

DIXIE BRANDS INC. AND SUBSIDIARIES

**CONSOLIDATED FINANCIAL STATEMENTS AS AT
AND FOR THE YEARS ENDED DECEMBER 31, 2018
AND 2017**

(Expressed in United States Dollars)

DIXIE BRANDS INC. AND SUBSIDIARIES
Management's Responsibility for Financial Reporting

To the Shareholders of DIXIE BRANDS INC. AND SUBSIDIARIES:

The accompanying consolidated financial statements and other financial information in this annual report were prepared by management of Dixie Brands Inc. and Subsidiaries (collectively, the "Company"), and reviewed and approved by the Board of Directors.

Management is responsible for the consolidated financial statements and believes that they fairly present the Company's financial condition and results of operations in conformity with International Financial Reporting Standards. Management has included in the Company's consolidated financial statements amounts based on estimates and judgments that it believes are reasonable, under the circumstances.

To discharge its responsibilities for financial reporting and safeguarding of assets, management believes that it has established appropriate systems of internal accounting control which provide reasonable assurance that the financial records are reliable and form a proper basis for the timely and accurate preparation of financial statements. Consistent with the concept of reasonable assurance, the Company recognizes that the relative cost of maintaining these controls should not exceed their expected benefits. Management further assures the quality of the financial records through careful selection and training of personnel and through the adoption and communication of financial and other relevant policies.

These financial statements have been audited by the Company's auditors, MNP, LLP, and their report is presented herein.

Charles Smith (signed)
Chief Executive Officer

Jim Feehan (signed)
Chief Financial Officer

April 30, 2019

DIXIE BRANDS INC. AND SUBSIDIARIES

Index to Consolidated Financial Statements

	Page
INDEPENDENT AUDITOR'S REPORT	1
CONSOLIDATED FINANCIAL STATEMENTS:	
Consolidated Statements of Financial Position	2
Consolidated Statements of Operations	3
Consolidated Statements of Changes in Shareholders' Equity (Deficit)	4
Consolidated Statements of Cash Flows	5-6
Notes to Consolidated Financial Statements.....	7-37

Independent Auditor's Report

To the Shareholders of Dixie Brands Inc.:

Opinion

We have audited the consolidated financial statements of Dixie Brands Inc. and its subsidiaries (the "Company"), which comprise the consolidated statement of financial position as at December 31, 2018, and the consolidated statements of operations, changes in shareholders' equity and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Basis for Opinion

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

Other Matter

The consolidated financial statements of the Company for the year ended December 31, 2017 were audited by another auditor who expressed an unmodified opinion on those consolidated financial statements on November 26, 2018.

Other Information

Management is responsible for the other information. The other information comprises Management's Discussion and Analysis.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. We obtained Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

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

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

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

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

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

The engagement partner on the audit resulting in this independent auditor's report is Sandra Alison Solecki.

Mississauga, Ontario

April 30, 2019

MNP LLP

Chartered Professional Accountants

Licensed Public Accountants

DIXIE BRANDS INC. AND SUBSIDIARIES

Consolidated Statements of Financial Position

As at December 31, 2018 and 2017

		<u>2018</u>	<u>2017</u>
ASSETS			
Cash		\$ 18,361,113	\$ 43,852
Accounts Receivable, net		2,266,733	1,859,405
Inventories	<i>Note 4</i>	950,938	509,708
Prepaid Expenses		411,295	33,965
Lease Receivable		-	21,405
Total Current Assets		<u>21,990,079</u>	<u>2,468,335</u>
Related Party Advances and Notes Receivable	<i>Note 11</i>	1,274,444	2,374,574
Property and Equipment, net	<i>Note 5</i>	959,374	900,047
Intangible Assets, net	<i>Note 6</i>	675,275	606,070
TOTAL ASSETS		<u>\$ 24,899,172</u>	<u>\$ 6,349,026</u>
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)			
LIABILITIES			
Accounts Payable		1,099,298	808,845
Prepaid License Fees	<i>Note 7</i>	4,000,000	-
Notes Payable, Current Portion	<i>Note 8</i>	775,000	5,441,721
Other Accrued Liabilities	<i>Note 17</i>	2,574,699	976,088
Accrued Payroll		276,426	105,470
Convertible Notes Payable	<i>Note 9</i>	-	364,574
Total Current Liabilities		<u>8,725,423</u>	<u>7,696,698</u>
Equipment Lease	<i>Note 17</i>	-	66,629
Notes Payable	<i>Note 8</i>	-	300,000
Derivative Liabilities	<i>Note 9</i>	238,100	498,232
Total Liabilities		<u>8,963,523</u>	<u>8,561,559</u>
SHAREHOLDERS' EQUITY (DEFICIT)			
Share Capital		40,226,961	8,959,408
Contributed Surplus		8,506,705	34,280
Common Shares to be issued		250,000	-
Accumulated deficit		(31,310,910)	(10,727,852)
Non-Controlling Interest	<i>Note 12</i>	(1,737,107)	(478,369)
Total Stockholders' Equity (Deficit)		<u>15,935,649</u>	<u>(2,212,533)</u>
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		<u>24,899,172</u>	<u>6,349,026</u>

Nature of Operations (Note 1)

Commitments and Contingencies (Note 17)

Subsequent Events (Note 19)

Approved on behalf of the Board on April 30, 2019

“Charles Smith” (signed)
 Director

“Vincent ‘Tripp’ Keber, III” (signed)
 Director

DIXIE BRANDS INC. AND SUBSIDIARIES

Consolidated Statements of Operations

For the Years Ended December 31, 2018 and 2017

		<u>2018</u>	<u>2017</u>
Revenues		\$ 5,791,451	\$ 3,339,387
Cost of Goods Sold		<u>2,773,549</u>	<u>1,763,777</u>
Gross Profit		<u>3,017,902</u>	<u>1,575,610</u>
Expenses:			
General and Administrative	<i>Note 14</i>	14,741,237	3,289,008
Sales and Marketing		1,189,618	793,275
Depreciation and Amortization		<u>196,904</u>	<u>251,611</u>
Total Expenses		<u>16,127,759</u>	<u>4,333,894</u>
Loss From Operations		<u>(13,109,857)</u>	<u>(2,758,284)</u>
Other Expense:			
Interest Expense	<i>Note 8</i>	644,598	744,129
Change in Fair Value of Derivative Liabilities	<i>Note 9</i>	(542,532)	110,610
Listing Expense	<i>Note 3</i>	6,695,137	-
Debt Settlement Expense	<i>Note 10</i>	1,535,015	-
Impairment of Contract asset		243,178	-
Other (Gains) / Loss		<u>(446,902)</u>	<u>726,915</u>
Total Other Expense		<u>8,128,494</u>	<u>1,581,654</u>
Net Loss Before Non-Controlling Interest		<u>(21,238,351)</u>	<u>(4,339,938)</u>
Non Controlling Interest		<u>(945,293)</u>	<u>(299,902)</u>
Net Loss Attributable to the Company		<u>\$ (20,293,058)</u>	<u>\$ (4,040,036)</u>
Earnings (Loss) Per Share - Basic and Diluted	<i>Note 13</i>	<u>\$ (0.36)</u>	<u>\$ (0.10)</u>
Attributable to Dixie Brands Inc.		\$ (0.35)	\$ (0.09)
Attributable to Non-Controlling Interest		\$ (0.01)	\$ (0.01)
Weighted-Average Shares Outstanding - Basic and Diluted	<i>Note 13</i>	<u>58,349,725</u>	<u>43,296,205</u>

DIXIE BRANDS INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Shareholders' Equity (Deficit) For the Years Ended December 31, 2018 and 2017

	Attributable to the shareholders of the Company									
	Common Shares #	Share Capital \$	Shares to be issued #	Shares to be issued \$	Preferred Shares #	Preferred Shares \$	Contributed Surplus	Accumulated Deficit	Non-Controlling Interest	TOTAL SHAREHOLDERS' EQUITY
BALANCE AS OF DECEMBER 31, 2016	43,205,668	\$ 8,887,136					\$ 13,002	\$ (6,687,816)	\$ (178,467)	\$ 2,033,855
Net Loss								\$ (4,040,036)	\$ (299,902)	\$ (4,339,938)
Issuance of Warrants							\$ 21,278			\$ 21,278
Incentive Share Compensation	479,796	\$ 72,272								\$ 72,272
BALANCE AS OF DECEMBER 31, 2017	43,685,463	\$ 8,959,408					\$ 34,280	\$ (10,727,852)	\$ (478,369)	\$ (2,212,533)
Adjustments Related to the Adoption of IFRS 9								\$ (290,000)		\$ (290,000)
Net Loss								\$ (20,293,058)	\$ (945,293)	\$ (21,238,351)
Series B Issuance					1,090,247	\$ 4,000,000				\$ 4,000,000
Series B Conversion	33,986,742	\$ 4,000,000			(1,090,247)	\$ (4,000,000)				\$ -
Series C Issuance	25,905,175	\$ 14,378,457								\$ 19,633,487
Academy Common Shares on Reverse Take-Over	6,640,300	\$ 6,640,301					\$ 5,255,031			\$ 6,734,757
Repurchase of Treasury Stock	(474,075)	\$ (550,000)					\$ 94,456			\$ (550,000)
Issuance of Treasury Stock	339,838	\$ 300,000	283,202	\$ 250,000						\$ 550,000
DBFN Convertible Debt	3,085,870	\$ 2,059,199					\$ 850,945		\$ (313,445)	\$ 2,596,699
Issuance of Warrants Related to Debt							\$ 6,617			\$ 6,617
Debt Conversion	1,613,130	\$ 1,424,025					\$ (14,319)			\$ 1,409,706
Issuance of Warrants							\$ 393,952			\$ 393,952
Exercise of Warrants	6,205,505	\$ 1,232,638					\$ (406,194)			\$ 826,444
Exercise of ACA Stock Options	75,000	\$ 70,842					\$ (70,842)			\$ -
Incentive Share Compensation	2,673,615	\$ 1,574,291								\$ 1,574,291
Stock Award	1,116,710	\$ 137,800								\$ 137,800
Stock Option							\$ 2,362,779			\$ 2,362,779
BALANCE AS OF DECEMBER 31, 2108	124,853,273	\$ 40,226,961	283,202	\$ 250,000	\$ -	\$ -	\$ 8,506,705	\$ (31,310,910)	\$ (1,737,107)	\$ 16,185,649

