the subordinated agreement to fix the bonus payment to 1.2% of \$60,000,000 which was payable at the earlier of the maturity date or the closing of the LXR Acquisition (*note 1*). On June 9, 2017, concurrent with the closing of the LXR Acquisition, the Company repaid the outstanding balance of the subordinated debt, including the final bonus payment and royalty, for a total amount of \$2,383,106, of which an amount of \$188,763 was recorded as debt extinguishment costs.

### (ii) Term loans with IQ

The Company, through its wholly-owned subsidiary LXR Canada Inc., has entered into the following term loans with IQ:

- (a) Term loan of \$300,000 bearing interest at the bank's prime rate (3.2% as at December 31, 2017 and December 31, 2016) plus an applicable margin of 3%. The loan is repayable by forty-eight monthly principal payments of \$6,250 with a 12-month moratorium from June 1, 2015 to May 31, 2016. The loan matured on November 30, 2017 and was fully repaid (December 31, 2016 – \$68,750).
- (b) Term loan of \$600,000 bearing interest at the bank's prime rate (3.2% as at December 31, 2017 and December 31, 2016) plus an applicable margin of 3%. The loan is repayable by sixty monthly principal payments of \$10,000 with a 12-month moratorium from June 1, 2015 to May 31, 2016. The loan matures on April 30, 2019. As at December 31, 2017, the long-term debt obligation under this loan amounted to \$180,000 (2016 – \$290,000).

The term loan requires that certain financial covenants be maintained by the Company, which were not all met as at December 31, 2017. Accordingly, the Company presented this term loan as a current liability on the consolidated statements of financial position.

- (c) Term loan of \$225,000 bearing interest at the bank's prime rate (3.2% as at December 31, 2017 and December 31, 2016) plus an applicable margin of 2.15%. The loan was fully repaid in October 2017 (2016 – \$11,194).

### (iii) Term capital expenditure loan

On January 15, 2016, the Company entered into a credit agreement (*note 9*) that included a capital expenditure term loan facility in the amount of US\$350,000 for the purpose of purchasing eligible equipment.

On June 9, 2017, concurrent with the closing of the LXR Acquisition, the Company repaid the capital expenditure term loan outstanding.

## Notes to the consolidated financial statements

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## 12. Convertible redeemable preferred shares

## Issued

Unlimited number of the following classes of shares:

	Number	Amount \$
<b>Convertible redeemable preferred shares of LXR International</b>		
Balance, January 1, 2017	351,667	19,982,261
Exercise of warrants	130,039	7,388,273
Issuance of convertible redeemable preferred shares	59,558	3,384,086
	<u>541,264</u>	<u>30,754,620</u>
<b>Dividends payable in convertible redeemable preferred shares</b>		
Balance, January 1, 2017	11,641	661,442
Dividends declared for the year	1,079	61,308
	<u>12,720</u>	<u>722,750</u>
<b>Warrants to purchase convertible redeemable preferred shares</b>		
Balance, January 1, 2017	195,100	9,582,300
Exercise of warrants	(130,039)	(6,386,841)
Expiration of warrants	(65,061)	(3,195,459)
	<u>—</u>	<u>—</u>
	<u>553,984</u>	<u>31,477,370</u>
Conversion into Class B common shares of LXR International	(553,984)	(31,477,370)
<b>Balance, December 31, 2017</b>	<u>—</u>	<u>—</u>

On June 10, 2016, the Company issued 351,667 convertible redeemable preferred shares, representing 26% of the Company's share capital, to a group of unrelated investors as part of the first closing of an equity financing, for total consideration of \$2,704,333. The financing was extended to January 31, 2017 to accommodate potential additional closings. The convertible redeemable preferred shares were convertible at the option of the holders into Class A common shares of LXR International at a rate of one Class A common share for one convertible redeemable preferred share and are mandatorily redeemable on June 17, 2019, at their initial share price of \$7.69 plus any unpaid annual cumulative dividends of 6%.

