

SHARC INTERNATIONAL SYSTEMS INC.
Condensed Consolidated Interim Financial Statements

For the six months ended June 30, 2018

(Unaudited – Expressed in Canadian dollars)

SHARC INTERNATIONAL SYSTEMS INC.

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the condensed financial statements; the statements must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor. The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of financial information by an entity's auditor.

Management has prepared the information and representations in this interim report. The condensed financial statements have been prepared in accordance with International Financial Reporting Standards and, where appropriate, reflect management's best estimates and judgment. The financial information presented throughout this report is consistent with the data presented in the condensed financial statements.

The company maintains adequate systems of internal accounting and administrative controls, consistent with reasonable cost. Such systems are designed to provide reasonable assurance that relevant and reliable financial information is produced.

Sharc International Systems Inc.
Condensed Consolidated Interim Statements of Financial Position
(Expressed in Canadian dollars)

	Note	June 30, 2018 (unaudited) \$	December 31, 2017 (audited) \$
ASSETS			
Current			
Cash		1,845,685	526,036
Receivables	5	365,839	350,215
Prepaid expenses		393,732	81,483
Inventory	6	884,150	528,838
Loans receivable	7	3,707	74,197
Total current assets		3,493,113	1,560,769
Equity investment	8	17,357	—
Restricted cash	9	50,000	50,000
Deposits		9,999	9,999
Property & Equipment	10	235,694	83,718
Total assets		3,806,163	1,704,486
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities	11	1,237,745	791,192
Loans payable	12	18,015	17,604
Deferred revenue	13	2,145	200,168
Warranty provisions	14	18,372	14,926
Total current liabilities		1,276,277	1,023,890
Loans payable	12	21,988	30,313
Warranty provisions	14	—	4,000
Convertible debentures	15	1,952,966	1,877,661
		3,251,231	2,935,864
SHAREHOLDERS' EQUITY			
Share capital	16	13,194,684	9,255,241
Subscriptions received	16	—	309,000
Reserves	16	2,708,797	2,594,075
Currency translation reserve		(62,230)	(10,715)
Convertible debentures – equity component	15	125,042	125,042
Deficit		(15,411,361)	(13,504,021)
Total shareholders' deficiency		554,932	(1,231,378)
Total liabilities and shareholders' deficiency		3,806,163	1,704,486

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

Nature of Operations and Going Concern [Note 1]

Commitments and Contingencies [Note 17]

Subsequent Events [Note 22]

Approved on behalf of the Board:

/s/ Lynn Mueller
Director

/s/ Mark McCooley
Director

Sharc International Systems Inc.

Condensed Consolidated Interim Statements of Loss and Comprehensive Loss

(Unaudited - Expressed in Canadian dollars)

	Note	Three Months Ended June 30, 2018 \$	Three Months Ended June 30, 2017 \$	Six Months Ended June 30, 2018 \$	Six Months Ended June 30, 2017 \$
Revenue		39,862	207,387	458,109	207,387
Cost of Sales		(12,203)	(309,628)	(211,398)	(449,300)
Gross Margin		27,659	(102,241)	246,711	(241,913)
Expenses					
Accounting and legal		81,645	23,997	132,802	66,786
Advertising and promotion		108,949	45,368	210,093	112,468
Consulting	11	219,718	133,325	442,930	335,505
Depreciation	10	12,266	3,139	24,531	6,278
Foreign exchange		126,561	12,477	(44,708)	17,309
Insurance		3,733	3,909	11,193	8,349
Office and miscellaneous		102,020	106,638	199,294	166,489
Regulatory and filing fees		16,298	4,419	24,196	15,990
Rent		35,147	33,868	73,588	61,829
Research and development		88,403	9,815	145,128	11,215
Share-based payments	11,16	2,387	172,362	105,065	368,673
Telephone and utilities		32,804	10,878	44,561	21,367
Travel		29,669	35,004	61,532	58,882
Wages and benefits	11	147,034	324,026	486,211	614,462
Warranty expense		—	18,067	—	18,171
		(1,006,634)	(937,292)	(1,916,416)	(1,883,773)
Government grants and assistance		—	—	—	—
Interest and financing expense	12,15	(132,064)	(21,187)	(237,635)	(39,415)
Loss on debt settlement	16	—	—	—	(7,000)
Loss for the period		(1,111,039)	(1,060,720)	(1,907,340)	(2,172,101)
Other comprehensive income (loss)					
Foreign currency translation		228,768	(13,331)	51,515	(14,680)
Net loss and comprehensive loss		(882,271)	(1,074,051)	(1,855,825)	(2,186,781)
Basic and diluted loss per common share		(0.03)	(0.04)	(0.06)	(0.08)
Weighted average number of common shares outstanding		33,098,575	28,111,433	30,795,583	27,449,908

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

Sharq International Systems Inc.

