

SHARC INTERNATIONAL SYSTEMS INC.
Condensed Consolidated Interim Financial Statements

For the six months ended June 30, 2021

(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 consolidated interim 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 30,2021 (unaudited) \$	December 31,2020 (audited) \$
ASSETS			
Current			
Cash		3,682,451	3,101,267
Receivables	4	262,067	71,993
Prepaid expenses		131,549	92,687
Inventory	5	1,017,344	651,971
Total current assets		5,093,411	3,917,918
Restricted cash	6	25,000	25,000
Deposits		1,200	1,200
Property and equipment	7	404,514	426,516
Total assets		5,524,125	4,370,634
LIABILITIES AND SHAREHOLDERS' DEFICIENCY			
Current liabilities			
Accounts payable and accrued liabilities	8	373,658	146,244
Deferred revenue	10	151,193	57,816
Convertible debentures	11	1,833,915	291,440
Lease liabilities	12	104,728	105,421
Total current liabilities		2,463,494	600,921
Loans payable	9	60,000	60,000
Warranty provisions		6,000	-
Convertible debentures	11	2,923,918	4,843,495
Lease liabilities	12	251,896	304,650
Total liabilities		5,705,308	5,809,066
SHAREHOLDERS' DEFICIENCY			
Share capital	13	22,601,974	18,952,467
Reserves	13	3,811,324	4,241,450
Convertible debentures - equity component	11	809,640	907,036
Deficit		(27,404,121)	(25,539,385)
Total shareholders' deficiency		(181,183)	(1,438,432)
Total liabilities and shareholders' deficiency		5,524,125	4,370,634

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 14]
Subsequent Events [Note 19]

Approved on behalf of the Board:
/s/ Lynn Mueller /s/ Eleanor Chiu
Director Director

SHARC International Systems Inc.

Condensed Consolidated Interim Statements of Loss and Comprehensive Loss

(Unaudited - Expressed in Canadian dollars)

	Note	<u>Three Months Ended June 30, Six Months Ended June 30,</u>			
		2021	2020	2021	2020
		\$	\$	\$	\$
Revenue		107,022	112,772	297,234	167,447
Cost of sales		(51,787)	(48,024)	(172,433)	(55,489)
Gross margin		55,235	64,748	124,801	111,958
Expenses					
Accounting and legal		78,523	43,883	98,836	54,609
Advertising and promotion		47,222	70,727	100,932	129,209
Bad debt recovery		-	-	-	(7,311)
Consulting	8	98,182	155,869	238,358	238,308
Depreciation	7	36,698	34,745	73,365	69,491
Insurance		8,918	9,797	15,961	16,122
Interest and financing expense	9,11,12	274,907	364,569	557,436	696,738
Office and miscellaneous		23,607	16,612	41,928	33,251
Regulatory and filing fees		26,295	17,759	41,793	33,177
Rent		12,000	12,000	24,000	24,000
Repairs and maintenance		(1,490)	5,118	14,591	18,637
Research and development		38,945	3,537	58,046	5,602
Share-based payments	8,13	99,864	40,687	267,427	237,449
Telephone and utilities		22,925	21,426	43,327	43,797
Travel		2,863	(158)	2,875	22,580
Wages and benefits	8	300,403	166,339	411,971	473,182
Warranty expense		6,000	-	6,000	-
		(1,075,862)	(962,910)	(1,996,846)	(2,088,841)
		(1,020,627)	(898,162)	(1,872,045)	(1,976,883)
Gain on debt settlement		-	587,857	-	587,857
Revaluation of warrants on debt settlement		-	(194,074)	-	(194,074)
Interest income		1,889	-	1,889	-
Foreign exchange		(4,701)	443	(10,321)	(316)
Loss before income taxes		(1,023,439)	(503,936)	(1,880,477)	(1,583,416)
Deferred tax recovery		8,760	275,494	15,741	483,698
Loss and comprehensive loss for the period		(1,014,679)	(228,442)	(1,864,736)	(1,099,718)
Basic and diluted loss per common share		(0.01)	(0.00)	(0.02)	(0.02)
Weighted average number of common shares outstanding		91,262,205	52,989,849	87,310,177	49,283,978

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

SHARC International Systems Inc.

Condensed Consolidated Interim Statements of Changes in Shareholders' Deficiency

(Unaudited - Expressed in Canadian dollars)