The convertible redeemable preferred shares were designated as a financial liability at fair value through profit or loss. Accordingly, the Company recorded an increase in fair value of \$17,277,928 as at December 31, 2016 resulting from an increase in valuation. The fair value of the Company and of the resulting convertible redeemable preferred shares was determined by using the most recent equity transaction entered into by LXR International with non-related parties and was established at an enterprise value of \$56.82 per share.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

The Company granted warrants for the purchase of convertible redeemable preferred shares. The warrants had an expiration date of January 31, 2017 and entitled the holders to purchase up to 195,100 convertible redeemable preferred shares of the Company at a share price of \$7.69. As at December 31, 2016, consistent with the fair value valuation methodology applied to the convertible redeemable preferred shares, the Company recorded the fair value of the outstanding warrants at \$49.13 per warrant. On January 30, 2017, the Company issued 130,039 convertible redeemable preferred shares at \$7.69 per share for proceeds of \$1 million in connection with the exercise of these warrants. The Company's share price was unchanged as at January 31, 2017, and accordingly, no fair value adjustment was recorded in the period on the remaining unexercised warrants. Upon expiration of the remaining unexercised warrants on January 31, 2017, the Company recorded a gain from the reduction of the related liability of \$3,195,459.

The Company reacquired control of Global (*note 8*) by repurchasing the interest of Global that it did not own for total consideration of \$3,384,086 through the issuance of 59,558 convertible redeemable preferred shares.

On March 31, 2017, the Board of Directors approved a payment in kind of the unpaid cumulative dividends of 6% in the normal course and in accordance with the terms of the convertible redeemable preferred shares shareholders' agreement. Accordingly, the Company issued 1,079 convertible redeemable preferred shares (11,641 as at December 31, 2016) and, consistent with the fair value valuation methodology applied to that financial instrument, recorded an amount of \$722,750 as dividend payable on such convertible redeemable preferred shares (\$661,442 as at December 31, 2016).

On June 9, 2017, concurrent with the closing of the LXR Acquisition, the convertible redeemable preferred shares, including the declared dividends payable, were converted into 553,984 common shares of LXR International, which were then exchanged in favour of 2,711,964 Class B common shares of LXRandCo.

### 13. Share capital

#### Issued

An unlimited number of the following classes of shares with no par value:

Class B common shares, voting and fully participating

	Number	Amount \$
Balance, January 1, 2017	3,126,563	100
Conversion of Class A shares of Gibraltar Growth Corporation	294,699	—
Issued in a Private Placement	2,500,000	—
Conversion of convertible redeemable preferred shares ( <i>note 12</i> )	—	31,477,370
Issued in LXR Acquisition ( <i>note 1</i> )	7,025,222	33,419,715
<b>Balance, December 31, 2017</b>	<b>12,946,484</b>	<b>64,897,185</b>

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

On June 9, 2017, concurrent with the closing of the LXR Acquisition, the convertible redeemable preferred shares having a net book value of \$31,477,370, including the declared dividends payable in convertible redeemable preferred shares, were converted into 553,984 common shares of LXR International increasing the total of LXR International common shares to 1,553,984. The common shares of LXR International were ultimately exchanged in favour of 7,025,221 Class B common shares of LXRandCo.

### **Forfeitable founders' shares**

As at December 31, 2017, the Company had issued 1,357,656 Class B common shares, in two tranches of 678,828 and 678,828 which are subject to forfeiture on June 9, 2022, unless the closing price of share price of the Class B common shares exceeds \$13.00 and \$15.00, respectively (as adjusted for stock split or combinations, stock dividends, reorganizations, or recapitalizations) for any 20 trading days within a 30 day-trading-day period.

### **Warrants**

As at December 31, 2017, 10,861,250 warrants to purchase common shares of the Company are outstanding. Each warrant became exercisable 30 days after the completion of the LXR Acquisition and is exercisable to purchase one Class B common share at an exercise price of \$11.50 per share. The warrants will expire on the fifth anniversary after the completion of the LXR Acquisition.

### **Stock-based compensation**

Under the Company's stock option plan, the Board of Directors (the "Board") is authorized, at its discretion, to issue stock options to its employees, directors, officers, consultants and other service providers.