Condensed Consolidated Interim Statements of Changes in Shareholders' Equity

(Unaudited - Expressed in Canadian dollars)

	Common Shares		Subscriptions	Reserves	Currency	Convertible	Deficit	Total
	Number	\$	Received	\$	translation	debtenture	\$	\$
					reserve			
					\$	\$		\$
Balance, December 31, 2016	26,379,302	7,876,677	–	2,183,696	36,934	–	(9,780,690)	316,617
Common shares issued	1,450,528	1,523,054	–	–	–	–	–	1,523,054
Residual value of warrants granted	–	(431,730)	–	431,730	–	–	–	–
Share issue costs	–	(174,960)	–	52,580	–	–	–	(122,380)
Shares issued for debt	100,000	112,000	–	–	–	–	–	112,000
Shares issued for services	25,000	28,000	–	–	–	–	–	28,000
Warrants exercised	303,714	148,820	–	–	–	–	–	148,820
Stock options exercised	35,714	18,750	–	–	–	–	–	18,750
Fair value of stock options exercised	–	92,154	–	(92,154)	–	–	–	–
Issuance of convertible debt	–	–	–	160,857	–	125,042	–	285,899
Warrants issued for loan extension	–	–	–	13,531	–	–	–	13,531
Share-based compensation	–	–	–	368,673	–	–	–	368,673
Currency translation adjustment	–	–	–	–	(14,680)	–	–	(14,680)
Net loss for the period	–	–	–	–	–	–	(2,172,101)	(2,172,101)
Balance, June 30, 2017	28,294,258	9,192,765	–	3,118,913	22,254	125,042	(11,952,791)	506,183
Shares issued for services	25,000	14,438	–	–	–	–	–	14,438
Stock options exercised	100,000	60,000	–	–	–	–	–	60,000
Fair value of stock options exercised	–	(11,962)	–	11,962	–	–	–	–
Reversal of forfeited options	–	–	–	(798,210)	–	–	798,210	–
Subscriptions received	–	–	309,000	–	–	–	–	309,000
Share-based payments	–	–	–	261,410	–	–	–	261,410
Currency translation adjustment	–	–	–	–	(32,969)	–	–	(32,969)
Net loss for the period	–	–	–	–	–	–	(2,349,440)	(2,349,440)
Balance, December 31, 2018	28,419,258	9,255,241	309,000	2,594,075	(10,715)	125,042	(13,504,021)	(1,231,378)
Common shares issued	9,777,735	3,911,098	(192,000)	–	–	–	–	3,719,098
Share issue costs	–	(243,110)	–	85,112	–	–	–	(157,998)
Stock option exercised	500,000	196,000	–	–	–	–	–	65,450
Fair value of stock options exercised	–	75,455	–	(75,455)	–	–	–	–
Subscriptions refunded	–	–	(117,000)	–	–	–	–	(117,000)
Share-based payments	–	–	–	105,065	–	–	–	105,065
Currency translation adjustment	–	–	–	–	(51,515)	–	–	(51,515)
Net loss for the period	–	–	–	–	–	–	(1,907,340)	(1,907,340)
Balance, June 30, 2018	38,696,993	13,194,684	–	2,708,797	(62,230)	125,042	(15,411,361)	554,932

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

Sharc International Systems Inc.
Condensed Consolidated Interim Statements of Cash Flows
(Unaudited - Expressed in Canadian dollars)

	Note	Six Months Ended June 30, 2018 \$	Six Months Ended June 30, 2017 \$
OPERATING ACTIVITIES			
Net loss for the period		(1,907,340)	(2,172,101)
Add items not affecting cash:			
Depreciation	10	24,531	6,278
Unrealized foreign exchange		(42,462)	(7,984)
Share-based payments	16[e]	105,065	368,673
Accrued interest expense	15	214,731	24,137
Shares issued for services	16[b]	—	28,000
Loss on debt settlement	16[b]	—	7,000
Changes in non-cash working capital items:			
Receivables		(12,797)	(148,368)
Prepaid expenses		(312,249)	41,402
Inventory		(354,965)	(83,544)
Accounts payable and accrued liabilities		304,167	69,350
Deferred revenue		(198,023)	(20,400)
Warranty provisions		(554)	1,463
Cash used in operating activities		(2,179,896)	(1,886,094)
INVESTING ACTIVITY			
Purchase of property and equipment	10	(176,507)	—
Purchase of 50% of Bandwidth Energy Limited	8	(17,357)	—
Cash used in investing activity		(193,864)	—
FINANCING ACTIVITIES			
Proceeds from loans payable	12	210,000	—
Repayment of loans payable	12	(219,150)	(217,419)
Repayment of loans receivable		70,490	1,050
Proceeds on exercise of stock options	16[b]	196,000	18,750
Proceeds on exercise of warrants		—	148,820
Proceeds on private placement, net of costs	16[b]	3,561,100	1,400,675
Proceeds on convertible debentures, net of costs	15	—	2,186,170
Subscriptions refunded		(117,000)	—
Cash provided by financing activity		3,701,440	3,538,046
Increase (Decrease) in cash		1,327,680	1,651,952
Impact of exchange rate changes on cash		(8,031)	(298)
Cash, beginning of the period		576,036	373,430
Cash, end of the period		1,895,685	2,025,084

Supplemental disclosure with respect to cash flow (Note 21)

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

Sharc International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

Sharc International Systems Inc. (the “**Company**” or “**SHARC**”) was incorporated under the *Business Corporations Act* (British Columbia) on February 4, 2011. The Company’s shares are listed on the Canadian Securities Exchange (the “**CSE**”) under the trading symbol “**SHRC**”. The Company is engaged in providing wastewater heat exchange expertise and products that service commercial, industrial, public utilities and residential development projects objectives of reducing their carbon footprint while saving on energy costs. The Company’s registered and records office is located at 1443 Spitfire Place, Port Coquitlam, British Columbia, Canada, V3C 6L4.

These condensed consolidated interim financial statements (the “**Financial Statements**”) have been prepared under the assumption that the Company will continue as a going concern. The going concern basis of presentation assumes that the Company will be able to meet its obligations and continue its operations for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. Realization values may be substantially different from the carrying values as shown, and these Financial Statements do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should the Company be unable to continue as a going concern.

