LOTUS
VENTURES INC.

FINANCIAL STATEMENTS

For the years ended August 31, 2018 and August 31, 2017

(Expressed in Canadian Dollars)

DeVISSER GRAY LLP
CHARTERED PROFESSIONAL ACCOUNTANTS

401-905 West Pender St
Vancouver BC V6C 1L6
t 604.687.5447
f 604.687.6737

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Lotus Ventures Inc.,

We have audited the accompanying financial statements of Lotus Ventures Inc., which comprise the statements of financial position as at August 31, 2018 and 2017, and the statements of comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Lotus Ventures Inc. as at August 31, 2018 and 2017 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

De Visser Gray LLP

CHARTERED PROFESSIONAL ACCOUNTANTS
Vancouver, British Columbia
December 21, 2018

LOTUS VENTURES INC.
STATEMENTS OF FINANCIAL POSITION
(Expressed in Canadian Dollars)

	As at	
	August 31, 2018	**August 31, 2017**
ASSETS		
Current		
Cash	$ 1,741,853	$ 2,149,325
GST receivable	279,272	7,916
Prepaid expenses and deposits	124,165	68,457
	2,145,290	2,225,698
Non-current		
Restricted cash (Note 5)	215,074	-
Option agreements (Note 4)	-	230,500
Property, plant and equipment (Note 5)	6,929,630	148,720
	7,144,704	379,220
Total assets	$ 9,289,994	$ 2,604,918
LIABILITIES		
Current		
Accounts payable and accrued liabilities	$ 1,666,847	$ 143,265
Due to related parties (Note 8)	-	14,713
Total liabilities	1,666,847	157,978
SHAREHOLDERS' EQUITY		
Share capital (Note 7)	$ 10,702,975	$ 4,200,973
Subscription receivable	(10,000)	-
Subscription receipts	-	6,000
Reserves	1,694,390	503,285
Deficit	(4,764,218)	(2,263,318)
Total shareholders' equity	7,623,147	2,446,940
Total liabilities and shareholders' equity	$ 9,289,994	$ 2,604,918

Note 6 Commitments
Note 12 Subsequent Events

The accompanying notes form an integral part of these financial statements.

Approved and authorized by the Board on December 21, 2018.

"*Dale McClanaghan*"	Director	"*Steve Mathiesen*"	Director
Dale McClanaghan		Steve Mathiesen	

LOTUS VENTURES INC.
STATEMENTS OF COMPREHENSIVE LOSS
(Expressed in Canadian Dollars)

	Year ended August 31, 2018	Year ended August 31, 2017
General and administrative expenses		
Advertising and promotion	$ 83,160	$ 31,750
Amortization	10,982	9,404
Bank fees	1,398	860
Consulting (Note 8)	855,507	356,220
Design expense	-	160,772
Foreign exchange loss (gain)	-	454
Insurance	4,410	2,900
Listing, filing and transfer fees	25,345	35,419
Office and miscellaneous	7,058	26,471
Professional fees	208,156	21,667
Rent	36,000	48,000
Share-based compensation (Note 7)	1,226,985	-
Travel	41,899	30,286
Net loss and comprehensive loss	$ (2,500,900)	$ (724,203)
Basic and diluted loss per share	$ (0.05)	$ (0.02)
Weighted average number of shares outstanding	52,106,850	35,452,901

The accompanying notes form an integral part of these financial statements.

LOTUS VENTURES INC.
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Expressed in Canadian Dollars)