LXR International granted on February 16, 2017, as part of a newly instituted employee stock option program, 62,334 options to purchase common shares of LXR International at \$7.69 per common share. The options vest at 25% on the first anniversary of the grant date and yearly thereafter (on each anniversary of such date), to the fourth anniversary of the grant date and shall remain exercisable up to February 16, 2027. On June 9, 2017, concurrent with the closing of the LXR Acquisition, the 62,334 options granted were exchanged in favour of 285,744 options to purchase Class B common shares of LXRandCo (the "Replacement Options"). The Replacement Options provide an optionnee to purchase Class B common shares of LXRandCo at a price of \$1.68 per share and the terms and conditions of the Replacement Options have remained the same as the initial terms and conditions.

Since the options modifications reduce the total fair value of the Replacement Options related share-based payment arrangement, the Company continues to account for the cost of compensation services received as consideration for the equity instruments granted as if the replacement had not occurred.

## Notes to the consolidated financial statements

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December 31, 2017 and 2016

The fair value of stock options granted is estimated at the date of grant using the Black-Scholes option pricing model and the following assumptions:

	December 31, 2017	December 31, 2016
Expected volatility	<b>32% yearly</b>	—
Risk-free interest rate	<b>1.48%</b>	—
Expected option life	<b>6.25 years</b>	—
Expected dividend yield	—	—

The stock option activity and the weighted average exercise price are summarized as follows:

	December 31, 2017		December 31, 2016	
	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$
Outstanding at beginning of year	—	—	—	—
Granted	<b>285,744</b>	<b>1.68</b>	—	—
Cancelled	<b>(3,946)</b>	<b>1.68</b>	—	—
Outstanding at end of year	<b>281,798</b>	<b>1.68</b>	—	—
Option exercisable at end of year	<b>48,765</b>	—	—	—

The weighted average remaining contractual term of options exercisable as at December 31, 2017 was 9.2 years.

The weighted average grant-date fair value related to the equity instruments granted during the year ended December 31, 2017 amounted to approximately \$49 per option, which represents the fair value of the equity options granted by LXR International. The stock-based compensation expense of \$1,621,168 for the year ended December 31, 2017 (nil – December 31, 2016), is recorded in the consolidated statements of loss and comprehensive loss in selling, general and administrative expenses and credited to additional paid-in capital.

As at December 31, 2017, the total remaining unrecognized compensation expense related to non-vested stock options amounted to \$1,890,693, which will be recognized over the weighted average remaining requisite service period of 3.25 years.

Pursuant to the closing adjustment of the LXR Acquisition (*note 1*), 3,946 options were cancelled and terminated.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

**Deferred share unit plan**

Deferred share units (“DSUs”) are awarded to eligible directors under a preliminary deferred share unit plan. Under this plan, each eligible director receives a portion of his or her compensation in the form of DSUs. The value of a granted DSU is calculated based on the 5-day variable weighted average share price of the Company leading up to the end of the quarter the closest to the DSU grant date. The plan has been approved by the Board of Directors in 2017 but subject to the approval of the Toronto Stock Exchange.

During the year 2017, the Company granted to directors 30,304 DSUs and recognized a compensation expense of \$213,375 for its deferred share unit plan under stock-based compensation expense. As at December 31, 2017, the Company re-assessed the value of the vested and granted DSU based on the closing price of the Class B common shares of the Company on the Toronto Stock Exchange and recorded a reduction in fair value of \$54,278 through stock-based compensation expense. The outstanding DSUs are presented as other liabilities in the consolidated statements of financial position.