DIXIE BRANDS INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Years Ended December 31, 2018 and 2017

	2018	2017
OPERATING ACTIVITIES		
Net Loss	\$ (21,238,351)	\$ (4,339,938)
Adjustments to Reconcile Net Loss to Net Cash Used in Operating Activities:		
Depreciation and Amortization	396,691	472,683
Amortization of Debt Discount	159,212	237,797
Change in Fair Value of Derivative Liabilities	(542,532)	110,610
Legal Fees paid via the issuance of Warrants	393,952	-
Incentive Share-Based Payment	1,712,091	72,272
Listing Expenses	6,695,137	-
Stock Incentive Expense	2,362,779	21,278
Change in Credit Loss Reserve	1,910,484	-
Loss on Disposal of Property and Equipment	32,703	17,702
Loss on Disposal of Intangible Assets	28,500	-
Impairment of Contract Asset	243,178	-
Amortization of Contract Asset	39,222	-
DBI Warrants Cancelled on Repurchase of Debt	1,512,312	-
Loss on Impairment of Investments	-	741,408
Changes in:		
Accounts Receivable	(386,159)	(1,171,139)
Lease Receivable	21,405	24,245
Inventories	(441,230)	(52,142)
Prepaid Expenses	(377,330)	61,608
Accounts Payable	152,349	281,136
Accrued Payroll	170,956	66,559
Other Accrued Liabilities	3,867,759	557,506
NET CASH USED IN OPERATING ACTIVITIES	(3,286,873)	(2,898,415)

DIXIE BRANDS INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Years Ended December 31, 2018 and 2017

INVESTING ACTIVITIES		
Purchases of Property and Equipment	(288,934)	(6,246)
Purchase of Intangibles	(297,491)	(45,000)
Additions to Related Party Advances and Notes Receivable	(990,354)	(1,160,188)
Payments Received on Notes Receivable	-	638,217
Investments in Affiliate	-	(596,743)
NET CASH USED IN INVESTING ACTIVITIES	(1,576,779)	(1,169,960)
FINANCING ACTIVITIES		
Proceeds from Share Issuances	25,419,539	-
Cash Received from the Acquisition of Academy Explorations	46,559	-
Cash Received from the Exercise of Warrants	826,444	-
Proceeds from Issuance of Notes Payable	350,000	3,323,722
Payments on Debt	(3,395,000)	-
Payments on Equipment Lease	(66,629)	(36,261)
CASH FROM FINANCING ACTIVITIES	23,180,913	3,287,461
NET INCREASE (DECREASE) IN CASH	18,317,261	(780,914)
CASH, BEGINNING OF YEAR	43,852	824,766
CASH, END OF YEAR	\$ 18,361,113	\$ 43,852
	2018	2017
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash Paid for Interest	\$ 642,793	\$ 605,076
SUPPLEMENTAL NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Conversion of Related Party Advances to Notes Receivable	\$ -	\$ 750,000

DIXIE BRANDS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the Years Ended December 31, 2018 and 2017

1. NATURE OF OPERATIONS

Dixie Brands Inc. (“DBI” or the “Company”), formerly known as Academy Explorations Limited (“Academy”), was incorporated under the Business Corporations Act (British Columbia) on July 20, 1970. The Company’s Subordinate Voting Shares (“SVS”) are listed on the Canadian Securities Exchange under the symbol “DIXI.U”. The head office and principal address of the Company is 4990 Oakland Street, Denver, Colorado 80239. The Company’s registered and records office address is 3400 One First Canadian Place, Toronto, Ontario M5X 1B4. The Company operates through its wholly-owned subsidiary, Dixie Brands (USA), Inc, a Delaware corporation (“OpCo”). DBI has four other subsidiaries: (i) Therabis, LLC (“Therabis”) (60% ownership); (ii) Aceso Wellness, LLC (“Aceso”) (100% ownership); (iii) DB Finance, LLC (“DBFN”) (85% ownership) and (iv) DB Products Nevada, LLC (“DBPN”) (70% ownership).

Dixie Brands, Inc., a Delaware corporation (“USA Inc.”), and Academy entered into a definitive agreement (the “Amalgamation Agreement”) by and among Academy, Dixie Brands Acquisition, Inc. (“Amalco”), and USA Inc. in respect of the Amalgamation (as defined below). Pursuant to the Amalgamation Agreement, on November 27, 2018, Academy agreed to acquire all the issued and outstanding common stock in the capital of USA Inc. in exchange for SVS of Academy by way of a “three-cornered” amalgamation (the “Amalgamation”).

The Amalgamation resulted in USA Inc. merging with AmalCo and becoming OpCo and OpCo becoming a wholly-owned subsidiary of DBI.

References herein to the “Company” prior to November 27, 2018 means the USA Inc.

DBI owns the intellectual property, product branding, formulations, proprietary ingredients, consulting expertise, and preparation methods related to a variety of marijuana infused products, referenced herein as the “Dixie Product Line”. DBI has relationships with entities in Colorado, California, Nevada and Maryland who are locally licensed to manufacture cannabis products, including the Dixie Product Line. DBI designs and distributes packaging, ingredients, and non-cannabis consumer goods.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation

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”) and Interpretations of the IFRS Interpretations Committee (“IFRIC”) in effect for the years ended December 31, 2018 and 2017.

These consolidated financial statements were approved and authorized for issue by the Board of Directors of the Company on April 30, 2019.

Basis of Measurement

These consolidated financial statements have been prepared on a historical cost basis except for derivative financial instruments, which have been measured at fair value.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Functional Currency

The Company and its subsidiaries' functional currency, as determined by management, is the United States ("U.S.") dollar. These consolidated financial statements are presented in U.S. dollars.

Foreign Currency Transactions

Transactions denominated in currencies other than the business unit's functional currency are recorded at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange prevailing at the consolidated statement of financial position. Unrealized gains and losses on translation of monetary assets and liabilities are reflected in the consolidated statement of operations for the year.

Fair Value Measurements

Certain of the Company's assets and liabilities are measured at fair value. In estimating fair value, the Company uses market-observable data to the extent it is available.

Basis of Consolidation

Subsidiaries are entities over which the Company has control. The Company controls an entity when the Company is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Subsidiaries are fully consolidated from the date on which control is acquired by the Company and they are deconsolidated from the date that control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company using consistent accounting policies. All inter-company balances, revenues and expenses and earnings and losses resulting from inter-company transactions are eliminated on consolidation.

Non-controlling interest in the net assets of consolidated subsidiaries are a separate component of the Company's equity. Non-controlling interests consist of the non-controlling interests on the date of the original acquisition plus the non-controlling interests' share of changes in equity since the date of acquisition. Changes in the Company's interest in a subsidiary that do not result in a loss of control are account for as equity transactions.

The accompanying consolidated financial statements include the accounts of the following entities, DBI, Aceso, Therabis, DBFN, DBPN and USA Inc.

Cash and Cash Equivalents

Cash and cash equivalents include cash deposits in financial institutions and other deposits that are readily convertible into cash.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Inventories

Inventories purchased from third parties, which include proprietary ingredients, finished goods, and packaging and supplies, are valued using the weighted average costing method at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs to sell. The Company reviews inventories for obsolete, redundant and slow-moving goods and any such inventories identified are written down to net realizable value. At December 31, 2018 and 2017, management determined that no such reserve is necessary.

Investment in Affiliates

During the years ended December 31, 2018 and 2017, DBI made investments of \$0 and \$596,743, respectively, in affiliates in Arizona and Washington that operate similar to DBPN. During the year ended December 31, 2017, the Company determined that the investments are no longer viable and therefore, fully impaired the investment and recorded a loss of \$741,408, which is included in other expenses in the accompanying consolidated statements of operations.