	Common shares						
	Number of Shares	**Amount**	**Subscription Receivable**	**Subscription receipts**	**Reserves**	**Deficit**	**Total**
Balance, August 31, 2017	**43,235,500**	**$ 4,200,973**	**$ -**	**$ 6,000**	**$ 503,285**	**$ (2,263,318)**	**$ 2,446,940**
Shares issued for cash – private placement	12,735,272	6,282,347	(10,000)	(6,000)	-	-	6,266,347
Shares issued – finders fees	3,325	998	-	-	-	-	998
Share issue costs	-	(132,165)	-	-	-	-	(132,165)
Warrants exercised	1,299,834	277,442	-	-	-	-	277,442
Options exercised	150,000	73,380	-	-	(35,880)	-	37,500
Share-based compensation	-	-	-	-	1,226,985	-	1,226,985
Net loss	-	-	-	-	-	(2,500,900)	(2,500,900)
Balance, August 31, 2018	**57,423,931**	**$ 10,702,975**	**$ (10,000)**	**$ -**	**$ 1,694,390**	**$ (4,764,218)**	**$ 7,623,147**
Balance, August 31, 2016	**32,102,750**	**$ 1,371,750**	**$ -**	**$ -**	**$ 503,285**	**$ (1,539,115)**	**$ 335,920**
Shares issued for cash	11,132,750	2,981,200	-	-	-	-	2,981,200
Share issue costs	-	(151,977)	-	-	-	-	(151,977)
Shares subscribed	-	-	-	6,000	-	-	6,000
Net loss	-	-	-	-	-	(724,203)	(724,203)
Balance, August 31, 2017	**43,235,500**	**$ 4,200,973**	**$ -**	**$ 6,000**	**$ 503,285**	**$ (2,263,318)**	**$ 2,446,940**

The accompanying notes form an integral part of these financial statements.

LOTUS VENTURES INC.
STATEMENTS OF CASH FLOWS
(Expressed in Canadian Dollars)

	Year ended August 31, 2018	Year ended August 31, 2017
Operating activities		
Net loss for the year	$ (2,500,900)	$ (724,203)
Items not affected by cash:		
Amortization	10,982	9,404
Share-based compensation	1,226,985	-
Changes in non-cash working capital items:		
GST receivable	(271,356)	6,941
Prepaid expenses	(55,708)	(18,457)
Accounts payable and accrued liabilities	(63,063)	36,486
Due to related parties	(14,713)	(6,964)
	(1,667,773)	(696,793)
Financing activities		
Cash received for shares issued	6,266,347	2,981,200
Shares subscribed	-	6,000
Share issue costs	(131,167)	(151,977)
Options exercised	37,500	-
Warrants exercised	277,442	-
	6,450,122	2,835,223
Investing activities		
Expenditures on property, plant and equipment	(5,189,821)	(131,700)
Net change in cash	(407,472)	2,006,730
Cash, beginning of the year	2,149,325	142,595
Cash, end of the year	**$ 1,741,853**	**$ 2,149,325**

Note 11 Supplemental Non-cash Disclosures

The accompanying notes form an integral part of these financial statements.

Note 1 **Nature and Continuance of Operations**

The public company predecessor to Lotus Ventures Inc. (the 'Company') was incorporated under the Business Corporations Act (B.C.) on May 12, 2010 as Strachan Resources Ltd. ('Strachan'). Strachan's common shares were previously listed for trading on the TSX Venture Exchange ('Venture'), and it was classified as a Capital Pool Company pursuant to Venture Policy 2.4 until the completion of the 2014 amalgamation agreement (the 'Transaction") described below. Effective December 8, 2014, the Company's common shares were listed for trading on the Canadian Securities Exchange ('CSE').

Under the terms of an amalgamation agreement with a BC private company also known as Lotus Ventures Inc. (Private Lotus) dated July 30, 2014, as amended September 1, 2014, the shareholders of each of that company and Strachan exchanged their respective shareholdings on a one-for-one basis for the share capital of a new corporation ('Amalco'). On November 27, 2014 the Transaction was completed and, legally, a new company, Amalco or the Company, was created.

Private Lotus' Option Exercise Agreement, described in Note 4, formed the basis for the Transaction with Strachan, as its terms contemplated and required the completion of a transaction whereby the shareholders of Private Lotus were to effectively obtain the right to trade their equity publically, or to otherwise obtain publically-traded securities by an exchange of equity interests.

In connection with the Transaction and to obtain regulatory consent to the delisting of its securities from trading on the Venture, on December 1, 2014, Amalco obtained a receipt for a non-offering prospectus in British Columbia.

These financial statements have been prepared on the going concern basis, which assumes the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The Company has incurred losses since inception, has no source of operating cash flow, and there can be no assurance that adequate financing will be available to conduct further development of its projects.

Management plans to continue to pursue equity or debt financing to support operations, and believes this plan will be sufficient to meet the Company's known liabilities and commitments as they become payable over the twelve months subsequent to the balance sheet date.

