

**Stem Holdings, Inc.**  
**Statements of Financial Position**  
**(All amounts are in USD, unless otherwise stated)**

	<b>Notes</b>	<b>As at June 2017 (Unaudited)</b>	<b>As at September 30, 2016 (Audited)</b>
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash and cash equivalents		\$ 1,147,992	\$ 798,198
Prepaid expenses and deposits		195,147	-
Notes receivable	12	75,000	31,250
Subscriptions receivable	7	-	1,170,000
<b>Total current assets</b>		<u>1,418,139</u>	<u>1,999,448</u>
Property and equipment	13	<u>2,704,631</u>	<u>-</u>
<b>Other Assets:</b>			
Due from affiliates		154,437	-
Project Costs		18,711	-
Deposits		174,308	-
Software		49,242	-
Total other assets		<u>396,698</u>	<u>-</u>
<b>Total Assets</b>		<u>\$ 4,519,468</u>	<u>\$ 1,999,448</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Total Liabilities</b>	16	<u>336,597</u>	<u>-</u>
<b>Shareholders' Equity</b>			
Share capital	6	6,390,798	2,492,250
Subscription receivable	7	-	(400,000)
Accumulated deficit		<u>(2,207,927)</u>	<u>(92,802)</u>
Total equity		<u>4,182,871</u>	<u>1,999,448</u>
<b>Total Liabilities and Shareholders' Equity</b>		<u>\$ 4,519,468</u>	<u>\$ 1,999,448</u>
<b>Commitments</b>	11		

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

Stem Holdings, Inc.  
 Statements of cash flows  
 (All amounts are in USD, unless otherwise stated)

	Period from October 1, 2016 to June 30, 2017	Period from June 7, 2016 to September 30, 2016
	(Unaudited)	(Audited)
<b>Operating Activities:</b>		
Net loss for the period	\$ (2,120,228)	\$ (92,802)
(Increase) decrease in operating assets:		
Depreciation and amortization	96,585	-
Impairment of Advance-related party	93,143	-
Stock-based compensation	1,159,977	-
Increase in accounts payable	89,117	-
(Increase) in prepaid expenses and deposits	24,936	(31,250)
<b>Net Cash Flows Used In Operating Activities</b>	<u>1,463,758</u>	<u>(124,052)</u>
<b>Investing Activities:</b>		
Purchases of property and equipment	(2,454,030)	-
Intangible property expenditures	(50,915)	-
Project cost expenditures	(18,711)	-
Advances to related entities, net of repayments	(336,918)	-
Deposits for leasehold improvements	(160,308)	-
<b>Net cash used in investing activities</b>	<u>(3,020,882)</u>	-
<b>Financing Activities:</b>		
Proceeds from issuance of common shares	4,316,071	922,250
<b>Principle payments on notes payable</b>	<u>(288,925)</u>	-
<b>Net Cash Provided By Financing Activities</b>	<u>4,027,146</u>	<u>922,250</u>
<b>Net increase in cash and cash equivalents</b>	349,794	798,198
Cash and cash equivalents at beginning of period	798,198	-
<b>Cash and cash equivalents at end of period</b>	<u>\$ 1,147,992</u>	<u>\$ 798,198</u>
<b>Supplemental cash flow information</b>		
Cash paid for interest	\$ <u>                    </u>	\$ <u>                    </u>
Cash paid for taxes	\$ <u>                    </u>	\$ <u>                    </u>
Non-cash supplemental information		
Insurance financing for note payable	\$ <u>213,083</u>	\$ <u>                    </u>
Purchase of real estate with seller financing	\$ <u>304,263</u>	\$ <u>                    </u>
Project costs transferred to property, plant and equipment	\$ <u>41,250</u>	\$ <u>                    </u>

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

**Stem Holdings, Inc.**  
**Statements of Loss and Comprehensive Loss**  
**(All amounts are in USD, unless otherwise stated)**