	Common Shares		Reserves	Convertible debenture	Deficit	Total
	Number	\$	\$	\$	\$	\$
Balance, December 31, 2019	38,877,126	13,212,855	2,985,374	497,891	(22,650,344)	(5,954,224)
Common shares issued	10,000,000	650,000	-	-	-	650,000
Issuance of convertible debt	-	-	606,790	606,790	-	1,213,580
Conversion of convertible debt	5,125,000	605,497	-	(94,339)	-	511,158
Shares for services	2,368,935	264,938	-	-	-	264,938
Stock options exercised	60,000	4,500	-	-	-	4,500
Fair value of stock options exercised	-	3,629	(3,629)	-	-	-
Share-based payments	-	-	237,449	-	-	237,449
Shares for debt	45,455	6,818	-	-	-	6,818
Revaluation of warrants issued for debt settlement	-	-	194,074	-	-	194,074
Reversal of expired and forfeited options	-	-	(5,298)	-	5,298	-
Loss for the period	-	-	-	-	(905,644)	(905,644)
Balance, June 30, 2020	56,476,516	14,748,237	4,014,760	1,010,342	(23,550,690)	(3,777,351)
Common shares issued	10,001,000	3,000,300	-	-	-	3,000,300
Share issue cost	-	(356,197)	203,789	-	-	(152,408)
Stock options exercised	235,000	25,250	-	-	-	25,250
Fair value of stock options exercised	-	20,354	(20,354)	-	-	-
Warrants exercised	5,793,832	865,097	-	-	-	865,097
Fair value of warrants exercised	-	78,421	(78,421)	-	-	-
Conversion of convertible debt	5,900,000	571,005	-	(103,306)	-	467,699
Share-based payments	-	-	121,676	-	-	121,676
Loss for the period	-	-	-	-	(1,988,695)	(1,988,695)
Balance, December 31, 2020	78,406,348	18,952,467	4,241,450	907,036	(25,539,385)	(1,438,432)
Common shares issued	1,500,000	450,000	-	-	-	450,000
Share issue cost	-	(61,326)	37,768	-	-	(23,558)
Stock options exercised	518,125	50,703	-	-	-	50,703
Fair value of stock options exercised	-	40,986	(40,986)	-	-	-
Warrants exercised	4,344,728	1,331,146	-	-	-	1,331,146
Fair value of warrants exercised	-	714,273	(714,273)	-	-	-
Issuance of convertible debt	-	-	19,938	22,621	-	42,559
Conversion of convertible debt	7,709,167	1,055,475	-	(120,017)	-	935,458
Shares for services	155,113	68,250	-	-	-	68,250
Share-based payments	-	-	267,427	-	-	267,427
Loss for the period	-	-	-	-	(1,864,736)	(1,864,736)
Balance, June 30, 2021	92,633,481	22,601,974	3,811,324	809,640	(27,404,121)	(181,183)

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	<u>Six Months Ended June 30,</u>	
		2021	2020
		\$	\$
OPERATING ACTIVITIES			
Loss for the period		(1,864,736)	(905,644)
Add items not affecting cash:			
Depreciation	7	73,365	69,491
Bad debt recovery		-	(7,311)
Share-based payments	13	267,427	237,449
Shares for services	13	10,833	141,041
Accrued interest expense	9,11,12	557,436	696,738
Gain on debt settlement		-	(587,857)
Deferred tax recovery		(15,741)	(483,698)
Changes in non-cash working capital items:			
Receivables		(190,453)	(90,483)
Prepaid expenses		7,730	8,090
Inventory		(365,373)	(125,424)
Accounts payable and accrued liabilities		222,276	(248,985)
Deferred revenue		93,377	186,025
Warranty provisions		6,000	-
Cash used in operating activities		(1,197,859)	(1,110,568)
INVESTING ACTIVITY			
Purchase of property and equipment		(35,023)	(4,696)
Cash used in investing activity		(35,023)	(4,696)
FINANCING ACTIVITIES			
Proceeds from loans payable	10	-	40,000
Proceeds on exercise of stock options	13	50,703	4,500
Proceeds on exercise of warrants	13	1,331,146	-
Proceeds on exercise of debenture warrants	11	206,000	-
Proceeds on private placement, net of costs	13	426,442	156,000
Proceeds on convertible debentures, net of costs	11	-	4,490,762
Repayment of convertible debenture	11	(124,286)	(2,067,603)
Repayment of loans payable	9	-	(428,400)
Payment of lease liabilities	12	(75,939)	(78,058)
Cash provided by financing activities		1,814,066	2,117,201
Increase in cash		581,184	1,001,937
Cash, beginning of period		3,101,267	109,510
Cash, end of the period		3,682,451	1,111,447

Supplemental disclosure with respect to cash flow (Note 17)

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, 2021
(Unaudited - Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

SHARC International Systems Inc. (the “**Company**” or “**SHARC Energy**”) 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**”, Frankfurt Stock Exchange (the “**FSE**”) under the trading symbol “**IWIA**” and the OTC under the symbol “**INTWF**”. 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 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. As at June 30, 2021, the Company has an accumulated deficit of \$27,404,121 and positive working capital of \$2,629,917. The Company will continue to pursue opportunities to raise additional capital through equity markets and/or debt to fund its operating activities. Management anticipates it has sufficient working capital to maintain its activities for the subsequent 12 months. These Financial Statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial position that would be necessary if the going concern assumption were inappropriate, and these adjustments could be material.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2021
(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, 2020, which have been prepared with International Financial Reporting Standards (“IFRS”). These Financial Statements were approved by the Company’s Board of Directors on August 20, 2021.

[b] Basis of measurement and consolidation

These Financial Statements have been prepared on a historical cost basis, except for certain financial assets and financial liabilities measured at fair value.

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

Company	Location	June 30, 2021 Ownership %	December 31, 2020 Ownership %
SHARC Energy Systems Inc. (“SES”)	Canada	100	100
SHARC Energy Systems Australasia Pty Ltd. (“SHARC Australasia”) ⁽¹⁾	Australia	80	80
2336882 Ontario Inc. ⁽¹⁾	Canada	100	100

(1)The subsidiary was inactive.

The Company includes assets, liabilities and operations of subsidiaries from the date of acquisition to the date of disposal.

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

Certain comparative period balances have been reclassified for comparative purposes.