**14. Income taxes**

A reconciliation of the statutory income tax rate to the effective tax rate is as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
	\$	\$
Income tax at statutory rate of 26.8%	<b>(4,772,172)</b>	(5,389,043)
Impact of foreign tax rate differences	<b>(409,346)</b>	(9,652)
Valuation allowance on deferred tax assets	<b>2,810,589</b>	(11,750)
Effect of change in future tax rate	<b>(499,946)</b>	—
Permanent differences	<b>2,774,137</b>	102,300
Accrual to return	<b>141,886</b>	(1,841)
Non-deductible change in fair value of convertible redeemable preferred shares	—	5,229,117
Other	<b>100,620</b>	34,504
	<b>145,768</b>	(46,365)

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

The tax effects of temporary differences and net operating losses that give rise to deferred income tax assets and liabilities are as follows:

	December 31, 2017 \$	December 31, 2016 \$
<b>Deferred income tax assets</b>		
Financing fees	81,130	20,405
Net-operating losses	139,790	-
Total deferred income tax assets	<u>220,920</u>	<u>20,405</u>
<b>Deferred income tax liabilities</b>		
Carrying values of property and equipment in excess of tax basis	172,213	684
Tax payable on investment tax credits	5,808	11,728
Non-deductible reserve and others	259,750	186,236
Total deferred income tax liabilities	<u>437,771</u>	<u>198,648</u>
Net deferred income tax liabilities	<u>(216,851)</u>	<u>(178,243)</u>

As at December 31, 2017, the Company's U.S. subsidiary has accumulated losses amounting to US\$4,338,046 which expire during the years 2032 to 2037. These tax losses have not been recorded in the consolidated financial statements. As at December 31, 2017, the Company's Canadian subsidiaries have accumulated losses amounting to \$3,530,562 which expire during the years 2032 to 2037. These tax losses have not been recorded in the consolidated financial statements. As at December 31, 2017, the Company's Germany subsidiary has accumulated losses amounting to €1,140,526 which can be used against future taxable income for an unlimited period.

## 15. Selling, general and administrative expenses

Included in selling, general and administrative expenses are the following expenses:

	December 31, 2017 \$	December 31, 2016 \$
Wages, salaries and employee benefits	10,327,232	4,376,215
Professional fees	928,161	136,000
Stock-based compensation	1,780,265	279,465
Non-recurring branding costs	119,821	-
Store-related opening and closing costs	1,373,181	1,335,670
Reporting issuer costs	151,960	-
Other	1,481,509	-
	<u>16,162,129</u>	<u>6,127,350</u>

## Notes to the consolidated financial statements

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December 31, 2017 and 2016

## 16. Related party transactions

In the normal course of its operations, the Company enters into transactions with related parties. These transactions are measured at the exchange amount, which is the amount of consideration determined and agreed to by the related parties. In addition to the related party transactions and balances disclosed elsewhere in these consolidated financial statements, significant transactions and balances between related parties are as follows:

	December 31, 2017 \$	December 31, 2016 \$
<b>Transactions with a commonly controlled company</b>		
Rental expense paid to a company controlled by common shareholders	144,000	136,000
<b>Transactions with a Board director and shareholder</b>		
Legal fees	233,250	88,315
<b>Transactions with an associate</b>		
Sales to Groupe Global LXR Inc.	—	549,783
<b>Business combination</b>		
Reacquisition of Groupe Global LXR Inc. <i>(note 8)</i>	<b>3,384,086</b>	—

## Transactions with key management personnel

The compensation earned by key management in aggregate was as follows:

	December 31, 2017 \$	December 31, 2016 \$
Wages, salaries, bonuses, consulting fees and stock-based compensation	<b>1,368,248</b>	147,385

## 17. Earnings (loss) per share

Basic earnings (loss) per share (“EPS”) amounts are calculated by dividing the profit (loss) for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year. Diluted EPS amounts are calculated by dividing the profit (loss) attributable to ordinary equity holders of the parent (after adjusting for dividends, accretion interest on the mandatorily redeemable preference shares and gain/loss from embedded derivative on preferred shares) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on conversion of all the dilutive potential ordinary shares into ordinary shares, unless these would be anti-dilutive.

For the years ended December 31, 2017 and 2016, as a result of the net loss during those years, the warrants, stock-based awards and convertible redeemable preferred shares are anti-dilutive.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

### 18. Segment information

The Company has determined that it conducts its activities in a single industry segment as an omni-channel retailer, being the only operating segment it uses to evaluate performance and allocate resources by the Chief operating decision maker. The single operating segment includes all sales channels accessed by the Company's customers, including sales through the Company's retail network of stores, wholesale partners and online through its website. With respect to geographic areas, the Company's continuing operations are mainly in Canada, the United States, the United Kingdom and European Union.