Note 2 **Basis of Preparation**

Statement of Compliance

These financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC").

Basis of Measurement

These financial statements have been prepared on a historical costs basis except for financial instruments classified as financial instruments at fair value through profit or loss, which are stated at their fair value. In addition, these financial statements have been prepared using the accrual basis of accounting.

Note 2 Basis of Preparation – (cont'd)

Basis of Measurement – (cont'd)

These financial statements are presented in Canadian dollars, which is also the Company's functional currency.

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 the reported expenses during the period. Actual results could differ from these estimates.

Note 3 Significant Accounting Policies

Financial instruments

Financial assets

The Company classifies its financial assets into one of the following categories, depending on the purpose for which the asset was acquired, as follows:

Fair value through profit or loss - This category comprises derivatives, or assets acquired or incurred principally for the purpose of selling or repurchasing such financial assets in the near term. They are carried in the statements of financial position at fair value with changes in fair value recognized in the statements of comprehensive loss or income. The Company has classified its cash as fair value through profit or loss.

Loans and receivables - These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are carried at cost less any provision for impairment. Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default.

Held-to-maturity investments - These assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Company's management has the positive intention and ability to hold to maturity. These assets are measured at amortized cost using the effective interest method. If there is objective evidence that the investment is impaired, determined by reference to external credit ratings and other relevant indicators, the financial asset is measured at the present value of estimated future cash flows. Any changes to the carrying amount of the investment, including impairment losses, are recognized in the statements of comprehensive loss or income. The Company has no held-to-maturity investments.

Available-for-sale - Non-derivative financial assets not included in the above categories are classified as available-for-sale. They are carried at fair value with changes in fair value recognized directly in equity. Where a decline in the fair value of an available-for-sale financial asset constitutes objective evidence of impairment, the amount of the loss is removed from equity and recognized in the statements of comprehensive loss or income. The Company has no available-for-sale assets.

Note 3 Significant Accounting Policies – (cont'd)

Financial instruments – (cont'd)

Financial assets – (cont'd)

All financial assets except for those at fair value through profit or loss are subject to review for impairment at least at each reporting date. Financial assets are impaired when there is any objective evidence that a financial asset or a group of financial assets is impaired. Different criteria to determine impairment are applied for each category of financial assets, which are described above.

Financial liabilities

The Company classifies its financial liabilities into one of two categories, depending on the purpose for which the asset was acquired, as follows:

Fair value through profit or loss **-** This category comprises derivatives, or liabilities acquired or incurred principally for the purpose of selling or repurchasing such financial liabilities in the near term. They are carried in the statements of financial position at fair value with changes in fair value recognized in the statements of comprehensive loss or income.

Other financial liabilities: This category includes accounts payable and accrued liabilities which are recognized at amortized cost.

Cash and cash equivalents

Cash in the statement of financial position comprises cash at banks and on hand. There were no cash equivalents at August 31, 2018 and 2017.

Intangible assets

Intangible assets are recognized when they become identifiable, which is to say when they arise from contractual or other rights, or when they are separable, or capable of being sold, transferred, licensed, rented or exchanged. They are initially recorded at cost, subject to the reliability of measurement, and are carried as assets to the extent that it is probable that the future economic benefits applicable to such costs will flow to the Company.

Property, plant and equipment

Property, plant and equipment are carried at cost, less accumulated amortization and accumulated impairment losses. Cost comprises the fair value of consideration given to acquire an asset and includes the direct expenditures associated with bringing the asset to the location and condition necessary for putting it into use along with the future cost of dismantling and removing the asset.
When parts of an item of fixed assets have different useful lives, they are accounted for as separate items (major components) of fixed assets.

Computer software is amortized on a 55% declining balance basis.

Building and equipment will begin amortization when put into use.

Note 3 Significant Accounting Policies – (cont'd)

Income taxes

Income tax is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity. Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at period end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax is recorded using the statement of financial position liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position date.

A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. To the extent that the Company does not consider it is probable that a future tax asset will be recovered, it provides a valuation allowance against that excess.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

Share capital

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

The Company has adopted a residual value method with respect to the measurement of shares and warrants issued as private placement units. The residual value method first allocates value to the more easily measurable component based on fair value and then the residual value, if any, to the less easily measurable component.