[c] Presentation currency

These Financial Statements are presented in Canadian dollars, which is the functional and presentationa currency of the Company and its subsidiaries.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2021
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[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.
- ii. The Company recognizes the deferred tax benefit related to deferred income and resource tax assets to the extent recovery is probable. Assessing the recoverability of deferred tax assets requires management to make significant estimates of future taxable profit. In addition, future changes in tax laws could limit the ability of the Company to obtain tax deductions from deferred income and resource tax assets.
- iii. In March 2020, the World Health Organization declared coronavirus COVID-19 a global pandemic. This contagious disease outbreak, which has continued to spread, and any related adverse public health developments, has adversely affected workforces, economies and financial markets globally, potentially leading to an economic downturn. It is not possible for the Company to predict the duration or magnitude of the adverse results of the outbreak and its effect on the Company's business or ability to raise funds.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
For the six months ended June 30, 2021
(Unaudited - Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

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. 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.
- iii. 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.
- iv. The Company has service agreements with regards to some of its product sales which requires management to make judgments regarding the timing and allocation of revenue. Specifically, installation is generally not assumed to have standalone value and is often recognized on the same basis as the remainder of the services fees. However, the Company defers the recognition of revenue associated with fees for services agreements or warranty costs that are built in to the original sales price and recognizes the associated revenue evenly over the term of the service or warranty is provided.
- v. The equity component of the convertible debenture is calculated using a discounted cash flow method which requires management to make an estimate on an appropriate discount rate.

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, 2020.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited - Expressed in Canadian dollars)

4. RECEIVABLES

	As at June 30, 2021	As at December 31, 2020
	\$	\$
GST recoverable (Canada)	54,489	43,760
Other receivable	3,683	426
Interest receivable	1,889	—
Trade receivables	202,006	27,807
Total	262,067	71,993

5. INVENTORY

	As at June 30, 2021	As at December 31, 2020
	\$	\$
Materials and supplies	10,294	10,294
Work-in-progress	950,594	486,709
Finished goods	56,456	154,968
Total	1,017,344	651,971

6. RESTRICTED CASH

The restricted cash balance of \$25,000 (December 31, 2020 - \$25,000) is comprised of a bank lien on funds held as collateral for the Company's corporate credit card limits.

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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(Unaudited - Expressed in Canadian dollars)

7. PROPERTY AND EQUIPMENT

	Equipment, furniture and fixtures \$	Demo units \$	Computer hardware \$	Leasehold improvements \$	Right of use asset \$	Total \$
Cost:						
Balance, December 31, 2019	46,080	337,547	27,926	19,025	548,680	979,258
Addition	4,696	-	12,619	4,516	-	21,831
Balance, December 31, 2020	50,776	337,547	40,545	23,541	548,680	1,001,089
Addition	23,805	-	27,558	-	-	51,363
Balance, June 30, 2021	74,581	337,547	68,103	23,541	548,680	1,052,452
Accumulated depreciation:						
Balance, December 31, 2019	32,364	307,548	27,435	19,025	45,280	431,652
Depreciation	3,213	14,893	3741	-	121,074	142,921
Balance, December 31, 2020	35,577	322,441	31,176	19,025	166,354	574,573
Depreciation	2,127	7,552	4,564	452	58,670	73,365
Balance, June 30, 2021	37,704	329,993	35,740	19,477	225,024	647,938
Net book value:						
As of December 31, 2020	15,199	15,106	9,369	4,516	382,326	426,516
As of June 30, 2021	36,877	7,554	32,363	4,064	323,656	404,514

SHARC International Systems Inc.
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8. RELATED PARTY DISCLOSURE

Transactions with related parties

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly. Key management personnel include officers and directors.

The Company incurred the following charges with key management personnel:

	Three months Ended June 30, 2021	Three months Ended June 30, 2020	Six months Ended June 30, 2021	Six months Ended June 30, 2020
	\$	\$	\$	\$
Consulting fees ^[i]	38,000	33,000	71,000	102,500
Wages and benefits ^[ii]	88,542	72,500	174,542	171,233
Share-based payments ^[iii]	82,055	51,874	216,914	143,996
	208,597	157,374	462,456	417,729

[i] The Company paid consulting fees to companies controlled by the Chief Financial Officer, the former Chief Operating Officer and former Senior Vice President of Finance.

[ii] The Company paid wages and benefits to the Chief Executive Officer and Director, a Director, the Chief Operating Officer and former Senior Vice President of Finance.

[iii] Share-based payments was recognized in connection with the vesting of options granted to directors and officers of the Company in the amount of \$82,055 and \$216,914 during the three and six months ended June 30, 2021 (June 30, 2020 - \$51,874 and \$149,294). Furthermore, options were terminated and cancelled during the six months ended June 30, 2021 which resulted in reversal of \$Nil (June 30, 2020 - \$5,298).

Included in accounts payable is \$1,180 (December 31, 2020 – \$Nil) due to related parties.

Other transactions

On February 11, 2020, the Company issued 5,027,600 units at a price of \$0.065 for the settlement of debt of \$326,794 owed to companies controlled by the Chief Financial Officer and a Director. (Note 13).

