



**HARBORSIDE INC.**  
**Unaudited Condensed Interim Consolidated Financial Statements**

**For the Three Months Ended March 31, 2022 and 2021**  
**(Expressed in United States Dollars)**

**HARBORSIDE INC.**  
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## Management's Responsibility for Financial Reporting

To the Shareholders of Harborside Inc.:

The accompanying unaudited condensed interim consolidated financial statements were prepared by management of Harborside Inc. (the "Company") and were reviewed by the Audit Committee and approved by the Board of Directors of the Company (the "Board").

Management is responsible for the unaudited condensed interim 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 unaudited condensed interim 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 unaudited condensed interim consolidated financial statements were approved by the Board of Directors of the company and were signed on behalf of Management by:

May 26, 2022

Edward M. Schmults ("Signed")  
Chief Executive Officer

Tom DiGiovanni ("Signed")  
Chief Financial Officer

# HARBORSIDE INC.

Unaudited Condensed Interim Consolidated Statements of Financial Position  
As At March 31, 2022 and December 31, 2021  
(Expressed in United States Dollars, except share amounts)

	Note	March 31, 2022	December 31, 2021
<b>ASSETS</b>			
Current Assets			
Cash		\$ 10,923,177	\$ 8,774,941
Restricted cash	16	2,850,076	316,464
Accounts receivable, net	4	3,776,052	4,546,357
Inventories	5	8,530,515	6,414,150
Biological assets	6	778,924	443,839
Prepaid expenses	7	4,610,677	4,332,566
Note receivable	10	1,151,773	1,065,393
Other current assets	8	<u>1,061,048</u>	<u>1,230,655</u>
Total current assets		33,682,242	27,124,365
Investments and advances	9	3,173,471	2,458,011
Property, plant and equipment, net	11	44,156,919	23,515,610
Right-of-use assets	13	22,544,724	4,433,397
Deposits and other assets		755,799	390,325
Due from other entities		484,399	-
Intangible assets	12	85,008,957	64,692,644
Goodwill	12	<u>76,646,668</u>	<u>31,206,577</u>
<b>TOTAL ASSETS</b>		<u>\$ 266,453,179</u>	<u>\$ 153,820,929</u>
<b>LIABILITIES</b>			
Current liabilities			
Accounts payable and accrued liabilities	14	\$ 43,873,392	\$ 23,692,814
Notes payable, net	15	13,530,716	-
Lease payable - current	13	2,448,420	714,181
Income taxes payable		15,596,577	10,156,438
Provisions	19	<u>36,498,436</u>	<u>36,051,249</u>
Total current liabilities		111,947,541	70,614,682
Term loan, net	17	27,690,207	-
Revolving credit facility, net	16	-	11,845,678
Derivative liabilities	18	454,996	779,643
Deferred tax liability	21	19,869,712	17,363,459
Lease payable	13	<u>29,817,720</u>	<u>5,614,703</u>
<b>TOTAL LIABILITIES</b>		189,780,176	106,218,165
<b>Shareholders' Equity</b>			
Share capital	22	184,572,983	150,373,620
Contributed surplus	23	12,931,653	10,553,806
Reserve for warrants	24	1,099,444	2,233,556
Accumulated deficit		(128,827,981)	(118,415,683)
Non-controlling interests	25	<u>6,896,904</u>	<u>2,857,465</u>
<b>TOTAL SHAREHOLDERS' EQUITY</b>		<u>76,673,003</u>	<u>47,602,764</u>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<u>\$ 266,453,179</u>	<u>\$ 153,820,929</u>

Nature of operations (Note 1)  
Commitments and contingencies (Note 28)  
Subsequent events (Note 32)

Approved on behalf of the Board of Directors:

Edward M. Schmults ("Signed")

Director

Matt Hawkins ("Signed")

Director

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

# HARBORSIDE INC.

Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)  
For the Three Months Ended March 31, 2022 and 2021  
(Expressed in United States Dollars, except share amounts)

		<u>For the Three Months Ended</u>	
		<u>March 31, 2022</u>	<u>March 31, 2021</u>
Net revenue		\$ 17,267,361	\$ 12,440,915
Cost of goods sold		11,758,024	6,614,257
<b>Gross profit before biological asset adjustments</b>		5,509,337	5,826,658
Changes in fair value less costs to sell of biological asset transformation	6	(1,264,212)	(717,230)
Realized fair value amounts included in inventory sold		2,230,543	(520,915)
<b>Gross profit</b>		6,475,668	4,588,513
<b>Expenses</b>			
General and administrative	20	7,481,573	4,324,066
Professional fees		1,270,485	3,184,888
M&A and transactional expenses		2,702,067	-
Share-based compensation	23	1,243,735	(1,000)
Allowance for expected credit losses		130,440	77,042
Depreciation and amortization	11, 12 & 13	1,209,643	214,108
<b>Total expenses</b>		14,037,943	7,799,104
<b>Operating income (loss)</b>		(7,562,275)	(3,210,591)
Interest income (expense), net		(1,364,123)	(915,562)
Other income (expense), net		(925,508)	322,796
Fair value gain in other current assets and derivative liabilities	8, 9 & 18	678,348	2,013,059
Foreign exchange loss		(49,576)	(45,199)
<b>Total other income (expense)</b>		(1,660,859)	1,375,094
<b>Net income (loss) before income taxes</b>		(9,223,134)	(1,835,497)
Income tax expense	21	(1,338,360)	(1,075,252)
<b>Net income (loss)</b>		(10,561,494)	(2,910,749)
Net loss attributable to non-controlling interests		(149,196)	-
<b>Net income (loss) attributable to Harborside Inc.</b>		<u>\$ (10,412,298)</u>	<u>\$ (2,910,749)</u>
<b>Weighted average number of shares outstanding</b>			
Basic and diluted	26	104,111,060	51,045,299
<b>Net loss per share</b>			
Basic and diluted	26	\$ (0.10)	\$ (0.06)
<b>Comprehensive income (loss):</b>			
Net income (loss)		\$ (10,561,494)	\$ (2,910,749)
Comprehensive income (loss) attributable to non-controlling interests		(149,196)	-
<b>Comprehensive income (loss) attributable to Harborside Inc. shareholders</b>		<u>\$ (10,412,298)</u>	<u>\$ (2,910,749)</u>

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

# HARBORSIDE INC.

Unaudited Condensed Interim Consolidated Statements of Changes in Shareholders' Equity

For the Three Months Ended March 31, 2022 and 2021

(Expressed in United States Dollars, except share amounts)

	Note	Share capital	Contributed surplus	Reserve for warrants	Accumulated Deficit	Subtotal	Non-controlling interests	Equity incl. non-controlling interests
<b>Balance, January 1, 2021</b>		\$ 97,423,381	\$ 9,305,199	\$ 1,093,592	\$ (92,257,217)	\$ 15,564,955	\$ 3,066,630	\$ 18,631,585
Exercise of stock options	23	24,094	-	-	-	24,094	-	24,094
Share-based compensation	23	-	(1,000)	-	-	(1,000)	-	(1,000)
Issuance of SVS and MVS in private offering	22	13,115,086	-	-	-	13,115,086	-	13,115,086
Private offering issuance costs	22	(1,194,390)	-	-	-	(1,194,390)	-	(1,194,390)
Issuance of warrants to the Bank	24	-	-	466,716	-	466,716	-	466,716
Issuance of broker warrants	22	-	-	1,134,112	-	1,134,112	-	1,134,112
Net loss for the period		-	-	-	(2,910,749)	(2,910,749)	-	(2,910,749)
<b>Balance, March 31, 2021</b>		<u>\$ 109,368,171</u>	<u>\$ 9,304,199</u>	<u>\$ 2,694,420</u>	<u>\$ (95,167,966)</u>	<u>\$ 26,198,824</u>	<u>\$ 3,066,630</u>	<u>\$ 29,265,454</u>
<b>Balance, January 1, 2022</b>		\$ 150,373,620	\$ 10,553,806	\$ 2,233,556	\$ (118,415,683)	\$ 44,745,299	\$ 2,857,465	\$ 47,602,764
Exercise of stock options	23	1,250	-	-	-	1,250	-	1,250
Share-based compensation	23	-	1,243,735	-	-	1,243,735	-	1,243,735
Expiry of Broker Warrants	24	-	1,134,112	(1,134,112)	-	-	-	-
Issuance of shares in acquisition	3 & 22	34,198,113	-	-	-	34,198,113	-	34,198,113
Purchases of business - initial equity related to non-controlling interests	25	-	-	-	-	-	4,188,635	4,188,635
Net loss for the period		-	-	-	(10,412,298)	(10,412,298)	(149,196)	(10,561,494)
<b>Balance, March 31, 2022</b>		<u>\$ 184,572,983</u>	<u>\$ 12,931,653</u>	<u>\$ 1,099,444</u>	<u>\$ (128,827,981)</u>	<u>\$ 69,776,099</u>	<u>\$ 6,896,904</u>	<u>\$ 76,673,003</u>

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

# HARBORSIDE INC.

Unaudited Condensed Interim Consolidated Statements of Cash Flows  
For the Three Months Ended March 31, 2022 and 2021  
(Expressed in United States Dollars, except share amounts)

	Note	For the Three Months Ended	
		March 31, 2022	March 31, 2021
<b>Operating Activities</b>			
Net loss for the period		\$ (10,561,494)	\$ (2,910,749)
<b>Adjustments to reconcile net loss to cash flow:</b>			
Share-based compensation	23	1,243,735	(1,000)
Depreciation and amortization	11, 12 & 13	1,718,885	727,240
Changes in fair value less costs to sell of biological asset transformation	6	1,264,212	717,230
Fair value gain in other current assets and derivative liabilities	18	(678,348)	(2,013,059)
Provision for expected credit losses	4	130,440	77,042
Interest income on notes receivable - related party, note receivable and investments and advances	9 & 27	(266,624)	(54,411)
Lease modification		-	(11,291)
Professional fees classified as financing activities - private placement of equity units		-	596,157
Amortization of other current assets and debt issuance costs		577,994	-
Accrued interest on lease liabilities	13	415,643	223,899
Loss on disposal of property, plant and equipment	11	77,163	-
Foreign exchange loss		49,576	45,199
		(6,028,818)	(2,603,743)
Changes in non-cash working capital:			
Accounts receivable, net	4	1,041,997	217,853
Inventories	5	(5,367)	(165,680)
Biological assets	6	(1,599,297)	(245,947)
Prepaid expenses	7	468,193	(9,042)
Due from other entities		(10,371)	-
Deposits and other assets		-	(44,919)
Accounts payable and accrued liabilities	14	4,083,714	560,727
Due to related parties		-	(144,000)
Income tax payable	21	1,201,043	1,253,496
Provisions	19	447,187	367,567
Accrued interest on note payable		65,000	139,436
Deferred tax liability	21	35,916	(178,243)
<b>Cash Flows used in Operating Activities</b>		<b>(300,803)</b>	<b>(852,495)</b>
<b>Financing Activities</b>			
Net proceeds raised in private offering	22	-	26,990,719
Net proceeds (repayment) from revolving credit facility	16	(12,000,000)	316,400
Net proceeds from term loan	17	14,648,017	-
Repayments of notes payable		(10,000)	-
Payments of principal portion of lease liabilities	13	(735,418)	(365,650)
Proceeds from exercise of stock options	23	1,250	24,094
<b>Cash Flows provided by Financing Activities</b>		<b>1,903,849</b>	<b>26,965,563</b>

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

# HARBORSIDE INC.

Unaudited Condensed Interim Consolidated Statements of Cash Flows  
For the Three Months Ended March 31, 2022 and 2021  
(Expressed in United States Dollars, except share amounts)

	Note	For the Three Months Ended	
		March 31, 2022	March 31, 2021
<b>Investing Activities</b>			
Investment in debentures	9	-	(5,000,000)
Cash received in Urbn Leaf Acquisition	3	3,268,427	-
Purchases of property, plant and equipment	11	(75,411)	(727,535)
<b>Cash Flows provided by (used in) Investing Activities</b>		<u>3,193,016</u>	<u>(5,727,535)</u>
Increase in cash and restricted cash		4,796,062	20,385,533
Effects of foreign exchange on cash and restricted cash		(114,214)	79,723
Cash and restricted cash, beginning of period		9,091,405	10,458,545
<b>Cash and restricted cash, end of period</b>		<u>\$ 13,773,253</u>	<u>\$ 30,923,801</u>
<b>Cash and restricted cash consisted of the following:</b>			
Cash		10,923,177	30,607,551
Restricted cash - interest reserves	16	2,850,076	316,250
		<u>\$ 13,773,253</u>	<u>\$ 30,923,801</u>
<b>Supplementary Information</b>			
Cash paid during the period for:			
Interest		\$ 387,944	\$ 242,001
<b>Non-Cash Investing and Financing Activities</b>			
Issuance of warrants to Bank	16 & 24	\$ -	\$ 466,716
Issuance of Broker Warrants	24	-	1,134,112
Expiry of Broker Warrants	24	(1,134,112)	-

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



# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 1. Nature of Operations

Harborside Inc. ("Harborside" or the "Company"), through its affiliated entities, is a fully licensed, vertically integrated omni-channel cannabis company, with its business consisting of three primary segments: (i) retail sales, including direct to consumer and delivery, (ii) cultivation, processing and manufacturing, including "white label" production of consumer packaged goods for other cannabis companies, and (iii) wholesale sales, including branded product sales of consumer packaged goods. The Company provides an omni-channel experience to customers in the adult-use and medical markets. The Company operates in and/or has ownership interests in California and Oregon, pursuant to state and local laws and regulations, and is focused on building and maintaining its position as one of California's premier vertically integrated cannabis companies.

As at March 31, 2022, the Company's retail presence includes the following:

- Four owned and operated Harborside branded retail dispensaries located in Oakland, San Jose, San Leandro and Desert Hot Springs, California;
- Eight owned and operated Urbn Leaf (as defined below) branded retail dispensaries located in San Diego, San Ysidro, Grover Beach, Seaside, La Mesa, Grossmont, San Jose and Vista, California;
- One owned and operated dispensary located in Eugene, Oregon (the "Terpene Station Dispensary");
- 21% interest in FGW Haight Inc. ("FGW"), a company with the conditional use approval necessary to operate a retail dispensary in the Haight Ashbury area of San Francisco. FGW received the necessary approvals and opened the Haight Ashbury San Francisco retail dispensary under the Harborside brand in April 2022 (Note 32); and,
- Retail delivery services which (a) cover the greater San Francisco Bay Area of California from its Harborside branded retail stores in Oakland and San Jose; (b) cover the Grover Beach and San Ysidro areas from its Urbn Leaf branded stores in each of these areas; and (c) include a partnership with a third party for delivery services in the greater San Diego area.

As at March 31, 2022, the Company owned and operated a cultivation and production facility in Salinas, California (the "Salinas Production Campus"), a manufacturing facility in Oakland, California and distribution centers in both San Jose and Los Angeles, California.

The Company owns or controls a number of different cannabis brands that it sells through wholesale and retail markets including "Harborside", "Harborside Farms", "Key", "Terpene Station", "Sublime", "Fuzzies", and "Urbn Leaf".

On April 4, 2022, the Company acquired 100% of the equity interests of LPF JV Corporation ("Loudpack"), a leading manufacturer, cultivator, and distributor of award-winning cannabis brands in California (Note 32).

The Company's subordinate voting shares ("SVS") are listed on the Canadian Securities Exchange (the "CSE") under the trading symbol "HBOR" and on the OTCQX under the trading symbol "HBORF". The Company's registered office is located at 181 Bay Street, Suite 1800, Toronto, Ontario, M5J 2T9, Canada, and the Company's head office is located at 1295 W Morena Blvd., San Diego, California 92110, United States.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies

#### 2.1 Statement of Compliance and Basis of Measurement

The Company's unaudited condensed interim consolidated financial statements for the three months ended March 31, 2022, including comparatives, have been prepared in accordance with International Accounting Standards 34, Interim Financial Reporting. Certain information and footnote disclosures normally included in the audited annual consolidated financial statements 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"), have been omitted or condensed. These unaudited condensed interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2021, and the related notes thereto, and have been prepared using the same accounting policies described therein.

These unaudited condensed interim consolidated financial statements were authorized for issuance by the Company's Board on May 26, 2022.

#### 2.2 Functional Currency

The functional currency of the Company and each of its subsidiaries is the United States ("U.S.") dollar. Unless otherwise indicated, these unaudited condensed interim consolidated financial statements are presented in U.S. dollars (\$) or "USD". All references to "C\$" or "CAD" pertain to Canadian dollars.