The fair value of the common shares issued in the private placements is considered to be the more easily measurable component and the common share are valued at their fair value, as determined by the closing quoted bid price on the announcement date. The balance, if any, is allocated to the attached warrants. Any fair value attributed to the warrants is recorded as reserves.

Share-based compensation

Employees (including directors and senior executives) of the Company may receive a portion of their remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

Note 3 Significant Accounting Policies – (cont'd)

Share-based compensation – (cont'd)

In situations where equity instruments are issued for goods or services, the share-based compensation is measured at the fair value of the goods and services received. Where the consideration cannot be specifically identified, they are measured at the fair value of the share-based compensation.

The costs of equity-settled transactions with employees are measured by reference to the fair value at the date on which they are granted.

The costs of equity-settled transactions are recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ("the vesting date"). The cumulative expense is recognized for equity-settled transactions at each reporting date until the vesting date reflects the Company's best estimate of the number of equity instruments that will ultimately vest.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based compensation arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Income (loss) per share

The Company presents basic and diluted income (loss) per share data for its common shares, calculated by dividing the loss attributed to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted income (loss) per share does not adjust the income (loss) attributed to common shareholders or the weighted average number of common shares outstanding when the effect is anti-dilutive.

Related party transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

Note 3 Significant Accounting Policies – (cont'd)

Adoption of new and revised accounting standards and interpretations

The Company has not yet adopted certain new standards, amendments and interpretations to existing standards, which have been published but are only effective for accounting periods beginning on or after September 1, 2017 or later periods.

(i) Effective for annual periods beginning on or after January 1, 2018

- New standard IFRS 9, *Financial Instruments, Classification and Measurement,* addresses classification and measurement of financial assets and will replace IAS 39, *"Financial Instruments: Recognition and Measurement."* IFRS 9 has two measurement categories: amortized cost and fair value. All equity instruments are measured at fair value. A debt instrument is at amortized cost only if the entity is holding it to collect contractual cash flows and the cash flows represent principal and interest. Otherwise, it is at fair value through profit and loss.

The Company plans to adopt these standards as soon as they become effective. Adoption of this standard is expected to have minimal impact on the Company's financial statements.

Note 4 Option Agreements

Busby and Correia Option Agreements

On April 30, 2014, private Lotus entered into an Assignment Agreement with Carl Busby ("Busby"). In consideration of the assignment of an underlying option agreement described below, the Company paid to Busby $62,500 by the issuance of 3,500,000 common shares at a price of $0.005 per share and 2,250,000 common shares at a price of $0.02 per share.

Upon completion of the Transaction, the Company obtained the right under an underlying Option Exercise Agreement to acquire a production facility and operating assets, to be operated under the Marijuana for Medical Purposes Regulation ('MMPR') upon obtaining a new production license. These assets currently produce medical marijuana pursuant to four licenses issued under the Medical Marijuana Access Regulations ('MMAR').

Private Lotus then entered into an Option Exercise Agreement dated September 1, 2014 with Carl Correia ("Correia") and 0998918 B.C. Ltd. of Vernon, British Columbia, which replaced the previous agreement in its entirety. Under this agreement, Private Lotus agreed to issue 1,700,000 common shares to each of Correia and 0998918 B.C. Ltd (issued). and Correia agreed to (a) serve as the Chief Operating Officer of the Company and the Person in Charge in the MMPR Application (b) prepare the MMPR application on behalf of the Company; (c) assist the Company to obtain approval of the application from Health Canada (d) assist the Company to obtain the MMPR License; and (e) assist the Company to negotiate a lease on the property on which the facility is located. The Company will also acquire Correia's know-how and experience regarding (a) the requirements with respect to the MMPR License process and requirements; (b) facility design for application for the MMPR License; (c) quality control pursuant to the MMPR License;

Note 4 Option Agreements – (cont'd)

Busby and Correia Option Agreements – (cont'd)

(d) security requirements pursuant to the MMPR License; (e) recruitment of appropriate Alternate Person in Charge and Person in Charge of Quality Control; (f) knowledge regarding the growing of medical marijuana; and (g) all information, documents and records prepared with respect to the MMPR License application and all lease rights to the facility.