SHARC International Systems Inc.
Notes to Condensed Consolidated Interim Financial Statements
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9. LOANS PAYABLE

- [i] In December 2018, the Company received a \$490,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 6% and was repayable on March 13, 2019. In the event of a default on repayment, the interest rate rises to 9%. The balance of the loan as at December 31, 2019 is \$260,570. The loan was repaid in full during the six months ended June 30, 2020.
- [ii] In April 2019, the Company received a \$150,000 loan from a third-party lender. The loan is guaranteed by the CEO, bears interest at 12% and is repayable on July 24, 2019. The balance of the loan as at December 31, 2019 is \$162,378, including accrued interest of \$12,378. The loan was repaid during the six months ended June 30, 2020.
- [iii] During the year ended December 31, 2020, the Company received \$60,000 in connection with the Canada Emergency Business Account Program from the Government of Canada. The loan is interest free until December 31, 2022. If \$40,000 of the loan is repaid by December 31, 2022, the remaining \$20,000 of the loan will be forgiven. If the loan cannot be repaid before the initial term of December 31, 2022, the loan will be extended automatically for a term of three years and interest will be payable at 5.0% annually, with no principal payments until December 31, 2025.

	As at June 30, 2021 \$	As at December 31, 2020 \$
Balance, beginning of year	60,000	422,948
Proceeds from loans	—	60,000
Repayment of loans	—	(428,400)
Interest expense	—	5,452
Foreign exchange	—	—
Balance, end of period	60,000	60,000

10. DEFERRED REVENUE

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

SHARC International Systems Inc.
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(Unaudited - Expressed in Canadian dollars)

11. CONVERTIBLE DEBENTURES

- [i] On May 30, 2017 and June 29, 2017, the Company issued two tranches of 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 valued at \$35,815 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).

On May 29, 2020, the Company settled with all holders ("**Debentureholders**") of the Company's 12% unsecured, convertible debentures which were set to mature on May 30, 2020 and June 29, 2020 (the "**Maturing Debentures**").

SHARC International Systems Inc.
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11. CONVERTIBLE DEBENTURES (CONTINUED)

The Debentureholders have entered into settlement agreements with the Company (the “**Settlement Agreements**”) for the remaining principal of \$2,343,000 pursuant to which the Debentureholders accepted 75% cash payout of the outstanding principal amount of the Maturing Debentures, the payout of any accrued and unpaid interest up to the date of maturity and the amendment of 1,673,571 common share purchase warrants (the “**Warrants**”) in consideration for the cancellation of the Maturing Debentures and a release of the Company’s obligations under the Maturing Debentures. The expiry date of the Warrants will be extended by two years from May 30, 2020 and June 29, 2020 to May 30, 2022 and June 29, 2022, respectively, and the exercise price of the Warrants are repriced to \$0.25 from \$1.05 (collectively, the “**Warrant Amendments**”).

Pursuant to the Settlement Agreements, the Company recognized a forgiveness of debt of \$585,750. The fair value of the Warrants Amendment was \$194,074 estimated by using the Black-Scholes valuation model with the following assumptions: expected dividend yield of 0%, expected volatility of 123.44% which is based on historical volatility, risk-free rate of return of 0.26% and an expected maturity of 2 years. These have been recorded as a gain on debt settlement and revaluation of warrants on debt settlement in the statement of loss and comprehensive loss.

Accretion charges, included in interest and financing expense, attributable to the debentures for the three and six months ended June 30, 2020 was \$105,081 and \$230,304, of which \$125,637 relates to accrued interest.

- [ii] On March 8, 2019, May 9, 2019 and June 28, 2019, the Company issued three tranches of unsecured convertible debenture units with total principal amounts of \$810,000, \$1,330,000 and \$550,000 respectively. The debentures mature on March 8, 2022, May 9, 2022 and June 28, 2022, respectively, and bear interest at an annual rate of 8% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.32 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 1,563 share purchase warrants, each exercisable into one common share of the Company at \$0.40 per share three years from issuance.

If at any time after the first year anniversary of the closing date the closing price of the common shares of the Company is \$0.64 or greater for 20 consecutive trading days, the Company may, at its option, convert the debenture and any accrued and unpaid interest thereon into common shares by disseminating a press release, in which case the debentures shall be converted into common shares on the second business day after dissemination of such press release. The warrants will not be subject to acceleration.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Total finders' fee of \$161,400 in cash and 162 debenture warrants, with a nominal value, were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as the units in the placement. The Company incurred legal, regulatory and other share issuance costs of \$238,117.

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 \$2,022,861 (\$1,722,363 net of transaction costs), the warrants were \$333,569 (\$193,996 net of transaction costs and tax effect) and the residual equity components were \$333,569 (\$193,996 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 months ended June 30, 2021 was \$105,527 and \$216,696, of which \$79,447 (June 30, 2020 - \$90,056 and \$240,849, of which \$105,867) relates to accrued interest.

During the year ended December 31, 2020, \$232,000 of principal amount was converted into 725,000 common shares. Upon conversion, the present value of the liability of \$187,814 and the residual equity reserve value of \$18,791 was transferred to share capital.

During the six months ended June 30, 2021, \$588,000 of principal amount was converted into 1,837,500 common shares. Upon conversion, the present value of the liability of \$493,378 and the residual equity reserve value of \$44,627 was transferred to share capital.