Property and Equipment, net

Property and equipment are stated at cost, net of accumulated depreciation and impairment losses, if any. Expenditures that materially increase the life of the assets are capitalized. Ordinary repairs and maintenance, supplies, and property equipment with a cost of \$1,000 or less are expensed as incurred. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset using the following terms and methods:

Furniture and Fixtures	5 – 7 Years
Equipment	5 - 7 Years
Computer Equipment	5 Years
Leasehold Improvements	Lesser of the lease term or useful life
Leased Equipment	Lesser of the lease term or useful life

The assets' residual values, useful lives and methods of depreciation are reviewed at each financial year-end and adjusted prospectively if appropriate. An item of equipment is retired upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on sale or retirement of the asset (calculated as the difference between the net disposal proceeds and the carrying value of the asset) is included in the Consolidated Statements of Operations in the year the asset is retired. Such assets are tested annually for impairment, or more frequently, if events or changes in circumstances indicate that they might be impaired.

Intangible Assets

Intangible assets are recorded at cost, less accumulated amortization and impairment losses, if any. Intangible assets consist of license agreements purchased from Left Bank (see Note 6) and others for the right to recipes and methodologies. Amortization is recorded on a straight-line basis over their estimated useful lives from July 1, 2018 to June 30, 2023, which do not exceed the contractual period, if any. The estimated useful lives, residual values, and amortization methods are reviewed at each year-end, and any changes in estimates are accounted for prospectively. At December 31, 2018 and 2017, the Company did not recognize any impairment losses. Intellectual property is measured at fair value at the time of acquisition and is amortized on a straight-line basis over the useful life of the asset.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Income Taxes

Income tax expense is recognized in the consolidated statements of operations based on the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at year-end. For the years ended December 31, 2018 and 2017, DBI is taxed as a C-Corporation. In addition to DBI's income, all of the subsidiaries of DBI are treated as limited liability companies and, accordingly, DBI's proportionate share of taxable income and losses are flowed through to DBI.

Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

The Company recognizes the tax benefit from an uncertain tax position only if it is probably that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that is probable of being realized upon ultimate settlement. The amount of unrecognized tax benefits is adjusted as appropriate for changes in facts and circumstances, such as significant amendments to existing tax law, new regulations or interpretations by the taxing authorities, new information obtained during a tax examination, or resolution of an examination.

Lease Accounting

The Company leases some items of property, plant and equipment. A lease of property, plant and equipment is classified as a capital lease if it transfers substantially all the risks and rewards incidental to ownership to the Company. A lease of property, plant and equipment is classified as an operating lease whenever the terms of the lease do not transfer substantially all of the risks and rewards of ownership to the lessee. Lease payments are recognized as an expense on a straight-line basis over the lease term, except when another systematic basis is more representative of the time pattern in which the economic benefits are consumed.

Provisions for Contingencies

Provisions for contingencies include mainly legal and other claims. A provision is recognized when the Company has a legal or constructive obligation as a result of a past event and it is probable that settlement of the obligation will require a financial payment or cause a financial loss, and a reliable estimate of the amount of the obligation can be made.

If some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement is recorded in the consolidated statement of financial position as a separate asset, but only if it is virtually certain that the reimbursement will be received.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognized as a financing expense.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Research and Development

Research costs are expensed as incurred. Development expenditures are capitalized only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Company intends to and has sufficient resources to complete development to use or sell the assets. Other development expenditures are recognized in profit or loss as incurred.

Share-based compensation

The Company has a share option plan of which further details are given in Note 10.

The Company measures equity-settled share-based payments based on their fair value at the grant date and recognizes compensation expense over the period in which the service and, where applicable, the performance conditions are fulfilled (“the vesting period”) with a corresponding increase in equity (“contributed surplus”). Fair value is measured using the Black-Scholes option pricing model. The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company’s best estimate of the number of equity instruments that will ultimately vest.

The dilutive effect of outstanding options, warrants and convertible debentures is reflected as additional share dilution in the computation of diluted earnings per share (further details are given in Note 13).

Earnings (loss) per share

The Company presents basic and diluted loss per share data for its common shares. Basic loss per share is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted loss per share is determined by adjusting the loss attributable to common shareholders and the weighted average number of common shares outstanding, adjusted for the effects of all dilutive potential common shares, which comprise convertible debentures, warrants and share options issued.

Convertible Debentures

Convertible notes are compound financial instruments which are accounted for separately by their components; a financial liability and an equity instrument. The financial liability, which represents the obligation to pay coupon interest on the convertible notes in the future, is initially measured at its fair value and subsequently measured at amortized cost. The residual amount is accounted for as an equity instrument at issuance.

Significant Accounting Judgments Estimates and Assumptions

The preparation of the Company’s consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, and revenue and expenses. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the review affects both current and future periods.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Significant judgments estimates and assumptions that have the most significant effect on the amounts recognized in the consolidated financial statements are described below.

Estimated Credit Loss Provision

The Company performs impairment testing for accounts receivable in accordance with IFRS 9. The Expected Credit Loss (“ECL”) model requires considerable judgement, including consideration of how changes in economic factors affect ECLs, which are determined on a probability-weighted basis. IFRS 9 outlines a three-stage approach to recognize ECLs which is intended to reflect the increase in credit risks of a financial instrument based on 1) 12-month expected credit losses or 2) lifetime expected credit losses. The Company measures provision for ECLs at an amount equal to lifetime ECLs.

Estimated Useful Lives and Depreciation of Property and Equipment

Depreciation of property and equipment is dependent upon estimates of useful lives which are determined through the exercise of judgment. The assessment of any impairment of these assets is dependent upon estimates of recoverable amounts that take into account factors such as economic and market conditions and the useful lives of assets.

Estimated Useful Lives and Amortization of Intangible Assets

Amortization of intangible assets is recorded on a straight-line basis over their estimated useful lives, which do not exceed the contractual period, if any. Intangible assets that have indefinite useful lives are not subject to amortization and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired.

Derivative liabilities

The Company uses the fair-value method of accounting for derivative liabilities and such liabilities are re-measured at each reporting date with changes in fair value recorded in the period incurred. The fair value is estimated using a Monte Carlo simulation model. Critical estimates and assumptions used in the model are discussed in Note 9.

Taxes

Provisions for taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. It is possible, however, that at some future date, an additional liability could result from audits by taxing authorities. If the final outcome of these tax related matters is different from the amounts that are initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Non-controlling Interest

Non-controlling interest represents equity interests owned by parties that are not shareholders of the ultimate parent. Non-controlling interest is initially measured either at fair value or at the noncontrolling interest's proportionate share of the recognized amounts of the acquiree's identifiable net assets. The choice of measurement is made on a transaction-by-transaction basis. The share of net assets attributable to non-controlling interests is presented as a component of equity. Their share of net income or loss is recognized directly in equity. Changes in the parent company's ownership interest that do not result in a loss of control are accounted for as equity transactions.

Adoption of New Accounting Standards

IFRS 9 Financial Instruments ["IFRS 9"]

IFRS 9 addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. The effective date of this standard was January 1, 2018. The Company has adopted this new standard as of its effective date on a retrospective basis with the exception of financial assets that were derecognized at the date of initial application, January 1, 2018. The 2017 comparatives were not restated. The new classification and measurement of the Company's financial assets are as follows:

Classification

The Company classifies its financial assets and financial liabilities in the following measurement categories: i) those to be measured subsequently at fair value through profit or loss (FVTPL); ii) those to be measured subsequently at fair value through other comprehensive income (FVOCI); and iii) those to be measured at amortized cost. The classification of financial assets depends on the business model for managing the financial assets and the contractual terms of the cash flows. Financial liabilities are classified as those to be measured at amortized cost unless they are designated as those to be measured subsequently at FVTPL (irrevocable election at the time of recognition). For assets and liabilities measured at fair value, gains and losses are either recorded in profit or loss or other comprehensive income.

Amortized cost

This category includes financial assets that are held within a business model with the objective to hold the financial assets in order to collect contractual cash flows that meet the solely principal and interest ("SPPI") criterion. Financial asset classified in this category are measured at amortized cost using the effective interest method.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Fair value through profit or loss

This category includes derivative instruments as well as quoted equity instruments which the Company has not irrevocably elected, at initial recognition or transition, to classify at FVOCI. This category would also include debt instruments whose cash flow characteristics fail the SPPI criterion or are not held within a business model whose objective is either to collect contractual cash flows, or to both collect contractual cash flows and sell. Financial assets in this category are recorded at fair value with changes recognized in profit or loss. Financial assets at fair value through other comprehensive income Equity instruments that are not held-for-trading can be irrevocably designated to have their change in fair value recognized through other comprehensive income instead of through profit or loss. This election can be made on individual instruments and is not required to be made for the entire class of instruments. Attributable transaction costs are included in the carrying value of the instruments. Financial assets at fair value through other comprehensive income are initially measured at fair value and changes therein are recognized in other comprehensive income.

Measurement

All financial instruments are required to be measured at fair value on initial recognition, plus, in the case of a financial asset or financial liability not at FVTPL, transaction costs that are directly attributable to the acquisition or issuance of the financial asset or financial liability. Transaction costs of financial assets and financial liabilities carried at FVTPL are expensed in profit or loss.

Financial assets and financial liabilities with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest. Financial assets that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of the subsequent accounting periods. All other financial assets including equity investments are measured at their fair values at the end of subsequent accounting periods, with any changes taken through profit and loss or other comprehensive income (irrevocable election at the time of recognition). For financial liabilities measured subsequently at FVTPL, changes in fair value due to credit risk are recorded in other comprehensive income.