The following tables summarize net revenue and assets held by geography for the year ended:

#### Revenue by Geographic Region

	December 31, 2017 \$	December 31, 2016 \$
Canada	5,745,269	4,692,521
United States	26,545,378	16,208,203
United Kingdom	390,497	—
European Union	4,387,993	990,086
	<b>37,069,137</b>	<b>21,890,810</b>

#### Non-current assets by Geographic Region

	December 31, 2017 \$	December 31, 2016 \$
Canada	6,218,351	803,700
United States	2,050,990	384,557
United Kingdom	134,304	—
European Union	438,645	182,255
	<b>8,842,240</b>	<b>1,370,512</b>

### 19. Financial risk management

The Company's activities expose it to a variety of financial risks, including risks related to foreign exchange, interest rate, credit, and liquidity.

## Notes to the consolidated financial statements

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December 31, 2017 and 2016

## Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Approximately 74% and 5% of the Company's sales are in U.S. dollars and in Euros, respectively. In addition, inventory-related purchases are mainly denominated in Japanese Yen, and accordingly, the Company is exposed to currency risk. The Company's currency risk is largely limited to currency fluctuations between U.S. dollars, Euros and Japanese Yen. The Company is exposed to currency risk through its cash, accounts receivable and accounts payable and accrued liabilities denominated in foreign currencies.

The Company's foreign exchange exposure is as follows:

	December 31, 2017			
	US \$	Euro €	Japanese Yen ¥	Pound Sterling £
Cash	1,005,220	193,059	5,739,450	32,185
Accounts receivable	2,661,833	425,627	50,437,522	131,686
Accounts payable and accrued liabilities	(1,604,594)	(38,099)	(232,356,513)	(19,368)
	<b>2,062,459</b>	<b>580,587</b>	<b>(176,179,541)</b>	<b>144,503</b>
	December 31, 2016			
	US \$	Euro €	Japanese Yen ¥	Pound Sterling £
Cash	549,760	29,027	8,157,676	—
Accounts receivable	736,979	76,189	28,798,174	—
Accounts payable and accrued liabilities	(286,573)	(47,860)	(270,362,261)	—
	<b>1,000,166</b>	<b>57,356</b>	<b>(233,406,411)</b>	<b>—</b>

Assuming that all other variables remain constant, a revaluation of these monetary assets and liabilities due to a 5% rise or fall in the Canadian dollar against the U.S. dollar would have resulted in an increase or decrease to net loss and comprehensive loss in the amount of approximately \$67,000. Assuming that all other variables remain constant, a revaluation of these monetary assets and liabilities due to a 5% rise or fall in the Canadian dollar against the Japanese Yen would have resulted in an increase or decrease to net loss and comprehensive loss in the amount of approximately \$150,000.

## Notes to the consolidated financial statements

(in Canadian dollars)

December 31, 2017 and 2016

### Market risk – 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. Financial instruments that potentially subject the Company to cash flow interest rate risk include financial assets and liabilities with variable interest rates. The Company is exposed to cash flow risk on its credit facility and other term loans that bear interest at variable interest rates.

Based on the currently outstanding line of credit and total long-term debt bearing interest at variable rates as at December 31, 2017, if interest rates had changed by 100 basis points, assuming that all other variables had remained the same, the impact would have increased or decreased finance costs by approximately \$30,000.

### Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company's liquidity follows a seasonal pattern based on the timing of inventory purchases and capital expenditures. The Company is exposed to this risk mainly in respect of its trade and other payables (except government remittances), line of credit, long-term debt and operating lease commitments.

The Company expects that its trade and other payables will be discharged within 90 days.