Option to Purchase Leased Armstrong Property

On November 7, 2015, the Company entered into an Option to Purchase Agreement ("Option to Purchase" or the "Option") as part of a three-year lease agreement for a 23 acre property near Armstrong, BC ("Lease Agreement" or the "Lease"). Under the Option to Purchase, the Company could purchase the leased property, on which the Company intends to build the facility proposed in its MMPR application to Health Canada. To exercise the Option to Purchase, the Company would be required to (a) consistently perform all obligations agreed to under the Lease Agreement; (b) provide written notice to the landlord at any time up to the exercise date, which is the later of 90 days prior to the expiry date of the initial lease term or 30 days prior to the expiry of the renewal term if the Lease is renewed; and (c) pay the landlord $1,100,000 if the Company does not renew the initial three-year Lease, or $1,200,000 if the Company renews the Lease for a renewal term.

As consideration for being granted the Option to Purchase, the Company must pay the landlord the following fees ("Option Fees") on the following dates: (i) $50,000 upon signing the lease (paid); (ii) $50,000 on the earlier of (1) the commencement of any pre-approved work on or to the premise in accordance with the Lease Agreement and (2) March 15, 2016 (paid) and (iii) $100,000 concurrently with the renewal notice if the Company renews the lease pursuant to the Lease Agreement. Upon exercise of the Option, the Option Fees (not including rent paid towards the lease) will be applied to the purchase price. The Option cannot be revoked within the time frame provided unless the Lease is terminated prior to the exercise date or the Company fails to comply with the above noted terms. If the Option is not exercised within the time frame and manner thus laid out, the Company loses entitlement to the Option to Purchase and forfeits all Option Fees paid.

On June 4, 2018, the Company exercised its Option to Purchase and paid the balance of $1,000,000 plus transaction costs of $21,057. Included within the acquisition costs was an aggregate of $225,000 allocated to certain pre-existing buildings based on estimates of their current fair values.

Upon exercise of this option, the historical costs applicable to this and the Busby and Correia options above have also been reclassified within property, plant and equipment (Note 5).

(Expressed in Canadian Dollars)

Note 5 Property, plant and equipment

	Land $	Buildings $	Software $	Equipment $	Construction in Progress $	Total $
Cost						
As at August 31, 2017	-	-	23,585	11,000	130,025	164,610
Additions during the year	1,026,557	225,000	-	17,950	5,522,385	6,791,892
As at August 31, 2018	1,026,557	225,000	23,585	28,950	5,652,410	6,956,502
Accumulated Amortization						
As at August 31, 2017	-	-	15,890	-	-	15,890
Additions during the year	-	6,750	4,232	-	-	10,982
As at August 31, 2018	-	6,750	20,122	-	-	26,872
Net Book Value						
As at August 31, 2017	-	-	7,695	11,000	130,025	148,720
As at August 31, 2018	**1,026,557**	**218,250**	**3,463**	**28,950**	**5,652,410**	**6,929,630**

To August 31, 2017 the Company had capitalized certain pre-construction related costs incurred in anticipation of its current project advancing, including $35,000 paid to the project manager. However, consistent with previous periods the annual lease payments continue to be expensed on the basis that they are not directly related to the actual construction process.

Effective September 1, 2017 the Company entered into a construction management services contract whereby the Company committed to pay an aggregate additional fees of $876,875, exclusive of the $35,000 noted above, in equal installments over a 12 month period (paid). Additional reimbursable costs incurred by the project manager are subject to a 10% surcharge. The Company is entitled to, and has, withheld 10% of all costs incurred, subject to certain completion requirements, and at August 31, 2018 owes $185,068 in connection with these holdbacks (included within accounts payable and accrued liabilities). The amount is also represented by an offsetting balance of restricted cash.

Note 6 Commitments

Cannabis Wheaton Streaming Agreement

On January 5, 2017, the Company entered into a binding interim agreement with Cannabis Wheaton Income Corp. now Auxly Cannabis Group Inc. (“XLY”), pursuant to which XLY agreed to subscribe for $5 million in common shares of the Company (the “Initial Subscription”). The Initial Subscription is conditional upon, (i) completion of XLY's satisfactory due diligence review of the Company; (ii) the parties mutually agreeing to the Company’s construction budget, design and timeline to build the facility; and (iii) the Company receiving confirmation from Health Canada requesting a pre-licensing inspection of the facility.