Summary of the Company's classification and measurements of financial assets and liabilities under IFRS9:

	Classification	Measurement
Cash	FVTPL	Fair value
Accounts receivable	Amortized cost	Amortized cost
Lease receivables	Amortized cost	Amortized cost
Related party advances and note receivables	Amortized cost	Amortized cost
Accounts payable and accrued liabilities	Amortized cost	Amortized cost
Convertible notes payable	Amortized cost	Amortized cost
Derivative Liability	FVTPL	Fair value
Long-term loans payable	Amortized cost	Amortized cost

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Impairment of financial assets

The adoption of IFRS 9 has fundamentally changed the Company's accounting of impairment losses for financial assets by replacing IAS 39's incurred loss approach with a forward-looking expected credit loss ("ECL") approach. IFRS 9 requires the Company to record an allowance for ECLs for all debt financial assets not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Company expects to receive. The shortfall is then discounted at an approximation to the asset's original effective interest rate.

IFRS 15 Revenue from Contracts with Customers [“IFRS 15”]

IFRS 15 was issued by the IASB in May 2014 and specifies how and when revenue should be recognized based on a five-step model, which is applied to all contracts with customers:

1. Identify the contract with a customer
2. Identify the performance obligation(s)
3. Determine the transaction price
4. Allocate the transaction price to the performance obligation(s)
5. Recognize revenue when/as performance obligation(s) are satisfied

IFRS 15 became effective for annual periods beginning on or after January 1, 2018 with early adoption permitted. The Company has adopted this new standard as of its effective date using the modified retrospective method of adoption, and have assessed no significant changes as a result of the adoption of this new standard on the current or prior periods.

Under IFRS 15, the revenue recognition model has changed from one based on the transfer of risks and rewards of ownership to the transfer of control. The Company's contracts with customers for the licensing of its formula and trademarks include multiple performance obligations. As the transfer of risks and rewards generally coincides with the transfer of control over time, the timing and amount of revenue considering discounts, rebates, and variable consideration, recognized from this principal revenue stream has not changed as a result of the adoption of this new standard.

The following is the Company's revenue recognition policy in accordance with IFRS 15:

IFRS 15, Revenue recognition

Revenue is recognized at the transaction price, which is the amount of consideration to which the Company expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties. The Company's contracts with customers for the grant of the right to use the license of the company include multiple performance obligations. The Company has concluded that revenues from licensing and manufacturing should be recognized over time.

Recent Accounting Pronouncements

The following IFRS standards have been recently issued by the IASB. The Company is assessing the impact of these new standards on future consolidated financial statements. Pronouncements that are not applicable or where it has been determined do not have a significant impact to the Company have been excluded herein.

IFRS 16, Leases

In January 2016, the IASB issued IFRS 16, Leases, which will replace IAS 17, Leases. This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than twelve months unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments.

The standard will be effective for annual periods beginning on or after January 1, 2019, with earlier application permitted for entities that apply IFRS 15 at or before the date of initial adoption of IFRS 16. The Company expects the impact on its consolidated financial statements to be insignificant. However, upon adoption of IFRS 16, the leases described in Note 11 will likely constitute right of use assets with a corresponding lease obligation.

3. REVERSE TAKEOVER TRANSACTION

As of September 28, 2018, the Company entered into a definitive agreement (the “Transaction”) with Academy Explorations Limited (“Academy”) pursuant to which the Company would affect a Reverse Takeover Transaction (“RTO”) of Academy. Immediately prior to the Transaction, Academy completed a share consolidation, resulting in an aggregate of approximately 26,567,234 post-consolidation common shares outstanding pre-Transaction, and a name change to Dixie Brands Inc. The former shareholders of Academy retained 6,641,807 shares in the continuing entity which is accounted for as a deemed issuance of shares.

As a result, a non-cash listing expense of \$6,695,137 has been recorded in the statement of operations and comprehensive loss. As part of the Transaction, unit holders of Dixie Brands, Inc. exchanged their ownership for Class B Redeemable shares in Dixie Brands Inc. (the legal subsidiary and accounting acquiror). The Transaction was completed on November 27, 2018 and the Class B Subordinate Voting Shares of the Company began trading on the Canadian Securities Exchange under the ticker “DIXI” on November 29, 2018.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Based on the statement of financial position of Academy at the time of the RTO, the net assets at estimated fair value that were acquired by the Company were listed as follows:

Consideration	
Shares - 6,640,301 shares (Note 10)	\$ 6,640,301
Options - 100,000 stock options (Note 10)	94,287
	<u>\$ 6,734,588</u>

Identifiable assets acquired	
Cash	\$ 46,559
Accounts receivable	130,996
Accounts payable	(138,104)
	39,451
Transaction cost	6,695,137
Total net identifiable assets and transaction costs	<u>\$ 6,734,588</u>

4. INVENTORIES

At December 31, inventories consist of the following:

	<u>2018</u>	<u>2017</u>
Raw Materials:		
Materials	\$ 255,850	\$ 308,916
Ingredients	460,391	117,332
Total Raw Materials	716,241	426,248
Finished Goods	234,697	83,460
Total Inventories	<u>\$ 950,938</u>	<u>\$ 509,708</u>
Cost of Goods Sold	<u>\$ 1,289,132</u>	<u>\$ 1,763,777</u>

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

5. PROPERTY AND EQUIPMENT

At December 31, 2018, property and equipment consists of the following:

	<u>Furniture and Fixtures</u>	<u>Equipment</u>	<u>Computer Equipment</u>	<u>Leasehold Improvements</u>	<u>Leased Equipment</u>	<u>Total</u>
Cost:						
December 31, 2017	\$ 174,934	\$ 232,433	\$ 64,643	\$ 508,378	\$ 406,809	\$ 1,387,197
Additions	-	212,934	42,500	-	33,500	288,934
Disposals	-	-	-	-	35,676	35,676
December 31, 2018	<u>174,934</u>	<u>445,367</u>	<u>107,143</u>	<u>508,378</u>	<u>404,633</u>	<u>1,640,455</u>
Accumulated Depreciations:						
December 31, 2017	67,907	130,941	37,345	170,654	80,303	487,150
Depreciation	24,991	53,123	12,349	55,571	47,897	193,931
December 31, 2018	<u>\$ 92,898</u>	<u>\$ 184,064</u>	<u>\$ 49,694</u>	<u>\$ 226,225</u>	<u>\$ 128,200</u>	<u>\$ 681,081</u>
Carrying Amounts:						
December 31, 2017	\$ 107,027	\$ 101,492	\$ 27,298	\$ 337,724	\$ 326,506	\$ 900,047
December 31, 2018	\$ 82,036	\$ 261,303	\$ 57,449	\$ 282,153	\$ 276,433	\$ 959,374

A reconciliation of the beginning and ending balances of property and equipment is as follows for 2017:

	<u>Furniture and Fixtures</u>	<u>Equipment</u>	<u>Computer Equipment</u>	<u>Leasehold Improvements</u>	<u>Leased Equipment</u>	<u>Total</u>
Cost:						
December 31, 2016	\$ 174,934	\$ 328,505	\$ 61,747	\$ 506,703	\$ 326,764	\$ 1,398,653
Additions	-	-	2,896	3,350	80,046	86,292
Disposals	-	96,073	-	1,675	-	97,748
December 31, 2017	<u>174,934</u>	<u>232,433</u>	<u>64,643</u>	<u>508,378</u>	<u>406,809</u>	<u>1,387,197</u>
Accumulated Depreciations:						
December 31, 2016	42,916	84,133	24,996	112,062	21,432	285,539
Depreciation	24,990	46,808	12,349	58,592	58,872	201,611
December 31, 2017	<u>\$ 67,906</u>	<u>\$ 130,941</u>	<u>\$ 37,345</u>	<u>\$ 170,654</u>	<u>\$ 80,304</u>	<u>\$ 487,150</u>

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

6. INTANGIBLE ASSETS

At December 31, intangible assets consist of the following:

	Balance at January 1, 2017	Purchases	Disposals	Amortization Expense	Balance at December 31, 2017
Formula	\$ -	\$ 45,000	\$ -	\$ 7,500	\$ 37,500
Intellectual Property	782,142	-	-	213,572	568,570
Total Intangible Assets	\$ 782,142	\$ 45,000	\$ -	\$ 221,072	\$ 606,070
	Balance at January 1, 2018	Purchases	Disposals	Amortization Expense	Balance at December 31, 2018
Formula	\$ 37,500	\$ -	\$ (28,500)	\$ 9,000	\$ -
Intellectual Property	568,570	297,491	-	190,786	675,275
Total Intangible Assets	\$ 606,070	\$ 297,491	\$ (28,500)	\$ 199,786	\$ 675,275