	<u>Notes</u>	<u>Period from October 1, 2016 to June 30, 2017</u>  (Unaudited)	<u>Period from June 7, 2016 to September 30, 2016</u>  (Audited)
<b>Revenues</b>		\$ -	\$ -
General and administration	9	2,125,380	92,802
<b>Operating loss</b>		<u>2,125,380</u>	<u>(92,802)</u>
Net loss before income taxes		2,125,380	(92,802)
Provision for income taxes	10	-	-
<b>Net loss and comprehensive loss for the period</b>		<u>\$ 2,125,380</u>	<u>\$ (92,802)</u>
<b>Basic and diluted loss per common share</b>	8	<u>\$ (0.39)</u>	<u>\$ (0.03)</u>

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

## **1. Incorporation and operations**

Stem Holdings, Inc. (the “Company”) is a Nevada corporation incorporated on June 7, 2016. The Company purchases, improves, and leases properties for use in the cannabis production, distribution and sales industry beginning in the state of Oregon. In September and October 2016, the Company subleased its first production facility and acquired its first commercial location, respectively. In February 2017 and May 2017, the Company acquired its second commercial location and acquired its second production facility, respectively. The Company will enter into 4 leases for these properties.

As shown in the accompanying consolidated financial statements, the Company has experienced recurring losses, and has accumulated a deficit of approximately \$2.2 million as of June 30, 2017. For the nine months ended June 30, 2017 we had a net loss of approximately \$2.1 million. The Company believes that its purchase of the farm property in Mulino, Oregon to be probable (see Note 9), and will require the Company to invest \$1.7 million in its purchase in the coming months. In addition, in July 2017, the Company has entered into 4 leases with tenants that are related to the Company and its officers and directors, in which it has committed the Company to build out its properties at an estimated cost of \$4.7 million (see Note 11). Given the current cash balance of approximately \$1.15 million, with the unknown amount of how much the leases noted above will generate over the coming months, these factors raise substantial doubt about the ability of the Company to continue to operate as a going concern for a period of at least one year after the date of the issuance of our audited financial statements for the upcoming period ended September 30, 2017.

Realization of a major portion of our assets as of June 30, 2017, is dependent upon our continued operations. The Company is dependent on generating additional revenue or obtaining adequate capital to fund operating losses until it becomes profitable. As noted above, the Company has entered into leases commencing in July 2017 covering 4 of its properties. In addition, the Company is evaluating various forms of financing which may be available to it, i.e., debt and/or equity financing while carefully evaluating the impact on share dilution. There can be no assurance that the Company will secure additional financing for working capital, increase revenues and achieve the desired result of net income and positive cash flow from operations in future years. These financial statements do not give any effect to any adjustments that would be necessary should the Company be unable to report on a going concern basis.

The financial statements of the Company for the period ended September 30, 2016 and for the nine months ended June 30, 2017 were authorized for issuance in accordance with a resolution of the Board of Directors on June 1, 2017.

## **2. Basis of preparation**

### **Statement of compliance**

The Company has prepared its financial statements in accordance with International Financial Reporting Standards (“IFRS”).

### **Basis of measurement**

These financial statements are stated in United States dollars and were prepared on a going concern basis, under the historical cost convention.

### **Use of estimates and judgments**

The preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and

judgments used are based on management's experience and the assumptions used are believed to be reasonable given the circumstances that exist at the time the financial statements are prepared.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Critical judgments in applying accounting policies:

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 and disclosed in the financial statements.

- Provisions:

- The Company is required to exercise judgment in assessing whether the criterion for recognition of a provision has been met.

#### **Functional and presentation currency**

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

### **3. Summary of significant accounting policies**

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

#### **Cash and cash equivalents**

Cash and cash equivalents include short-term investments with original maturities of three months or less and are recorded at cost, which approximates fair market value given the short-term nature.

#### **Leases**

Leases, on terms for which the Company assumes substantially all the risks and rewards of ownership, are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognized in the Company's statement of financial position. Operating lease payments are recognized in general and administrative expenses in profit or loss on a straight-line basis.