The contractual maturities and carrying amounts of financial liabilities are summarized in the following table:

	<b>Maturing in under 1 year</b>	<b>Maturing in 1 to 5 years</b>	<b>Total</b>
	\$	\$	\$
Accounts payable and accrued liabilities	5,829,675	—	5,829,675
Line of credit	—	8,602,491	8,602,491
Long-term debt	188,810	22,929	211,739
	<u>6,018,485</u>	<u>8,625,420</u>	<u>14,643,905</u>

The Company manages its risk of failing to discharge its financial liabilities in a timely manner by factoring its operating requirements and through the use of various financing sources, as needed.

## Notes to the consolidated financial statements

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December 31, 2017 and 2016

### Credit risk

The Company is exposed to credit risk resulting from the possibility that counterparties may default on their financial obligations to it. The Company's maximum exposure to credit risk at the reporting date is equal to the carrying value of accounts receivable. Accounts receivable primarily consist of receivables from retail customers who pay by credit card and receivables from other companies for sales of wholesale products. Credit card payments have minimal credit risk and corporate receivables are closely monitored. In addition, a portion of the total trade accounts receivable is insured against possible losses.

As at December 31, 2017, 5 trade partners accounted for respectively 10%, 10%, 13%, 14% and 15%, for an aggregate of 62% of total trade accounts receivable. As at December 31, 2016, 5 trade partners accounted for respectively 11%, 15%, 17%, 20% and 27%, for an aggregate of 90% of total trade accounts receivable. Pursuant to their respective terms, trade accounts receivable are aged as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
	\$	\$
0 – 30 days	<b>3,445,675</b>	1,179,312
31- 60 days	<b>1,297,791</b>	449,810
61- 90 days	<b>132,021</b>	27,363
91 – 120 days	<b>29,480</b>	26,724
	<b>4,904,967</b>	1,683,209

Based on past experience, the Company believes that no significant allowance for doubtful accounts is necessary in respect of trade accounts receivable as current trade receivables and 31-60 days old receivables together represent 97% of total gross trade accounts receivable (2016 – 97%). This balance includes the amounts owed by the Company's most significant retail partners and relates to customers that have a good payment history with the Company.

### Fair values

Financial assets and financial liabilities, except for convertible redeemable preferred shares, are measured on an ongoing basis at fair value or amortized cost. Convertible redeemable preferred shares are measured at fair value through profit or loss. The disclosures in the "Financial instruments" section of note 2 describe how the categories of financial instruments are measured and how income and expenses, including fair value gains and losses, are recognized.

The carrying amount of the line of credit approximates its fair value due to a floating rate that could currently be obtained by the Company for credit facility with similar conditions and maturities.

## Notes to the consolidated financial statements

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The classification of other financial instruments, as well as their carrying values and fair values, are shown in the table below:

	December 31, 2017		December 31, 2016	
	Carrying value	Fair value	Carrying value	Fair value
	\$	\$	\$	\$
<b>Financial liabilities</b>				
Convertible redeemable preferred shares	—	—	20,643,703	20,643,703

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies; however, considerable judgment is required to develop these estimates. Accordingly, the estimated fair values are not necessarily indicative of the amounts the Company could realize or would pay in a current market exchange. The estimated fair value amounts can be materially affected by the use of different assumptions or methodologies.

The Company categorizes its financial assets and liabilities measured at fair value into one of three different levels depending on the observability of the inputs used in the measurement.

Level 1: This level includes assets and liabilities measured at fair value based on unadjusted quoted prices for identical assets and liabilities in active markets that are accessible at the measurement date.

Level 2: This level includes valuations determined using directly (i.e., as prices) or indirectly (i.e., derived from prices) observable inputs other than quoted prices included within Level 1. Derivative instruments in this category are valued using models or other standard valuation techniques derived from observable market inputs.

Level 3: This level includes valuations based on inputs that are less observable, unavailable or where the observable data does not support a significant portion of the instruments' fair value.

The methods and assumptions used to estimate the fair value of financial instruments are described below:

- The estimated fair value of long-term debt bearing variable rates is considered to approximate its carrying value (Level 2).
- The estimated fair value of convertible redeemable preferred shares was determined by using an arms'-length transaction price (*note 12*) (Level 2).

There were no significant transfers between Level 1, Level 2 and Level 3 of the fair value hierarchy during the years ended December 31, 2017 and 2016.