7. PREPAID LICENSE FEES

On May 7, 2018 Dixie Brands, Inc. entered into a license agreement with Auxly Cannabis Group Inc. (“Auxly”) (formerly Cannabis Wheaton Income Corp.). The agreement grants Auxly the right to prepare, distribute, promote, and sell Dixie Brands, Inc. products. The license agreement is to expire, without notice on May 7, 2028, unless it has been earlier terminated, renewed or extended. The terms of the agreement may be extended by Auxly for two additional periods (5 years per period). Under the agreement, Auxly shall pay the Company a royalty fee of 7.5% of the gross revenues attributable to the sales of the Company’s products. The total amount of the prepayment received was \$4,000,000. In the event that “elixirs”, “mints” and “chocolates” are not permitted under the Cannabis Act in Canada by December 31, 2018 (in a form and substance substantially similar to how Licensor currently produces such products, the amount of the fee pre-payment shall immediately revert to the sum of seven hundred and fifty thousand dollars and Dixie Brands, Inc shall return to Auxly any fee pre-payment, in excess of that amount. See Note 18 for return of pre-payment.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

8. NOTES PAYABLE

At December 31, notes payable consist of the following:

	<u>2018</u>	<u>2017</u>
Unsecured convertible promissory note dated April - September 2016, matured in July, 2017 and was subsequently extended July 2018; 50% of payment is due in full at maturity and 50% will be converted into shares of DBFN, interest is accrued at 8% per annum, paid quarterly. On July 31, 2018, this debt was modified to such that 50% of the note will be converted into DBI shares instead of paid out in cash.	\$ -	\$ 1,075,000
Unsecured promissory notes dated April 2016, payment in full is due on demand, interest is accrued at 12% per annum for the first 6 months and at 18% thereafter, paid quarterly.	-	150,000
Unsecured promissory notes dated July 2016, matured in July 2018; payment in full is due on the maturity date of the note, interest is accrued at 12% per annum, paid quarterly.	-	250,000
Unsecured promissory notes dated November - December, 2016, matured in May - June, 2018; payment in full is due on the maturity date of note, interest is accrued at 12% per annum, paid quarterly.	-	900,000
Unsecured promissory notes dated January - June, 2017, matured in July, 2018 - January 2019; payment in full is due on the maturity date of the note, interest is accrued at 12% per annum, paid quarterly.	-	2,045,000
Unsecured promissory notes dated October - December, 2017, matured in October - December, 2018; payment in full is due on maturity date of the note, interest is accrued at 12% per annum, paid quarterly.	-	825,000
Unsecured promissory notes dated March 2018, matured in September 2018; payment in full is due on the maturity date of the note, interest is accrued at 12% per annum, paid quarterly.	-	-
Secured promissory note dated September 8, 2017, which matures on July 13, 2018; interest is accrued at of 8% per annum. On May 14, 2108 this note is extended to May 14, 2019. Payment in full is due on the extended maturity date of the note, the modified interest accrues at 12% per annum, payment is made quarterly	250,000	250,000
Secured promissory note dated September 8, 2017, which matures on July 13, 2018; interest is accrued at of 8% per annum. On May 14, 2108 this note is extended to May 14, 2019. Payment in full is due on the extended maturity date of the note, the modified interest accrues at 12% per annum, payment is made quarterly	275,000	275,000
Unsecured promissory note dated May 2018, which matures in May 2019; payment in full is due on maturity date of the note, interest is accrued at 12% per annum, paid quarterly.	250,000	-
	<u>775,000</u>	<u>5,770,000</u>
Total Notes Payable	775,000	5,770,000
Less: Discounts	-	28,279
Less: Current Portion of Notes Payable	<u>775,000</u>	<u>5,441,721</u>
Notes Payable, Net of Current Portion	<u>\$ -</u>	<u>\$ 300,000</u>

In 2018, DBI settled promissory notes collectively totaling \$2,450,000 through conversion into common shares and through Series C financing (see Note 10).

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

In addition, DBI settled promissory notes collectively totaling \$3,245,000 with cash through Series C financing proceeds.

Total interest expense incurred in the year relating to notes payables is \$644,598.

In 2018, the Company distributed 27,548 warrants (136,334 in 2017) to purchase DBI's common shares at \$1.42 per share, in connection with the issuance of debt (see Note 10). The instrument meets the equity criteria under IFRS 9. As such the warrants have been classified as an equity instrument. The DBI notes' fair value were recorded on initial recognition and will be accreted to the full principal over the expected term.

The fair value of the warrants was calculated using a Monte Carlo simulation, with the following assumptions:

	<u>2018</u>	<u>2017</u>
Risk-free Rate	2.63%	1.39%
Expected Dividend Yield	0%	0%
Expected Term (in years)	1.56	0.5
Warrant Components	Initial Allocated Value	
	<u>2018</u>	<u>2017</u>
Notes	\$ 93,383	\$ 2,023,722
Warrant	<u>6,617</u>	<u>21,278</u>
Total Principal	<u>\$ 100,000</u>	<u>\$ 2,045,000</u>

9. CONVERTIBLE NOTE AND DERIVATIVE LIABILITIES

At December 31, convertible note payable consist of the following:

	<u>2018</u>	<u>2017</u>
Unsecured convertible promissory note dated July, 2016, matured in July, 2017 and was subsequently extended July 2018; payment is due in full at maturity or to be converted into shares of DBI, interest is accrued at 8% per annum, paid quarterly.	\$ -	\$ 500,000
Less: Unamortized accretion expense	<u>-</u>	<u>135,426</u>
Convertible Note Payable	<u>\$ -</u>	<u>\$ 364,574</u>

DIXIE BRANDS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the Years Ended December 31, 2018 and 2017

DBI issued a convertible promissory note in July 2016 for \$500,000 (“Note”). The Note matures on the earlier of 2 years or the Company raising at least \$10 million of capital. The Note is convertible into Series B preferred shares at 50% of the price per share under the Series B raise. Since the number of shares to be issued is unknown, the instrument did not meet the “fixed for fixed” criteria under IAS 32 - Financial Instruments: Presentation (“IAS 32”). As such, the conversion option was classified as a derivative liability and accounted for at fair value through profit and loss (“FVTPL”). The Note’s fair value was recorded on initial recognition and will be accreted to the full principal over the expected term. Key assumptions used in the valuation include an expected term of two years from the inception date. Issuance costs were allocated to the conversion option and expensed in the period incurred, as these instruments are at FVTPL. In April 8, 2018, the Company paid the convertible note in cash for \$500,000.

The fair values of the conversion option (“derivative liability”) was \$498,232 as at December 31, 2017 and was calculated using a Monte Carlo simulation, with the following assumptions:

	<u>Inception</u>	<u>December 31, 2017</u>
Risk-free Rate	1.20%	1.39%
Expected Dividend Yield	0%	0%
Expected Term (in years)	2.0	0.50
Volatility	77%	69%

In 2018, this derivative liability was derecognized, at the settlement date of the convertible note, into the Income Statement as a gain on change in fair value of derivative liability.

During the year ended December 31, 2018, the Company entered into the manufacturing agreement with one of its customers, Cypress Manufacturing Company (“Cypress”). Included in this manufacturing agreement, Cypress will be granted stock options (“Incentive Options Award”) by the Company to purchase voting common stock as an incentive for meeting mutually agreed upon revenue targets, pursuant to the Company’s Employee Stock Option Plan. Since the number of options to be granted is unknown, the instrument did not meet the “fixed for fixed” criteria under IAS 32 - Financial Instruments: Presentation (“IAS 32”). As such, the conversion option was classified as a derivative liability and accounted for at fair value through profit and loss (“FVTPL”). Key assumptions used in the valuation include an expected term of two years from the inception date. The fair value of the conversion option (“derivative liability”) was valued at \$282,400 on inception date (August 1, 2018) and revalued to \$238,100 on December 31, 2018, using Monte Carlo simulations, with the following assumptions:

	<u>Inception</u>	<u>December 31, 2018</u>
Risk-free Rate	2.60%	2.59%
Expected Dividend Yield	0%	0%
Expected Term (in years)	1.50	1.08
Volatility	70%	74%

The total change in the fair value of the derivative liabilities during the year ended December 31, 2018 is \$542,532.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

10. SHAREHOLDERS' EQUITY

All Common Share and Preferred Share amounts are applied retrospectively to reflect the RTO share split on the basis of 1 to 10.535, unless otherwise noted.

Comparative Figures

Changes in terminology of line items are due to the fact that the entity is now subject to the Business Corporations Act (British Columbia) in Canada as opposed to United States in the prior year.

Shareholder Equity as at			
December 31, 2017	2018 Format		2017 Format
Share Capital	8,959,408	Additional Paid in Capital	8,800,000
Contributed Surplus	34,280	Contributed Surplus	-
Accumulated Deficit	(10,727,852)	Reserve	193,688
Non-Controlling Interest	(478,369)	Accumulated Deficit	(10,727,852)
	<u>(2,212,533)</u>	Non-Controlling Interest	<u>(478,369)</u>
			<u>(2,212,533)</u>

Share Capital

Series B Issuance

During the year ended December 31, 2018, the Company raised \$4,000,000 in Series B financing through the issuance of 1,090,247 Preferred Shares (Pre-RTO shares). At the conclusion of Series C financing (defined below), 1,090,247 preferred shares were converted into 3,226,079 shares of common stock (33,986,742 post-RTO shares).

As a part of the Series B financing, the Company incurred \$792,948 of share issuance costs which have been paid with the issuance of 75,265 pre-RTO Common Shares (792,915 post-RTO shares).