[iii] On December 20, 2019, the Company issued unsecured convertible debenture units with total principal amount of \$1,030,000. The debenture matures on December 20, 2022, and bears interest at an annual rate of 8% due semi-annually. The debenture is convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.10 per common share. Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture

If at any time after May 21, 2020 the closing price of the common shares of the Company is \$0.40 or greater for 20 consecutive trading days, the Company may, at its option, convert the debenture and any accrued and unpaid interest thereon into common shares by disseminating a press release, in which case the debentures shall be converted into common shares on the second business day after dissemination of such press release.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Total finders' fee of \$30,000 in cash and 30 debenture warrants, with a nominal value, were incurred on the issuance. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in this placement. The Company incurred legal, regulatory and other share issuance costs of \$761.

The convertible debenture is a compound financial instrument with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debenture 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 component was \$774,544 (\$751,412 net of transaction costs), and the residual equity components were \$255,456 (\$178,853 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 months ended June 30, 2021 was \$Nil and \$Nil of which \$Nil (June 30, 2020 - \$32,618 and \$70,277, of which \$39,689) relates to accrued interest.

During the year ended December 31, 2020, \$1,030,000 of principal amount was converted into 10,300,000 common shares. Upon conversion, the present value of the liability of \$791,044 and the residual equity reserve value of \$178,854 was transferred to share capital.

During the six months ended June 30, 2021, 15 debenture warrants issued under this financing were exercised for proceeds of \$15,000. On initial recognition, the liability component was \$13,844, the warrants were \$Nil (\$Nil net of transaction costs and tax effect) and the residual equity components were \$1,156 (\$844 net of transaction costs and tax effect). The \$15,000 principal was immediately converted into 150,000 common shares (Note 13). Upon conversion, the liability and equity components were transferred to share capital.

[iv] On February 13 and February 24, 2020, the Company issued unsecured convertible debenture units with total principal amounts of \$1,764,000 and \$276,000 respectively. The debentures mature on February 13 and February 24, 2023, respectively, and bear interest at an annual rate of 2% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.10 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 5,000 share purchase warrants, each exercisable into one common share of the Company at \$0.20 per share three years from issuance.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Total finders' fee of \$102,000 in cash and 203 debenture warrants were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as this units in the placement. The Company incurred legal, regulatory and other share issuance costs of \$12,763.

The convertible debenture is a compound financial instrument with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debenture 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 component was \$1,268,870 (\$1,197,488 net of transaction costs), the warrants were \$385,564 (\$259,772 net of transaction costs and tax effect) and the residual equity components were \$385,564 (\$259,772 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 debenture for the three and six months ended June 30, 2021 was \$62,637 and \$132,824, of which \$17,910 (June 30, 2020 - \$63,858 and \$95,323, of which \$20,400) relates to accrued interest.

During the six months ended June 30, 2021, \$414,500 of principal amount was converted into 4,145,000 common shares. Upon conversion, the present value of the liability of \$294,382 and the residual equity reserve value of \$52,769 was transferred to share capital.

During the six months ended June 30, 2021, 91 debenture warrants issued under this financing were exercised for proceeds of \$91,000. On initial recognition, the liability component was \$62,957, the warrants were \$13,432 (\$9,806 net of transaction costs and tax effect) and the residual equity components were \$14,610 (\$10,664 net of transaction costs and tax effect). The \$91,000 principal was immediately converted into 910,000 common shares (Note 13). Upon conversion, the liability and equity components were transferred to share capital.

[v] On May 29, 2020 and June 12, 2020, the Company issued unsecured convertible debenture units with total principal amounts of \$2,000,000 and \$700,000 respectively. The debentures mature on May 29 and June 12, 2023, respectively, and bear interest at an annual rate of 2% due semi-annually. The debentures are convertible, in whole or in part, at the option of the holder at any time after the first anniversary of the date of issuance and prior to the maturity date into common shares of the Company at a conversion price of \$0.15 per common share.

Each debenture unit consisted of one \$1,000 principal amount unsecured convertible debenture and 3,333 share purchase warrants, each exercisable into one common share of the Company at \$0.25 per share three years from issuance.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Total finders' fee of \$134,475 in cash and 269 debenture warrants, with a nominal value, were incurred on the issuances. Each debenture warrant is exercisable into one debenture unit of the Company at \$1,000 per unit three years from issuance under the same terms as the units in the placement.

The convertible debenture is a compound financial instrument with the equity component being the residual value after accounting for the debt component. The Company valued the debt component of the debenture 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 component was \$1,679,650 (\$1,595,994 net of transaction costs), the warrants were \$510,175 (\$347,018 net of transaction costs and tax effect) and the residual equity components were \$510,175 (\$347,018 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 debenture for the three and six months ended June 30, 2021 was \$95,032 and \$185,424, of which \$27,000 (June 30, 2020 - \$25,825 and \$25,825, of which \$4,144) relates to accrued interest.

During the six months ended June 30, 2021, 100 debenture warrants issued under this financing were exercised for proceeds of \$100,000. On initial recognition, the liability component was \$70,898 the warrants were \$13,879 (\$10,132 net of transaction costs and tax effect) and the residual equity components were \$15,223 (\$11,113 net of transaction costs and tax effect). The \$100,000 principal was immediately converted into 666,667 common shares (Note 13). Upon conversion, the liability and equity components were transferred to share capital.