Upon completion of the Initial Subscription, XLY shall receive the greater of (i) access to and control of 10,000 square feet of the initial production area, or (ii) 50% of the actual cultivation yield generated, together with certain ancillary rights, including access to and use of the Company’s related infrastructure at the facility, for a period of 10 years.

Note 6 Commitments – (cont'd)

Additionally, XLY has a right of first refusal to finance any proposed expansion of the facility, subject to certain pre-determined parameters, in the amount up to $7 million by way of a subscription for additional common shares of the Company (the "Expansion Subscription").

Should XLY exercise its right of first refusal and complete the Expansion Subscription, XLY shall receive 50% of the actual cultivation yield produced in the expansion area of the facility for a period of 10 years.

On February 9, 2018, XLY advanced $1,000,000 by way of a private placement to fund a portion of the Initial subscription. See Notes 7(a) and 12.

4th Gen Duwyn Farms Inc. Licensing Agreement

On December 14, 2017, the Company announced that it has entered into a Licensing Agreement (the "Agreement") with 4th Gen Duwyn Farms Inc. ("DFI") to license the Company's intellectual property ("IP"), including its proprietary facility design, to a newly formed company owned by the Company and DFI ("DMFI"). Under the agreement, Lotus will provide DFI access to its IP including building design, standard operating procedures, training and license application support in return for DFI selling 100% of the production from the facility to Lotus for a period of 15 years at a discount to wholesale pricing.

Note 7 Share Capital

a) Authorized

The authorized share capital of the Company consists of an unlimited number of common shares without any special rights or restrictions.

During the year ended August 31, 2018, the Company completed the following share issuances:

- On September 14, 2017, the Company completed a non-brokered private placement of 880,991 units at $0.30 per unit for gross proceeds of $264,297. Each unit consists of one common share, and one-half of one transferable share purchase warrant. Each whole warrant is exercisable for one common share at $0.35 per share, and expires three years from the closing date.

- In relation to this private placement, the Company paid cash finder's fees of $16,415 and issued 3,325 finders units consisting of one common share, and one half share purchase warrant, exercisable at $0.35 per share and expiring three years from the grant date.

- On January 10, 2018, 150,000 options expiring January 4, 2021 were exercised at $0.25 per share for gross proceeds of $37,500. See Note 4(b).

- On January 22, 2018, the Company completed a non-brokered private placement of 10,036,100 units at $0.50 per unit for gross proceeds of $5,018,050. Each unit consists of one common share, and one five-year share purchase warrant exercisable at $0.70 per share. Finder's fees of $115,750 were paid in relation to this financing.

Note 7 Share Capital – (cont'd)

a) Authorized – (cont'd)

- On February 9, 2018, the Company completed a private placement with Auxly Cannabis Group Inc. ("XLY") who subscribed to 1,818,181 units in the Company at a price per unit of $0.55. Each unit consists of one common share, and one half share purchase warrant exercisable at $1.00 for a period of 36 months from the date of issue.

- During the year, 1,299,834 shares were issued pursuant to the exercise of the following warrants (see Note 7(c)):
  - 1,000,000 warrants granted December 16, 2015 and exercisable at $0.20;
  - 100,000 warrants granted January 25, 2016 and exercisable at $0.20;
  - 125,000 warrants granted December 6, 2016 and exercisable at $0.25;
  - 24,834 warrants granted August 15, 2017 and exercisable at $0.35; and
  - 50,000 warrants granted September 14, 2017 and exercisable at $0.35.

During the year ended August 31, 2017, the Company completed the following share issuances:

- On October 14, 2016, the Company completed a non-brokered private placement of 2,023,750 units at $0.20 per unit for gross proceeds of $404,750. Each unit consists of one common share and one share purchase warrant, exercisable at $0.25 per share, and expiring five years from the grant date.