#### 2.3 Basis of Consolidation

These unaudited condensed interim consolidated financial statements incorporate the accounts of the Company and its wholly-owned subsidiaries as follows:

Name	Jurisdiction	Purpose	Percentage	Percentage
			Owned (%)	Owned (%)
			March 31,	December 31,
			2022	2021
Harborside Inc.	Ontario, Canada	Parent	100	100
658 East San Ysidro Blvd LLC	California, U.S.	Real Estate Holding Company	100	-
680 Broadway Master, LLC	California, U.S.	Operating Company	50	-
909 West Vista Way LLC	California, U.S.	Real Estate Holding Company	100	-
Accucanna Holdings Inc.	California, U.S.	Holding Company	100	100
Accucanna LLC	California, U.S.	Operating Company	100	100
Accucanna RE, LLC	California, U.S.	Operating Company	100	100
Banana LLC	California, U.S.	Operating Company	75	-
Belling Distribution, Inc.	California, U.S.	Operating Company	100	-
Calgen Trading Inc.	California, U.S.	Operating Company	100	-
Encinal Productions RE, LLC	California, U.S.	Operating Company	100	100
FFC1, LLC	California, U.S.	Holding Company	100	100
FGW Haight Inc.	California, U.S.	Operating Company	21	21
FLRish Farms Cultivation 2, LLC	California, U.S.	Operating Company	100	100
FLRish Farms Management & Security Services, LLC	California, U.S.	Management Company	100	100
FLRish, Inc.	California, U.S.	Management Company	100	100
FLRish IP, LLC	California, U.S.	Holding Company	100	100
FLRish Retail, LLC	California, U.S.	Holding Company	100	100
FLRish Retail Management & Security Services, LLC	California, U.S.	Management Company	100	100
Haight Acquisition Corporation	Delaware, U.S.	Holding Company	100	100
JLM Investment Group, LLC	California, U.S.	Holding Company	67	-
Lafayette Street Property Management LLC	California, U.S.	Operating Company	90	-
LGC Holdings USA, Inc.	Nevada, U.S.	Holding Company	100	100

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.3 Basis of Consolidation (continued)

Name	Jurisdiction	Purpose	Percentage	Percentage
			Owned (%)	Owned (%)
			March 31,	December 31,
			2022	2021
LGC LOR DIS 1, LLC	Oregon, U.S.	Operating Company	100	100
LGC LOR DIS 2, LLC	Oregon, U.S.	Operating Company	100	100
Lineage GCL California, LLC	California, U.S.	Holding Company	100	100
Lineage GCL Oregon Corporation	Oregon, U.S.	Holding Company	100	100
Oakland Machining Supply SLB LLC	California, U.S.	Holding Company	100	100
Patients Mutual Assistance Collective Corporation	California, U.S.	Operating Company	100	100
San Jose Wellness Solutions Corp.	California, U.S.	Operating Company	100	100
San Leandro Wellness Solutions Inc.	California, U.S.	Operating Company	100	100
SaVaCa, LLC	California, U.S.	Holding Company	100	100
Savature Inc.	California, U.S.	Operating Company	100	100
SBC Management LLC	California, U.S.	Management Company	100	-
Sublime Machining Inc.	California, U.S.	Operating Company	100	100
Sublimation Inc.	Delaware, U.S.	Holding Company	100	100
ULBP Inc.	California, U.S.	Operating Company	100	-
ULRB LLC	California, U.S.	Operating Company	80	-
UL Benicia LLC	California, U.S.	Operating Company	80	-
UL Chula Two LLC	California, U.S.	Operating Company	51	-
UL Holdings Inc.	California, U.S.	Holding Company	100	-
UL Kenamar LLC	California, U.S.	Operating Company	100	-
UL La Mesa LLC	California, U.S.	Operating Company	60	-
UL Management LLC	California, U.S.	Management Company	100	-
UL San Jose LLC	California, U.S.	Operating Company	100	-
UL Visalia LLC	California, U.S.	Operating Company	80	-
Unite Capital Corp.	Ontario, Canada	Holding Company	100	100
Uprooted, Inc.	California, U.S.	Operating Company	100	-
Uprooted LM LLC	California, U.S.	Operating Company	100	-

The unaudited condensed interim consolidated financial statements as at March 31, 2022 and December 31, 2021 include the accounts of the Company, its wholly-owned subsidiaries and entities over which the Company has control as defined in IFRS 10, *Consolidated Financial Statements* ("IFRS 10"). Entities over which the Company has control are presented on a consolidated basis from the date control commences. Control, as defined by IFRS 10 for purposes of determining the consolidated basis of financial statement presentation exists when the Company is exposed to, or has right to, variable returns as well as the ability to affect those returns through the power to direct the relevant activities of the entity. All of the consolidated entities were under control, as defined in IFRS 10 for purposes of determining the consolidated basis of financial statement presentation, during the entirety of the periods for which their respective results of operations were included in the consolidated statements. The unaudited condensed interim consolidated financial statements include all the assets, liabilities, revenues, expenses and cash flows of the Company and its subsidiaries that it controls after eliminating intercompany balances and transactions.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.4 COVID-19 Estimation Uncertainty

The global pandemic outbreak of the novel strain of coronavirus ("COVID-19") has resulted in governments worldwide enacting emergency measures to combat the spread of the virus. In response to the outbreak, governmental authorities in the United States, Canada and internationally have introduced various recommendations and measures to try to limit the pandemic, including travel restrictions, border closures, non-essential business closures, quarantines, self-isolations, shelters-in-place and social distancing. For the time being and until economies stabilize, the Company has shifted its strategic approach and the manner in which it operates its business to continue providing affordable and high-quality products to its customers and ensure that its workplace and stores have appropriate measures in place to limit social interactions and enforce social distancing measures in accordance with applicable regulations. At the same time, the Company has also taken steps to alter its marketing methods, conserve cash and adjust its overall strategic direction to preserve the health of its business. COVID-19 has cast uncertainty on the assumptions used by management in making its judgments and estimates. At this point, the extent to which COVID-19 may impact the Company is uncertain; however, it is possible that COVID-19 may have a material adverse effect on the Company's business, results of operations and financial condition.

#### 2.5 Summary of Significant Accounting Policies

The Company completed one business combination during the three months ended March 31, 2022. The acquisition of UL Holdings Inc. ("Urbn Leaf") was accounted for in accordance with IFRS 3 (Note 3). Except as described below, due to the business combination (Note 3), the accounting policies applied in the preparation of the unaudited condensed interim consolidated financial statements are consistent with those applied and disclosed in the Company's audited consolidated financial statements for the year ended December 31, 2021.

#### 2.6 Due from other entities

Due from other entities represents balances for pre-operating entities for which the Company is expecting to acquire future interests. The Company, through its affiliated entities, manages pre-operating costs for other entities which include permitting fees, license applications, leasehold improvements and other charges for future retail, manufacturing, production and cultivation operating entities. Those expenses are held as due from the respective operating entity.

#### 2.7 Revenue Recognition

##### *Loyalty Rewards Program*

The Company's Urbn Leaf branded retail dispensaries offer a loyalty rewards program to participating customers that allows customers to earn reward points to be used on future purchases of goods at a price that reflects a discount from the stand-alone selling price of a product. This program provides participating retail customers with a material right which is accounted for as a separate performance obligation.

Based on the stand-alone selling price allocation, management allocates a portion of the gross sales revenue generated to the material right. As the points are redeemed, a proportionate amount of the material right is recognized as revenue and at period end the amount of the material right represented by the unredeemed points is carried forward as a liability until points are redeemed or expire.

As at March 31, 2022, the Company had a loyalty program liability of \$1,129,021, which is recorded as a component of accounts payable and accrued liabilities in the accompanying Unaudited Condensed Interim Consolidated Statements of Financial Position.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.8 Financial Instruments

The Company classifies and measures financial instruments in accordance with IFRS 9, *Financial Instruments*. On initial recognition, a financial asset is classified as fair value through profit or loss ("FVTPL"), fair value through other comprehensive income ("FVTOCI"), or amortized cost. Purchases and sales of financial assets are recorded on a settlement date basis.

Subsequent to initial recognition, all investments are measured at fair value. All gains and losses arising from changes in fair value of the investments are presented in the Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss) in the period in which the gains or losses arise. The Company will only reclassify a financial asset when the Company changes its business model for managing the financial asset. All reclassifications are recorded at fair value at the date of reclassification, which becomes the new carrying value.

##### *i. Financial assets classified at fair value through profit and loss*

Financial assets are classified as FVTPL if the asset is an equity investment, if the Company has not elected to classify investments as FVTOCI, or if the Company's business model for holding the investment is achieved other than by both collecting contractual cash flows and by selling the assets. As at March 31, 2022 and December 31, 2021, the Company did not have any financial assets at FVTOCI.

FVTPL assets are initially recorded at fair value with realized gains and losses on disposition and subsequent changes in fair value recorded in net income (loss). Directly attributable transaction costs are recorded in net income (loss) as incurred.

##### *ii. Non-derivative financial liabilities*

Non-derivative financial liabilities are recognized initially on the date the Company becomes a party to the contractual obligations of the financial instrument. All non-derivative financial liabilities are recognized initially at fair value along with directly attributable transaction costs. Subsequent to initial measurement, non-derivative financial liabilities are measured at amortized cost using the effective interest method.

##### *iii. Derivative financial instruments - warrants and options*

A financial derivative, such as warrants or options, which will be settled with the Company's own equity instruments will be classified as an equity instrument if the derivative is to acquire a fixed number of the Company's own equity instruments for a fixed amount of U.S. dollars.

A financial derivative will be considered a financial liability at FVTPL if it is used to acquire a variable number of equity instruments and the options or warrants were not offered pro-rata to all existing owners of the class of non-derivative equity instruments.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.8 Financial Instruments (continued)

The following table presents the Company's classification of financial assets and financial liabilities as at March 31, 2022:

<b>Financial assets/financial liabilities</b>	<b>Classification</b>
Cash and restricted cash	Amortized cost
Accounts receivable, net	Amortized cost
Other current assets	FVTPL
Investments and advances	FVTPL
Deposits and other assets	Amortized cost
Due from other entities	Amortized cost
Accounts payable and accrued liabilities	Amortized cost
Notes payable, net	Amortized cost
Term loan, net	Amortized cost
Revolving credit facility, net	Amortized cost
Derivative liabilities	FVTPL

The Company recognizes a provision for expected credit losses on financial assets that are measured at amortized cost. The Company assumes that the credit risk on a financial asset has increased if it is more than 60 days past due. The Company considers a financial asset to be impaired either when the financial asset is more than 90 days past due, or it is determined that the borrower is unlikely to pay its credit obligations to the Company in full.

The carrying amount of a financial asset is reduced (either partially or in full) to the extent that management determines that there is no realistic prospect of recovery. This is generally the case when the Company concludes that the debtor does not have assets or sources of income that could generate sufficient cash flows to repay the amounts.

The Company assesses information available including, on a forward-looking basis, the expected credit loss associated with its assets carried at amortized cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk. To assess whether there is a significant increase in credit risk, the Company compares the risk of a default occurring on the asset at the reporting date with the risk of default at the date of initial recognition based on all information available and reasonable and supportive forward-looking information. For accounts receivable only, the Company applies the simplified approach as permitted by IFRS 9. The simplified approach to the recognition of expected losses does not require the Company to track the changes in credit risk; rather, from the dates of the trade receivables, the Company recognizes a loss provision based on lifetime expected credit losses at each reporting date.

Expected credit losses are measured as the difference in the present value of the contractual cash flows that are due to the Company under the contract, and the cash flows that the Company expects to receive. The Company assesses information available, including past due status, credit ratings, the existence of third-party insurance, and forward-looking macro-economic factors in the measurement of the expected credit losses associated with its assets carried at amortized cost. The Company measures expected credit loss by considering the risk of default over the contract period and incorporates forward-looking information into its measurement.

# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
For the Three Months Ended March 31, 2022 and 2021  
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## 2. Summary of Significant Accounting Policies (continued)

### 2.9 Critical Accounting Estimates and Judgments

The preparation of these unaudited condensed interim consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised in any future periods affected. Significant judgments, estimates, and assumptions that have the most significant effect on the amounts recognized in the unaudited condensed interim consolidated financial statements are described below.

#### *Business combination*

In a business acquisition, substantially all identifiable assets, liabilities and contingent liabilities acquired are recorded at their respective fair values at the acquisition date. The date on which the acquirer obtains control of the acquiree is generally the date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree - the closing date. However, the acquirer might obtain control on a date that is either earlier or later than the closing date. Management exercises judgment in considering all pertinent facts and circumstances in identifying the acquisition date.

The Company examines three elements to determine whether control exists. When these three elements of control are present, then an investor is considered to control an investee and consolidation is required. When one or more of the elements is not present, an investor will not consolidate but instead be required to determine the nature of its relationship with the investee. The Company exercises its judgment when determining control over an investee, when it has all of the following attributes: power over the investee, such as the ability to direct relevant activities of the investee; exposure, or rights, to variable returns from its involvement with the investee, such as returns that are not fixed and have the potential to vary with performance of the investee; and the ability to use its power over the investee to affect the amount of the investor's returns, such as identifying the link between power and returns.

Classification of an acquisition as a business combination or an asset acquisition depends on whether the assets acquired constitute a business, which can be a complex judgment. Whether an acquisition is classified as a business combination or an asset acquisition can have a significant impact on the entries made at and after acquisition. In determining the fair value of all identifiable assets, liabilities and contingent liabilities acquired, the most significant estimates relate to contingent consideration and intangible assets. Contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination.

Management exercises judgment in estimating the probability and timing of when contingent securities are expected to be issued which is used as the basis for estimating fair value. For any intangible asset identified, depending on the type of intangible asset and the complexity of determining its fair value, an independent valuation expert or management may develop the fair value, using appropriate valuation techniques which are generally based on a forecast of the total expected future net cash flows. The evaluations are linked closely to the assumptions made by management regarding the future performance of these assets and any changes in the discount rate applied. Purchase consideration also includes consideration of any pre-existing relationships that are effectively settled at their fair values due to the acquisition.

# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
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## 2. Summary of Significant Accounting Policies (continued)

### 2.9 Critical Accounting Estimates and Judgments (continued)

#### *Fair value of biological assets and inventories*

Determination of the fair value of biological assets and inventories requires management to make assumptions about how market participants assign fair values to these assets. These assumptions primarily relate to the level of effort required to bring cannabis up to the point of harvest, costs to convert the harvested cannabis to finished goods, sales price, risk of loss, expected future yields from the cannabis plants and estimating values during the growth cycle.

The valuation of biological assets at the point of harvest is the cost basis for all cannabis-based inventories and thus any critical estimates and judgments related to the valuation of biological assets are also applicable for inventories.

Significant assumptions used in determining the fair value of biological assets include:

- Estimating the stage of growth of cannabis up to the point of harvest;
- Pre-harvest and post-harvest costs;
- Expected selling prices;
- Expected yields for cannabis plants to be harvested, by strain of plant; and
- Wastage of plants at various stages.

The valuation of work in process and finished goods also requires the estimate of conversion costs incurred, which become part of the carrying amount for inventories. The Company must also determine if the cost of any inventories exceeds its net realizable value ("NRV"), such as cases where prices have decreased, or inventories have spoiled or otherwise been damaged. The Company estimates the NRV of inventories, taking into account the most reliable evidence available at each reporting date. The future realization of these inventories may be affected by market-driven changes that may reduce future selling prices. A change to these assumptions could impact the Company's inventory valuation and impact gross profit.

#### *Provision for expected credit losses ("ECL")*

Determining a provision for ECLs for accounts receivable held at amortized cost requires management to make assumptions about the historical patterns for the probability of default, timing of collection and the amount of incurred credit losses, which are adjusted based on management's judgment about whether economic conditions and credit terms are such that actual losses may be higher or lower than what the historical patterns suggest.

#### *Estimated useful lives of depreciation and amortization of property, plant and equipment and intangible assets*

Depreciation and amortization of property, plant 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 which considers factors such as economic conditions, market conditions and the useful lives of assets.



# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
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## 2. Summary of Significant Accounting Policies (continued)

### 2.9 Critical Accounting Estimates and Judgments (continued)

*Estimated useful lives of depreciation and amortization of property, plant and equipment and intangible assets (continued)*

Amortization of intangible assets is dependent upon estimates of useful lives and residual values which are determined through the exercise of judgment. 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 they might be impaired. The assessment of any impairment of these assets is dependent upon estimates of recoverable amounts which considers factors such as general and industry-specific economic and market conditions.

*Impairment of long-lived assets*

Long-lived assets, including property, plant and equipment and intangible assets, are reviewed for indicators of impairment at each reporting period or whenever events or changes in circumstances indicate that the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset or a cash generating unit ("CGU") is the higher of its fair value less costs to sell or its value in use. If the carrying amount of an asset or a CGU exceeds its recoverable amount, an impairment charge is recognized immediately in profit or loss for the amount by which the carrying amount of the asset exceeds the recoverable amount.

*Goodwill impairment*

When determining the recoverable amount of the CGU or CGUs to which goodwill is allocated, the Company relies on a number of factors, including historical results, business plans, forecasts and market data. Changes in the condition for these judgments and estimates can significantly affect the recoverable amount.