The Company has incurred losses and negative operating cash flows since its inception. As of June 30, 2018, the Company has accumulated a deficit of \$15,411,361 (December 31, 2017 - \$13,504,021) and working capital of \$2,216,836 (December 31, 2017 - \$536,879). Although it is difficult to predict future liquidity requirements, management believes the Company expects to have sufficient working capital to fund its operations until the first quarter of 2019. Given its current working capital, the Company may not be able to meet its financial obligations and sustain its operations in the normal course of business, all of which cast substantial doubt about the Company’s ability to continue as a going concern. The Company’s ability to meet its long term business strategy depends on its ability to obtain additional equity financing and to generate operational cash flow from sales of its products and government grants available for green energy technologies.

The Company’s longer term business strategy for generating cash flow is to continue to develop the United Kingdom, with particular emphasis on Scotland where government initiatives & incentives to support the adoption of low carbon technologies are stimulating market activity, while continuing to develop its commercial and marketing platform with North America and the wider European Union. In addition, the Company will look to take advantage of regions that incentivize green energy technologies, add additional green energy products to the pipeline and continue to invest in internal research and development for improvements to existing products or new product lines.

Share International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION

[a] Statement of compliance

These Financial Statements have been prepared in accordance with International Accounting Standard (“IAS”) 34 “Interim Financial Reporting”. They do not include all of the information required for full annual financial statements and should be read in conjunction with the Company's audited annual financial statements for the fiscal year ended December 31, 2017, which have been prepared with International Financial Reporting Standards (“IFRS”). These Financial Statements were approved by the Company’s Board of Directors on August 29, 2018.

[b] Basis of measurement

These Financial Statements have been prepared on a historical cost basis, except for the revaluation of certain financial assets and financial liabilities to fair value.

[c] Functional and foreign currency

These Financial Statements are presented in Canadian dollars, which is the Company’s functional currency. Foreign currency transactions are translated into Canadian dollars using the exchange rates at the date of the transactions. Foreign exchange gains or losses resulting from the settlement of transactions and from the translation at period and year-end rate of monetary assets and liabilities denominated in foreign currencies are recognized in net income or loss.

[d] Significant accounting estimates and judgments

The preparation of these Financial Statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. These Financial Statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the Financial Statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company reviews its estimates and underlying assumptions on an ongoing basis.

Critical Judgments

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the Financial Statements:

- i. Research costs are recognized as an expense when incurred but development costs may be capitalized as intangible assets if certain conditions are met as described in IAS 38, *Intangible Assets*. Management has determined that development costs do not meet the conditions for capitalization under IAS 38 and all research and development costs have been expensed.

Share International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

Critical Judgments (continued)

- ii. Management is required to assess the functional currency of the Company. In concluding that the Canadian dollar is the functional currency of the Company, management considered the currency that mainly influences the operating expenditures in the jurisdiction in which the Company operates.
- iii. The determination of categories of financial assets and financial liabilities has been identified as an accounting policy which involves judgments or assessments made by management.
- iv. Management is required to determine whether or not the going concern assumption is appropriate for the Company at the end of each reporting period. Considerations taken into account include available information about the future including the availability of financing and revenue projection, as well as current working capital balance and future commitments of the Company.

Estimation Uncertainty

The following are key assumptions concerning the future and other key sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year:

- i. Provisions for income taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxation authorities. Where the final outcome of these tax-related matters is different from the amounts that were originally recorded, such differences will affect the tax provisions in the period in which such determination is made.
- ii. The fair value of accrued liabilities at the time of initial recognition is made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors.
- iii. Warranty provisions are recognized for the future obligations to provide services for the repairs and maintenance of products sold to its customers. The Company assesses its warranty provision based on experience. Actual costs incurred may differ from those amounts estimated.

Sharc International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

- iv. The Company estimates the net realizable values of inventories, taking into account the most reliable evidence available at each reporting date. The future realization of these inventories may be affected by future technology or other market drive changes that may reduce future selling prices.
- v. Revenues are recognized on service agreements with regards to some of its product sales which requires management to make judgements regarding the timing and allocation of revenue. Specifically, installation is generally not assume to have standalone value and is often recognized on the same basis as the remainder of the service fees. However, the Company defers the recognition of revenue associated with fees for service agreements or warranty costs that are built in to the original sales price and recognizes the associated revenue evenly over the term the service or warranty is provided.

3. SIGNIFICANT ACCOUNTING POLICIES

These Financial Statements have been prepared on the basis of accounting policies and methods of computation consistent with those applied in the Company’s audited annual financial statement for the fiscal year ended December 31, 2017.

These Financial Statements include the accounts of the Company’s subsidiaries:

Company	Location	December 31, 2018 Ownership %	December 31, 2017 Ownership %
International Wastewater Heat Exchange Systems Inc. (“ IWHES ”)	Canada	100	100
Sharc Energy Ltd (formerly IWWS (UK) Ltd. (“ Sharc UK ”)	United Kingdom	100	100
Sharc Caledonia Ltd. (“ Caledonia ”)	United Kingdom	40	40
Sharc Highlands Ltd. (“ Highlands ”)	United Kingdom	100	—
Bandwidth Energy Ltd. (“ Bandwidth ”)	United Kingdom	50	—
Green Sharc Ltd. ⁽¹⁾	United Kingdom	100	100
Sharc Energy Services (UK) Ltd. ⁽¹⁾	United Kingdom	100	100
2336882 Ontario Inc. ⁽¹⁾	Canada	100	100

⁽¹⁾The subsidiary was inactive at period end.