- On November 17, 2016, the Company completed a non-brokered private placement of 962,500 units at $0.20 per unit for gross proceeds of $192,500. Each unit consists of one common share and one share purchase warrant, exercisable at $0.25 per share, and expiring five years from the grant date.

b) Share purchase options

The Company operates an employee stock option plan. Share-based payments to directors, officers, employees and consultants are measured at the fair value of the instruments issued and amortized over the vesting periods. Share-based payments to non-employees are measured at the fair value of goods or services received or the fair value of the equity instruments issued, if it is determined the fair value of the goods or services cannot be reliably measured, and are recorded at the date the goods or services are received. The corresponding amount is recorded to the stock option reserve. The fair value of options is determined using a Black–Scholes pricing model which incorporates all market vesting conditions. The number of shares and options expected to vest is reviewed and adjusted at the end of each reporting period such that the amount recognized for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest.

(Expressed in Canadian Dollars)

Note 7 Share Capital – (cont'd)

b) Share purchase options – (cont'd)

During the year ended August 31, 2018, the Company granted the following options:

- On November 9, 2017, the Company granted 1,465,000 share purchase options exercisable for ten years at a price of $0.35 per share.
- On March 20, 2018, the Company granted 1,490,000 share purchase options exercisable for ten years at a price of $0.50 per share.

The fair value of these share purchase options was estimated using the Black-Scholes Option Pricing Model based on the following weighted average assumptions:

Risk-free interest rate (%)	1.91 - 2.26
Expected life (years)	10
Expected volatility (%)	133.1761 – 144.68
Expected dividend yield (%)	-

On January 10, 2018, 150,000 options expiring January 4, 2021 were exercised at $0.25 per share. The fair value of the options was $35,880 and was reallocated from reserves to share capital.

During the year ended August 31, 2017, no options were granted or exercised.

During the year ended August 31, 2018, share-based compensation expense was $1,226,985 (2017 - $nil).

b) Share purchase options – (cont'd)

Details of granted, exercised, and outstanding stock options are as follows:

	Year Ended August 31, 2018		Year Ended August 31, 2017	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
		$		$
Balance at the beginning of the year	2,785,000	0.22	2,785,000	0.22
Granted	2,955,000	0.43	-	-
Exercised	(150,000)	0.25	-	-
Outstanding, end of the year	5,590,000	0.33	2,785,000	0.22

As at August 31, 2018, the weighted-average contractual remaining life of the options was 5.83 years (August 31, 2017 – 2.88 years).

(Expressed in Canadian Dollars)

Note 7 Share Capital – (cont'd)

c) Share purchase warrants

Details of outstanding share purchase warrants are as follows:

	Year Ended August 31, 2018		Year Ended August 31, 2017	
	Number of Warrants	Weighted Average Exercise Price	Number of Warrants	Weighted Average Exercise Price
		$		$
Balance at the beginning of the year	10,418,250	0.28	3,058,750	0.23
Issued	11,387,348	0.71	7,359,500	0.30
Exercised	(1,299,834)	0.21	-	-
Outstanding, end of the year	20,505,764	0.52	10,418,250	0.28

As at August 31, 2018, the weighted-average contractual remaining life of the share purchase warrants was 3.44 years (August 31, 2017 – 3.40 years).

During the year ended August 31, 2018, the Company extended the exercise period of 1,000,000 warrants exercisable for one share at $0.20 per share from December 29, 2017 to December 29, 2020.

Note 8 Related Party Transactions

	2018	2017
Compensation:		
Consulting fees	$ 183,500	$ 86,500
Share-based payments	336,470	-
	$ 519,970	$ 86,500

During the year ended August 31, 2018, the Company accrued management consulting fees of $94,500 (2017 - $43,250) to a private company controlled by the Company's President and CEO. As at August 31, 2018, $nil (2017 - $14,713) was payable to this private company for the unpaid portion of these fees.

During the year ended August 31, 2018, the Company accrued management consulting fees of $89,000 (2017 - $43,250) to the Company's COO.

Note 9 Capital Management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern and to maintain a flexible capital structure which optimizes the cost of capital within a framework of acceptable risk. In the management of capital, the Company includes the components of shareholders' equity, as well as cash and cash equivalents. There are

(Expressed in Canadian Dollars)

Note 9 Capital Management – (cont'd)

no external restrictions on the use of the Company's capital other than as provided in Policy 2.4 Capital Pool Companies of the TSX Venture Exchange.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust its capital structure, the Company may issue new shares, issue new debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents

The Company's financial instruments are exposed to the following risks:

Credit Risk

The Company's primary exposure to credit risk is the risk of illiquidity of cash amounting to $1,741,853 at August 31, 2018. As the Company's policy is to limit cash holdings to instruments issued by major Canadian banks, or investments of equivalent or better quality, the credit risk is considered by management to be negligible.