#### **Taxes**

Income tax expense is comprised of both current and deferred income taxes. Income tax expense is recognized in the statement of income and comprehensive income except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized on the temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same

taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

### **Share capital**

Equity instruments are contracts that give a residual interest in the net assets of the Company. Financial instruments issued by the Company are classified as equity only to the extent that they do not meet the definition of a financial liability or financial asset. The Company's common shares are classified as equity instruments.

### **Financial instruments**

Financial instruments are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Non - derivative financial instruments are recognized initially at fair value, plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs.

Subsequent to initial recognition, financial instruments are measured as described below:

- **Loans and receivables**

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an activemarket. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period which are classified as non-current assets. The Company's receivables comprise other receivables and cash in the statement of financial position.

Loans and receivables are initially recognized at fair value plus transaction costs and, subsequently, carried at amortized cost using the effective interest method.

A provision for impairment of trade receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in profit or loss. When a trade receivable is uncollectable, it is written off against the allowance account for trade receivables.

- **Other financial liabilities**

Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis. Liabilities in this category include bank indebtedness, accounts payable and accrued liabilities, and long- term debt.

Financial assets are derecognized when the contractual rights to the cash flows from the financial asset expire or when the contractual rights to those assets are transferred.

### **Fair value of financial instruments**

For financial instruments that are traded in active markets at each reporting date, the fair value is determined by reference to quoted market prices or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs.

For financial instruments not traded in an active market at each reporting date, the fair value is determined using appropriate valuation techniques. Such techniques may include using recent arm's length market

transactions, reference to the current fair value of another instrument that is substantially the same, a discounted cash flow analysis, or other valuation models.

#### **Earnings per share**

The Company presents basic and diluted per share amounts (“EPS”) data for its common shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of common shares outstanding during the period.

#### **4. Recent accounting pronouncements**

A number of new standards, and amendments to standards and interpretations, are not yet effective for the periods ended October 12, 2016, and have not been applied in preparing these financial statements. The following pronouncements are considered by the Company to be the most significant of several that may affect the financial statements:

IFRS 9 “Financial Instruments” was issued in November 2009 as the first step in the IASB’s project to replace IAS 39 “Financial Instruments: Recognition and Measurement”. IFRS 9 introduces new requirements for classifying and measuring financial assets that have a proposed implementation date of January 1, 2018. The IASB intends to expand IFRS 9 during the intervening period to add new requirements for classifying and measuring financial liabilities, derecognition of financial instruments, impairment and hedge accounting. The Company does not expect this standard to have a significant effect on the financial statements.

Amendments to IAS 36 “Impairment of Assets” addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The Company does not expect the amendments to IAS 36 to have a significant effect on the financial statements.

IFRS 15 “Revenue from Contracts with Customers” was issued to replace IAS 18 “Revenue”, which establishes a new five-step control-based revenue recognition model for determining the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 is not expected to have a significant impact on the financial statements.

IFRS 16 “Leases” was issued to introduce a single lease accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. The new standard is effective for annual periods beginning on or after January 1, 2019. The Company intends to adopt the standard for the fiscal year beginning July 1, 2019. The extent of the impact of the adoption of the standard has not yet been determined.

#### **5. Financial risk management overview**

The Company has exposure to the following risks:

- Liquidity risk
- Market risk

This note presents information about the Company’s exposure to each of the above risks, the Company’s objectives, and processes for measuring and managing risk and the Company’s management of capital.

##### **Liquidity risk**

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity

to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

#### **Market risk**

Market risk is the risk that changes in market prices such as interest rates or foreign exchange rates that will affect the Company's income. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

#### **Interest rate risk**

The Company is exposed to interest rate risk to the extent that cash held in interest bearing accounts are at floating or short-term rate of interest. The Company does not have any financial or interest rate contracts in place as of June 30, 2017.

## **6. Shareholders' capital**

#### **Authorized shares**

The authorized share capital of the Company consists of:

- 50,000,000 shares of Series A Preferred Shares with a par value of \$0.001 per share.
- 50,000,000 shares of Series B Preferred Shares with a par value of \$0.001 per share.
- 100,000,000 shares of common stock with a par value of \$0.001 per share.

#### **Issued and outstanding**

#### **Preferred shares**

The Company does not have any preferred shares issued and outstanding.