*Incremental borrowing rate for leases under IFRS 16*

IFRS 16 requires lessees to discount lease payments using the rate implicit in the lease if that rate is readily available. If that rate cannot be readily determined, the lessee is required to use its incremental borrowing rate. As information from the lessor regarding the fair value of underlying assets and initial direct costs incurred by the lessor related to the leased assets is generally not available, the Company uses its incremental borrowing rate when initially recording real estate leases. The Company determines the incremental borrowing rate as the interest rate the Company would pay to borrow the funds necessary to obtain an asset of a similar value to the right-of-use asset, in a similar economic environment over a similar term.

*Leases*

Each capitalized lease is evaluated to determine if the Company would exercise any of the renewal options offered. Several material factors are considered in determining if the renewal option would be exercised, such as length of the renewal, renewal rate, and ability to transfer locations.

*Share-based payment arrangements*

The Company measures the cost of equity-settled transactions with officers and directors by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair values for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining and making assumptions about the most appropriate inputs to the valuation model including the expected life, volatility, dividend yield and forfeiture rate. Similar calculations are made to value warrants. Such judgments and assumptions are inherently uncertain and changes in these assumptions will affect the fair value estimates.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.9 Critical Accounting Estimates and Judgments (continued)

##### *Compound financial instruments*

The conversion feature and the warrants component of convertible debentures and convertible notes payable, and warrants denominated and exercisable in a foreign currency, are accounted for as derivative liabilities as their fair value is affected by changes in the fair value of the Company's SVS and in response to changes in foreign exchange rates. The estimates, assumptions and judgments made in relation to the fair value of derivative liabilities are subject to measurement uncertainty. The conversion feature and warrant component of the convertible debentures and warrants denominated and exercisable in a currency in other than the Company's functional currency, are required to be measured at fair value at each reporting period.

The valuation techniques used to determine fair value require inputs that involve assumptions and judgments such as estimating the future volatility of the stock price, expected dividend yield, and expected life. Such judgments and assumptions are inherently uncertain.

##### *Income taxes*

Income taxes and tax exposures recognized in the unaudited condensed interim consolidated financial statements reflect management's best estimate of the outcome based on facts known at the reporting date. The Company recognizes a liability when, based on its estimates, it anticipates a future income tax payment. A difference between an expected amount and the final tax outcome has an impact on current and deferred taxes in the period when the Company becomes aware of this difference.

In addition, when the Company incurs losses that cannot be associated with current or past profits, it assesses the probability of taxable profits being available in the future based on its budgeted forecasts. These forecasts are adjusted to take into account certain non-taxable income and expenses and specific rules on the use of unused credits and tax losses. When the forecasts indicate that sufficient future taxable income will be available to deduct the temporary differences, a deferred tax asset is recognized for all deductible temporary differences.

In addition, changes in tax laws could limit the ability of the Company to obtain tax deductions in future periods. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Company to realize the net deferred tax assets recorded at the reporting date could be impacted.

##### *Provisions*

The Company recognizes provisions if there is a present obligation (legal or constructive) that has arisen as the result of a past event, it is probable that the Company will be required to settle the obligation and the obligation can be reliably estimated. The Company's provision as at March 31, 2022 and December 31, 2021 relates to uncertain tax positions under Internal Revenue Code ("IRC") §280E for Patients Mutual Assistance Collective Corporation ("PMACC") and San Jose Wellness Solutions Corp. ("SJW"). Many of the central issues relating to the interpretations of IRC §280E remain unsettled, and there are critical accounting issues regarding the allocation of expenses to the cost of goods sold (thus avoiding disallowance as deductions under IRC §280E). The Company evaluated these uncertain tax treatments, using a probability-weighted approach to assess the range of possible outcomes as required in its adoption of IFRIC 23 and, although the Company strongly disagrees with the positions taken by the Internal Revenue Service and the findings of the U.S. Tax Court, it has determined that a reserve for uncertain tax position should be recorded for all years subject to statutory review (Note 19). The amount recognized as a provision reflects management's best estimate of the consideration required to settle the present obligation at the reporting date, considering the risks and uncertainties surrounding the obligation.

# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
For the Three Months Ended March 31, 2022 and 2021  
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## 2. Summary of Significant Accounting Policies (continued)

### 2.9 Critical Accounting Estimates and Judgments (continued)

#### *Going concern*

At the end of each reporting period, management exercises judgment in assessing the Company's ability to continue as a going concern by reviewing the Company's performance, resources and future obligations. The conclusion that the Company will be able to continue as a going concern is subject to critical judgments of management with respect to assumptions surrounding the short and long-term operating budgets, expected profitability, investment and financing activities and management's strategic planning. The assumptions used in management's going concern assessment are derived from actual operating results along with industry and market trends, and are consistent with those used to evaluate impairment of goodwill and intangible assets as at March 31, 2022. Management believes there is sufficient capital to meet the Company's business obligations for at least the next twelve months, after considering expected cash flows and the Company's cash position at period-end.

As indicated in Note 19, the Company has recognized a provision for particular uncertain tax positions which are related to PMACC and SJW. Management has considered, in consultation with outside counsel, that the final amount to be paid is uncertain and the timing of any payments arising from these proceedings or any future proceeding exceeds twelve months from the date that these unaudited condensed interim consolidated financial statements were authorized to be issued. No payments related to any of the provision amounts are expected to be paid until 2023 or later. The Company believes it will have funds in the future to satisfy any such required cash outflows from its operating cash flow performance and other sources of financing. However, it is possible that the Company will need to obtain additional capital to meet these uncertain cash flow requirements and there is no assurance that such capital will be available or available on favorable terms.

Management continues to monitor the Company's operational performance, progress of the tax litigation and appeals process, and its ability to raise funds.

These unaudited condensed interim consolidated financial statements do not reflect adjustments to the reported carrying values of assets and liabilities; reported revenues and expenses; or, classifications in the Unaudited Condensed Interim Consolidated Statements of Financial Position that would be necessary if the Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations.

### 2.10 Adoption of New Accounting Policies

The Company adopted the following standard effective January 1, 2022. These changes were made in accordance with the applicable transitional provisions.

#### *IAS 41 Agriculture*

As part of its 2018-2020 annual improvements to IFRS standards process, the IASB issued an amendment to IAS 41. The amendment removes the requirement in paragraph 22 of IAS 41 for entities to exclude taxation cash flow when measuring fair value of a biological assets using a present value technique. This will ensure consistency with the requirements in IFRS 13. The amendment is effective for annual periods beginning on or after January 1, 2022. The adoption of the standard did not have a material impact on the Company's unaudited condensed interim consolidated financial statements.

### 2.11 New, Amended, and Future IFRS Pronouncements

The Company has implemented all applicable IFRS standards recently issued by the IASB. Pronouncements that are not applicable or where it has been determined do not have a significant impact to the Company have been excluded herein.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 2. Summary of Significant Accounting Policies (continued)

#### 2.11 New, Amended, and Future IFRS Pronouncements (continued)

The Company is currently assessing the impact that adopting the new standards or amendments will have on its unaudited condensed interim consolidated financial statements. No material impact is expected upon the adoption of the following new standards issued but not yet effective:

##### *Amendments to IAS 1 - Classification of Liabilities as Current or Non-current*

The amendment clarifies the requirements relating to determining if a liability should be presented as current or non-current in the statement of financial position. Under the new requirement, the assessment of whether a liability is presented as current or non-current is based on the contractual arrangements in place as at the reporting date and does not impact the amount or timing of recognition. The amendment applies retrospectively for annual reporting periods beginning on or after January 1, 2023 (extended from January 1, 2022), with earlier application permitted.

##### *IAS 1 Presentation of Financial Statements and IFRS Practice Statement 2 Making Materiality Judgments (Amendments)*

In February 2021, the IASB issued amendments to IAS 1 *Presentation of Financial Statements* and IFRS Practice Statement 2 *Making Materiality Judgments*. The amendments help entities provide accounting policy disclosures that are more useful to primary users of financial statements by:

- Replacing the requirement to disclose "significant" accounting policies under IAS 1 with a requirement to disclose "material" accounting policies. Under this, an accounting policy would be material if, when considered together with other information included in an entity's financial statements, it can reasonably be expected to influence decisions that primary users of general purpose financial statements make on the basis of those financial statements.
- Providing guidance in IFRS Practice Statement 2 to explain and demonstrate the application of the four-step materiality process to accounting policy disclosures.

The amendments shall be applied prospectively. The amendments to IAS 1 are effective for annual periods beginning on or after January 1, 2023, with earlier application permitted.

##### *IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors (Amendment)*

In February 2021, the IASB issued amendments to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. The amendments introduce a new definition of 'accounting estimates' to replace the definition of 'change in accounting estimates' and also include clarifications intended to help entities distinguish changes in accounting policies from changes in accounting estimates. The amendments are effective for annual periods beginning on or after January 1, 2023, with earlier application permitted.

##### *IAS 12 Income Taxes (Amendment)*

In May 2021, the IASB issued amendments to the recognition exemptions under IAS 12 *Income Taxes*. The amendments narrowed the scope of the recognition exemption to require an entity to recognize deferred tax on initial recognition of particular transactions, to the extent that transaction gives rise to equal amounts of deferred tax assets and liabilities. These amendments apply to transactions for which an entity recognizes both an asset and liability, for example leases and decommissioning liabilities. The amendments are effective for annual periods beginning on or after January 1, 2023 with earlier application permitted.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 3. Business Combination

The Company completed one business combination during the three months ended March 31, 2022. The Urbn Leaf Acquisition (as defined below) was accounted for in accordance with IFRS 3. Due to the complexity associated with the valuation process and short period of time between the acquisition date and the period end, the identification and measurement of assets acquired, and liabilities assumed, as well as the measurement of consideration is provisional and subject to adjustment on completion of the valuation process and analysis of resulting tax effects. Management will finalize the accounting for acquisitions no later than one year from the date of the respective acquisition date and will reflect these adjustments retrospectively as required under IFRS 3. Differences between these provisional estimates and the final acquisition accounting may occur and these differences could have a material impact on the Company's future financial position and results of operations.

A provisional estimate of the fair value of the assets to be acquired and the liabilities to be assumed by the Company in connection with the acquisition is as follows:

	<u>Urbn Leaf Acquisition</u>
Acquisition date	March 1, 2022
Fair value of:	
Share capital issued	\$ 33,049,800
Non-controlling interests assumed	4,188,635
Settlement of note payable	<u>1,121,733</u>
Total purchase consideration	<u>\$ 38,360,168</u>
	<u>Urbn Leaf Acquisition</u>
Purchase consideration paid	\$ 38,360,168
Fair value of net assets acquired:	
Cash and restricted cash	3,268,427
Accounts receivable, net	402,681
Inventory	2,110,998
Due from other entities	474,028
Note receivable	1,140,600
Prepaid expense and other current assets	746,412
Property, plant and equipment, net (Note 11)	21,434,786
Right-of-use assets (Note 13)	18,478,790
Intangible assets (Note 12)	20,876,011
Deposits and other assets	584,925
Accounts payable and accrued liabilities	(16,096,874)
Lease liabilities (Note 13)	(26,257,031)
Deferred tax liability	(2,470,337)
Income taxes payable	(4,239,096)
Term loan, net	(13,005,439)
Notes payable	<u>(13,380,491)</u>
Total identifiable net assets acquired	(5,931,610)
Goodwill (Note 12)	<u>44,291,778</u>
Net assets acquired	<u>\$ 38,360,168</u>

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 3. Business Combination (continued)

Goodwill arising from acquisitions consist largely of the synergies and economies of scale expected from combining the operations of the businesses. These synergies include the use of the Company's existing infrastructure to expand operations, sales and profits as well as eliminations of redundant facilities and functions. None of the goodwill recognized is expected to be deductible for tax purposes.

#### *The Urbn Leaf Acquisition*

Urbn Leaf is a leading California cannabis retailer that owns and operates eight retail dispensaries in California, located in San Diego, San Ysidro, La Mesa, Grossmont, Vista, Grover Beach, Seaside and San Jose. Urbn Leaf also operates retail delivery services that cover the Grover Beach and San Ysidro areas from its Urbn Leaf branded retail dispensaries and has a partnership with a third party for delivery services in the greater San Diego area.

On March 1, 2022, pursuant to the terms of the definitive agreement announced on November 29, 2021, Harborside acquired 100% of the equity interest of Urbn Leaf (the "Urbn Leaf Acquisition") for a total purchase consideration of (a) the issuance of 60,000,000 SVS, valued at approximately \$33,050,000 and (b) the settlement of the principal and accrued interest of an unsecured promissory note valued at approximately \$1,100,000.

In connection with the Urbn Leaf Acquisition, the Company granted certain officers of the Company (i) options to purchase an aggregate of 5,758,797 SVS and (ii) restricted share units representing the right to receive up to an aggregate of 912,599 SVS, subject to the satisfaction of certain vesting conditions. Each option is exercisable into one SVS at an exercise price of C\$0.70 per SVS for a period of five years following the date of grant, in accordance with the terms of the Plan (as defined in Note 23).

Acquisition-related costs of approximately \$1,464,000 were included as a component of M&A and transactional expenses in the accompanying Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss).

#### *The Sublime Acquisition*

On July 2, 2021, the Company acquired 100% of the issued and outstanding shares of Sublime, for total purchase consideration of approximately \$44,700,000 (the "Sublime Acquisition"), refer to Note 3 of the audited consolidated financial statements for the year ended December 31, 2021. On January 24, 2022, the Company determined that the working capital surplus amounted to approximately \$2,085,000 representing 11,289.57 MVS.

### 4. Accounts receivable, net

The Company's accounts receivable, net is comprised of the following as at March 31, 2022 and December 31, 2021:

	<u>March 31, 2022</u>	<u>December 31, 2021</u>
Trade receivables	\$ 4,535,790	\$ 5,110,877
Sales tax receivables	55,927	53,301
Total	4,591,717	5,164,178
Provision for credit loss	<u>(815,665)</u>	<u>(617,821)</u>
Total accounts receivable, net	<u>\$ 3,776,052</u>	<u>\$ 4,546,357</u>

Accounts receivable are recognized initially at fair value and subsequently measured at amortized cost, less any provisions for expected credit losses.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 4. Accounts receivable, net (continued)

The Company provides trade credit to its wholesale, white label and distribution customers in the normal course of business and has established credit evaluation and monitoring processes to mitigate credit risk. Credit risk for these customers is assessed on a quarterly basis and a provision for expected credit losses is recorded where required. The Company does not offer extended payment terms to its retail customers. Retail transactions are paid for at the point of sale. Accordingly, credit risk from retail customers is limited to outstanding balances due from debit card processors. As at March 31, 2022 and December 31, 2021, there was \$144,047 and \$167,396, respectively, outstanding from debit card processors that is included within trade receivables.

The Company assesses the risk of collectability of accounts receivable on a quarterly basis. Estimates of expected credit losses take into account the Company's collection history, deterioration of collection rates during the average credit period, as well as observable changes in and forecasts of future economic conditions that affect default risk. Where applicable, the carrying amount of a trade receivable is reduced for any expected credit losses through the use of a provision for expected credit losses. The provision for expected credit losses reflects the Company's best estimate of probable losses in the trade receivables accounts.

Activity in the provision for expected credit losses was as follows:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Balance, beginning of period	\$ 617,821	\$ 242,721
Provision for expected credit losses assumed in acquisitions	120,000	277,224
Current year additions to provision for expected credit losses	135,094	499,157
Amounts reversed	<u>(57,250)</u>	<u>(401,281)</u>
Balance, end of period	<u>\$ 815,665</u>	<u>\$ 617,821</u>

The Company's aging of accounts receivable was as follows as at March 31, 2022 and December 31, 2021:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Current	\$ 1,815,942	\$ 2,132,748
1 - 30 days	710,991	1,033,575
31 - 60 days	381,147	812,801
61 - 90 days	310,128	396,747
Over 90 days	<u>1,373,509</u>	<u>788,307</u>
Total	<u>\$ 4,591,717</u>	<u>\$ 5,164,178</u>

### 5. Inventories

The Company's inventory includes both purchased items and internally produced inventory. The Company's inventory was comprised of the following items as at March 31, 2022 and December 31, 2021:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Raw materials	\$ 1,840,044	\$ 1,633,803
Work-in-process	660,178	1,075,499
Finished goods	<u>6,030,293</u>	<u>3,704,848</u>
Total	<u>\$ 8,530,515</u>	<u>\$ 6,414,150</u>

During the three months ended March 31, 2022 and 2021, inventory expensed to cost of goods sold was approximately \$10,426,000 and \$6,483,000, respectively. Management determined net realizable value as the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to complete a sale.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 5. Inventories (continued)

There was no impairment recorded during the three months ended March 31, 2022 and 2021.