Series C Issuance

During the year ended December 31, 2018, the Company raised \$19,633,487 in net proceeds in Series C financing through the issuance of 2,458,963 pre-RTO DBI Financing Units (25,905,175 post-RTO Units). Each Financing Unit consists of one Common Share and one Warrant. As part of the Series C financing, the Company also issued 153,121 pre-RTO Financing Units (1,613,130 post-RTO Units) to cancel \$1,375,000 of debt, 91,667 of warrants, and \$55,200 of accrued but unpaid interest on note payables.

As a part of the Series C financing, the Company incurred \$2,761,970 of share issuance costs. As of December 31, 2018, \$741,976 of costs have been paid in cash, \$140,000 have been paid with the issuance of 15,053 pre-RTO Common Shares (158,583 post-RTO shares), and the remaining \$1,879,994 costs remain unpaid at December 31, 2018.

Conversion of DBFN Note

During the year ended December 31, 2018, the Company signed modification agreements with DBFN note holders to extinguish 50% of the principal amount of the note payable through the issuance of 292,916 pre-

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

RTO Common Shares (3,085,870 post-RTO Shares). DBI incurred a loss of \$1,535,015 on the settlement of this note.

Stock Incentive Plan

The Company's 2015 Incentive Shares Plan (the Plan), which is shareholder-approved, permits the grant of shares to its employees and other service providers for up to 400,000 shares of common stock (4,214,000 post-RTO shares) with various vesting terms. Share awards generally vest over three years. The entire plan had accelerated vesting during 2018 upon RTO and all outstanding shares became fully vested. The fair value of each share award on the grant date was calculated using Black Scholes model, with the following assumptions:

	December 31, 2018
Grant Date Fair Value	\$0.69
Exercise Price	\$0.00
Expected Dividend Yield	\$0.00
Risk-Free Interest Rate	2.76%
Expected Option Life in Years	3
Expected Volatility	70%

A summary of activity under the Plan for the years ending December 31, 2018 and 2017 is presented below:

	<u>Restricted Stock Units</u>
Outstanding at January 1, 2017	630,467
Granted	410,865
Vested	(479,796)
Forfeited	-
	<hr/>
Outstanding at December 31, 2017	561,537
Granted	2,107,000
Vested	(2,668,537)
Forfeited	-
	<hr/>
Outstanding at December 31, 2018	-
Vested and expected to vest at December 31, 2018	<u><u>4,214,000</u></u>

The weighted-average grant-date fair value of shares granted during the years December 31, 2018 and 2017 is \$0.69 and \$0.16, respectively. The total compensation expense recognized during the years ended December 31, 2018 and 2017 is \$1,574,291 and \$72,272, respectively, and is included in general and administrative expense in the accompanying consolidated statements of operations. Key assumptions used in the valuation include forfeitures are accounted for on an individual basis and the risk free rate was 2.76% at December 31, 2018 and 1.05% at December 31, 2017.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Stock Awards

Under Stock Award program, the Company has written agreement of issuance of 120,000 shares (1,264,200 post-RTO shares) to TBSK LLC (“TBSK”). 14,000 shares were issued under Stock Incentive Plan and the remaining 106,000 shares were issued to TBSK in full in 2018.

Stock Options

A summary of the status of the stock options outstanding follows:

	Stock options	Weighted average exercise price
	#	\$
Balance, as at December 31, 2017	—	—
Issued ⁽¹⁾	15,362,265	0.73
Exercised ⁽²⁾	(75,000)	(0.08)
Balance, as at December 31, 2018	15,287,265	0.65

- (1) Each stock option entitles the holder to purchase one common share
Included in 15,362,265 stock options, 100,000 academy stock options are exercisable at C\$0.08.
- (2) 75,000 academy stock options are exercised on December 14, 2018

Share Purchase Warrants

Each whole warrant entitles the holder to purchase one common share of the Company. A summary of the status of the warrants outstanding as follows:

	Warrants classified as equity	Weighted average exercise price
	#	\$
Balance, as at December 31, 2016	807,687	1.42
Issued	1,436,279	1.42
Balance, as at December 31, 2017	2,243,966	1.42
Issued	31,350,348	1.42
Exercised	(6,205,505)	(1.42)
Cancelled	(965,712)	(1.42)
Balance, as at December 31, 2018	26,423,097	1.42

Non-Participating Voting Shares

Before RTO, the Company issued 500,000 Non-Participating Voting Shares to management. These Non-Participating Shares have no economic value or rights to dividends. They were first issued in the form of management options, exercisable at \$20 per share and were later automatically exercised to shares upon RTO. Each Non-Participating Voting share entitles the holder to one hundred votes and each Subordinated Voting Share entitles the holder to one vote, voting together as a single class.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

11. RELATED PARTY TRANSACTIONS

Transactions with related parties are entered into in the normal course of business and are measured at the amount established and agreed to by the parties.

Left Bank LLC d/b/a Dixie Elixirs & Edibles (“Left Bank”)

One Director of the Company is the sole owner of Left Bank.

The Company purchased the intellectual properties (Note 6) from Left Bank in 2015 for \$1,000,000.

The Company leases the facility for DBI from Left Bank under a sub-lease agreement that expired in November 2018. Currently the Company leases the building under a month to month agreement. Annual rent is not to exceed \$209,907. Total rent expense paid to Left bank for the years ended December 31, 2018 and 2017 is \$192,415 and \$202,093, respectively. Left Bank holds inventory on behalf of the Company at the facility for a total amount of \$111,253 at December 31, 2018.

In July 2018, DBI entered into a new manufacturing agreement with Left Bank for a total term of 3 years which entitles DBI to 85% of the gross revenue generated by Left Bank and DBI also reimburses certain production costs generated by Left Bank.

In addition to the above arrangements between the Company and Left Bank, DBI incurred shared expenses with Left Bank for accounting services provided by DBI accounting team and consultants for \$126,000, owed by Left Bank. The Company also incurred various shared expenses with Left Bank for \$393,511, owed by Left Bank.

Purchases and sales between Left Bank and DBI are recorded in accounts payable or accounts receivable. In 2018, the Company earned \$3,242,216 of packaging revenue and \$143,470 of raw materials and ingredients resale revenue. DBI also incurred \$1,359,171 of cost of goods sold reimbursements based on the new manufacturing agreement with Left Bank. As a result, the Company wrote off the accounts receivable balance from Left Bank of \$1,359,171 to offset the accounts payable balance.

At December 31, 2018 and 2017, the Company had \$2,793,198 and \$812,930, respectively of accounts receivable from Left Bank. The Company recorded an ECL provision for Left Bank under IFRS 9 for \$1,390,000 for accounts receivable and for \$143,820 for notes receivable.

Dixie Holdings

Dixie Holdings is jointly owned by the CEO of DBI and one of the Directors of the Company. DBI purchased intangible assets from Dixie Holdings (Note 6) in 2018 for \$297,492.

DBI has a note receivable from Dixie Holdings, for \$186,816 and \$67,700, as at December 31, 2018 and 2017, respectively. The note accrued interest at 2% per annum and are payable at maturity in December 2018. Interest on this note is not significant as at December 31, 2018 and 2017. On December 31, 2018, the full balance of \$186,816 was written off as bad debt expenses.

During the year, DBI wrote off an additional \$136,333 of related party advances from Dixie Holdings as bad debt expenses.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Silver State Wellness

Silver State Wellness owns 30% of DBPN. In October 2016, DBPN issued \$675,000 under a note receivable bearing interest at 12% from Silver State Wellness. DBPN had non-interest-bearing advances receivable from Silver State Wellness for \$656,887 and \$868,207 as at December 31, 2018 and 2017, respectively.

DBPN has equity contributions receivable of \$228,263 as at December 31, 2018 and 2017 from Silver State Wellness. At December 31, 2018 and 2017, the Company had \$1,107,741 and \$868,207, respectively of accounts receivable from Silver State Wellness including \$655,209 of affiliate packaging revenue and \$133,882 of materials and ingredients resale revenue. The Company also incurred \$761,513 of COGS reimbursement due to Silver State Wellness based on the licensing agreement. The Company recorded an ECL provision for Silver State Wellness under IFRS 9 for \$530,369.

DBI has \$10,006 worth of accounts receivable and Therabis also has \$28,781 worth of accounts receivable from Silver State Wellness.

Rose Capital Fund

Rose Capital Fund owns 25% of Therabis. In May 2018, Therabis issued \$775,000 under promissory notes bearing interest at 12% to Rose Capital Fund.

During the year, RSG 3 (which is Rose Capital Fund), and Rose Capital Fund I LP, exercised a total of \$826,444 worth of warrants.

Auxly

One of the Directors of the Company is an officer of Auxly. During the year the Company entered into a licensing agreement with Auxly and received a prepayment of \$4,000,000. Subsequent to the year end, \$3,250,000 has been returned to Auxly (see Note 7).

Series C Financing Settlements

During the year, DBI paid out a total of \$2,845,000 of promissory notes payable to related party debtholders through the issuance of Series C financing. In addition, \$450,000 worth of notes payable were converted into common shares of the Company through Series C financing.