#### **Common shares**

The holders of common shares are not entitled to receive dividends, and are entitled to one vote per share at meetings of the Company. All shares rank equally with regard to the Company's residual assets.

	June 30, 2017		September 30, 2016	
	Number of		Number of shares	
	shares			
Balance, beginning of period	4,734,163	\$ 2,492,250	2,750,000	\$ 2,750
Common shares issued under private placements	1,440,447	3,898,548	1,817,497	2,089,500
Common shares issued under a private placement, for a stock subscription receivable		-	166,666	400,000
Balance, end of period	6,174,610	\$ 6,390,798	4,734,163	\$ 2,492,250

The Company issued share capital as of June 30, 2017, and September 30, of \$6,384,624 and \$2,492,250, respectively, by way of non-brokered private placements, as follows:

- On inception (June 7, 2016), 2,750,000 common shares at \$0.001 per share to founders of the Company for \$2,750.
- During July – August 12, 2016, 1,010,000 common shares at \$0.15 per share to unaffiliated investors for \$151,500.
- During August 25 – September 30, 2016, 974,163 common shares at \$2.40 per share to unaffiliated



- investors for \$2,338,000.
- During October 1, 2016 – June 30, 2017, 1,440,447 common shares at \$2.70 per share to unaffiliated investors for \$3,898,548.
- A summary of stock-based compensation for the nine months ended June 30, 2017 is as follows:
- 

**Stock Grants:**

	Shares	Stock Based Compensation Expense
Officers (common stock)	150,000	\$ 360,000
Non-Employments Consultants (common stock)	50,000	\$ 120,000
<b>Total</b>	<u>200,000</u>	<u>\$ 480,000</u>

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- For both the employee and non-employee common stock grants noted above were valued at \$2.40 per share in the quarter ended June 30, 2017.
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- The Company received subscriptions in a private placement offering and received amounts for its acquisition completed for the following shares during the nine months ended June 30, 2017:
- 

**7. Subscription receivable**

During the nine months ended June 30, 2017, the Company collected in full its subscription receivable of \$1,170,000 for the issuance of 487,500 common shares that was outstanding as of September 30, 2016. This is included in the total above.

On August 30, 2016, the Company received a subscription for \$800,000 for the issuance of 333,333 shares and issued 166,666 shares of common stock, to be held in escrow, pending the receipt of \$400,000. According to the securities purchase agreement with the shareholder, the payment was received and the common shares are to be released from escrow on or before April 15, 2017. On April 7, 2017, the Company and Investor amended the original agreement to reduce the subscription entered from its original total of \$800,000, of which \$400,000 was a receivable to \$600,000 comprising an aggregate of 250,000 shares of the Company's common stock. The remaining balance of the then updated subscription receivable of \$200,000 was satisfied and received in April 2017.

These amounts are not included in the subscription totals for the nine months ended June 30, 2017 noted above.

**8. Earnings per share**

The following summarizes the weighted average common shares used in calculating per share amounts:

	October 1, 2016 to June 30, 2017	June 7, 2016 to September 30, 2016
Net loss for the period	\$ (2,120,228)	\$ (92,802)
Weighted average shares:		
Basic	5,474,458	2,684,936
Diluted	5,474,458	2,684,936
Basic and diluted loss per common share	<u>\$ (0.39)</u>	<u>\$ (0.03)</u>

## 9. General and administrative expenses

	October 1, 2016 to June 30, 2017	June 7, 2016 to September 30, 2016
Professional fee's	\$ 254,182	60,412
Consulting fee's	89,500	
General and admin	528,578	32,390
Impairment of advance	93,143	
Stock based compensation	1,159,977	
	<u>\$ 2,125,380</u>	<u>\$ 92,802</u>

## 10. Income taxes

The major components of income tax expense for the period ended June 30, 2017 are as follows:

	June 30, 2017
Net loss for the period	\$ (2,125,380)
Expected income tax recovery	\$ (722,629)
Change in unrecognized tax asset	722,629
	<u>\$ -</u>

The Company's effective tax rate for the period ended June 30, 2017 was 34%. The Company records a valuation allowance to reduce the deferred income tax assets to the amount that is more likely than not to be realized. In making such determinations, management considers all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. As a result, there are no income tax benefits reflected in the statement of operations to offset pre-tax losses.