All significant intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Sharq International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

4. RECENT ACCOUNTING PRONOUNCEMENTS

New Standards Recently Adopted

The following is an overview of new accounting standards that the Company adopted effective January 1, 2017:

- **IFRS 9 *Financial Instruments*** - This standard provides added guidance on the classification and measurement of financial liabilities. The standard is effective for annual periods beginning on or after January 1, 2018.
- **IFRS 15 *Revenue from Contracts with Customers*** - This standard covers principles for reporting about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. IFRS 15 is effective for annual periods beginning on or after January 1, 2018.
- **IFRS 2 *Classification and Measurement of Share-based Payment Transactions*** – This standard was issued in June 2016. The amendments provide requirements on accounting for the effect of vesting and non-vesting conditions on the measurement of cash settled share-based payments, share-based transactions with a net settlement feature for withholding tax obligations and a modification to the terms and conditions of a share-based payment that changes the classification of the transactions from cash-settled to equity-settled. This standard is effective for reporting periods beginning on or after January 1, 2018.

The adoption of the above standards did not have a material impact on the Financial Statements.

New Standards Not Yet Effective

The following is an overview of new accounting standards that the Company will be required to adopt in future years. The Company does not expect to adopt any of these standards before their effective dates. The Company continues to evaluate the impact of these standards on its Financial Statements.

- **IFRS 16 *Leases*** - This standard was issued in January 2016 and specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. This standard is effective for reporting periods beginning on or after January 1, 2019.

Sharq International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

5. RECEIVABLES

	As at June 30, 2018 \$	As at December 31, 2017 \$
GST Recoverable (Canada)	114,107	113,684
VAT and government assistance receivable (UK)	69,676	88,550
Holdback receivables	56,676	60,165
Other receivables	36,482	13,279
Trade Receivables	88,898	74,537
Total	365,839	350,215

6. INVENTORY

	As at June 30, 2018 \$	As at December 31, 2017 \$
Materials and supplies	56,865	260,593
Work-in-progress	827,285	268,245
Total	884,150	528,838

7. LOANS RECEIVABLE

During the year ended December 31, 2015 the Company advanced \$80,000 to the CEO of the Company. During the year ended December 31, 2016, \$40,000 was repaid. The advance bears interest at a rate of 3% per annum and is due on demand. As at June 30, 2018 the outstanding balance was \$Nil (\$41,832) as the loan was repaid. In addition, there is an advance of \$Nil (March 31, 2017 - \$27,702) to the CEO which is non-interest bearing and is due on demand

8. EQUITY INVESTMENT

During the year ended December 31, 2015, the Company acquired a 40% interest in Caledonia for £4,000 (\$7,817). As the Company exerts significant influence over Caledonia but does not control it, the investment is accounted for as an equity investment.

The Company's unrecognized share of the loss for the six months ended June 30, 2018 was \$39,071 for a balance at June 30, 2018 of \$253,119 (December 31, 2017 - \$214,498).

As at December 31, 2017 and June 30, 2018, the equity investment was \$Nil.

The table below discloses selected financial information for Caledonia on a 100% basis:

Sharq International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

8. EQUITY INVESTMENT (CONTINUED)

	As at June 30, 2018 \$	As at December 31, 2017 \$
Current Assets	122,072	79,043
Non-current assets	1,187,832	1,221,276
Current liabilities	(111,847)	(110,445)
Non-current liabilities	(1,625,527)	(1,509,863)
Revenue	78,061	90,234
Total comprehensive loss	97,677	(274,779)

During the six months ended June 30, 2018, the Company acquired a 50% interest in Bandwidth for £10,000 (\$17,357). As the Company exerts significant influence over Caledonia but does not control it, the investment is accounted for as an equity investment. As of June 30, 2018, the Bandwidth has had no operational activity and has cash of £20,000 (\$34,714).

9. RESTRICTED CASH

The restricted cash balance is comprised of a guaranteed investment certificate and security deposit held as collateral for the Company's corporate credit cards.

10. PROPERTY AND EQUIPMENT

	Equipment, furniture and fixtures \$	Demo units \$	Computer hardware \$	Leasehold improvements \$	Building \$	Total \$
Cost:						
Balance, December 31, 2016	46,080	—	27,926	19,025	—	93,031
Addition	19,733	271,613	—	—	—	291,346
Balance, December 31, 2017	65,813	271,613	27,926	19,025	—	384,377
Addition	—	—	—	—	176,507	176,507
Balance, June 30, 2018	65,813	271,613	27,926	19,025	176,507	560,884
Accumulated depreciation:						
Balance, December 31, 2016	19,346	—	22,531	9,278	—	51,155
Depreciation	7,133	235,599	2,967	3,805	—	249,504
Balance, December 31, 2017	26,479	235,599	25,498	13,083	—	300,659
Depreciation	3,954	18,007	668	1,902	—	24,531
Balance, June 30, 2018	30,433	253,606	26,166	14,985	—	325,190
Net book value:						
As of December 31, 2017	39,333	36,014	2,248	5,942	—	83,718
As of June 30, 2018	35,380	18,007	1,760	4,040	208,284	235,694

Sharc International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2018
(Unaudited - Expressed in Canadian dollars)

11. RELATED PARTY DISCLOSURE

[a] Transactions with related parties

Related parties include members of the board of directors (“the **Board**”) and officers of the Company, and enterprises controlled by these individuals. The following fees and expenses were incurred in the normal course of business

	Three Months Ended June 30, 2018 \$	Three Months Ended June 30, 2017 \$	Six Months Ended June 30, 2018 \$	Six Months Ended June 30, 2016 \$
Consulting fees ^[i]	26,936	51,000	41,936	81,000
Wages and benefits ^[ii]	94,466	78,558	193,753	160,608
Share-based payments ^[iii]	—	142,111	—	303,961
Inventory ^[iv]	23,736	—	23,736	—
Research and development ^[v]	3,145	—	3,145	—
	148,283	271,669	262,570	545,569

[i] The Company paid consulting fees to companies controlled by the Chief Financial Officer, Chief Operating Officer and a Director of Sharc UK.