### 6. Biological Assets

Biological assets consist of cannabis plants. The changes in the carrying value of biological assets was as follows:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Balance, beginning of period	\$ 443,839	\$ 1,321,069
Costs capitalized	2,883,591	9,671,956
Changes in fair value less costs to sell due to biological asset transformation	(1,264,212)	(3,845,228)
Transferred to inventory upon harvest	<u>(1,284,294)</u>	<u>(6,703,958)</u>
Balance, end of period	<u>\$ 778,924</u>	<u>\$ 443,839</u>

The Company measures its biological assets at their fair value less costs to sell. This is determined using a model which estimates the expected harvest yield in grams for plants currently being cultivated, and the expected selling price less costs to sell per gram.

The Company's method of accounting for biological assets attributes value accretion on a straight-line basis throughout the life of the biological asset from initial cloning to the point of harvest. The following inputs and assumptions are all categorized within Level 3 on the fair value hierarchy and were used in determining the fair value of biological assets:

<b>Inputs and assumptions</b>	<b>Description</b>	<b>Correlation between inputs and fair value</b>
Average selling price per gram	Represents the average selling price per gram of dried cannabis net of excise taxes, where applicable, for the period for all strains of cannabis sold, which is expected to approximate future selling prices.	If the average selling price per gram was higher (lower), estimated fair value would increase (decrease).
Average attrition rate	Represents the weighted average number of plants culled at each stage of production.	If the average attrition rate was lower (higher) estimated fair value would increase (decrease).
Weighted average yield per plant	Represents the weighted average number of grams of dried cannabis inventory expected to be harvested from each cannabis plant.	If the weighted average yield per plant was higher (lower), estimated fair value would increase (decrease).
Standard cost per gram to complete production	Based on actual production costs incurred divided by grams produced in the period.	If the standard cost per gram to complete production was lower (higher), estimated fair value would increase (decrease).
Weighted average effective yield	Represents the estimated percentage of harvested product that meets specifications in order to be sold as a dried cannabis product.	If the weighted average effective yield was higher (lower), the estimated fair value would increase (decrease).
Stage of completion in production process	Calculated by taking the weighted average number of days in production over a total average grow cycle of approximately thirteen weeks.	If the number of days in production was higher (lower), estimated fair value would increase (decrease).

Biological assets as at March 31, 2022 and December 31, 2021 include an allocation of depreciation of \$237,396 and \$270,484, respectively.



# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 6. Biological Assets (continued)

The following table quantifies each significant unobservable input, and provides the impact that a 10% increase or decrease in each input would have on the fair value of biological assets:

		As at March 31, 2022		As at December 31, 2021	
	Assumptions:	Input	10% change	Input	10% change
i	Weighted average of expected loss of plants until harvest [a]	3%	\$ 2,551	3%	\$ 1,529
ii	Expected yields (dry grams of cannabis per plant) [b]	51 grams	\$ 77,838	52 grams	\$ 44,454
iii	Weighted average number of growing weeks completed as a percentage of total growing weeks as at year-end	54%	\$ 77,838	58%	\$ 44,454
iv	Estimated selling price (per gram) [c]	\$1.28 per gram dried flower \$0.15 per gram dried trim	\$ 212,962	\$1.25 per gram dried flower \$0.14 per gram dried trim	\$ 171,702
v	After harvest cost to complete and sell (per gram)	\$0.76 per gram dried flower \$0.15 per gram dried trim	\$ 135,125	\$0.88 per gram dried flower \$0.14 per gram dried trim	\$ 127,249

[a] Weighted average of expected loss of plants until harvest represents loss via plants that do not survive to the point of harvest. It does not include any financial loss on a surviving plant.

[b] Expected average yields for cannabis plants vary based on the mix of strains and number of plants existing at each reporting date. As at March 31, 2022 and December 31, 2021, it was expected the Company's biological assets would yield 26 and 21 grams of dried flower per plant, respectively, and 25 and 31 grams of dried trim per plant, respectively.

[c] The estimated selling price (per gram) represents the actual average sales price for the Company's strains sold as bulk products.

The Company estimates the harvest yields for cannabis at various stages of growth. As at March 31, 2022 and December 31, 2021, it is expected that the Company's biological assets will yield approximately 2,761,032 and 2,031,834 grams of dry cannabis flower, respectively, and 2,586,347 and 3,080,842 grams of dry trim, respectively, when harvested. The fair value adjustments on biological assets are presented separately on the Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss).

The Company's estimates, by their nature, are subject to changes that could result from volatility of market prices, unanticipated regulatory changes, harvest yields, loss of crops, changes in estimates and other uncontrollable factors that could significantly affect the future fair value of biological assets.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 7. Prepaid Expenses

On August 1, 2021, the Company entered into a prepayment of inventory agreement with Loudpack for \$1,500,000 of goods at wholesale cost. Under the terms of the agreement, the Company receives a minimum discount of 10% on all purchases from Loudpack. As at March 31, 2022, the prepayment had a remaining balance of \$427,764 which is included as a component of advances made to suppliers and consultants. Subsequent to the three months ended March 31, 2022, the prepayment of inventory was applied as purchase consideration in the Loudpack Acquisition (Note 32).

As at March 31, 2022 and December 31, 2021, prepaid expenses were comprised of the following:

	<u>March 31, 2022</u>	<u>December 31, 2021</u>
Excise taxes	\$ 1,105,779	\$ 467,844
Insurance and rent	819,096	986,549
Advances made to suppliers and consultants	1,340,741	1,872,237
Payroll and income taxes	65,805	509,304
Taxes and fees	53,470	11,249
Licenses and other	<u>1,225,786</u>	<u>485,383</u>
Total prepaid expenses	<u>\$ 4,610,677</u>	<u>\$ 4,332,566</u>

### 8. Other current assets

On December 18, 2020, the Company entered into a securities purchase agreement (the "FGW Agreement") to acquire a 50.1% interest in FGW (the "FGW Transaction"), with an initial ownership interest of 21% (refer to Note 3 of the audited consolidated financial statements for the year ended December 31, 2021). Upon closing of the FGW Transaction, FGW issued the Company a convertible note, in the principal amount of \$1,265,000 (the "FGW Note"). Upon receipt of certain regulatory approvals from the Director of the Office of Cannabis in San Francisco relating to the FGW Transaction (the "Specified Approval") and conversion of the FGW Note in accordance with its terms, the Company's total ownership in FGW will increase to 80%.

As at March 31, 2022 and December 31, 2021, the Company used the Monte Carlo Simulation option-pricing model ("Monte Carlo model") to estimate the fair value of the conversion option embedded in the FGW Note and determined the fair value of the conversion option to be \$1,061,048 and \$1,230,655, respectively, which was recorded as a component of other current assets. The \$169,607 change in fair value for the three months ended March 31, 2022 is included as a component of fair value gain in other current assets and derivative liabilities in the accompanying Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss).

### 9. Investments and Advances

The changes in investments and advances were as follows for the three months ended March 31, 2022:

	<u>Investments FVTPL</u>
Balance as at December 31, 2021	\$ 2,458,011
Interest accrued	199,110
Changes in fair value	<u>516,350</u>
Balance as at March 31, 2022	<u>\$ 3,173,471</u>

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 9. Investments and Advances (continued)

#### *Convertible Debentures*

On March 5, 2021, the Company, through one of its subsidiaries, purchased \$5,000,000 of 15% Senior Secured Convertible Debentures (the "Debentures") of Loudpack with an original maturity date of December 31, 2022. The Debentures bore interest at the rate of 15% and were secured by first and second priority liens on assets of Loudpack and its subsidiaries, as well as joint and several guarantees provided by direct and indirect subsidiaries of Loudpack and certain of its members. Prior to maturity, the Debentures were subject to both optional and mandatory conversion features as well as an optional redemption feature and additional restrictions imposed upon Loudpack by the Company pertaining to the ultimate use of the funds used to purchase the Debentures. The Debentures were also subject to an optional conversion feature at maturity.

On April 4, 2022, the Company completed the acquisition of Loudpack (Note 32). Concurrent with the closing of the acquisition, the Debentures were restructured such that they will remain outstanding through April 4, 2025.

For the three months ended March 31, 2022, the Company accrued interest income of \$199,110 related to the Debentures.

The Company used the Monte Carlo model to estimate the fair value of the Debentures at issuance and at each reporting date. The Monte Carlo model uses certain Level 2 inputs in its valuation model. The key Level 2 inputs used by management to determine the fair value are: (i) the expected future volatility in the price of the Company's SVS, (ii) the risk-free interest rate, and (iii) the expected life of the instruments. The risk-free interest rate is based on data from the Federal Reserve Statistical Release and is extrapolated for interim periods. The expected lives are based on the anticipated date of public listing. Volatility was calculated by using the stock price returns from the comparable public companies as there was insufficient trading history in the Company's shares.

The following assumptions were used to value the Debentures as at March 31, 2022:

	<b>March 31, 2022</b>
Risk-free interest rate	1.95%
Share price - U.S. \$	\$ 0.61
Expected volatility	71.25%
Expected remaining life	1.50 years
Fair value	\$ 3,173,471

For the three months ended March 31, 2022, the Company recorded fair value changes of \$516,350 which was recorded as a component of fair value gain in other current assets and derivative liabilities in the accompanying Unaudited Condensed Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss).

### 10. Note receivable

On April 16, 2021, Urbn Leaf entered into a membership interest repurchase agreement to sell back their 33.3% membership interest in 2220 NBC, LLC for \$1,150,000. The note receivable was assumed as part of the Urbn Leaf Acquisition (Note 3). The note receivable accrues interest at a rate of 10% per annum on the outstanding daily unpaid principal amount. Initial payments are to be paid on January 1, 2022 or the commencement of operations, whichever occurs first. The initial payment date may be extended by an additional six months from January 1, 2022 to July 1, 2022. Payments are to be made following a five-year amortization schedule of equal monthly payments following the initial payment date.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 10. Note receivable (continued)

As at March 31, 2022, principal and accrued interest amounted to \$1,151,773.

### 11. Property, Plant and Equipment, net

As at March 31, 2022 and December 31, 2021, the Company's property, plant and equipment, net consisted of the following:

	Land	Retail and Agricultural Buildings	Agricultural and Manufacturing Equipment	CIP	Furniture, fixtures, and equipment	Leasehold improvements	Total
<b>At Cost</b>							
As at December 31, 2020	\$ 3,404,572	\$ 11,068,493	\$ 5,964,202	\$ 835,706	\$ 2,097,842	\$ 405,102	\$ 23,775,917
Additions	-	2,995	125,721	2,998,291	113,922	68,322	3,309,251
Business acquisitions	310,000	2,290,000	326,178	517,524	278,129	1,124,688	4,846,519
Disposals and transfers	-	-	(72,210)	(25,994)	(29,312)	129	(127,387)
Reclass on completed phase of construction	-	1,684,336	641,997	(2,343,381)	17,048	-	-
As at December 31, 2021	3,714,572	15,045,824	6,985,888	1,982,146	2,477,629	1,598,241	31,804,300
Additions	-	-	8,762	62,554	-	4,095	75,411
Business acquisition (Note 3)	5,720,255	8,420,084	-	112,570	1,316,420	5,865,457	21,434,786
Disposals and transfers	-	-	(82,367)	-	-	-	(82,367)
As at March 31, 2022	\$ 9,434,827	\$ 23,465,908	\$ 6,912,283	\$ 2,157,270	\$ 3,794,049	\$ 7,467,793	\$ 53,232,130
<b>Accumulated depreciation</b>							
As at December 31, 2020	-	1,946,969	2,782,406	-	982,358	154,577	5,866,310
Disposals and transfers	-	35,242	(26,120)	-	(9,746)	(31,753)	(32,377)
Depreciation expense	-	805,892	1,178,227	-	398,340	72,298	2,454,757
As at December 31, 2021	-	2,788,103	3,934,513	-	1,370,952	195,122	8,288,690
Disposals and transfers	-	-	(5,204)	-	-	-	(5,204)
Depreciation expense	-	268,482	331,741	-	103,266	88,236	791,725
As at March 31, 2022	\$ -	\$ 3,056,585	\$ 4,261,050	\$ -	\$ 1,474,218	\$ 283,358	\$ 9,075,211
<b>Net Book Value</b>							
As at December 31, 2021	3,714,572	12,257,721	3,051,375	1,982,146	1,106,677	1,403,119	23,515,610
As at March 31, 2022	\$ 9,434,827	\$ 20,409,323	\$ 2,651,233	\$ 2,157,270	\$ 2,319,831	\$ 7,184,435	\$ 44,156,919

Depreciation expense of \$791,725 and \$572,517 was recorded for the three months ended March 31, 2022 and 2021, respectively, as follows:

	March 31, 2022	March 31, 2021
Cost of goods sold - wholesale	\$ 509,243	\$ 513,132
Expenses	282,482	59,385
Total depreciation and amortization relating to property, plant and equipment, net	\$ 791,725	\$ 572,517

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 12. Intangible Assets and Goodwill

There were no indicators of impairment during the period end. A reconciliation of the beginning and ending balances of intangible assets and goodwill for the three months ended March 31, 2022 was as follows:

	Intangible Assets				Total	Goodwill
	Licenses	Trademark	Developed technology	Customer relationships		
<b>At Cost</b>						
Balance as at December 31, 2020	\$ 57,874,884	\$ 46,666	\$ -	\$ -	\$ 57,921,550	\$ 14,366,055
Additions:						
Sublime acquisition	13,400,000	6,800,000	3,200,000	6,300,000	29,700,000	17,372,223
Accucanna acquisition	2,900,000	-	-	-	2,900,000	3,343
Impairment	(24,674,884)	(23,267)	-	-	(24,698,151)	(535,044)
Balance as at December 31, 2021	49,500,000	6,823,399	3,200,000	6,300,000	65,823,399	31,206,577
Additions (Note 3):						
Urbn Leaf acquisition	20,876,011	-	-	-	20,876,011	44,291,778
Sublime acquisition	-	-	-	-	-	1,148,313
Balance as at March 31, 2022	<u>\$ 70,376,011</u>	<u>\$ 6,823,399</u>	<u>\$ 3,200,000</u>	<u>\$ 6,300,000</u>	<u>\$ 86,699,410</u>	<u>\$ 76,646,668</u>
<b>Accumulated Amortization</b>						
As at December 31, 2021	\$ -	\$ 247,628	\$ 316,558	\$ 566,569	\$ 1,130,755	\$ -
Amortization	-	113,335	160,000	286,363	559,698	-
As at March 31, 2022	<u>\$ -</u>	<u>\$ 360,963</u>	<u>\$ 476,558</u>	<u>\$ 852,932</u>	<u>\$ 1,690,453</u>	<u>\$ -</u>
<b>Net book value</b>						
As at December 31, 2021	49,500,000	6,575,771	2,883,442	5,733,431	64,692,644	31,206,577
As at March 31, 2022	<u>\$ 70,376,011</u>	<u>\$ 6,462,436</u>	<u>\$ 2,723,442</u>	<u>\$ 5,447,068</u>	<u>\$ 85,008,957</u>	<u>\$ 76,646,668</u>

The fair value of the acquired intangible assets and goodwill from the Urbn Leaf Acquisition are provisional pending receipt of the final valuation for the assets.

Amortization expense of \$559,698 and \$2,435 was recorded for the three months ended March 31, 2022 and 2021, respectively.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 13. Right-of-use Assets and Lease Liabilities

#### *Right-of-use Assets*

As at March 31, 2022 and December 31, 2021, the Company's right-of-use assets consisted of the following:

	<b>Right-of-use Assets - Buildings</b>
<b>Cost</b>	
Balance as at December 31, 2021	\$ 6,101,302
Acquired leases	<u>18,478,790</u>
Balance as at March 31, 2022	<u>\$ 24,580,092</u>
<b>Accumulated amortization</b>	
Balance as at December 31, 2021	1,667,905
Amortization expense	<u>367,463</u>
Balance as at March 31, 2022	<u>\$ 2,035,368</u>
<b>Net book value</b>	
As at December 31, 2021	<u>4,433,397</u>
As at March 31, 2022	<u>\$ 22,544,724</u>

#### *Lease Liabilities*

The Company's lease liabilities consist of various real property leases. The lease liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate. The incremental borrowing rate for the additions during the three months ended March 31, 2022 and 2021 was 9.5% and 8.5%, respectively, for leases acquired in acquisitions.

The following is a summary of the activity in the Company's lease liability for the three months ended March 31, 2022:

Balance as at December 31, 2021	\$ 6,328,884
Acquired leases	26,257,031
Lease payments	(735,418)
Interest expense	<u>415,643</u>
Ending lease liability as at March 31, 2022	32,266,140
Less: current portion	<u>(2,448,420)</u>
Non-current lease liability	<u>\$ 29,817,720</u>

The Company also leases office and other retail space from related parties (Note 27). The Company recognized no material expenses related to short-term leases and leases of low-value assets for the three months ended March 31, 2022.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 14. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities of the Company are principally comprised of amounts outstanding for trade purchases incurred in the normal course of business.