At June 30, 2017, the Company had net operating loss ("NOL") carry forwards aggregating approximately \$722,629 which, if not used, expire in 2036. The utilization of these NOL may become subject to limitations based on past and future changes in ownership of the Company pursuant to Internal Revenue Code Section 382.

## 11. Commitments

In July 2016, the Company entered into a 10-year lease for a commercial building from an unrelated third party in Springfield, Oregon. At the time the original lease was entered into, the Company had expected to close on significant subscriptions from its private placement. However, when those did not immediately materialize, the Company entered into an agreement with the landlord to cancel the lease and in addition, paid the landlord \$15,000 not to rent out the property until such time the Company could enter into a new lease. In September 2016, the Company entered into a new 10-year lease with the landlord that commenced in November 2016. The lease requires the Company to pay a base rental fee of \$7,033 plus an additional estimated \$315 per month in real estate taxes in which the base rental fee escalates each year by approximately 2%. All taxes (including reconciling real estate taxes), maintenance and utilities are included at the end of each year as a one-time payment. In addition, the Company also remitted \$14,000 for a security deposit to the landlord. The Company expects to sublease out this space in the near future.

In August 2016, the Company and certain shareholders of the Company entered into a "Multi Party" Agreement, in which the Company became obligated to lease or acquire three separate real estate assets,

and separately, if certain events occur (see below), additional real estate assets held by entities related to those shareholders. In September 2016, the Company entered into the lease as more fully described above, and in November 2016, acquired a property after the shareholder that owned the purchase agreement transferred that purchase agreement to the Company, in accordance with the Multi Party agreement (see Note 4). As of the date of these financial statements, the Company has entered into negotiations for the acquisition of the third property in Mulino, Oregon, but as of yet has not exchanged final closing documents, and at this time, is uncertain if or when it will. Should the Company obtain in excess of \$10,000,000 through a combination of its private placements and its merger with Patch Holdings, Inc. (see Note 5), it is required to purchase certain real estate properties owned by entities affiliated with certain of its shareholders.

In addition, certain shareholders of the Company have begun organizing entities that will operate directly in the cannabis industry, and the Company intends to offer leases of its properties to these entities in the near future. The Multi Party Agreement also requires that in the event that the US Government amends Title 21 of the United States Code, otherwise known as the Controlled Substances Act, to remove cannabis as a Schedule I drug, and the Company raises more than \$10 million in equity and merger funding, the Company is required to enter into agreements to acquire those related entities and issue such equity that the shareholders of the related entities obtain 75% of the then issued and outstanding equity of the Company, regardless of the profitability or financial condition of the related entities at the time of their acquisition.

In February 2017, the Company entered into a 1-year lease for the occupancy of the Stem Holdings, Inc.'s corporate office located in Boca Raton, Florida. The lease requires the Company to pay a base rental fee of \$785.00 per month. All taxes, maintenance and utilities are included. In addition, the Company also remitted \$785 for a security deposit to the landlord.

In February 2017, the Company entered into an advisory agreement with an unrelated third party with a term of 12 months. As part of that agreement, the third party agreed to provide assistance for the Company with respect to eligibility for becoming quoted on the OTCQB/OTCQX and advising and assisting the Company in complying with its ongoing OTCQB/OTCQX disclosure obligation under current federal and state securities laws. These services to the Company are exchanged for a \$10,000 upfront payment, and \$5,000 payment upon the acceptance on OTCQB/OTCQX.