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11. CONVERTIBLE DEBENTURES (CONTINUED)

Convertible debenture transactions and the amount of convertible debentures outstanding are summarized below:

	Note 11 i \$	Note 11 ii \$	Note 11 iii \$	Note 11 iv \$	Note 11 v \$	Total \$
Cost:						
Balance, December 31, 2019	2,238,333	1,884,243	755,937	-	-	4,878,513
Principal	-	-	-	2,040,000	2,700,000	4,740,000
Equity component	-	-	-	(363,874)	(484,765)	(848,639)
Warrant component	-	-	-	(363,874)	(484,765)	(848,639)
Transaction costs	-	-	-	(114,763)	(134,475)	(249,238)
Accretion expense	230,304	489,102	79,674	231,527	196,158	1,226,765
Interest payment	(125,637)	(204,863)	(44,567)	(35,758)	(31,144)	(441,969)
Principal payment	(1,757,250)	-	-	-	-	(1,757,250)
Gain on settlement of debt	(585,750)	-	-	-	-	(585,750)
Conversion of debt	-	(187,814)	(791,044)	-	-	(978,858)
Balance, December 31, 2020	-	1,980,668	-	1,393,258	1,761,009	5,134,935
Principal	-	-	15,000	91,000	100,000	206,000
Equity component	-	-	(1,156)	(14,611)	(15,223)	(30,990)
Warrant component	-	-	-	(13,433)	(13,879)	(27,312)
Accretion expense	-	216,696	-	132,824	185,424	534,944
Interest payment	-	(79,378)	-	(17,908)	(27,000)	(124,286)
Conversion of debt	-	(493,378)	(13,844)	(357,338)	(70,898)	(935,458)
Balance, June 30, 2021	-	1,624,608	-	1,213,792	1,919,433	4,757,833

Of the total convertible debentures payable, the current amount is \$1,833,915 (December 31, 2020 - \$291,440).

Debenture warrant transactions and the number of debenture warrants outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2019	192	1,000
Issued	472	1,000
Balance, December 31, 2020	664	1,000
Exercised	(206)	1,000
Balance, June 30, 2021	458	1,000

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11. CONVERTIBLE DEBENTURES (CONTINUED)

	Exercise Price \$	Number of Warrants Outstanding
March 8, 2022	1,000	49
May 9, 2022	1,000	80
June 28, 2022	1,000	33
December 20, 2022	1,000	15
February 13, 2023	1,000	93
February 24, 2023	1,000	19
May 29, 2023	1,000	100
June 12, 2013*	1,000	69
Balance, June 30, 2021	1,000	458

* Subsequent to June 30, 2021, 29 warrants were exercised (Note 19)

Payments required over the next five years are as follows:

	March 8, 2022 \$	May 9, 2022 \$	June 28, 2022 \$	Feb. 13, 2023 \$	Feb.24, 2023 \$	May 29, 2023 \$	June 12, 2023 \$	Total \$
2021	28,400	24,400	22,000	14,715	1,540	20,000	5,844	116,899
2022	720,729	626,538	571,269	29,430	3,080	40,000	11,590	2,002,636
2023	-	-	-	1,475,714	154,828	2,016,556	585,198	4,232,296
2024	-	-	-	-	-	-	-	-
2025	-	-	-	-	-	-	-	-
	749,129	650,938	593,269	1,519,859	159,448	2,076,556	602,632	6,351,831

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12. LEASE LIABILITIES

Lease liabilities

The Company leases vehicles and office space in Canada. The lease liabilities were measured at the present value of the remaining lease payments as of January 1, 2019, discounted using an incremental borrowing rate at that date of 12%. The Company recorded a ROU asset of the same amount (Note 7).

	As at June 30, 2021 \$	As at December 31, 2020 \$
Balance, beginning of period	410,071	511,807
Additions	—	—
Interest	22,492	54,381
Derecognition	—	—
Lease payments	(75,939)	(156,117)
Balance, end of period	356,624	410,071
Less: non-current portion	(251,896)	(304,650)
	104,728	105,421
Undiscounted lease payments		
Not later than one year		140,361
Later than one year and not later than 5 years		285,822
June 30, 2021		426,183

The Company elected not to apply the new lease standard to short term leases with an initial term of 12 months or less but rather to recognise the lease expense on a straight line basis. For the three and six months ended June 30, 2021, \$12,000 and \$24,000 of variable lease payments (June 30, 2020 - \$12,000 and \$24,000) were included in rent expense on the statement of loss and comprehensive loss.

13. 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.

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13. SHARE CAPITAL (CONTINUED)

[b] Common shares

The Company had the following share capital transactions during the year ended December 31, 2020:

- [i] On January 13, 2020, the Company issued 1,093,750 common shares pursuant to a consulting agreement. The valuation was based on the fair value of the shares issued.
- [ii] On February 11, 2020, the Company issued 10,000,000 units at a price of \$0.065 for cash proceeds of \$156,000 and the settlement of debt of \$494,000 owed to officers, directors and consultants (the “**Financing**”). Debt settlement of officers and directors of the Company account for \$326,794 of the total settlements (Note 8).

Each unit consists of one common share and one common share purchase warrant. Each common share purchase warrant is exercisable into one common share at a price of \$0.10 for a period of two years from closing. In the event that the Company’s shares trade above \$0.25 for a period of 10 consecutive trading days at any time after June 12, 2020, the Company may accelerate the expiry date of the warrants by giving notice to the holders thereof and in such case, the warrants will expire on the 30th day after the date of giving such notice.