The Company's accounts payable and accrued liabilities consist of the following as at March 31, 2022 and December 31, 2021:

	<u>March 31, 2022</u>	<u>December 31, 2021</u>
Accounts payable	\$ 22,886,542	\$ 9,752,220
Accrued cultivation, excise, local and sales taxes	14,226,608	8,870,792
Accrued liabilities	2,898,429	2,954,185
Accrued payroll	2,732,792	2,115,617
Accrued loyalty rewards program	<u>1,129,021</u>	<u>-</u>
Total accounts payable and accrued liabilities	<u>\$ 43,873,392</u>	<u>\$ 23,692,814</u>

### 15. Notes payable

The Company assumed notes payable through the Urbn Leaf Acquisition (Note 3). The notes payable consisted of the following as at March 31, 2022:

	<u>Total outstanding</u>
Bridge financing	\$ 5,833,009
Urbn Leaf - Lafayette Street	304,109
Urbn Leaf - UL Visalia LLC	247,973
SBC Private loans	513,650
Senior Secured Debt	<u>7,479,000</u>
Total notes payable	14,377,741
Less unamortized deferred financing costs	<u>(847,025)</u>
Total notes payable, net	<u>\$ 13,530,716</u>

The associated loan fees charged with obtaining the notes payable are recorded as a reduction to the carrying amount and are being amortized as interest expense within the unaudited condensed interim consolidated financial statements over the term of the notes.

#### *Senior Secured Debt*

In December 2020, Urbn Leaf received a loan ("Senior Secured Debt") in the amount of \$5,400,000. The Senior Secured Debt matures on December 21, 2022, at which time all outstanding principal plus an additional fee of \$2,079,000 is due. Monthly payments are interest only with a variable interest rate of the higher of 12.5% or the prime rate plus 9%. As at March 31, 2022, the interest rate was 12.5%. The loan is secured by certain collateral, specified under the Credit and Guaranty Agreement dated December 21, 2022, in respect of the loan.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 15. Notes payable (continued)

#### *Bridge financing*

On July 23, 2021, Urbn Leaf entered into a bridge financing in the form of a \$5,200,000 secured promissory note. The bridge financing bore interest at a rate of 15% per annum with principal and accrued interest due and payable on December 31, 2021, or earlier, depending on timing of certain events as defined in the promissory note, but subject to certain extension provisions set out in the promissory note. Urbn Leaf had the option to extend the maturity date of the bridge financing by 60 days which extended the note to February 28, 2022 (the "Initial Extension"). The Initial Extension triggered an extension fee equal to 1% of the outstanding principal amount plus all accrued interest thereon for every 30 days that the maturity date is extended. Following the Initial Extension, Urbn Leaf had the option to extend the maturity date by an additional 60 days which extended the note to April 30, 2022 for an additional extension fee for every 30 days that the maturity date was extended.

On April 29, 2022, the Company announced that the bridge financing assumed as part of the Urbn Leaf Acquisition had been repaid by: (i) a cash payment in the amount of \$358,541; and (ii) the issuance of approximately \$5,870,000 worth of SVS at a price of C\$0.45 per SVS (16,660,993 SVS) (Note 32).

#### *Urbn Leaf - Lafayette Street*

The membership interests of Lafayette Street Property Management, LLC were acquired using an unsecured, non-interest bearing note payable in the amount of \$2,500,000. The terms of the note were a \$500,000 down payment, and the remaining \$2,000,000 to be paid over twenty-four months in equal installments.

#### *Urbn Leaf - UL Visalia LLC*

On July 30, 2019, Urbn Leaf funded 80% of the membership interest of UL Visalia LLC for a total payment of \$1,000,000. The terms of the payment plan included two initial payments totaling \$500,000 and the remaining \$500,000 repaid pursuant to a second amendment to the amended memorandum of understanding. The note payable is unsecured and non-interest bearing.

#### *SBC Private loans*

In December 2016, SBC Management LLC ("SBC") re-purchased the stock it had previously issued to the legacy partner for a total consideration of \$950,000. The unsecured loan bore interest at a rate of 10% per annum and matured on January 26, 2022. The loan was assumed as part of the Urbn Leaf Acquisition on March 1, 2022 in the amount of \$280,265. On May 11, 2022, the Company repaid the principal and accrued interest totaling \$250,665 (Note 32).

In May 2017, SBC borrowed \$100,000 from an individual at an interest rate of 12% per annum. The unsecured loan is interest only, with interest payments of \$1,000 per month through May 9, 2022, at which time the full principal balance is due. The loan was assumed as part of the Urbn Leaf Acquisition on March 1, 2022 in the amount of \$100,000. On May 19, 2022, the Company entered into the third amendment to the promissory note extending the maturity date to May 9, 2023 (Note 32).

In August 2017, SBC borrowed \$50,000 from the same individual at an interest rate of 12% per annum. The unsecured loan is interest only, with interest payments of \$500 per month through August 16, 2022, at which time the full principal balance is due. The loan was assumed as part of the Urbn Leaf Acquisition on March 1, 2022 in the amount of \$50,000. On May 19, 2022, the Company entered into the third amendment to the promissory note extending the maturity date to May 9, 2023 (Note 32).

In April 2018, SBC borrowed \$89,000 from an individual for an equipment purchase, with 3% simple interest. The unsecured loan matured in May 2020 and was verbally agreed to be repaid subsequent to the closing of the acquisitions. The loan was assumed as part of the Urbn Leaf Acquisition on March 1, 2022 in the amount of \$77,010. On May 18, 2022, the Company repaid the principal and accrued interest totaling \$77,010 (Note 32).



# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 16. Revolving Credit Facility

On March 19, 2021, the Company entered into a \$12,000,000 senior secured revolving credit facility (the "Facility") with a federally regulated commercial bank (the "Bank"), as amended on June 29, 2021 and December 6, 2021. The Facility included a maturity date of March 2023, and featured a variable interest rate based on the prime rate charged by the Bank plus 2.5%, with a floor rate of 5.75%. In conjunction with the Term Loan (Note 17), the Facility was paid in full and terminated in February 2022. The Facility required an interest reserve, which was released upon termination of the Facility.

As consideration for the Facility, the Company, among other things: (i) delivered a commercial security agreement, an assignment of deposit accounts, and a security agreement in respect of cash collateral to the Bank; (ii) made an upfront cash payment based on the principal amount of the Facility to the Bank as an original issue discount; and (iii) issued 4,100 warrants to the Bank to purchase MVS (the "Bank Warrants"), each of which entitled the Bank to purchase one MVS of the Company at a price of C\$369, at any time prior to March 19, 2023. The Bank Warrants were subject to the Mandatory Conversion that occurred on March 31, 2022 (Note 22).

The fair value of the warrants was determined using a Black-Scholes-Merton option pricing model with the following assumptions as at March 19, 2021:

Risk-free interest rate		0.17%
Exercise price - U.S. \$	\$	2.95
Share price - U.S. \$	\$	1.98
Expected volatility		131%
Expected remaining life		2 years
Fair value	\$	466,716

The Bank Warrants were included as a component of deposits and other assets in the accompanying Unaudited Condensed Interim Consolidated Statements of Financial Position. The Bank Warrants were amortized on a straight-line basis over the two-year term of the Facility. In connection with the payoff and termination of the Facility, during the three months ended March 31, 2022, the Company amortized the remaining warrants and deferred financing costs of approximately \$230,000 and \$136,000, respectively.

### 17. Term Loan

On November 29, 2021, in conjunction with the intended acquisitions of Urbn Leaf and Loudpack, the Company announced that it had signed a non-binding term sheet with Pelorus Fund REIT, LLC ("Pelorus") for a total of approximately \$77,300,000 of debt financing (the "Term Loan") which would be used primarily to retire certain existing loans, including the Facility, and provide additional working capital to the Company, Urbn Leaf and Loudpack. The Company executed the loan and security agreement on February 10, 2022.

The Term Loan was funded in two tranches, with the first occurring prior to closing on the acquisitions of Urbn Leaf and Loudpack, and the second tranche funded to the Company post-closing of the Loudpack Acquisition (Note 32). The first tranche was funded in three separate loans, with a loan to each of Urbn Leaf, Loudpack and the Company. The Company received approximately \$15,500,000, Loudpack received approximately \$16,400,000 and Urbn Leaf received approximately \$13,500,000 of the aggregate funds under the first tranche. From its share of the proceeds of the Term Loan, the Company repaid the \$12,000,000 outstanding under the Facility (Note 16).

The Term Loan contains a nominal interest rate of 10.25% and requires monthly interest payments until the maturity date. The Company is obligated to make principal payments in the amount of 7.5% of the then outstanding balance on both the 36th and 48th payment dates. The remaining principal is due on the maturity date of February 10, 2027.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 17. Term Loan (continued)

The Term Loan is subject to debt service ratio requirements, interest reserves, certain cross-corporate guarantees and defaults, subordination agreements and intercreditor agreements, along with a general corporate guaranty from the Company and is secured by certain real estate assets, cannabis licenses and other assets of the Company, Urbn Leaf and Loudpack. As at March 31, 2022, the Company was in compliance with these covenants.

The interest reserve as at March 31, 2022 amounted to \$2,850,076 and is recorded as restricted cash in the accompanying Unaudited Condensed Interim Consolidated Statements of Financial Position.

The associated loan fees charged with obtaining the Term Loan were recorded as a reduction to the carrying amount and are being amortized as interest expense within the unaudited condensed interim consolidated financial statements over the five-year term.

As at March 31, 2022, the outstanding balance less unamortized deferred financing costs was \$27,690,207. As at March 31, 2022, unamortized deferred financing costs amounted to \$1,215,448.

### 18. Derivative Liabilities

The following table provides a reconciliation of the beginning and ending balance of derivative liabilities and the change in fair value of derivative liabilities:

	<b>SVS Warrants and MVS Warrants Liability</b>
Balance as at December 31, 2021	\$ 779,643
Change in fair value of derivative liabilities	(331,605)
Effects of foreign exchange	6,958
Balance as at March 31, 2022	<u>\$ 454,996</u>

#### *Private Placement Offering of SVS Warrants and MVS Warrants*

On February 18, 2021, the Company issued warrants to purchase SVS ("SVS Warrants") and warrants to purchase MVS ("MVS Warrants"), in connection with an upsized brokered private placement of units. The warrants are classified as a liability based on the fixed-for-fixed criterion under IAS 32, *Financial Instruments: Presentation*. Due to the Mandatory Conversion (see Note 22), the MVS Warrants are instead calculated using the corresponding amount of SVS using a ratio of 100 SVS per MVS.

The Company used the Monte Carlo model to estimate the fair value of the derivative liabilities at issuance and at each reporting date. The Monte Carlo model uses certain Level 2 inputs in its valuation model. The key Level 2 inputs used by management to determine the fair value are: (i) the expected future volatility in the price of the Company's SVS, (ii) the risk-free interest rate, and (iii) the expected life of the instruments. The risk-free interest rate is based on data from the Federal Reserve Statistical Release and is extrapolated for interim periods. The expected lives are based on the expected lives of the instrument. Volatility was calculated by using the stock price returns from the comparable public companies as there was insufficient trading history in the Company's shares.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 18. Derivative Liabilities (continued)

#### *Private Placement Offering of SVS Warrants and MVS Warrants (continued)*

The following assumptions were used to value the SVS Warrants as at March 31, 2022 and December 31, 2021:

	<u>March 31, 2022</u>	<u>December 31, 2021</u>
Risk-free interest rate	2.26%	0.92%
Exercise price - CAD	C\$3.69	C\$3.69
Share price - CAD	C\$0.76	C\$0.46
Expected volatility	77.02%	108.74%
Expected remaining life	1.89 years	2.13 years
Fair value	\$454,996	\$328,867

The following assumptions were used to value the MVS Warrants as at December 31, 2021:

	<u>December 31, 2021</u>
Risk-free interest rate	0.92%
Exercise price - CAD	C\$369
Expected volatility	108.74%
Expected remaining life	2.13 years
Fair value	\$450,776

### 19. Provisions

#### *IRC §280E*

Certain subsidiaries of the Company operate in the cannabis industry and are subject to IRC §280E, which prohibits businesses engaged in the trafficking of controlled substances (including cannabis as specified in Schedule I of the Controlled Substances Act) from deducting ordinary and necessary business expenses. This can result in permanent tax differences resulting from normal business expenses which are deemed non-allowable under IRC §280E. Many of the central issues relating to the interpretation of IRC §280E remain unsettled, and there are critical tax accounting issues regarding the allocation of expenses to the cost of goods sold (thus avoiding disallowance as deductions under IRC §280E). IFRIC 23 - *Uncertainty over Income Tax Treatments* provides guidance that adds to the requirements in IAS 12 by specifying how to reflect the effects of uncertainty in accounting for income taxes. The Company evaluated these uncertain tax treatments, using a probability-weighted approach to assess the range of possible outcomes as required in its adoption of IFRIC 23 and, although it strongly disagrees with the positions taken by the Internal Revenue Service and the findings of the U.S. Tax Court, the Company has determined that a reserve for an uncertain tax position should be recorded for all years subject to statutory review.

The Company has engaged outside counsel in an attempt to successfully negotiate the settlement and subsequent payment of its potential liabilities under IRC §280E, but it does not currently expect any resultant potential liabilities or any possible payments resulting from the cases to be resolved within 12 months of the issuance of these unaudited condensed interim consolidated financial statements.

Although the Company, as described above, is actively engaged in working towards a settlement agreement and subsequent repayment plan with the Internal Revenue Service, an uncertain tax position has been recorded based on the unknown outcome of the settlement discussions. As at March 31, 2022 and December 31, 2021, the reserve totaled \$36,498,436 and \$36,051,249, respectively, a sum which includes the separate tax proceedings described below.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 19. Provisions (continued)

#### *PMACC*

PMACC is currently involved in two separate tax proceedings. The first, *PMACC v. Commissioner*, was an appeal to the United States Court of Appeals for the Ninth Circuit of an adverse Tax Court decision that was issued on November 29, 2018. In that decision, the Tax Court disallowed PMACC's allocation of certain items of expense to cost of goods sold, holding that they were instead deductions barred by IRC §280E. At issue are PMACC's corporate tax returns for the fiscal years ended July 31, 2007 through July 31, 2012. The Tax Court held that the expenses were ordinary and substantiated business expenses but, because PMACC's business consists of trafficking in a Schedule I controlled substance, the expenses must be disallowed. On October 21, 2019, after a review process under Rule 155, the Tax Court determined that PMACC's total liability was \$11,013,237 plus accrued interest. In its ruling, the Tax Court rejected the assertion of penalties by the Internal Revenue Service ("IRS"), finding that the unsettled state of the law and the fact that PMACC acted reasonably and in good faith, meant that penalties under IRC §6661(a) would be inappropriate. Accordingly, management has not included penalties in the estimated provision at period end. In December 2019, PMACC appealed the Tax Court decision to the United States Court of Appeals for the Ninth Circuit, which heard oral arguments in the case on February 9, 2021 and affirmed the Tax Court decision on April 22, 2021.

In a second Tax Court proceeding related to deductions barred by IRC §280E, the IRS issued a notice of deficiency disallowing all deductions taken in their entirety and asserting that PMACC owed \$16,035,218 in additional taxes and penalties for fiscal 2016. The Company filed its initial petition in this case to the Tax Court on February 13, 2020. As the Ninth Circuit has ruled on the earlier PMACC tax case, this matter is expected to be put back on the Tax Court calendar sometime during the year ended December 31, 2022.

#### *SJW*

SJW is involved in two separate tax proceedings. The first involves the 2010, 2011, and 2012 tax years, and in this case, the IRS asserted a tax deficiency of \$2,120,215. The second proceeding involves the 2014 and 2015 tax years and in the second case the IRS asserted that SJW owed an additional \$2,064,363 in taxes and penalties. Both of these proceedings involve substantially the same issues as the PMACC cases.

On February 17, 2021, the U.S. Tax Court ruled in favor of the Commissioner of Internal Revenue with respect to the cases for SJW. The Company appealed the Tax Court decisions on May 14, 2021. In an effort to resolve the matter as part of a global settlement, the Company has withdrawn its appeal.

### 20. General and Administrative Expenses

For the three months ended March 31, 2022 and 2021, general and administrative expenses consisted of the following:

	<b>March 31, 2022</b>	<b>March 31, 2021</b>
Advertising and promotion	\$ 258,903	\$ 157,099
Banking and processing fees	533,633	230,964
Other general administrative	22,135	11,656
Office and general expenses	2,335,090	1,016,859
Salaries and benefits	3,395,605	2,740,600
Sales and marketing	541,257	-
Taxes and licenses	240,232	133,814
Travel and entertainment	<u>154,718</u>	<u>33,074</u>
Total	<u>\$ 7,481,573</u>	<u>\$ 4,324,066</u>

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 21. Income Taxes

Harborside Inc. is treated as a U.S. corporation for U.S. federal income tax purposes under IRC §7874 and is subject to U.S. federal income tax. However, for Canadian tax purposes, the Corporation is expected, regardless of any application of IRC §7874, to be treated as a Canadian resident company (as defined in the ITA) for Canadian income tax purposes. As a result, the Corporation will be subject to taxation both in Canada and the U.S. Notwithstanding the foregoing, it is management's expectation that Harborside's activities will be conducted in such a manner that income from operations will be not subject to double taxation.