On April 15, 2017, the Company entered into a "Contract for Sale" for a farm property in Mulino Oregon, pursuant to which the seller will sell the premises to the Company upon the completion of the Company's due diligences investigations and completion of the closing conditions precedent to each party's obligations under the Contract for Sale. The purchase price is \$1,700,000 that will be reduced by a rental credit of \$105,000 (as indicated below) which is equivalent to 7 months at \$15,000 a month. A note payable will be executed in the amount of \$1,200,000 with a maturity two years from closing date. The balance of \$395,000 will be paid at closing which shall occur the earlier of (i) the 30<sup>th</sup> day after the Company obtains Water Rights from Oregon Liquor Control Commission ("OLCC") permits, and (ii) October 5, 2017, or such other date as the parties may agree upon in writing. In April 2017 in order for the Company to make use of the Premises while completing its due diligence and while the parties complete their conditions to closing under the Contract for Sale, seller and Company have agreed to lease the premises to Company upon the following terms and conditions. The term of the lease commences April 5, 2017 and expires the earlier to occur 1) the termination of the contract of sale by either party thereto in accordance with its terms; 2) the closing date. The lease requires the Company to pay a base rental fee of \$15,000 for the first 7 months with no lease deposit required. All taxes (including real estate taxes, and personal property taxes) are the responsibility of the Company. As of the date of filing of this Form 10-Q, the Company believes it probable that it will close on the Contract for Sale of the property.

In June 2017, the Company entered into an investor relation advisory agreement with an unrelated third party with a term of 12 months. As part of that agreement, the third party agreed to provide assistance for the Company with respect to strategic investor relations, road shows, investment banking, and corporate presentations. These services to the Company are exchanged for a \$6,000 a month.

## 12. Notes Receivable

On October 28, 2016, the Company loaned \$100,000 to certain officers and shareholders of the Company, under a promissory note (the "Note") due March 30, 2017 which bears interest at rate of 12% per annum. The Note provides for monthly interest payments in the amount of \$1,000 commencing December 1, 2016 until the Note is fully paid. On March 15, 2017, an extension was granted through July 1<sup>st</sup>, 2017 by which the indebtedness in the amount of \$100,000 is to be liquidated by four equal monthly installments of \$25,000 of which the Company has received the first \$25,000 payment under the updated terms as of the date of this filing. As of June 30, 2017, the parties agreed that rather than the Payors repaying the Company the remaining balance on the note, the Payors, party to this agreement, will directly pay for certain agreed improvements on the properties to the extent of the remaining balance of the note. In exchange for this undertaking by the Payors party to this agreement, the Company agrees it shall cancel the indebtedness represented by the note, together with any interest accrued or to be accrued thereon. No payments were made by the debtors for improvements on behalf of the Company as of June 30, 2017. The Note is secured by a pledge of 50,000 shares of Company common stock owned by the debtors.

## 13. Property and equipment

At June 30, 2017 property and equipment consisted of the following:

Signage	\$	19,118
Furniture and equipment		90,612
Leasehold improvements		471,321
Architectural and Design		75,313
Buildings		1,578,627
Construction in progress(1)		564,552
Subtotal		<u>2,799,543</u>
Accumulated depreciation		(94,912)
Property, plant and equipment, net		<u><u>2,704,631</u></u>

- (1) Because the Company believes it is probable that it will close on the Mulino property (see Note 9), the Company has treated the costs to improve the property as construction in progress and not as project costs as of June 30, 2017.

On November 1, 2016, the Company acquired certain real property located at 1027 Willamette Street, Eugene, OR 97401 (the "Property") for a total cash purchase price plus closing costs of approximately \$918,000.

On February 6, 2017, the Company acquired certain real property located at 7827 SE Powell Blvd, Portland, OR 97206 (the "Property") for a total purchase price plus closing costs of approximately \$656,498. As part of the consideration for closing on the property, the Company issued a short term note payable to the seller in the Amount of approximately \$304,000.