On March 5, 2020, related parties and consultants agreed to amend the exercise price of 7,027,596 out of 10,000,000 common share purchase warrants originally granted in the Financing to \$0.25 from \$0.10.

- [iii] On February 17, 2020 the Company issued 550,000 common shares in connection with the termination of the former Chief Operating Officer and an employee. The valuation was based on the fair value of the shares issued.
- [iv] On March 16, 2020 the Company issued 180,558 common shares pursuant to an employment agreement. The valuation was based on the fair value of the shares issued.
- [v] On May 7, 2020, the Company issued 45,455 common shares valued at \$6,818 to settle an outstanding debt of \$8,925. As a result, the Company recognized a gain on debt settlement of \$2,107.
- [vi] On June 24, 2020, the Company issued 544,627 common shares valued at \$103,479 pursuant to a consulting agreement.
- [vii] On December 19, 2020, the Company issued 10,001,000 common shares pursuant to a non-brokered private placement at a price of \$0.30 per common share for gross proceeds of \$3,000,300. Total finders' fee of \$150,015 in cash and 1,000,100 compensation warrants were incurred on the issuances. Each compensation warrant is exercisable into one common share of the Company at \$0.45 per common share for a period of two years from issuance. The Company incurred legal, regulatory and other share issuance costs of \$426.

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13. SHARE CAPITAL (CONTINUED)

[b] Common shares (continued)

- [viii] During the year ended December 31, 2020, the Company issued 11,025,000 common shares pursuant to the conversion of \$1,262,000 of convertible debt. The fair value of the convertible debt liability at the time of conversion is \$978,857 and the convertible debt equity portion is \$197,645 for a total value of \$1,176,502 transferred to share capital (Note 11[ii] and [iii]).
- [iv] During the year ended December 31, 2020, the Company issued 295,000 common shares pursuant to the exercise of stock options for aggregate gross proceeds of \$29,750. The fair value of the options of \$23,983 was transferred from reserves to share capital.
- [x] During the year ended December 31, 2020, the Company issued 5,793,832 common shares pursuant to the exercise of warrants for aggregate gross proceeds of \$865,097. The fair value of the warrants of \$78,421 was transferred from reserves to share capital.

The Company had the following share capital transactions during the six months ended June 30, 2021:

- [i] On January 26, 2021, the Company issued 1,500,000 common shares at a price of \$0.30 for gross proceeds of \$450,000 pursuant to a non-brokered private placement. Total finders' fees of \$22,500 in cash and 150,000 compensation warrants were incurred in the issuance. Each compensation warrant is exercisable into one common share of the Company at \$0.45 per common share for a period of two years following the date of the issuance. The Company incurred legal, regulatory and other share issuance costs of \$1,058.
- [ii] On June 8, 2021, the Company issued 155,113 common shares valued at \$68,250 pursuant to a consulting agreement.
- [ii] During the six months ended June 30, 2021, the Company issued 518,125 common shares pursuant to the exercise of stock options for aggregate gross proceeds of \$50,703. The fair value of the options of \$40,986 was transferred from reserves to share capital.
- [iii] During the six months ended June 30, 2021, the Company issued 4,344,728 common shares pursuant to the exercise of warrants for aggregate gross proceeds of \$1,331,146. The fair value of the warrants of \$714,273 was transferred from reserves to share capital.
- [iv] During the six months ended June 30, 2021, the Company issued 5,982,500 common shares pursuant to the conversion of \$1,002,500 of convertible debt. The fair value of the convertible debt liability at the time of conversion is \$787,760 and the convertible debt equity portion is \$97,396 for a total value of \$885,156 transferred to share capital (Note 11[ii] and [iv]).
- [v] During the six months ended June 30, 2021, 206 debenture warrants were exercised for total proceeds of \$206,000. Upon issuance, the debentures were immediately converted into 1,726,667 common shares (Note 11[iii], [iv] and [v]).

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13. 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 \$
Balance, December 31, 2019	20,437,472	0.50
Issued	30,199,194	0.22
Exercised	(5,793,832)	(0.15)
Expired	(10,145,145)	(0.60)
Balance, December 31, 2020	34,697,689	0.29
Issued	938,300	0.26
Exercised	(4,344,728)	(0.31)
Balance, June 30, 2021	31,291,261	0.29

Date of Expiry	Exercise Price \$	Number of Warrants Outstanding
November 22, 2021	0.35	1,057,143
February 11, 2022	0.25	7,027,596
March 8, 2022	0.40	1,266,030
May 3, 2022	0.40	2,078,790
May 30, 2022	0.25	103,572
June 28, 2022	0.40	859,650
June 29, 2022	0.25	659,286
December 18, 2022	0.45	1,000,100
December 23, 2022	1.00	700,000
January 26, 2023	0.45	150,000
February 13, 2023	0.20	6,070,000
February 24, 2023	0.20	1,420,000
May 29, 2023	0.25	6,565,997
June 12, 2023	0.25	2,333,097
Balance, June 30, 2021		31,291,261

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13. SHARE CAPITAL (CONTINUED)

[d] Stock options

During the three and six months ended June 30, 2021, the Company recorded share-based payments of \$99,864 and \$267,427 (June 30, 2020 - \$95,687 and \$237,449). The fair values of share options granted during the six months ended June 30, 2021 and 2020 are estimated using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2021	2020
Risk-free interest rate	Nil	1.42%
Estimated annualized volatility	Nil	114.79%
Expected life	Nil	5.0 years
Expected dividend yield	Nil	0%
Exercise price	Nil	\$0.09
Fair value per option	Nil	\$0.0736
Share price	Nil	\$0.09