[ii] The Company paid wages and and benefits to the Chief Executive Officer and Director, a Director and the Chief Operating Officer.

[iii] Share-based payments was recognized in connection with the vesting of options granted to directors and officers of the Company.

[iv] The Company paid consulting fees to companies controlled by the Chief Operating Officer that were capitalized to inventory costs.

[v] The Company paid fees to companies controlled by a Director of Sharc UK that recorded as research and development expense..

[vi] Other transactions with related parties included:

Cost of sales of \$Nil (\$2,832) and expenses associated with ongoing projects capitalized to inventory or research and development costs which have been expensed of \$Nil (\$2,832) due to a company controlled by a director of Sharc UK.

Included in accounts payable is \$225,486 (December 31, 2017 – \$205,587) due to related parties.

Sharc International Systems Inc.
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12. LOANS PAYABLE

- [i] During the year ended December 31, 2015 Sharc UK received a loan of \$102,035 (£50,000) from an unrelated company. The loan accrues interest at a rate of 12.5% per annum and is payable on April 17, 2020. The loan must be repaid in monthly payments of £1,125 with the first payment required on June 17, 2015. An arrangement fee of £1,000 was paid prior to the loan being advanced. The loan is guaranteed by the CEO of Sharc UK. During the six months ended June 30, 2018, the Company made payments totaling \$11,716 (£6,750), of which \$2,716 (£1,545) related to interest and \$9,151 (£5,205), related to principal. The balance of the loan as at June 30, 2018 is \$40,003 (£23,047), of which \$18,015 (£10,379) is recognized as short-term.

- [ii] In February 2017, the Company received a loan of \$80,000 from the former CFO of the Company. The loan bore interest at a rate of 35% per month and was repayable on demand. The loan was repaid in March 2017.

- [iii] In November 2016, the Company received a loan of \$200,000. The loan was guaranteed by the CEO of the Company. The loan bore interest at a rate of 2% per month and was repayable within 60 days. The outstanding balance of the loan and accrued interest as at December 31, 2016 was \$204,816. On January 25, 2017, the Company received a loan extension to March 26, 2017. In consideration, the interest rate on the loan increased to 2.5% per month and the Company issued 28,571 share purchase warrants exercisable at \$1.40 for a period of two years from the date of issuance. The fair value of the share purchase warrants was \$13,531 estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 99.66% which is based on historical volatility, risk-free rate of return of 0.76% and an expected maturity of 2 years. The loan was repaid in March 2017.

- [iv] In February 2018, the Company received a \$150,000 loan from a third-party lender. The loan was unsecured, bears interest at 12% and due on demand. The loan was repaid in May 2018 for \$154,500.

- [v] In March 2018, the Company received a \$60,000 loan from a company controlled by the Chief Financial Officer. The loan was unsecured, non-interest bearing and due on demand. The loan was repaid in May 2018.

- [vi] In June 2018, Highlands received a £1,000,000 loan facility from a third party lender. This facility is to be used to pay invoices in respect of eligible costs incurred in connection with the Clyde Gateway Project. The loan is guaranteed by Sharc UK, bears interest at 3.5%, and is repayable in monthly payments £7,148.83 (or pro-rata depending on how much is drawn down) for 180 consecutive payments beginning 4 months from initial draw down. As of June 30, 2018, the facility has not been drawn from.

- [vii] In June 2018, Highlands received a £450,000 loan facility from a third party lender. This facility is to be used to pay costs incurred in connection with the Clyde Gateway Project. The loan provides the lender a bond and floating charge on Highlands, bears interest at 4.73% and interest is capitalized and added to the term loan to be repaid on June 25, 2024 (the “**Termination Date**”) or at such other times and in such amounts as the the Company and the lender may agree. As of June 30, 2018, the facility has not been drawn from.

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12. LOANS PAYABLE (CONTINUED)

	Six months ended June 30, 2018 \$	Year ended December 31, 2017 \$
Balance, beginning of period	47,917	267,402
Proceeds from loans	210,000	80,000
Repayment of loans	(221,716)	(324,330)
Interest expense	7,216	23,575
Foreign exchange	(3,414)	1,270
Balance, end of period	40,003	47,917
Less: non-current portion	(21,988)	(30,313)
	18,015	17,604

13. DEFERRED REVENUE

Deferred revenue relates to on-going projects and service agreements at period end. Revenue will be recognized on a completion and sale of the projects and over the length of term for the service agreements.

14. WARRANTY PROVISIONS

	Six months ended June 30, 2018 \$	Year ended December 31, 2017 \$
Balance, beginning of period	18,926	169,370
Warranty provisions recognized	—	13,798
Warranty expenses incurred	(554)	(164,242)
Balance, end of period	18,372	18,926
Less: non-current portion	(18,372)	(4,000)
	—	14,926

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15. CONVERTIBLE DEBENTURES

On May 30, 2017 and June 29, 2017, the Company issued two tranches of senior unsecured convertible debenture units with total principal amounts of \$1,320,000 and \$1,023,000, respectively. The debentures mature on May 30, 2020 and June 29, 2020, respectively, and bear interest at an annual rate of 12% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time prior to the maturity date into common shares of the Company at a conversion price of \$1.05 per common share.

Each debenture unit consisted of one \$1,000 principal amount senior unsecured convertible debenture and 714 share purchase warrants, each exercisable into one common share of the Company at \$1.05 per share three years from issuance.