The Company's income tax expense allocated for the three months ended March 31, 2022 and 2021 was follows:

	<u>March 31, 2022</u>	<u>March 31, 2021</u>
Current tax	\$ 1,302,444	\$ 1,253,495
Deferred tax	<u>35,916</u>	<u>(178,243)</u>
Income tax expense	<u>\$ 1,338,360</u>	<u>\$ 1,075,252</u>

The net tax provision differs from that expected by applying the U.S. federal tax rate of 21.0% to net loss before income taxes mainly due to limitations in the deductibility of certain expenses for tax purposes under IRC §280E as well as fair value adjustments for biological assets and derivative liabilities.

Deferred taxes reflect the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax values.

Deferred tax assets and liabilities have been offset where they relate to income taxes levied by the same taxation authority and the Company has the legal right and intent to offset.

Movements in the net deferred tax liabilities during the three months ended March 31, 2022 was as follows:

	<u>March 31, 2022</u>
Balance, beginning of period	\$ 17,363,459
Recognized in loss	35,916
Net deferred tax liability from acquisitions (Note 3)	<u>2,470,337</u>
Balance, end of period	<u>\$ 19,869,712</u>

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 22. Share Capital

The following is a reconciliation of the issued and outstanding shares as at March 31, 2022 and December 31, 2021:

	<b>Subordinate Voting Shares (SVS)</b>	<b>Multiple Voting Shares (MVS)</b>
Balance, December 31, 2020	26,535,608	179,096.42
Conversion of MVS to SVS	5,769,075	(57,690.75)
Issuance of new shares	5,806,700	302,965.06
Issuance on exercise of options	1,414,024	-
Issuance on settlement of RSUs	-	1,600.00
Balance, December 31, 2021	39,525,407	425,970.73
Issuance of new shares	60,000,000	11,289.57
Issuance on exercise of options	25,000	-
Conversion of MVS to SVS	<u>43,726,030</u>	<u>(437,260.30)</u>
Balance, March 31, 2022	<u>143,276,437</u>	<u>-</u>

On February 18, 2021, the Company closed an upsized brokered private placement of units at a price of C\$2.55 per SVS Unit (as defined below) and C\$255.00 per MVS Unit (as defined below) for aggregate gross proceeds of C\$35,103,045 (the "Offering"). Beacon Securities Limited and ATB Capital Markets acted as co-lead agents in connection with the Offering (the "Agents").

Each unit issued to nonresidents of the U.S. (each, an "SVS Unit") was comprised of one SVS and one warrant. Each SVS Warrant is exercisable to acquire one SVS of the Company for a period of 36 months following the close of the Offering at an exercise price of C\$3.69 per SVS, subject to adjustment and acceleration in certain events. A total of 5,806,700 SVS Units were issued pursuant to the Offering.

All investors that are considered residents of the U.S. were issued units (each, an "MVS Unit") comprised of MVS of the Company and MVS Warrants, based on the same economic equivalency of each MVS converting into 100 SVS. The holders of MVS were entitled to one vote in respect of each SVS into which such MVS could be converted. A total of 79,592 MVS Units were issued, pursuant to the Offering. As a result of the Mandatory Conversion, all MVS issued have been converted into SVS, and holders of MVS Warrants are now entitled to receive, upon exercise of such MVS Warrants, one hundred (100) SVS per MVS Warrant at an exercise price of \$369 per MVS Warrant.

The SVS Warrants and MVS Warrants were valued on February 18, 2021 at \$6,128,298 and \$8,403,774, respectively, based on an implied share price of C\$1.34 and C\$134.06, respectively, valued based on the Monte Carlo model. The key assumptions used have been discussed in Note 18.

In consideration for their services, the Company paid the Agents a cash commission equal to C\$1,451,340 and issued the Agents an aggregate of 569,154 Broker Warrants ("Broker Warrants"). Each Broker Warrant is exercisable until February 18, 2022 into one SVS Unit (each comprised of one SVS and one SVS Warrant) at an exercise price of C\$2.55 per SVS Unit. Upon exercise of a Broker Warrant, each underlying SVS Warrant would be exercisable at C\$3.69 per SVS Warrant until February 18, 2024. The Broker Warrants were not exercised and expired during February 2022.

The Broker Warrants were valued on February 18, 2021 at \$1,134,112 based on an implied share price of C\$2.53 valued based on the Monte Carlo model. The key assumptions used have been discussed in Note 24.

The total share issuance costs related to the Offering was C\$1,756,873, which includes the commission noted above and other professional fees.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 22. Share Capital (continued)

On March 31, 2022, the Company enacted the Mandatory Conversion of all the MVS into SVS at a ratio of 100 SVS for each MVS outstanding. In addition, each holder of MVS Warrants will now be entitled to 100 SVS for each MVS underlying its MVS Warrants, upon exercise of such MVS Warrants.

### 23. Contributed Surplus

#### *Stock Options*

Prior to June 30, 2020, the Company maintained an equity incentive plan (the "Old Plan") whereby certain key employees, officers, directors, consultants and advisors could be granted stock options, RSAs, restricted share units, share appreciation rights, performance compensation awards, dividend equivalents and other share-based awards of the Company.

The stock options which were awarded under the Old Plan vest on a graded-vesting schedule, generally, over a two-year period and expire 10 years after the grant date. The Company uses a graded vesting schedule to record compensation expense, which results in greater compensation expense earlier in the vesting period after an award is granted. All stock options granted are settled in the Company's shares. If an employee terminates employment with the Company prior to awards vesting, the unvested awards are forfeited and the historical compensation expense for unvested options is reversed in the period of termination.

On June 30, 2020, the Company adopted a new equity incentive plan (the "Plan") whereby certain key employees, officers, directors, consultants and advisors may be granted stock options, RSAs, restricted share units, share appreciation rights, performance compensation awards, dividend equivalents and other share-based awards of the Company.

The stock options awarded under the Plan vest in accordance with the terms established by the Board at the time of grant. The Plan was ratified by the Company's shareholders on November 24, 2020.

On January 17, 2022, the Company adopted an amended and restated equity incentive plan (the "A&R Plan") to amend the Plan in order to increase the maximum number of SVS which may be allocated for issuance pursuant to Incentive Stock Options (as defined in the A&R Plan) to up to 23,355,026 SVS or such lesser amount as determined by the Board. The A&R Plan was ratified by the Company's shareholders on February 22, 2022.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 23. Contributed Surplus (continued)

#### Stock Options (continued)

The following table summarizes the stock option activities for the three months ended March 31, 2022 and the year ended December 31, 2021:

	Number of options outstanding	Weighted average exercise price \$
Balance, December 31, 2020	6,635,898	1.47
Options exercised	(1,414,024)	0.14
Options expired/forfeited/cancelled	(1,819,582)	1.81
Options granted	<u>1,221,860</u>	0.62
Balance, December 31, 2021	4,624,152	1.51
Options exercised	(25,000)	0.05
Options expired/forfeited/cancelled	(141,250)	1.95
Options granted	5,758,797	0.56
Replacement options granted	<u>84,420</u>	3.44
Balance, March 31, 2022	<u>10,301,119</u>	0.99

During the three months ended March 31, 2022, the Company recorded aggregate share-based compensation of \$1,222,369 for all stock options vesting during the period. During the three months ended March 31, 2021, the Company recorded negative aggregate share-based compensation of \$(1,000) due to forfeiture reversals and an adjustment for previously accelerated options.

During the three months ended March 31, 2022 and 2021, the Company received cash consideration of \$1,250 and \$24,094, respectively, for the exercise of 25,000 and 468,750 vested options, respectively.

On February 4, 2022, the Company issued 84,420 replacement options to certain existing holders of Sublime options as part of the Sublime Acquisition. The Company accounted for the replacement options in accordance with IFRS 2 and IFRS 3 and recognized post-acquisition costs for share-based compensation of \$916,112 related to the issuance of these options.

On March 1, 2022, the Company granted options to purchase an aggregate of 5,758,797 SVS (Note 3).

The fair value of stock options granted by the Company during the three months ended March 31, 2022 and 2021, under the Plan, were estimated on the grant date using the Black-Scholes-Merton option pricing model with the relevant assumptions outlined in the table below. The expected volatility was estimated based on volatility ranges acceptable in practice. The expected life in years represents the period of time that options granted are expected to be outstanding. The risk-free rate was based on the Bank of Canada three-year bond yield rate at the time of the grant of the award. Expected annual rate of dividends was assumed to be zero based on the fact that the Company has never paid cash dividends and does not expect to pay cash dividends in the foreseeable future.

	For the three months ended	
	March 31, 2022	March 31, 2021
Stock price at grant date	CAD 0.70 - 2.98	CAD 0.95 - 1.83
Exercise price at grant date	CAD 0.70 - 5.42	CAD 0.95 - 1.83
Expected life in years	3 - 7.5 years	3 - 4.5 years
Expected volatility	100%	100%
Expected annual rate of dividends	0%	0%
Risk-free annual interest rate	0.32% - 2.48%	0.27% - 0.43%



# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 23. Contributed Surplus (continued)

#### *Stock Options (continued)*

As at March 31, 2022, the options outstanding and exercisable for SVS and with the corresponding exercise price and weighted average remaining life was as follows:

Date of grant	Expiry date	Number of options outstanding	Number of options exercisable	Exercise price (USD)	Weighted average remaining life
April 25, 2018	July 1, 2022	200,000	200,000	\$ 4.150	0.25
July 5, 2019	July 5, 2022	262,500	262,500	\$ 0.055	0.26
May 24, 2018	July 19, 2022	11,957	11,957	\$ 8.363	0.30
December 14, 2018	July 19, 2022	8,152	8,152	\$ 5.522	0.30
September 1, 2020	July 19, 2022	510,000	510,000	\$ 0.760	0.30
May 24, 2018	May 24, 2023	2,989	2,989	\$ 8.363	1.15
December 14, 2018	December 14, 2023	2,989	2,989	\$ 5.522	1.71
September 1, 2020	September 1, 2025	865,000	536,390	\$ 0.760	3.42
December 23, 2020	December 23, 2025	765,000	25,000	\$ 1.465	3.73
June 11, 2021	June 11, 2026	581,235	-	\$ 1.769	4.20
July 2, 2021	July 2, 2026	536,875	-	\$ 1.425	4.26
August 1, 2016	August 1, 2026	35,478	35,478	\$ 0.050	4.34
March 1, 2022	March 1, 2027	5,758,797	-	\$ 0.560	4.92
July 26, 2017	July 26, 2027	1,060	1,060	\$ 0.050	5.32
April 25, 2018	April 25, 2028	556,667	556,667	\$ 4.150	6.07
May 7, 2018	May 7, 2028	15,000	15,000	\$ 4.150	6.11
May 15, 2018	May 15, 2028	43,000	43,000	\$ 4.150	6.13
June 25, 2018	June 25, 2028	10,000	10,000	\$ 4.150	6.24
February 4, 2022*	August 22, 2028	47,933	47,933	\$ 3.370	6.40
September 12, 2018	September 12, 2028	50,000	50,000	\$ 4.150	6.46
February 4, 2022*	December 31, 2028	29,922	29,922	\$ 3.370	6.76
February 4, 2022*	July 16, 2029	5,648	2,640	\$ 4.250	7.30
February 4, 2022*	July 16, 2029	917	151	\$ 3.370	7.30
Total		<u>10,301,119</u>	<u>2,351,828</u>		4.05

\*Replacement options issued as part of the Sublime Acquisition.

The weighted average remaining contractual life of outstanding options as at March 31, 2022 is 4.05 years.

#### *Restricted Stock Units ("RSUs")*

On March 1, 2022, the Company granted an aggregate of 912,599 RSUs (Note 3).

The fair value on the grant date of the RSUs was measured at \$489,627 (or \$0.54 per RSU) based on the intrinsic value on the grant date. During the three months ended March 31, 2022, the Company recorded share-based compensation expense of \$21,366, in relation to the vesting of the RSUs.

As at March 31, 2022, the Company has an aggregate of 987,599 RSUs outstanding which includes grants prior to March 1, 2022.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 24. Reserve for Warrants

The activity for warrants outstanding for the three months ended March 31, 2022 and the year ended December 31, 2021 is summarized as follows:

	<b>Subordinate Voting Shares</b>		
	<b>Number of warrants outstanding</b>	<b>Weighted average exercise price CAD \$</b>	<b>Weighted average exercise price USD \$</b>
Balance, December 31, 2020	3,279,300	8.49	6.10
Warrants expired	(2,806,981)	8.75	6.88
Broker Warrants expired	(160,775)	7.00	5.50
Broker Warrants expired	(311,544)	6.90	5.42
Issuance of SVS Warrants	5,806,700	3.69	2.91
Issuance of Broker Warrants	<u>569,154</u>	2.55	2.01
Balance, December 31, 2021	6,375,854	3.59	2.54
Conversion of MVS Warrants to SVS	7,959,200	3.69	2.95
Conversion of warrants to the Bank to SVS	410,000	3.69	2.95
Warrants expired	<u>(569,154)</u>	2.55	2.04
Balance, March 31, 2022	<u>14,175,900</u>	2.18	1.74

  

	<b>Multiple Voting Shares</b>		
	<b>Number of warrants outstanding</b>	<b>Weighted average exercise price CAD \$</b>	<b>Weighted average exercise price USD \$</b>
Balance, December 31, 2020	-	-	-
Issuance of MVS Warrants	79,592	369.00	291.00
Issuance of warrants to the Bank	<u>4,100</u>	369.00	291.00
Balance, December 31, 2021	83,692	369.00	291.00
Conversion of MVS Warrants to SVS	(79,592)	369.00	291.00
Conversion of warrants to the Bank to SVS	<u>(4,100)</u>	369.00	291.00
Balance, March 31, 2022	<u>-</u>	-	-

### ***Warrants***

On February 18, 2021, the Company issued 5,806,700 SVS and 79,592 MVS Warrants in connection with the Offering (Note 22). Each SVS Warrant entitles the holder thereof to purchase one SVS of the Company at an exercise price of C\$3.69 per share until February 18, 2024. Each MVS Warrant entitles the holder thereof to purchase one MVS of the Company at an exercise price of C\$369 per share until February 18, 2024. Due to the Mandatory Conversion, all MVS Warrants previously exercisable into MVS, are now exercisable into SVS. In particular, each holder of MVS Warrants is now entitled to receive, upon exercise of the MVS Warrants, one hundred SVS per MVS Warrant at an exercise price of \$369 per MVS Warrant.

The SVS Warrants and MVS Warrants are being accounted for as a derivative liability (Note 18).

On March 19, 2021, the Company issued 4,100 warrants to purchase MVS to the Bank in connection with the Facility (Note 16), exercisable at a price of C\$369 per MVS, at any time prior to March 19, 2023. The MVS Warrants were subject to the terms of the Mandatory Conversion.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 24. Reserve for Warrants (continued)

#### *Warrants (continued)*

The warrants issued to the Bank were accounted for as other assets and were amortized on a straight-line basis over the two-year term of the Facility. The Company amortized the remaining balance of the warrants in conjunction with the paydown of the Facility (Note 16).

#### *Broker Warrants*

As detailed in Note 22, the Company issued 569,154 Broker Warrants to the Agents as compensation in connection with the Offering. Each Broker Warrant was exercisable until February 18, 2022 into one SVS Unit (each comprised of one SVS and one SVS Warrant) at an exercise price of C\$2.55 per SVS Unit. Upon exercise of a Broker Warrant, each underlying SVS Warrant would have been issued and been exercisable at C\$3.69 per share until February 18, 2024. All of the Broker Warrants expired on February 18, 2022, and no underlying SVS Warrants were issued.

The Broker Warrants were valued based on the Monte Carlo model at the date of measurement with the following assumptions:

	<u>February 18, 2021</u>
Risk-free interest rate	0.35%
Exercise price - CAD	C\$2.55
Share price - CAD	C\$2.65
Expected volatility	111.40%
Expected remaining life	1 year
Fair value - CAD	C\$1,439,960
Fair value - U.S.	\$1,134,112

The following table summarizes information of warrants outstanding as at March 31, 2022:

<b>Date of expiry</b>	<b>Number of warrants outstanding</b>	<b>Weighted Average Exercise price (CAD)</b>	<b>Weighted Average Exercise price (USD)</b>	<b>Weighted average remaining life</b>
March 19, 2023	410,000	3.69	2.95	0.97
February 18, 2024	5,806,700	3.69	2.95	1.89
February 18, 2024	<u>7,959,200</u>	3.69	2.95	1.89
Total	<u>14,175,900</u>	3.69	2.95	1.86

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 25. Non-controlling interests

On February 15, 2022, the Company entered into a definitive securities purchase agreement (the "Subsequent FGW Agreement"), whereby a further 29.9% interest in FGW (the "Subsequent Shares") would be acquired, subject to certain material closing conditions, including approvals from regulatory authorities. The acquisition of the Subsequent Shares will increase the Company's interest in FGW to 80%, subject to obtaining the Specified Approval and converting the FGW Note. The Company also retains the right of first refusal to purchase, in its discretion, in whole or in part and in one or more closings, the remaining 20% of FGW, subject to regulatory approvals. Pursuant to the Subsequent FGW Agreement, the Company will pay an aggregate purchase price of \$1,300,650 for the Subsequent Shares to be satisfied in MVS priced at the greater of: (i) the 30-day volume weighted average price of the SVS on the CSE ending on the day prior to closing of the purchase of the Subsequent Share multiplied by 100; (ii) C\$150 per MVS; or (iii) such other price as may be approved by the CSE. Prior to the closing of the acquisition of the Subsequent Shares, the Subsequent FGW Agreement will be amended to reflect the occurrence of the Mandatory Conversion. As at March 31, 2022, there were no changes in the ownership for FGW.