The Company incurred \$283,000 of finder's fees payable to certain Directors of the Company.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Related party advances and notes receivable:

At December 31, related party advances and notes receivable consist of the following:

	<u>2018</u>	<u>2017</u>
Left Bank	\$ 1,755,886	\$ 974,988
Dixie Holdings	186,816	67,700
Silver State Wellness	<u>1,331,887</u>	<u>500,000</u>
 Total Related Party Notes Receivable	 <u>3,274,589</u>	 <u>1,542,688</u>
 Related Party Advances	 97,155	 831,886
Less: Fair Value Adjustments on Notes Receivable	429,919	-
Less: Allowance on Related Party Advances	<u>1,667,381</u>	<u>-</u>
 Total Related Party Advances and Notes Receivable	 <u>\$ 1,274,444</u>	 <u>\$ 2,374,574</u>

DBI holds two notes receivable from Left Bank. The first note for \$633,333 and the second note is for \$1,122,553. During the year, both notes receivables were extended to June 2022. The notes accrue interest at 2% per annum and are payable at maturity in June 2022. Interest on these notes is not significant as at December 31, 2018 and 2017.

Compensation of key management personnel:

The Company's key management personnel have the authority and responsibility for planning, directing and controlling the activities of the Company and consists of the Company's executive management team and management directors.

	<u>2018</u>	<u>2017</u>
Management Compensation	\$ 621,365	\$ 500,000
Stock Incentives	2,362,780	-
Share-Based Compensation	<u>1,712,091</u>	<u>-</u>
	<u>\$ 4,558,436</u>	<u>\$ 500,000</u>

During 2018, the Company issued a total of \$398,094 of cash bonuses to key management personnel. Throughout the year, there are \$1,712,091 worth of incentive shares being exercised through the Series C offering. The Company also issued a total of \$2,362,780 worth of stock options to key management personnel.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

12. NON-CONTROLLING INTEREST

The Company has non-controlling interests attributable to the non-controlling interest. The following table summarizes the comprehensive income attributable to the non-controlling shareholders for the year ended December 31, 2018 and December 31, 2017:

	2018	2017
Net Assets of the NCI, January 1,	(478,369)	(178,467)
Net Income Attributable to NCI	(945,293)	(299,902)
Adjustment to NCI Due to DBFN Debt Conversion	(313,445)	-
Net Assets of the NCI, December 31,	(1,737,107)	(478,369)

13. EARNINGS (LOSS) PER SHARE

The following is a reconciliation for the calculation of basic and diluted earnings (loss) per share for the year ended December 31, 2018.

	<u>2018</u>	<u>2017</u>
Net Loss	\$ (21,238,351)	(4,339,938)
Weighted-Average Number of Shares and Units Outstanding	58,349,725	43,296,205
Earnings (Loss Per Share - Basic and Diluted)	<u>\$ (0.36)</u>	<u>\$ (0.10)</u>
Attributable to Dixie Brands Inc	\$ (0.35)	\$ (0.09)
Attributable to Non-Controlling Interest	\$ (0.01)	\$ (0.01)

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

14. GENERAL AND ADMINISTRATIVE EXPENSES

For the years ended December 31, 2018 and 2017, general and administrative expenses consisted of the following:

	<u>2018</u>	<u>2017</u>
Bad Debt	\$ 3,708,095	\$ 211,539
Salaries and Benefits	2,665,705	1,608,072
Stock Incentives	2,362,780	-
Professional Fees	1,809,778	102,044
Share-Based Compensation	1,712,091	72,272
Other General and Administrative	601,825	409,034
Office Expense	534,379	7,931
Legal	343,408	207,585
Travel and Entertainment	297,008	87,740
Rent	271,433	227,066
Lobbying Expense	162,648	100,000
Insurance	118,254	111,349
Employee Benefits	114,611	144,376
Amortization of Contract Assets	39,222	-
	<u>\$ 14,741,237</u>	<u>\$ 3,289,008</u>

15. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

The Company has adopted IFRS 9 - Financial Instruments (“IFRS 9”), which replaced IAS 39 - Financial Instruments: Recognition and Measurement. The revised guidance changed the classification and measurement of financial assets and liabilities. Under IFRS 9, financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows.

Under IFRS 9, the Company has recorded \$2,085,689 as expected credit loss (ECL) on trades receivable as at December 31, 2018 (January 1, 2018 - \$190,000). The Company has also recorded \$1,331,887 in ECL on the notes receivable from Silver State Wellness (“SSW”) (January 1, 2018 - \$100,000). The Company has further recorded \$143,820 in ECL on the notes receivable from Left Bank (“LB”).

IFRS 9 contains three primary measurement categories for financial assets: measured at amortized cost, FVTPL and fair value through other comprehensive income. The Company’s financial assets are measured at amortized cost or FVTPL.

The Company determines classification of financial assets at initial recognition. The Company’s accounting policy in respect to its financial instruments is as follows:

(i) Financial assets are classified and measured at FVTPL unless they meet the following criteria for amortized cost:

- The Company plans to hold the financial assets in order to collect contractual cash flows; and
- Payments received on the financial assets are solely payments of principal and interest on the principal amount outstanding.

(ii) Financial liabilities - non-derivative financial liabilities are measured at amortized cost unless they have been designated as FVTPL. Derivative liabilities are initially measured at FVTPL, with subsequent changes in fair market value recognized in the Consolidated Statements of Operations.

(iii) Compound financial instruments - the component parts of compound instruments issued by the Company are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability is measured separately using an estimated market rate for a similar liability without an equity component and the residual is allocated to the conversion option. The liability component is subsequently recognized on an amortized cost basis using the effective interest method until extinguished upon conversion or at the instrument’s maturity date. The equity component is recognized and included in equity and is not subsequently re-measured. In addition, the conversion option classified as equity will remain in equity until the conversion option is exercised, in which case, the balance recognized in equity will be transferred to share capital. Transaction costs are divided between the liability and equity components in proportion to their values.

Financial instruments recorded at fair value are classified using a fair value hierarchy that reflects the significance of the inputs used to make the measurements. The hierarchy is summarized as follows:

- Level 1 quoted prices (unadjusted) that are in active markets for identical assets or liabilities
- Level 2 inputs that are observable for the asset or liability, either directly (prices) for similar assets or liabilities in active markets or indirectly (derived from prices) for identical assets or liabilities in markets with insufficient volume or infrequent transactions
- Level 3 inputs for assets or liabilities that are not based upon observable market data

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

The Company classifies its financial instruments as follows:

Financial Instrument	Classification	Fair Value Hierarchy
Cash	FVTPL	Level 1
Accounts and Lease receivables	Amortized cost	N/A
Accounts payable and accrued payroll and other liabilities	Amortized cost	N/A
Promissory notes receivable	Amortized cost	N/A
Derivative liabilities	FVTPL	Level 3
Convertible notes payable	Amortized cost	N/A
Notes payable	Amortized cost	N/A

A summary of activity for level 3 derivative liabilities for the years ending December 31, 2018 and 2017 is presented below:

	<u>Derivative Liability</u>
Balance as at January 1, 2017	\$ 387,622
Additions	-
Change in Fair Value	<u>110,610</u>
Balance as of December 31, 2017	498,232
Contract Asset	238,100
Change in Fair Value	<u>(498,232)</u>
Balance as of December 31, 2018	<u>\$ 238,100</u>

There are no material reclassifications between fair value levels during the years ended December 31, 2018 and 2017.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

16. INCOME TAXES

The income tax recovery recorded differs from the amount obtained by applying the statutory Canadian rate of 26.5% (2017 – 21% United States) to the loss before income taxes for the year and is reconciled as follows:

	2018	2017
Net Income (Loss) before recovery of income taxes	(21,238,351)	(4,339,938)
Expected income tax (recovery) expense	(5,628,160)	(911,387)
Effect of jurisdiction rate differences	180,560	(176,592)
Non-controlling interest differences	250,500	75,182
Permanent non-deductible items	244,650	35,593
Warrant and convertible debt costs	256,990	137,050
Listing expense	1,774,210	-
Impact of Tax Cuts and Jobs Acts (US)	-	593,512
Return to provision adjustments and other items	74,090	(136,705)
Change in unrecognized deferred tax asset	2,847,160	383,347
Income tax (recovery) expense	-	-

The Company's income tax (recovery) is allocated as follows:

Current tax (recovery) expense	-	-
Deferred tax (recovery) expense	-	-

The components of the Company's unrecognized deferred income tax asset are as follows:

Allowance for Doubtful Accounts	376,830	-
Intangible Assets	75,510	67,793
Stock Based Compensation	1,023,730	39,962
Investment in Partnerships	221,120	-
Other Temp Differences	360,890	97,224
Non-capital losses carried forward - US	2,835,230	1,853,145
Non-capital losses carried forward - CDN	115,440	-
	-	-
Total Deferred Tax Assets	5,008,750	2,058,124
Deferred Tax Assets not Recognized	(5,008,750)	(2,058,124)
Net Deferred Tax Assets	-	-

The Company has not recorded a deferred tax asset related to these carry forward losses and temporary differences as it is not probable that future taxable income will be available against which these unused tax attributes can be utilized.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

IRC Section 280E

As the Company derives revenue from third parties in the cannabis industry and taking into account the potential impact of ongoing US tax cases that interpret the application of IRC Section 280E, the Company may be subject to the limits of IRC Section 280E under which the Company is only allowed to deduct expenses directly related to the cost of producing the products or cost of production. This results in permanent differences between ordinary and necessary business expenses deemed unallowable under IRC Section 280E. The Company does not believe it is subject to the 280E. However, similar to all ancillary companies in the cannabis sector, there is a general risk that the regulators may consider application of Section 280E.