The Company may abridge the exercise period of the warrants at any time after the date that is four months after the closing date, by providing written notice to the warrant holders within 30 days, in the event that the volume weighted average closing price of the Company's common shares is greater than \$2.10 per common share for twenty consecutive trading days. The warrants will, unless exercised, expire on the 30th day after the Company provides such written notice to the warrant holders.

Total finders' fees of \$157,010 in cash and 110,900 finders' warrants were incurred on the issuances. Each finders' warrant is exercisable into one common share of the Company at \$1.40 per share two years from issuance. The fair value of \$35,815 was assigned to the 110,900 finders' warrants using the Black-Scholes valuation model with the following weighted average assumptions: expected dividend yield of 0%, expected volatility of 102.68% which is based on historical volatility, risk-free rate of return of 0.85% and an expected maturity of 2 years.

The convertible debentures are compound financial instruments with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debentures by calculating the present value of the principal and interest payments, discounted at a rate of 20%, being management's best estimate of the rate that a non-convertible debenture with similar terms would bear. The equity component consists of the warrants and the equity conversion feature. The values attributed to each was based on the relative fair value approach.

On initial recognition, the liability components were \$1,962,798 (\$1,801,419 net of transaction costs), the warrants were \$190,101 (\$125,042 net of transaction costs and tax effect) and the residual equity components were \$190,101 (\$125,042 net of transaction costs and tax effect).

Accretion charges, included in interest and financing expense on the statement of loss and comprehensive loss, attributable to the debentures for the three and six month period ended June 30 2018 was \$110,848 and \$214,731 (three and six months June 30, 2017 – \$19,929 and \$19,929) of which \$139,425 relates to accrued interest as at June 30, 2018

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16. SHARE CAPITAL

[a] Authorized Share Capital

The authorized share capital consisted of unlimited number of common shares. The common shares do not have a par value. All issued shares are fully paid.

[b] Common shares

[i] On December 23, 2016, the Company closed a non-brokered private placement pursuant to which the Company issued 650,095 common share at a price of \$1.05 per share for total gross proceeds of \$682,600. In connection to this financing, the Company paid finder's fees and expenses of \$49,788.

On April 7, 2017, the Company amended the terms of the placement to be a brokered placement which consisted of a unit at a price of \$1.05 per unit. As a result, investors in the December 23, 2016 closing were issued a warrant on the same terms as the brokered placement (see Note 16 [b][v]).

[ii] On January 11, 2017, the Company issued 100,000 common shares to settle outstanding debt of \$105,000. The fair value of \$112,000 was assigned to the common shares based on the common share price on the date of issuance. As a result, the Company recognized a loss on debt settlement of \$7,000 on the consolidated statement of loss and comprehensive loss.

[iii] On January 16, 2017, the Company issued 25,000 common shares for services. The valuation was based on the fair value of the shares issued.

[iv] On February 27, 2017, the Company closed the first tranche of a brokered private placement pursuant to which the Company issued 759,957 units at a price of \$1.05 per unit for aggregate gross proceeds of \$797,955. Each unit consisted of one common share and one common share purchase warrant. Each warrant is exercisable at a price of \$1.40 until February 27, 2019. The value of \$79,795 was assigned to the 759,957 warrants using the residual value method.

In connection with the placement, the Company paid finders' fees and expenses of \$91,097 and issued 56,997 finders' warrants. Each warrant is exercisable at a price of \$1.05 until February 27, 2019. The fair value of \$28,866 was assigned to the 56,997 finders' warrants as estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 108.30% which is based on historical volatility, risk-free rate of return of 0.76% and an expected maturity of 2 years.

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16. SHARE CAPITAL (CONTINUED)

[b] Common shares (continued)

- [v] On April 7, 2017, the Company completed the final tranche of a brokered private placement pursuant to which the Company issued 690,571 additional units at a price of \$1.05 per unit for aggregate gross proceeds of \$725,100. Each unit consists of one common share and one common share purchase warrant of the Company. Each warrant entitles the holder to purchase one common share until February 27, 2019 at an exercise price of \$1.40 per share. The value of \$181,275 was assigned to the 690,591 warrants using the residual method.

In connection with the final tranche of the placement, the Company paid finders' fees of \$31,283 and issued 29,793 finders' warrants. Each finders' warrant entitles the holder to purchase one common share until February 27, 2019 at an exercise price of \$1.05 per share

In conjunction with the closing, the Company amended the terms of the non-brokered private placement completed on December 23, 2016 to offer each participant in the non-brokered placement one warrant for each common share purchased on the same terms as the brokered placement. Accordingly, the Company issued a total of 650,095 warrants to purchasers from the non-brokered placement. The Company also issued an additional 36,464 finders' warrants. Each finders' warrant entitles the holder to purchase one common share until December 23, 2018 at an exercise price of \$1.05 per share.

The value of \$181,275 was assigned to the 1,340,666 warrants using the residual method.

The fair value of \$23,714 was assigned to the 66,257 finders' warrants as estimated by using the Black-Scholes valuation model with the following weighted average assumptions: expected dividend yield of 0%, expected volatility of 107.34%-113.03% which is based on historical volatility, risk-free rate of return of 0.76% and an expected maturity of 1.71-1.89 years.

- [vi] On August 3, 2017, the Company issued 25,000 common shares for services. The valuation was based on the fair value of the shares issued.