## Notes to the consolidated financial statements

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December 31, 2017 and 2016

**20. Management of capital**

As at December 31, the Company's capital is as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
	\$	\$
Credit facility	<b>8,189,476</b>	3,399,362
Current portion of long-term debt	<b>128,810</b>	2,841,026
Long-term debt	<b>82,929</b>	187,727
Convertible redeemable preferred shares	—	30,226,003
Shareholders' equity (deficiency)	<b>19,091,145</b>	(29,134,153)
<b>Total capital under management</b>	<b>27,492,360</b>	<b>7,519,965</b>

The Company's objectives in managing capital are to ensure sufficient liquidity to pursue its organic growth, to establish a strong capital base so as to maintain investor, creditor and to provide an adequate return to shareholders.

The Company's primary uses of capital are to finance increases in non-cash working capital along with capital expenditures for its store expansion program.

The Company currently funds these requirements from cash flows from operations as well as its financial resources, which include cash balance, the line of credit (*note 9*), long-term debt (*note 11*) and through its issuances of Class B common shares (*note 15*). The Board of Directors does not establish quantitative return on capital criteria for management, but rather promotes year-over-year sustainable profitable growth. The Company is not subject to any externally imposed capital requirements.

There have been no changes with respect to the overall capital risk management strategy during the years ended December 31, 2017 and 2016.

## Notes to the consolidated financial statements

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### 21. Guarantees

Some agreements to which the Company is party, specifically those related to debt agreements and the leasing of its premises, include indemnification provisions that may require the Company to make payments to a third party for breach of fundamental representation and warranty terms in the agreements, with respect to matters such as corporate status, title of assets, environmental issues, consents to transfer, employment matters, litigation, taxes payable and other potential material obligations. The maximum potential amount of future payments that the Company could be required to make under these indemnification provisions is not reasonably quantifiable as certain indemnifications are not subject to a monetary limitation. As at December 31, 2017, management does not believe that these indemnification provisions would require any material cash payment by the Company, and insurance coverage, estimated by management to be reasonable and sufficient, exists in order to minimize the previously mentioned risks.

The Company indemnifies its directors and officers against claims reasonably incurred and resulting from the performance of their services to the Company, and maintains liability insurance for its directors and officers as well as those of its subsidiary.

### 22. Finance costs

	December 31, 2017 \$	December 31, 2016 \$
Credit facility and line of credit	202,491	327,406
Subordinated debt	93,453	186,570
Accretion expense on subordinated debt bonus <i>(note 11)</i>	18,279	473,072
Long-term debt	24,676	114,509
Amortization of financing fees and transaction costs	671,597	372,429
	<b>1,010,496</b>	<b>1,473,986</b>

### 23. Commitments and contingencies

#### a) Commitments

The Company has various operating leases for their warehouse, retail stores and head office. The annual minimum payments under these operating leases are as follows:

	\$
2018	759,816
2019	250,975
2020	149,818

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The schedule above includes commitments to a company controlled by the Company's Chief Executive Officer and Chief Operating Officer in the amounts of \$144,000, \$146,880 and \$149,818 for 2018 to 2020, respectively.

### b) Contingencies

On October 31, 2017, a formal claim was received by the Company totalling approximately \$1.1 million related to a terminated financing arrangement for the services of a financial advisor in the search of private equity capital. Management continues to believe that the claim is without merit, intends to defend itself vigorously, and therefore, no provision has been recorded in the consolidated financial statements.

### 24. Comparative figures

Certain comparative financial figures have been reclassified from those previously presented to conform to the presentation in the 2017 consolidated financial statements.

### 25. Subsequent events

On February 12, 2018, the Company issued 2,728,500 Class B common shares to a syndicate of underwriters including Canaccord, Desjardins Securities Inc., Cormark Securities Inc. and Industrial Alliance Securities Inc. at a price of C\$5.25 per share for gross proceeds of \$14,324,625. The net proceeds of the offering are expected to be used to accelerate the expansion of the Company's omni-channel sales network and for general corporate purposes.