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

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2019	608,000	0.28
Issued	6,325,000	0.16
Exercised	(295,000)	(0.10)
Expired	(100,000)	(0.26)
Balance, December 31, 2020	6,538,000	0.17
Issued	—	—
Exercised	(518,125)	(0.10)
Balance, June 30, 2021	6,019,875	0.18

Date of Expiry	Exercise Price \$	Number of Options Outstanding	Number of Options Exercisable
July 12, 2021	1.05	100,000	100,000
October 29, 2024	0.09	333,000	333,000
January 19, 2025	0.075	2,515,000	2,515,000
February 26, 2025	0.125	950,000	950,000
March 16, 2025	0.105	200,000	200,000
July 15, 2025	0.25	700,000	233,333
December 20, 2025	0.345	1,221,875	396,875
Balance, June 30, 2021	0.18	6,019,875	4,728,208

As of June 30, 2021, the weighted average remaining life for outstanding options was 4.00 years (December 31, 2020 – 4.24 years).

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13. SHARE CAPITAL (CONTINUED)

[e] Restricted Share Units (“RSU”)

On August 7, 2020, the Company adopted an RSU plan for directors, officers, employees and consultants of the Company. Under the terms of the plan, each vested RSU awarded entitles the RSU holder to receive, subject to adjustment as provided for in the RSU Plan, either one common share in the Company or, at the Company’s option, an equivalent cash payment. The maximum number of RSUs granted should not exceed 10% of the issued shares of the Company aggregated with all other security-based compensation arrangements. The Company did not grant any RSU’s for the period ended June 30, 2021.

14. COMMITMENTS AND CONTINGENCIES

[a] Parent Company Guarantee to Scottish Water Horizon Ltd. (“SWH”) for the Finance Facility to Bandwidth Energy Ltd. (“Bandwidth”)

During the year ended December 31, 2018, the Company entered into a joint arrangement and held a 50% interest in Bandwidth for £10,000 (\$17,357) with the other 50% held by SWH. As the Company held joint control of the arrangement but the legal form of the arrangement and the contractual terms of the arrangement did not give or specify that the parties had rights to the assets, and obligations for the liabilities and therefore, the investment was treated as a joint venture and accounted for as an equity investment.

The Company provided a guarantee to SWH for the finance facility provided to Bandwidth for the execution of certain works, namely the design, installation, testing and commissioning of a new sewage heat recovery system (“**Aqualibrium**”) totalling £604,726. The guarantee is limited to 50% of the finance facility provided, excluding any interest accrued per the original loan facility.

On September 17, 2019, the Company agreed to sell its 50% interest in Bandwidth for £10,000 cash to SWH, the other 50% shareholder, and terminated the agreement (“**Termination Agreement**”) for Aqualibrium with Bandwidth for £15,000.

[b] Parent Company Guarantee for Bandwidth for Installation and Operations and Maintenance of Aqualibrium

The Company provided certain guarantees over the installation and operations and maintenance of Aqualibrium (the “**Performance Guarantees**”). During the year ended December 31, 2019, on sale of the Company’s interest in Bandwidth to SWH, the parties entered into a Termination Agreement (Note 14[a]).

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15. CAPITAL MANAGEMENT

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' deficiency.

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 period. The Company is not subject to externally imposed capital requirements.

16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value

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 cash, receivables, accounts payable and accrued liabilities and loans payable approximate their carrying values due to the short-term to maturity. The fair value of long-term liabilities are initially recorded at fair value and subsequently carried at amortized cost using rates comparable to market interest rates.

[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, 2021 the Company is nominally exposed to credit risk arising from receivables.

[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. The Company is exposed to liquidity risk.

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16. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

[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, 2021 the Company is not exposed to any significant interest rate risk.

17. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

The following is the non-cash operating, investing and financing activities:

	Six months ended June 30, 2021 \$	Six months ended June 30, 2020 \$
Conversion of convertible debt into common shares	1,055,475	605,497
Fair value of stock options and warrants exercised	755,259	3,629
Finders' warrants issued as share issuance costs	37,768	—
Reversal of share-based payments	—	5,298
Issuance of convertible debt – equity component	30,990	848,639
Issuance of convertible debt – warrant component	27,312	848,639
Inventory transferred to property and equipment	—	91,923
Private placement units issued for debt	—	494,000
Prepaid expenses paid by common shares	54,167	190,979
Equipment in accounts payable and accrued liabilities	16,340	—

18. SEGMENTED INFORMATION

The Company has a single operating segment, the sales and marketing of sewage heat recovery systems. As at June 30, 2021 and December 31, 2020, all of the Company's operations, assets and employees are in Canada.

19. SUBSEQUENT EVENTS

Subsequent to June 30, 2021:

- [a] Holders of convertible debentures converted \$275,500 of principal into 2,003,331 common shares.
- [b] 196,647 common share purchase warrants were exercised for gross proceeds of \$49,162.
- [c] 29 debenture units were exercised for total proceeds of \$29,000. Upon exercise, the debentures were immediately converted into 193,333 common shares. Pursuant to the issuance of the debenture units, 96,657 common share purchase warrants were issued.