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16. SHARE CAPITAL (CONTINUED)

[b] Common shares (continued)

- [vii] On May 11, 2018, the Company closed the first tranche of a non-brokered private placement raising gross proceeds of \$2,332,598 from the issuance and sale of 5,831,495 units at a price of \$0.40 per unit. \$309,000 of subscriptions were received prior to December 31, 2017. \$192,000 was included in this tranche. The remaining \$117,000 was refunded at the request of subscribers. Each unit consists of 1 common share and 1 common share purchase warrant. Each common share purchase warrant entitles the holder to acquire one common share at an exercise price of \$0.60 for a period of 24 months from the closing date of the private placement. In the event that the Company's common shares trade at a closing price on the Exchange of greater than \$1.00 per share for a period of 10 consecutive trading days at any time after the closing date, the Company may accelerate the expiry date of the common share purchase warrants by giving notice to the holders thereof and in such case the warrants will expire on the 30th day after the date hereafter.

In connection with the private placement, the Company paid finder's fees of \$64,238 and issued 133,000 finder's warrants. Each warrant has the same terms as common share purchase warrants issued under the private placement. The fair value of \$30,840 was assigned to the 133,000 finders' warrants as estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 109.70% which is based on historical volatility, risk-free rate of return of 1.93% and an expected maturity of 2 years

- [viii] On June 7, 2018, the Company closed the second tranche of a non-brokered private placement raising gross proceeds of \$1,578,500 from the issuance and sale of 3,946,250 units at a price of \$0.40 per unit. Each unit consists of 1 common share and 1 common share purchase warrant. Each common share purchase warrant entitles the holder to acquire one common share at an exercise price of \$0.60 for a period of 24 months from the closing date of the private placement. In the event that the Company's common shares trade at a closing price on the Exchange of greater than \$1.00 per share for a period of 10 consecutive trading days at any time after the closing date, the Company may accelerate the expiry date of the common share purchase warrants by giving notice to the holders thereof and in such case the warrants will expire on the 30th day after the date hereafter.

In connection with the private placement, the Company paid finder's fees of \$93,760 and issued 234,400 finder's warrants. Each warrant has the same terms as common share purchase warrants issued under the private placement. The fair value of \$54,272 was assigned to the 234,400 finders' warrants as estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 107.85% which is based on historical volatility, risk-free rate of return of 1.90% and an expected maturity of 2 years

- [ix] During the six months ended June 30, 2018, the Company issued 500,000 common shares pursuant to the exercise of stock options for aggregate gross proceeds of \$196,000. The fair value of the options of \$75,455 was transferred from reserves to share capital.

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16. SHARE CAPITAL (CONTINUED)

[c] Common share purchase warrants

Common share purchase warrant transactions and the number of common share purchase warrants outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2016	494,286	0.61
Issued	4,036,919	1.24
Exercised	(303,714)	(0.67)
Balance, December 31, 2017	4,227,491	1.22
Issued	10,145,135	0.60
Balance, June 30, 2018	14,372,626	0.78

Date of Expiry	Exercise Price \$	Number of Warrants Outstanding
August 22, 2018	0.70	109,714
September 2, 2018	0.70	59,429
October 21, 2018	1.58	21,429
December 23, 2018	1.40	650,095
December 23, 2018	1.05	36,464
February 27, 2019	1.40	1,450,528
February 27, 2019	1.05	86,790
May 30, 2020	1.05	942,857
May 30, 2019	1.40	66,000
June 6, 2019	1.40	28,571
June 29, 2020	1.05	730,714
June 29, 2019	1.40	44,900
May 11, 2020	0.60	5,964,495
June 7, 2020	0.60	4,180,640
Balance, June 30, 2018	0.78	14,372,626

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16. SHARE CAPITAL (CONTINUED)

[e] Stock options

During the three and six months ended June 30, 2018 and 2017, the Company recorded share-based payments of \$2,387 and \$105,065 and \$172,362 and \$368,673, respectively. The fair values of share options granted during the six months ended June 30, 2018 (there were no grants during six months ended June 30, 2017) are estimated using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2018	2017
Risk-free interest rate	1.80%	Nil
Estimated annualized volatility based on comparable companies	119.79%	Nil
Expected life	1 year	Nil
Expected dividend yield	0%	Nil
Exercise price	\$0.41	Nil
Fair value	\$0.1814	Nil
Share price	\$0.40	Nil

Stock option transactions and the number of stock options outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2016	1,738,572	1.07
Issued	(135,714)	0.58
Exercised	2,500,000	0.52
Cancelled	(1,460,000)	1.05
Balance, December 31, 2017	2,642,858	0.58
Issued	550,000	0.41
Exercised	(500,000)	(0.39)
Balance, June 30, 2018	2,692,858	0.58

Date of Expiry	Exercise Price \$	Number of Options Outstanding	Number of Options Exercisable
July 28, 2018	0.63	752,750	752,750
October, 27, 2020	1.47	142,858	142,858
July 12, 2021	1.05	100,000	100,000
October 3, 2018	0.44	1,247,250	1,247,250
October 23, 2018	0.60	200,000	200,000
March 13, 2019	0.46	250,000	250,000
Balance, June 30, 2018	\$0.58	2,692,858	2,692,858

As of June 30, 2018, the weighted average remaining life for outstanding options was 0.72 years (December 31, 2017 – 0.92 years).

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17. COMMITMENTS AND CONTINGENCIES

[a] Operating lease

The Company entered into a lease agreement commencing March 1, 2017 for a one-and-a-half year term at an annual rate of \$77,753 with the option to renew the lease for an additional 2-year term. In the event of failure to reach an agreement on base rent prior to commencement of the renewed term, the Company will provide ninety days' notice to vacate the property plus 3 months' rent at a rate of 110% of the base rate.