17. COMMITMENTS AND CONTINGENCIES

The Company may, from time to time, be subject to various administrative, regulatory, and other legal proceedings arising in the ordinary course of business. Contingent liabilities associated with legal proceedings are recorded when a liability is probable, and the contingent liability amount can be reasonably estimated.

The Company's operations are subject to a variety of local and state regulations. Failure to comply with one or more of those regulations could result in fines, restrictions on its operations, or losses of permits that could result in the Company ceasing operations. While management of the Company believes that the Company is in compliance with applicable local and state regulation as at December 31, 2018, medical and adult use cannabis regulations continue to evolve and are subject to differing interpretations. As a result, the Company may be subject to regulatory fines, penalties, or restrictions in the future.

Capital lease

During 2016, the Company acquired certain equipment through a lease. Since the term of the lease is approximately the same as the estimated useful life of the assets and the present value of the future minimum lease payments at the beginning of the lease approximated the fair value of the leased assets at that date, the lease is considered a capital lease and has been so recorded. At December 31, 2018 and 2017, this equipment had a depreciated cost of \$51,090 and \$34,322, respectively.

The balance of the liability under the capital lease at December 31, 2018 and 2017, in the amount of \$27,685 and \$66,629, respectively, net of unamortized discount of \$1,011 and \$4,610, respectively, represents the present value of the balance due in future years for lease rentals, discounted at 7.75%. The liability is payable in monthly installments of \$3,562 for principal and interest to August 2019.

The following is a schedule by years of the future minimum lease payments under the capital leases together with the present value of the net minimum lease payments as at December 31, 2018:

Year Ending December 31, 2018	\$ 28,696
Less the amount representing interest	1,011
Present value of net minimum lease payments	<u>\$ 27,685</u>

DIXIE BRANDS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the Years Ended December 31, 2018 and 2017

The minimum lease payments have not been reduced by minimum sublease rentals due in the future under the non-cancellable sublease mentioned in the preceding paragraph as they are not significant.

Gary Hodges and Karen Hodges v. Left Bank LLC, Dixie Brands, Inc.

This case concerns allegations made by Plaintiffs arising from a July 21, 2016 automobile accident in which the son of the Plaintiffs died. The Plaintiffs have asserted claims of Vicarious Liability and Piercing the Corporate Veil. The matter is scheduled for Trial June 3, 2019. Mediation is scheduled for May 2, 2019.

If Plaintiffs are allowed to assert a claim for exemplary damages, the exemplary damages may be no more than the actual damages. Actual damages are capped at \$436,070 absent a finding by the Judge the tort arose to the level of felonious killing. There is a 60% risk the Judge will find the tort to have been a felonious killing. In that event, an award will likely exceed the limits of the applicable primary insurance policy of \$1,000,000. There is a 35 to 40% likelihood a jury will find Dixie to be jointly liable for any award. There is a 75% likelihood the case will be settled at the upcoming mediation with little to no contribution by Dixie.

Douglas J. Horn and Cindy Harp-Horn v. Medical Marijuana Inc., et. al.,

This case concerns allegations made by Plaintiffs arising from a September 2012 purchase and alleged use of a portion of a single bottle of Dixie X CBD Dew Drops 500 mg Tincture product.

Because the Plaintiff has not offered any settlement, this claim is likely to proceed to trial. The Company maintains a position of no liability to Plaintiffs and the Company's position is defensible. Overall global exposure for both defendants in the case is in the \$350,000 to \$450,000 range, which the Company will be liable for half. However, the Company individual exposure cannot be reliably estimated at this time.

18. FINANCIAL RISK MANAGEMENT

Market risk

Strategic and operational risks arise if the Company fails to carry out business operations and/or to raise sufficient equity and/ or debt financing. These strategic opportunities or threats arise from a range of factors that might include changing economic and political circumstances and regulatory approvals and competitor actions. The risk is mitigated by consideration of other potential development opportunities and challenges which management may undertake.

Credit risk

The Company's exposure to non-payment or non-performance by our counterparties is a credit risk. The maximum credit exposure as at December 31, 2018 is the carrying amount of cash, accounts receivable and related party advances and promissory notes receivable. The Company has a significant outstanding balance in accounts receivable over 90 days as of December 31, 2018. The Company mitigates its credit risk on its other receivables and promissory notes receivable through its review of the counterparties and business review. The Company considers a variety of factors when determining interest rates for notes receivable, including the creditworthiness of the counterparty, market interest rates prevailing at the note's origination and duration and terms of the note. Notes that are overdue are assessed for impairment.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

The Company has a concentration of credit risk with Left Bank, a related party (Note 11). The Company provided note receivables to Left Bank in the amount of \$1,755,886 as at December 31, 2018 and \$943,129 as at December 31, 2017. The Company also has significant amounts of accounts receivable from Left Bank for \$2,793,198 in 2018 and \$812,930 in 2017. The Company expects to recover these amounts going forward but as there has been a history of slow payments from Left Bank, the Company provides provisions for Left Bank notes receivable for \$143,820 and for Left Bank accounts receivable for \$1,390,000.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company ensures that there is sufficient capital in order to meet short-term business requirements, after taking into account the Company's cash holdings. As at December 31, 2018, the Company's financial liabilities consist of accounts payable and accrued liabilities, which have contractual maturity dates within one-year, and notes payable, which have a contractual maturity within 18 months. The Company manages its liquidity risk by reviewing its capital requirements on an ongoing basis. Based on the Company's ability to complete equity cash raises, management regards liquidity risk to be low.

Asset forfeiture risk

Because the cannabis industry remains illegal under U.S. federal law, any property owned by participants that conduct business with affiliates in the cannabis industry, which either are used in the course of conducting such business, or are the proceeds of such business, could be subject to seizure by law enforcement and subsequent civil asset forfeiture. Even if the owner of the property are never charged with a crime, the property in question could still be seized and subject to an administrative proceeding by which, with minimal due process, it could be subject to forfeiture.

Banking risk

Notwithstanding that a majority of states have legalized recreational marijuana, there has been no change in U.S. federal banking laws related to the deposit and holding of funds derived from activities related to the cannabis industry. Given that U.S. federal law provides that the production and possession of cannabis is illegal, there is a strong argument that banks cannot accept for deposit funds from businesses involved with the cannabis industry. Consequently, businesses involved in the cannabis industry often have difficulty accessing the U.S. banking system and traditional financing sources. The inability to open bank accounts with certain institutions may make it difficult to operate ordinary businesses.

Interest rate risk

Interest rate risk is the risk that the fair value or the future cash flows of a financial instrument will fluctuate as a result of changes in market interest rates. The Company's interest-bearing loans and borrowings are all at fixed interest rates. The Company considers interest rate risk to be immaterial.

DIXIE BRANDS INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements
For the Years Ended December 31, 2018 and 2017

Capital structure risk management

The Company considers its capital structure to include debt financing, contributed capital, accumulated deficit, non-controlling interests and any other component of members' equity. The Company's objectives when managing its capital are to safeguard its ability to continue as a going concern, to meet its capital expenditures for its continued operations, and to maintain a flexible capital structure which optimizes the cost of capital within a framework of acceptable risk. The Company manages its capital structure and adjusts it as appropriate given changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust its capital structure, the Company may issue new units, issue new debt, or acquire or dispose of assets. The Company is not subject to externally imposed capital requirements. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. There have been no changes to the Company's capital management approach during the year ended December 31, 2018.

19. SUBSEQUENT EVENTS

On January 2, 2019, the Company purchased an additional 25% of its subsidiary Therabis, LLC, or 25,000 units, for a total purchase price of \$7,422,827, plus expenses not to exceed \$63,774. The initial closing payment was in the amount of \$3,922,827 with a deferred closing payment in the amount of \$3,500,000. With this purchase, Dixie Brands holds an 85% ownership in Therabis, LLC. In addition to the total purchase price of \$7,422,827, DBI also paid Rose Capital the outstanding balance of the Promissory Notes of \$877,173, of which principal totals \$775,000 and interest totals \$102,173 was paid.

On March 5, 2019, the Company entered into a Packaging and Supply Agreement with Choice Labs, whereby Dixie Brands' portfolio of products will be manufactured, sold and distributed across the state of Michigan. The companies had a selection of products available for sale in Michigan provisioning centers by late March.

On March 12, 2019, the Company signed a joint venture agreement with Khiron Life Sciences Corp. ("Khiron"), a vertically integrated cannabis leader with core operations in Latin America. With the execution of this agreement, a new company called Dixie Khiron JV Corp. has been established with 50% owned by each of the Company and Khiron.

On February 19, 2019, the Company paid \$3,250,000 to Auxly as a result of "elixirs", "mints" and "chocolates" not being permitted under the Cannabis Act in Canada by December, 31, 2018. On March 12, 2019 the Company amended the initial agreement with Auxly to exclude the exclusive rights in Mexico. The Company paid Auxly \$187,500 on March 12, 2019 as part of the amendment.