Fair Value of Financial Instruments

The fair value of the Company's financial assets approximates the carrying amount. Financial instruments measured at fair value are classified into one of three levels in the fair value hierarchy according to the relative reliability of the inputs used to estimate the fair values. The three levels of the fair value hierarchy are:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

The fair value classification of the Company's financial instruments as at August 31, 2018 is as follows:

		As at August 31, 2018	
	Fair value level	Fair value through profit or loss	Loans and receivables at amortized cost
Financial assets			
Cash	1	$ 1,741,853	$ -
		$ 1,741,853	$ -

(Expressed in Canadian Dollars)

Note 9 **Capital Management – (cont'd)**

The fair value classification of the Company's financial instruments as at August 31, 2017 is as follows:

		As at August 31, 2017	
	Fair value level	Fair value through profit or loss	Loans and receivables at amortized cost
Financial assets			
Cash	1	$ 2,149,325	$ -
		$ 2,149,325	$ -

During the years ended August 31, 2018 and 2017, there were no transfers between level 1, level 2 and level 3 classified assets.

Note 10 **Income Taxes**

The reconciliation of the income tax provision compute at statutory rates is as follows:

	2018	2017
Net loss for the year before tax	$ (2,500,900)	$ (724,203)
Expected income tax recovery	(666,907)	(188,293)
Net adjustment for deductible and non-deductible amounts	295,621	(34,371)
Unrecognized benefit of tax pool assets	371,286	222,664
	$ -	$ -

Note 10 **Income Taxes – (cont'd)**

There are no deferred tax assets or liabilities presented in the statement of financial position.

Deductible temporary differences, unused tax losses and unused tax credits for which no deferred tax assets have been recognized are attributable to the following:

	2018	2017
Deferred income tax assets:		
Non-capital loss carryforwards	$ 3,424,392	$ 2,112,608
Share issuance costs	206,120	125,582
PP&E	26,872	15,891
Deferred income tax assets	$ 3,657,384	$ 2,254,081

(Expressed in Canadian Dollars)

Note 10 <u>Income Taxes</u> – (cont'd)

Subject to certain restrictions, the Company has non-capital losses available for possible deduction against future years' taxable income of approximately $3,422,392 (2017 - 2,112,608). The Company has not recognized any future benefit for these tax losses, as the likelihood of their utilization is unknown. If unused, these non-capital losses will expire as follows:

2030	$	15,020
2031		96,701
2032		99,425
2033		330,994
2034		130,993
2035		223,573
2036		479,087
2037		736,815
2038		1,309,784
	$	3,422,392

Note 11 <u>Supplemental Non-cash Disclosures</u>

The Company incurred $1,401,577 (2017 - $20,802) in property, plant and equipment acquisition costs which were included in accounts payable and accrued liabilities as at August 31, 2018.

Note 12 <u>Subsequent Events</u>

- Subsequent to year end, XLY completed the Initial Subscription for aggregate gross proceeds of $4,000,000. The financing was comprised of an equity component of 3,755,868 common shares issued at $0.71 per share, for proceeds of $2,666,667. The remaining $1,333,333 of proceeds is expected to initially be recorded by the Company as deferred revenue, the future recognition of which by the Company is subject to the exercise, by XLY, of certain call options in respect to the Company's future cannabis production. The amount is expected to be recognized as income if and as XLY exercises its call options to acquire up to 50% of the Company's production yield at various prices, based on the discount, if any, of the call prices to current equivalent market values.

- On September 13, 2018, 100,000 share purchase warrants exercisable at $0.25 were exercised for gross proceeds of $25,000.

- In October 2018, the Company completed a private placement of 11,260,000 units ("Units) at a price of $0.25 per Unit for gross proceeds of $2,815,000. Each Unit consists of one common share and one share purchase warrant ("Warrant"). Each Warrant entitles the holder to purchase one additional common share of the Company at a price of $0.30 per share for a period of five years from closing.