[b] Government Grants from the Energy Deployment Division of the Scottish Government

During the six months ended June 30, 2018, in connection with two wastewater heat recovery demonstration projects Sharc UK received \$43,911 (year ended December 31, 2017 - \$295,590), in aggregate \$339,501 in government grants from the Energy Deployment Division of the Scottish government. The funds received to date have been offset against the capitalized inventory costs associated with the projects. Per the underlying funding agreements, the parties jointly forecasted the expected revenue that would be generated from the projects for the first five years after completion. Under the terms of the grant, should the projects actual revenue exceed 10% or more of the forecasted revenue, the Scottish government reserves the right to require the Company to repay part of the grant.

[c] Low Carbon Infrastructure Transition Programme ("LCITP") Grant for Clyde Gateway

The Company has received grant funding of £1,684,188 for 50% of the eligible capital costs associated with the Clyde Gateway Project. No funds have been received to date. Per the underlying funding agreements, the parties jointly forecasted the expected revenue that would be generated from the projects for the first five years after completion. Under the terms of the grant, should the projects actual revenue exceed 10% or more of the forecasted revenue, the Scottish government reserves the right to require the Company to repay part of the grant.

18. SEGMENTED INFORMATION

The Company has a single operating segment, the sales and marketing of pharmaceutical drugs developed by the Company or by its collaborative partners. Substantially all of the Company's operations, assets, and employees are in Canada.

Geographic information as at June 30, 2018 is as follows:

	Canada	United Kingdom	Total
Asset			
Inventory	\$ 343,487	\$ 540,663	\$ 884,150
Equipment	43,055	224,416	267,471
	\$ 386,542	\$ 765,079	\$ 1,151,621

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18. SEGMENTED INFORMATION

Geographic information as at December 31, 2017 is as follows:

	Canada	United Kingdom	Total
Asset			
Inventory	\$ 327,911	\$ 200,927	\$ 528,838
Equipment	65,771	17,947	83,718
	\$ 393,682	\$ 218,874	\$ 612,556

Geographic information for the period ended June 30, 2018 is as follows:

	Canada	United Kingdom	Total
Revenues	\$ 429,100	\$ 29,009	\$ 458,109
Cost of sales	(192,018)	(19,380)	(211,398)
Gross Margin	\$ 237,082	\$ 9,629	\$ 246,711
Loss for the period	\$ (1,482,696)	\$ (424,644)	\$ 1,907,340

Geographic information for the year ended June 30, 2017 is as follows:

	Canada	United Kingdom	Total
Revenues	\$ 206,938	\$ 449	\$ 207,387
Cost of sales	(168,828)	(280,472)	(449,300)
Gross Margin	38,110	(280,023)	(241,913)
Loss for the period	\$ (1,592,808)	\$ (579,293)	\$ (2,172,101)

19. CAPITAL DISCLOSURES

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern in order to support the development of its business and maintain the necessary corporate and administration functions to facilitate these activities. The capital of the Company consists of items included in shareholders' equity.

The Company manages and adjusts its capital structure when changes to the risk characteristics of the underlying assets or changes in economic conditions occur. To maintain or adjust the capital structure, the Company may attempt to raise new funds.

There were no changes to the Company's approach to capital management during the year. The Company is not subject to externally imposed capital requirements.

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20. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value

The fair value of the Company's financial instruments is approximated by their carrying value due to their short-term nature.

IFRS 13 establishes a fair value hierarchy for financial instruments measured at fair value that reflects the significance of inputs used in making fair value measurements as follows:

Level 1 – quoted prices in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liabilities, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and

Level 3 – inputs for the asset or liability that are not based upon observable market data.

The fair value of cash is based on Level 1 inputs. The fair value of the Company's receivables, loans receivable, accounts payable and accrued liabilities, loans payable and convertible debentures approximate their carrying values due to the short-term to maturity.

[a] Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's cash and receivables are exposed to credit risk. The Company reduces its credit risk on cash by placing these instruments with institutions of high credit worthiness. Receivables are primarily from sales or loans. The Company believes these parties to be of sound creditworthiness, and to date, all receivables have been settled in accordance with agreed upon terms and conditions. As at June 30, 2018 and December 31, 2017, the Company is exposed to credit risk arising from receivables and loans receivable.

[b] Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company manages liquidity risk by maintaining sufficient cash balances to enable settlement of transactions on the due date. The Company addresses its liquidity through debt financing. While the Company has been successful in securing financings in the past, there is no assurance that it will be able to do so in the future.

[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. As at June 30, 2018, the Company is not exposed to any significant interest rate risk.

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20. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

[c] Market risk (continued)

[ii] Currency risk

Foreign exchange risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. As at June 30, 2018 the Company has exposure to the British pound that is subject to fluctuations as a result of exchange rate variations to the extent that transactions are made and balances are held in this currency. The Company has not hedged its exposure to currency fluctuations. The sensitivity of the Company's net loss to changes in the exchange rate between the Canadian dollar and the British pound resulting from a 10% change in the British pound exchange rate relative to the Canadian dollar would change the Company's net loss by approximately \$40,490 (December 31, 2017 - \$5,000)

21. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

	Six months Ended June 30, 2018 \$	Six months Ended June 30, 2017 \$
<hr/>		
Cash and cash equivalents consist of:		
Cash	1,845,685	2,025,084
Restricted Cash	50,000	—
	<hr/>	<hr/>
	1,895,685	2,025,084

Non-cash transactions:

Finders' warrants issued as share issuance costs	85,112	—
Fair value of stock options exercised	75,455	92,154

22. SUBSEQUENT EVENTS

[a] Subsequent to June 30, 2018, 109,714 warrants expired unexercised.