On March 1, 2022, the Company acquired several non-controlling interests through the Urbn Leaf Acquisition (Note 3).

As at March 31, 2022, the Company held the following ownership interests:

FGW Haight Inc.	21.00%
680 Broadway Master, LLC	50.00%
UL Chula Two LLC	51.00%
UL La Mesa LLC	59.56%
JLM Investment Group, LLC	66.66%
Banana LLC	75.00%
UL Benicia LLC	80.00%
UL Visalia LLC	80.00%
ULRB LLC	80.00%
Lafayette Street Property Management, LLC	90.00%

The Company acquired the remaining 50% interest in 680 Broadway Master, LLC on May 18, 2022 (Note 32).

The change in non-controlling interests for the three months ended March 31, 2022 was as follows:

Balance, December 31, 2021	\$ 2,857,465
Purchases of businesses - initial equity related to non-controlling interests (Note 3)	4,188,635
Share of loss for the period	<u>(149,196)</u>
Balance, March 31, 2022	<u>\$ 6,896,904</u>

### 26. Net loss per share

Basic loss per share is calculated by dividing net profit or loss attributable to ordinary equity holders of the Company (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the period. For purposes of calculating loss per share, the dilutive effect of outstanding MVS is converted into 100 SVS on a weighted-average basis for the number of days the MVS' are outstanding.

On March 31, 2022, the Company enacted the Mandatory Conversion of all the MVS into SVS at a ratio of 100 SVS for each MVS outstanding (Note 22).

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 26. Net loss per share (continued)

The following is a reconciliation for the calculation of basic and diluted loss per share for the three months ended March 31, 2022 and 2021:

	<u>March 31, 2022</u>	<u>March 31, 2021</u>
Net loss attributable to Harborside Inc.	\$(10,412,298)	\$ (2,910,749)
Dilutive weighted average number of shares outstanding	104,111,060	51,045,299
Basic and diluted loss per share	\$ (0.10)	\$ (0.06)

### 27. Related Party Transactions and Key Management and Director Compensation

#### (a) Key Management and Director Compensation

Key management includes directors and officers of the Company. Total compensation (comprised of salaries, benefits, one-time bonuses and share-based compensation) awarded to key management for the three months ended March 31, 2022 and 2021 was as follows:

	<u>March 31, 2022</u>	<u>March 31, 2021</u>
Short-term employee benefits, including salaries and director fees	\$ 502,384	\$ 338,897
Share-based compensation - Directors and Executives	<u>255,269</u>	<u>140,771</u>
Total	<u>\$ 757,653</u>	<u>\$ 479,668</u>

On July 19, 2021, Matt Hawkins, Chairman of the Board, assumed the position of Interim CEO of Harborside. In connection with the Urbn Leaf Acquisition, the Company announced the resignation of Mr. Hawkins as Interim CEO and the appointment of Edward Schmults as CEO. As at March 31, 2022, \$21,000 was payable to Cresco Capital Management II, LLC, an entity doing business as Entourage ("Entourage"), through which Mr. Hawkins is compensated for his services as the Interim CEO of the Company. Entourage is controlled and directed by Matt Hawkins and Andrew Sturner, directors of the Company. Effective April 4, 2022, Mr. Sturner resigned from the board of directors (Note 32).

As at March 31, 2022, \$12,977 was payable to Newhouse Development LLC ("Newhouse"), a company controlled by Tom DiGiovanni, the Chief Financial Officer ("CFO"), through which Mr. DiGiovanni is compensated for his services as CFO of the Company (December 31, 2021 - \$34,720).

As at March 31, 2022, \$202,540 was payable to Will Senn, Chief Corporate Development Officer, for deferred compensation.

As at March 31, 2022, \$136,388 was payable to the directors for the first quarter director fees (December 31, 2021 - \$161,198).

All amounts outstanding are unsecured, non-interest bearing and due on demand.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 27. Related Party Transactions and Key Management and Director Compensation (continued)

#### (b) Related Parties

		Transactions for the three months ended		Balance outstanding	
		March 31, 2022	March 31, 2021	March 31, 2022	December 31, 2021
<b>Purchases of goods or services from related parties:</b>					
Sublime	Matthew Hawkins and Andrew Sturner, directors of the Company are partners at Entourage Effect Capital which is an investor in Sublime. As at July 2, 2021, Sublime was acquired by the Company.	\$ -	\$ 84,475	\$ -	\$ -
Flow Cannabis Co.	Kevin Albert, a director of the Company, serves as a director on the board of Flow Cannabis Co.	\$ -	\$ 833	\$ 1,517	\$ 1,517
Branson Corporate Services Ltd. ("Branson")	Branson provided finance, accounting and administrative services to the Company. Mr. Bilodeau holds a 16% ownership interest in Branson. As at July 2021, Mr. Bilodeau is no longer a related party of the Company. As at March 31, 2022, the Company no longer uses Branson.	\$ -	\$ 42,649	\$ -	\$ -
Black Oak Ventures ("Black Oak")	Black Oak provided certain investor relations services to the Company. Black Oak's principal is an immediate family member of Mr. Bilodeau. As at July 2021, Mr. Bilodeau is no longer a related party of the Company. As at March 31, 2022, the Company no longer uses Black Oak.	\$ -	\$ 18,000	\$ -	\$ -
<b>Sales to related parties:</b>					
Sublime	Matthew Hawkins and Andrew Sturner, directors of the Company are partners at Entourage Effect Capital which is an investor in Sublime. As of July 2, 2021, Sublime was acquired by the Company.	\$ -	\$ 227,810	\$ -	\$ -

All purchases of goods and services were at arm's length market rates. All sales of goods were at arm's length market rates. Effective April 4, 2022, Mr. Sturner and Mr. Albert resigned from the board of directors (Note 32).

#### (c) Other Related Parties

On June 1, 2020, the Company entered into an additional consulting agreement with Newhouse to provide financial and accounting services, related to one of the Company's management services agreements, in exchange for cash compensation. The services are being provided by an immediate family member of the Company's CFO. As at March 31, 2022, a total of \$12,977 was payable to Newhouse, of which \$5,175 was related to the June 1, 2020 agreement and \$7,802 was related to the agreement described in section (a) above.

On July 19, 2021, the Company entered into two consulting agreements with Entourage in exchange for cash compensation. The first was for Matthew Hawkins to provide management services as Interim CEO, and the second was for Entourage to provide business and executive management services related to retail, wholesale and manufacturing operations. As at March 31, 2022, a total of \$41,000 was payable to Entourage, of which \$21,000 was related to the agreement described in section (a) above.

An immediate family member of Mr. Senn is employed by the Company. Short term employee benefits including salary expense was \$7,727 for the three months ended March 31, 2022.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 27. Related Party Transactions and Key Management and Director Compensation (continued)

#### (c) Other Related Parties (continued)

Lafayette Street Property Management, LLC leases a building in Stockton, California in which an officer of the Company owns a 45% interest. The Company paid \$12,000 during the three months ended March 31, 2022 for rent expense.

UL La Mesa LLC leases a building in La Mesa, California in which an immediate family member of an officer of the Company owns a 36.25% interest. The monthly rent for this property is \$10,000, plus triple-net expenses as at March 31, 2022. The Company paid \$10,000 during the three months ended March 31, 2022 for rent expense.

### 28. Commitments and Contingencies

From time to time, the Company may become defendants in legal actions and the Company intends to take appropriate action with respect to any such legal actions, including defending itself against such legal claims as necessary. As the Company's growth continues, it may become party to an increasing number of litigation matters and claims. The outcomes of litigation and claims cannot be predicted with certainty, and the resolution of any future matters could materially affect the Company's financial position, results of operations or cash flows.

#### *IRC §280E*

Many of the central issues relating to the interpretation of IRC §280E remain unsettled and there are critical tax accounting issues regarding the allocation of expenses to the cost of goods sold (thus avoiding disallowance as deductions under IRC §280E) that have never been addressed by any Treasury regulation or court case. IFRIC 23 - *Uncertainty over Income Tax Treatments* provides guidance that adds to the requirements in IAS 12, *Income Taxes*, by specifying how to reflect the effects of uncertainty in accounting for income taxes. The Company evaluated its uncertain tax treatments using a probability-weighted approach to assess the range of possible outcomes as required in its adoption of IFRIC 23 and, although it strongly disagrees with the findings of the Internal Revenue Service and the U.S. Tax Court, determined that a reserve for an uncertain tax position should be recorded. As at March 31, 2022 and December 31, 2021, the reserve totaled \$36,498,436 and \$36,051,249, respectively.

On February 17, 2021, the U.S. Tax Court ruled in favor of the Commissioner of Internal Revenue with respect to SJW to disallow all of SJW's deductions pursuant to IRC §280E for all the years at issue. On May 14, 2021, the Company appealed the Tax Court ruling. In an effort to resolve the matter as part of a global settlement, the Company withdrew its appeal.

#### *Michael Adams v. Patients Mutual Assistance Collective Corp dba Harborside Health et al.*

On or about January 10, 2020, PMACC was served with a complaint filed by plaintiff and putative class representative Mr. Michael Adams. The complaint, filed on January 7, 2020 in Superior Court of the State of California for Alameda County, alleges violations of the California Business and Professions Code with respect to PMACC's employee wage payment practices, and seeks class certification with respect to a group of individual plaintiffs alleged to be similarly situated to Mr. Adams. In late April 2020, the Company filed a demurrer/motion to strike as to plaintiff's complaint; the Court granted the Company's demurrer/motion to strike in part, with leave for the plaintiffs to amend and refile their original complaint. At the May 4, 2021 mediation, the parties did not reach a settlement agreement, however, the parties agreed to continue discovery. A deposition had been scheduled for February 28, 2022 which was postponed. The parties continue to engage in pre-trial discovery. A trial date remains to be set. The Company further believes that it has meritorious defenses to the alleged causes of action and it is the intent of the Company to prevail in this matter.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 28. Commitments and Contingencies (continued)

#### *Gia Calhoun v. FLRish, Inc.*

On January 6, 2020, the Company's subsidiary FLRish, Inc. was served with a complaint filed by plaintiff and putative class representative Ms. Gia Calhoun. The complaint, filed on December 17, 2019 in the U.S. Federal District Court for the Northern District of California (the "Court"), alleges violations of the Telephone Consumer Protection Act, ("TCPA") and seeks class certification with respect to a group of individual plaintiffs alleged to be similarly situated to Ms. Calhoun. On April 6, 2020, the Company filed a motion to stay all proceedings in the matter pending a ruling by the U.S. Supreme Court in the case *Barr v. Am. Ass'n of Political Consultants, Inc.*, concerning the constitutionality of Section 227(b) of the TCPA. On May 13, 2020, the Court granted the Company's motion to stay all proceedings in the matter pending the U.S. Supreme Court's decision in the *Barr* case. The Court further informed the parties that it would be willing to entertain another motion to stay pending the Supreme Court's granting review on the issue of what constitutes an "automatic telephone dialing system" ("ATDS") in the *Duguid v. Facebook* petition. On July 6, 2020, the U.S. Supreme Court ruled on *Barr* and invalidated the government-debt call exception but severed that provision and did not strike down the entire automated call restriction of the TCPA. With respect to the Company's litigation, per the Court's order the parties filed a joint status report on July 13, 2020. On July 17, 2020, the parties appeared before the Court for a case management conference. In the interim, the Supreme Court granted review on the issue of what constitutes an ATDS in the *Duguid v. Facebook* petition, and the Company subsequently proposed that the Court extend the stay until the Supreme Court issues a decision on Facebook's petition.

At the case management conference on July 17, 2020 the Court ruled:

1. No class-related discovery is permitted;
2. Within the next 90 days, the Company may take discovery on plaintiff's DNC claim;
3. Within the next 90 days, plaintiff may take discovery on the issue of whether an ATDS was used to call Plaintiff. However, the court expressly ruled that the parties may not engage in any expert discovery on ATDS issue.

On April 1, 2021, the Supreme Court issued its decision in the Facebook case, narrowly interpreting ATDS. The Court held, "Congress' definition of an autodialer requires that in all cases, whether storing or producing numbers to be called, the equipment in question must use a random or sequential number generator." Though not dispositive, the Company believes the ruling is favorable to its defense. At a May 7, 2021 case management conference, the Court lifted the stay on class-related discovery that the Court had previously imposed on July 17, 2020. By mutual agreement of the parties, the Court imposed a stay of the case for 90 days and set a case management conference for December 17, 2021. On August 17, 2021, Ms. Calhoun filed a motion for leave to file an amended complaint, adding a claim on behalf of a class of persons who requested to opt-out of receiving text messages and expanding the time period for other claims. On August 18, 2021, the Company filed a motion for partial summary judgment on the claim that an ATDS was used. On January 19, 2022, mediation took place. The parties did not reach a settlement agreement and agreed to continue discovery. The Company further believes that it has meritorious defenses to the alleged causes of action and it is the intent of the Company to prevail in this matter.

#### *John Doe v. FLRish*

On December 13, 2021, the Company received a Summons and Complaint filed in the Alameda Superior Court by a John Doe plaintiff. The Complaint asserts three clauses of action, all on behalf of plaintiff and a purported class defined as "[a]ll persons who, on or after four years prior to the filing of the initial complaint in this action through the date of class certification, purchased medicinal-cannabis from Defendants."



# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 28. Commitments and Contingencies (continued)

#### *John Doe v. FLRish (continued)*

Plaintiff's First Cause of Action is a claim for violation of the California Confidentiality of Medical Information Act (the "CMIA"). Plaintiff's Second Cause of Action is a claim under California's Unfair Competition Law, Cal. Bus. & Prof (the "UCL"). Plaintiff's Third Cause of Action is a claim for "Invasion of Privacy", under the UCL and privacy rights under the common law, the California Constitution, the California Consumer Privacy Act of 2018, and the CMIA.

On March 16, 2022, the Company filed a demurrer asserting that the plaintiff's complaint fails to state a viable cause of action or state any claim upon which relief can be granted and should be dismissed. The Company further believes that it has meritorious defenses to the alleged causes of action and it is the intent of the Company to prevail in this matter.

#### *Trademark Agreement Lawsuit*

On September 18, 2018, Sublime entered into a trademark assignment agreement with Sublime Concentrates, Inc. (the "Counterparty") for use of certain trademarks. The Counterparty filed suit against Sublime alleging breach of contract regarding the nonpayment for the transfer of the trademark assets. No trial date has been set as both parties continue to engage in settlement negotiations. The Company continues to evaluate and monitor a range of possible outcomes.

#### *Alex Fang v. Sublime*

On August 27, 2021, the Company was served with a Demand for Arbitration by Mr. Alex Fang, a former employee and founder of Sublime. The Company filed its counterclaim alleging breach of fiduciary duty and fraudulent misrepresentation. The Company believes that it has meritorious defenses to the alleged causes of action and it is the intent of the Company to prevail in this matter.

#### *Tony Banks v. Sublime*

On October 22, 2021, the Company received a Complaint filed in the Alameda Superior Court demanding civil penalties related to alleged violations of California labor code. The complaint alleges wage and hour violations on behalf of the Plaintiff and all aggrieved employees pursuant to the Labor Code Private Attorneys General Act. The parties have agreed to submit the case to mediation and are in the process of securing a mediator. Mediation has been set for October 11, 2022. It is the intent of the Company to prevail at mediation.

#### *Lilu Financials LLC v. UL Holdings Inc., UL Management LLC and Will Senn*

On September 24, 2021, the Company was served with a Summons and Complaint alleging violations of the contract between the parties. This matter is in the discovery phase, which is stayed by order of the court pending a ruling on a motion for Lilu Financials LLC ("Lilu") to post an undertaking pursuant to the Code of Civil Procedure. The hearing for the motion was set for April 15, 2022 and the Company prevailed. Lilu has filed a motion to amend the Complaint. The hearing in the matter is set for June 3, 2022. It is the intent of the Company to prevail in this matter.