#### **14. Acquisition of Patch International, Inc.**

In November 2016, the Company entered into an agreement to acquire 100% of the issued and outstanding shares of Patch International, Inc. (“Patch”). In order to close the transaction, Patch is required to submit for approval to certain Canadian government courts, hold a general meeting of its shareholders and have the shareholders vote to approve the merger, and certain other customary requirements. As of the time of the agreement, Patch did not have any operations, and is considered a dormant entity. The Company will issue shares of its common stock based on a price of \$2.40 per common share, with the number of shares to be issued based on the amount of cash held at the time of closing of the transaction, converted from Canadian dollars into US dollars. In addition, the Company has agreed to issue to Patch shareholders additional shares at the same \$2.40 per share in the event that the Company collects on a fully reserved receivable in the amount of \$500,000 owed to Patch by a related party. As of the date of the acquisition and of these financial statements, the Company considers the receivable uncollectible (as did Patch, which reserved 100% of the outstanding receivable in its audited financial statements) and does not anticipate issuing additional shares for its collection.

On January 20, 2017, the Patch Shareholders held their general meeting and they voted to be acquired by the Company. On January 23, 2017, the Company issued 1,048,762 of its shares to acquire 100% of the issued and outstanding shares of Patch for consideration in the amount of \$2,452,058. The Company has been informed that two shareholders, representing less than 2% of Patch shares outstanding have chosen to not vote for the merger. Under Canadian law, the Company committed to purchase these shares for cash consideration in the amount \$53,534.53 US dollars. The Company has treated the payment to acquire the dissenter shares as a reduction in the cash acquired.

The Company has not accounted for the acquisition of Patch as a business combination. Because Patch was a dormant entity with its only asset being cash, the acquisition was treated essentially as an acquisition of cash.

#### **15. Stock Purchase Options**

During the nine months ended June 30, 2017, the Company entered into three separate consulting agreements, the first in November 2016, the second in January 2017 & February 2017, and the third in June 2017, and as part of those agreements agreed to issue a total of 500,000 options to purchase the common stock of the Company, with an exercise price of \$2.40 per share and a term of 4 years. Pursuant to the first agreement to issue options to acquire a total of 200,000 of the Company’s common stock, options to acquire 100,000 shares vested immediately, options to acquire 50,000 shares that vest 6 months upon a registration statement being declared effective in which the underlying shares to the options are registered and the final option to acquire 50,000 shares vests 1 year after a registration statement is declared effective in which the underlying shares to the option are registered connection with the execution of a consulting agreement. Pursuant to the second consulting agreement, 100,000 options vested immediately and pursuant to the third consulting agreement, one third of option to acquire the 100,000 options vests immediately and the remaining two thirds vest monthly for the next 30 months which equals 2,222 a month. In June 2017, the Company agreed to issue options for a total of 200,000 shares of stock of the Company to three separate entities and individuals for consulting and professional services. All of the June 1, 2017 options had an exercise price of \$2.40 per share, have a term of 4 years and the Company believes that the fair value of the underlying common on the date of issuance was \$2.40 per share. The first 100,000 share issuance vested entirely at issuance, while the following two 50,000 share issuances vested quarterly over 1 year from issuance.

In total, the Company recorded stock based compensation expense to the consultants of approximately \$582,000 as a result of these options in the nine months ended June 30, 2017. In addition, due to the vesting provisions, the Company revalued the unvested options issued in the first and second fiscal quarter as June 30, 2017 and determined that the value of the options issued in the first quarter had reduced in value from the original valuation recorded by \$0.97 per option share and the second quarter issuances had reduced in value by \$0.79 per option share. This resulted in a reduction of consulting costs for the option based compensation of approximately \$107,000 in the period ended June 30, 2017.

During the period ended June 30, 2017, the Company entered into two separate employment agreements, both dated June 1, 2017, and as part of those agreements agreed to issue a total of 150,000 options to purchase the common stock of the Company, with an exercise price of \$2.40 per share and a term of 3 years. Pursuant to these agreements, 150,000 shares vested immediately month. In total, the Company recorded stock based compensation expense to the officers of \$205,500 as a result of these options in the nine months ended June 30, 2017.

A summary of the change in stock purchase options outstanding for the period ended June 30, 2017 is as follows:

	Options Outstanding	Exercise Price	Remaining Contractual Life (Years)
Balance – September 30, 2016	-	-	-
Options issued	650,000	\$ 2.40	4
Options expired	-	-	-
Options exercised	-	-	-
Balance – June 30, 2017	<u>650,000</u>	<u>\$ 2.40</u>	<u>4</u>

The Company valued the options issued using a Black Scholes Merton option pricing model using the following assumptions:

Stock price on date of grant	\$ 2.40
Risk free rate of interest	5.0%
Expected life of warrant – in months	48
Dividend rate	0
Historic volatility*	160-224%

\* the Company has used the historic volatility of 6 companies engaged in providing ancillary type services to the cannabis industry as an approximation of its expected volatility.