#### *Stillwell v. 680 Broadway Master, LLC (a subsidiary of Urbn Leaf)*

On December 23, 2021, Urbn Leaf received a Summons and Complaint filed by Stillwell in Monterey County Superior Court alleging certain violations of labor and employment law. 680 Broadway Master LLC entered into a stipulation with Claimant to refer the matter to binding arbitration. On September 21, 2021, Claimant refiled the matter in arbitration. This matter is currently in the discovery phase. It is the intent of the Company to prevail in this matter.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 28. Commitments and Contingencies (continued)

*Bubba Likes Tortillas, LLC v. New Origins Management, Inc., San Diego Alternative Treatment Center Cooperative d.b.a. Southwest Patient Group, Wayne Alexander Scherer, Rezwan H. Kwan, and Does 1-100*

In 2021, Urbn Leaf received a Summons and Complaint filed by Bubba Likes Tortillas, LLC alleging violations of the contract between the parties. Southwest Patient Group changed its name to Uprooted Inc. and was subsequently acquired by UL Holdings Inc. These claims occurred prior to UL Holdings Inc. acquiring Uprooted Inc. It is the intent of the Company to prevail in this matter.

#### *Employment Agreements*

Certain of the Company's employees have employment agreements under which the Company is obligated to make severance payments, accelerate vesting of stock options and provide other benefits in the event of the employee's termination, change in role or a change in control as defined in such agreements.

### 29. Capital Management

The Company's objectives when managing its capital are to ensure that there are adequate capital resources to safeguard the Company's ability to continue as a going concern, meet capital expenditures required 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 shares, issue new debt or acquire or dispose of assets. With the exception of certain restrictive covenants included in the Senior Secured Debt and Term Loan (Note 15 and 17), the Company is not subject to externally imposed capital requirements. The Board does not establish quantitative criteria related to a return on capital for management, but rather relies on the management team's expertise to sustain future development of the business.

Management has chosen to mitigate the risk and uncertainty associated with raising additional capital within current economic conditions by:

- (i) minimizing discretionary disbursements;
- (ii) reducing operating expenditures throughout the Company; and
- (iii) exploring alternative sources of liquidity.

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 material changes to the Company's capital management approach during the three months ended March 31, 2022 and 2021.

### 30. Financial Risk Management

The Company is exposed to a variety of financial instrument related risks. Management, in conjunction with the Company's Board of Directors, mitigates these risks by assessing, monitoring and approving the Company's risk management processes.

#### **(a) Liquidity Risk**

Liquidity risk is the risk that the Company will not have sufficient cash resources to meet its financial obligations as they come due. The Company manages its liquidity risk by reviewing its capital requirements on an ongoing basis. The Company's liquidity and operating results may be adversely affected if the Company's access to the capital market is hindered, whether as the result of a downturn in stock market conditions generally or related to matters specific to the Company. The Company generates cash flow primarily from its operating and financing activities.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 30. Financial Risk Management (continued)

#### (a) Liquidity Risk (continued)

As at March 31, 2022 and December 31, 2021, the Company had a cash and restricted cash balance of \$13,773,253 and \$9,091,405, respectively, to settle current liabilities of \$111,947,541 and \$70,614,682, respectively. The higher amount of current liabilities as at March 31, 2022 and December 31, 2021 is primarily due to the Company's provision for an uncertain tax position (Note 19) and debt assumed as part of the Urbn Leaf Acquisition (Note 3 and 15).

In addition to the commitments outlined in Note 13, *Right-of-use Assets and Lease Liabilities*, and Note 28, *Commitments and Contingencies*, the Company has the following contractual obligations as at March 31, 2022:

	<b>Less than 1</b>				
	<b>Year</b>	<b>1 to 3 Years</b>	<b>4 to 5 Years</b>	<b>&gt; 5 Years</b>	<b>Total</b>
Accounts payable and accrued liabilities	\$ 43,873,392	\$ -	\$ -	\$ -	\$ 43,873,392
Notes payable	13,530,716	-	-	-	13,530,716
Term loan	-	<u>2,167,924</u>	<u>2,005,330</u>	<u>24,732,401</u>	<u>28,905,655</u>
	<u>\$ 57,404,108</u>	<u>\$ 2,167,924</u>	<u>\$ 2,005,330</u>	<u>\$ 24,732,401</u>	<u>\$ 86,309,763</u>

The Company manages liquidity risk by maintaining adequate cash reserves and by continuously monitoring forecasted and actual cash flows. Where sufficient liquidity may exist, the Company may pursue various debt and equity instruments for either short or long-term financing of its operations.

Management believes there is sufficient capital to meet short-term obligations, after taking into account the cash flow requirements from operations, the expected timing of any payments related to the provision for uncertain tax position (Note 19) and the Company's cash position as at March 31, 2022.

#### (b) Credit Risk

Credit risk is the risk of potential loss to the Company if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's credit risk is primarily attributable to cash, accounts receivable, and investments and advances, which expose the Company to credit risk should the borrower default on maturity of the instruments. Cash and restricted cash are primarily held with reputable banks, and at secure facilities controlled by the Company. Management believes that the credit risk concentration with respect to financial instruments included in cash, restricted cash and accounts receivable is minimal.

#### (c) Market Risk

##### (i) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate volatility as its Notes payable have variable interest rates (Note 15).

##### (ii) Foreign Exchange Risk

Foreign exchange risk is the risk that the Company will be subject to foreign currency fluctuations in satisfying obligations related to its foreign activities. The Company's main operations are based in the U.S., and the majority of its business is transacted in USD. The Company's primary exposure to foreign exchange risk and rate fluctuations relates to bank deposits held in Canada and transactions denominated in CAD.

# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
For the Three Months Ended March 31, 2022 and 2021  
(Expressed in United States Dollars, except share amounts)

## 30. Financial Risk Management (continued)

### (c) Market Risk (continued)

#### *(iii) Equity Price Risk*

The Company is exposed to price risk with respect to equity prices. Equity price risk is defined as the potential adverse impact on the Company's earnings due to movements in individual equity prices or general movements in the level of the stock market or the cannabis sub-market. The Company's investments are subject to fluctuations in fair value arising from changes in the equity markets.

### (d) Asset Forfeiture Risk

As the cannabis industry remains illegal under U.S. federal law, any property owned by participants in the cannabis industry which is used in the course of conducting such business, or is derived from 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 were 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.

### (e) Banking Risk

Notwithstanding that a majority of states have legalized cannabis for either adult or medical use, and the passage of the SAFE Banking Act by the U.S. House of Representatives, 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 under the Controlled Substances Act, there is a valid argument that banks cannot accept funds for deposit from businesses involved with the cannabis industry.

Accordingly, due to the present state of the laws and regulations governing financial institutions in the U.S., only a small percentage of banks and credit unions offer financial services to the cannabis industry. Although the Company has strong relationships with several banking partners, regulatory restrictions make it extremely difficult for any cannabis company to obtain financing from U.S. federally regulated entities. Additionally, U.S. federal prohibitions on the sale of cannabis may result in cannabis manufacturers and retailers being restricted from accessing the U.S. banking system and they may be unable to deposit funds in federally chartered banking institutions. While the Company does not anticipate material impacts from dealing with banking restrictions, additional banking restrictions could nevertheless be imposed that would result in existing deposit accounts being closed and/or the inability to make further bank deposits. The inability to open bank accounts would make it more difficult for the Company to operate and would substantially increase operating costs and risk.

## 31. Segmented Information

The Company's operations comprise a single operating segment engaged in the cultivation, branding, manufacturing, wholesale distribution and retail sale of cannabis and cannabis products within the U.S. All revenues were generated in the United States for the three months ended March 31, 2022 and 2021 and all property, plant and equipment and intangible assets are located in the United States.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 32. Subsequent Events

The Company has evaluated subsequent events through May 26, 2022.

#### *Loudpack Acquisition*

On April 4, 2022, pursuant to the terms of the definitive agreement announced on November 29, 2021, the Company completed the acquisition of Loudpack (the "Loudpack Acquisition"). Pursuant to the terms of the Loudpack Acquisition, Harborside acquired 100% of the equity interests of Loudpack through the issuance of 90,752,140 SVS, 2,000,000 warrants, the restructuring and assumption of approximately \$50 million of debt and cash consideration of approximately \$5 million. The warrants issued are exercisable to purchase SVS at a price of \$2.50 per SVS, anytime within five years of the closing date. Harborside has the option to accelerate the expiration date of the warrants in the event that the volume weighted average trading price of the SVS is equal to or greater than \$5.00.

In connection with the Loudpack Acquisition, the Company announced the appointment of Marc Ravner as Director (see below) and President of Integration of the Company.

The financial effects of this transaction have not been recognized at March 31, 2022. The operating results and assets and liabilities of the acquired company will be consolidated from April 4, 2022.

#### *(i) Acquisition-related costs*

Acquisition-related costs of approximately \$1,593,000 will be included in professional fees in the unaudited condensed interim consolidated financial statements in the reporting period ending June 30, 2022. A portion of the professional fees will be settled with shares (see "Shares for Debt" below).

#### *(ii) Information not disclosed as not yet available*

At the time the unaudited condensed interim consolidated financial statements were authorized for issuance, the Company had not yet completed the purchase accounting for the Loudpack acquisition. In particular, the fair values of assets and liabilities have not been determined provisionally as the independent valuations have not been finalized. It is also not yet possible to provide detailed information about each class of acquired receivables and any contingent liabilities of the acquired entity.

#### *Name Change to StateHouse Holdings Inc. and Share Consolidation*

On April 4, 2022, the Company announced that it plans to file articles of amendment to officially be renamed StateHouse Holdings Inc. ("StateHouse") (the "Name Change") and to effect the consolidation (the "Consolidation") of all of its issued and outstanding SVS and related warrants, options and RSU's. Pursuant to the Consolidation, shareholders are expected to receive one post-Consolidation SVS, SVS warrant, option or RSU for every six pre-Consolidation SVS, SVS warrant, option or RSU (the "Consolidation Ratio"), subject to the Company continuing to meet minimum listing requirements of the CSE. Accordingly, following the Name Change and Consolidation, shareholders currently holding six SVS of the Company, will instead own one SVS. In the event that the Consolidation would result in the issuance of fractional SVS, each fractional post-Consolidation SVS will be rounded down to the nearest whole, with any fractional SVS deemed to have been tendered for cancellation for no consideration. The trading price of the SVS is expected to reflect the Consolidation Ratio immediately upon the resumption of trading following the Name Change and Consolidation. The Company expects the Name Change and Consolidation to be completed on or about June 24, 2022, following which the post-Consolidation SVS will trade on the CSE under the new ticker symbol "STHZ". The Name Change and Consolidation were approved by the shareholders of the Company on February 22, 2022.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 32. Subsequent Events (continued)

#### *Changes to the Board of Directors and Appointment of New Officers*

On April 4, 2022, Kevin Albert, Andrew Sturner and Peter Kampian departed the Board to create vacancies for new members (the "Resignations"). On the same day, the Company announced that Marc Ravner, Tiffany Liff and Jonathon Roy Pottle had joined the Board, effective immediately, as approved by the shareholders of the Company on February 22, 2022. Mr. Sturner transitioned into the role of a Board observer, alongside Roger Jenkins and Will Senn, who retained their existing roles as Board observers.

In addition to Mr. Ravner's appointment as President of Integration of the Company (see above), the Company also announced that Robert Bacchi had been appointed Chief Technology Officer of the Company.

#### *Grant of Incentive Options and RSUs to the Board and Management*

Following completion of the Loudpack Acquisition, the Company granted (i) options to purchase an aggregate of 10,801,203 SVS; and (ii) RSUs representing the right to receive up to an aggregate of 787,401 SVS, subject to the satisfaction of certain vesting conditions, to certain employees of the Company. In addition, the Company granted RSUs representing the right to receive up to an aggregate of 1,950,000 SVS, subject to the satisfaction of certain vesting conditions, to members of its newly reconstituted Board.

The Company also granted options to purchase up to 50,000 SVS to each of Mr. Albert, Mr. Sturner and Mr. Kampian, for certain advisory and consulting services to be provided to the Company following the Resignations, and options to purchase up to 50,000 SVS to Mr. James Scott, in connection with his role as Chair of the special committee of the Company.

Each option granted is exercisable into one SVS at an exercise price of C\$0.75 per SVS for a period of five years following the date of grant. All options and RSUs were granted in accordance with the A&R Plan adopted by the Board on January 17, 2022 and approved by shareholders on February 22, 2022.

On April 29, 2022, the Company also announced the grant of options to certain members of management to purchase up to an aggregate 1,540,000 SVS. The options are exercisable at the greater of C\$0.75 per SVS and the closing market price of the SVS on the date of grant of options. 25% of the total number of options granted will become fully vested on each of the first, second, third and fourth anniversary of the date of grant.

#### *Shares for Debt*

On April 4, 2022, the Company agreed to issue an aggregate of 1,443,493 SVS at a deemed issuance price of C\$0.72 per SVS to settle C\$1,035,647 owing to certain advisors of the Company (the "Indebtedness") for certain advisory services provided to the Company in connection with the Urbn Leaf Acquisition and the Loudpack Acquisition. The Company chose to satisfy the Indebtedness with SVS in order to preserve its cash for development of its business.

#### *Term Loan*

The second tranche of the Term Loan was disbursed to the Company on April 8, 2022, following the close of the acquisitions of Loudpack and Urbn Leaf. The Company received approximately \$31,909,000 in net proceeds.

# HARBORSIDE INC.

## Notes to the Unaudited Condensed Interim Consolidated Financial Statements For the Three Months Ended March 31, 2022 and 2021 (Expressed in United States Dollars, except share amounts)

### 32. Subsequent Events (continued)

#### *Cachee Gold Mines Corp. ("Cachee")*

On April 27, 2022, the Company entered into an amendment to the share purchase agreement with Cachee (refer to Note 9 of the 2021 audited consolidated financial statements). The amended agreement deleted certain sections and replaced it with a cash payment of \$50,000, payable as follows: (i) \$15,000, not later than April 29, 2022, (ii) \$15,000, not later than July 29, 2022; and (iii) \$20,000, not later than October 31, 2022. The Company received the first installment payment \$15,000 on April 29, 2022.

#### *Repayment of Bridge Financing*

On April 29, 2022, the Company announced that the Bridge Financing assumed as part of the Urbn Leaf Acquisition had been repaid by: (i) a cash payment in the amount of \$358,541; and (ii) the issuance of approximately \$5,870,000 worth of SVS at a price of C\$0.45 per SVS (16,660,993 SVS).

#### *LUX Settlement*

On March 24, 2022, the Company entered into a \$1,250,000 settlement agreement with Altai Partnership, LLC ("Altai") in relation to the acquisition by the Company of Lucrum Enterprises Inc. (the "LUX Acquisition") d/b/a LUX Cannabis Dispensary ("LUX") (refer to Note 9 of the audited consolidated financial statements for the year ended December 31, 2021). Management has determined there was uncertainty related to the collectability of the settlement payments and therefore will recognize any gains from recovery of impairment as installment payments are received. In April 2022, the Company received the first installment payment of \$500,000.

#### *New retail store openings*

On April 2, 2022, the Urbn Leaf branded dispensary located in Grossmont, California, commenced operations and on April 28, 2022, the Harborside branded dispensary located in San Francisco, California, commenced operations.

#### *SBC Private Loans*

On May 11, 2022, the Company repaid the principal and accrued interest totaling \$250,665 in relation to its December 2016 SBC loan.

On May 18, 2022, the Company repaid the principal and accrued interest totaling \$77,010 in relation to its April 2018 SBC loan.

On May 19, 2022, the Company entered into the third amendments to the promissory notes in relation to its May 2017 and August 2017 SBC loans extending the maturity dates to May 9, 2023.

#### *Sale of certain assets of Sublime Machining, Inc. ("Sublime Machining")*

On May 13, 2022, the Company entered into a letter of intent to sell certain assets of Sublime Machining, including its California State Manufacturing License, all necessary permits from the City of Oakland and Alameda County to conduct a cannabis business and all "as is" equipment and furnishings located in the Oakland facility needed to produce pre-rolls, vape cartridges and gummies. The consideration for the sale is \$200,000.

# HARBORSIDE INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
For the Three Months Ended March 31, 2022 and 2021  
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## 32. Subsequent Events (continued)

### *Seaside Acquisition*

On May 18, 2022, the Company entered into an agreement to acquire a further 50% ownership interest in its Seaside, California retail dispensary (the "Seaside Acquisition"). The Seaside Acquisition will result in the Company owning all of its issued and outstanding securities of 680 Broadway Master, LLC, which owns the Seaside retail store, bringing the Company's interest in the Seaside retail store to 100%. The Seaside Acquisition was the result of a legal settlement with the Company's former partner in the Seaside retail store. As a result, the total cost of the Seaside Acquisition was only \$444,000, with \$100,000 to be paid upfront (the "First Installment") and the balance payable over seven years, with \$50,000 being paid on the first to sixth anniversaries of the First Installment, and \$44,000 being paid on the seventh anniversary of the First Installment.