During the period ended June 30, 2017, the Company entered into two separate consulting agreements, the first in November 2016, and the second in February 2017, and as part of those agreements agreed to issue a total of 300,000 options to purchase the common stock of the Company, with an exercise price of \$2.40 per share and a term of 4 years. Pursuant to the first agreement to issue options to acquire a total of 200,000 of the Company's common stock, options to acquire 100,000 shares vested immediately, options to acquire 50,000 shares that vest 6 months upon a registration statement being declared effective in which the underlying shares to the options are registered and the final option to acquire 50,000 shares vests 1 year after a registration statement is declared effective in which the underlying shares to the option are registered connection with the execution of a consulting agreement. Pursuant to the second consulting agreement, one third of option to acquire the 100,000 options vest immediately and the remaining two thirds vest monthly for the next 30 months which equals 2,222 a month. In total, the Company recorded stock based compensation expense to the consultants of \$361,986 as a result of these options in the nine months ended June 30, 2017.

**16. Note Payable**

As of February 2017, the Company entered into a 10-month premium finance agreement and disclosure statement in consideration for a one year Directors and Officers insurance policy in the principal amount of \$212,500 and an additional service fee, included in the financed principal of \$5,700. The note bears an annual interest rate of 5.81% and requires the Company to make monthly payments of \$21,820 over the term of the note. As of June 30, 2017, the obligation left on the note is \$101,915.

**17. Related party transactions**

Prior to the formation of the Company, one of its shareholders entered into an agreement to acquire a commercial property located in Eugene Oregon, as more fully described in Note 4, which sale agreement was later transferred to the Company (see Note 9) after its formation. That shareholder and two other shareholders also advanced funds that were applied as escrow deposits upon closing in the amount of \$34,750 which has been included as an asset as part of project costs and in current liabilities section of these financial statements as Due to Shareholders. As of June 2017, \$29,250 was repaid to one of the shareholders.

During the period ended September 30, 2016, the Company advanced \$20,412 in payment of legal fees to entities being formed by certain shareholders of the Company, which is shown as a long term related party receivable in these financial statements. In December 2016, the Company advanced, on behalf of the related entities, an additional \$45,000 in payment of legal fees and a payment of \$4,750 for licensing fees, on behalf of related entities, to the Oregon Liquor Control Commission, the entity that regulates cannabis production and distribution in Oregon.

In the quarter ended March 31, 2017, the Company determined that it could no longer continue capitalizing the amounts advanced and impaired approximately \$93,000 (the amounts advanced during that quarter). In the quarter ended June 30, 2017, the Company believed it could capitalize the advances made during the quarter ended June 30, 2017 because in July 2017, as part of the lease agreements entered into with the related parties (see Note 11), the leases contained agreements to repay those amounts advanced to date. As of June 30, 2017, the Company has recorded as receivable from the related parties \$154,437. Should collection occur in future periods of the amounts previously impaired, the Company will record those as income at the time of collection.

**18. Subsequent events**

Subsequent to June 30, 2017, and up to the date of this filing, 78,583 shares of our common stock, as part of our continuing private placement at \$2.40 per share, were issued for consideration of \$188,600 in cash.

In July 2017, the Company commenced rental operations through real estate leases with entities that engage in the cultivation, processing and sale of cannabis. All of the leases noted below have entities as lessees that are related parties to the Company (through common ownership and management). As part of the lease agreements noted below, the Company has committed to funding buildouts separate from the actual purchase price of the properties that in total amounts to approximately \$4.7 million.

### 1027 Willamette

In July 2017, the Company entered into an operating lease agreement with a marijuana dispensary (the "Lessee") to move into the Company's acquired property located at 1027 Willamette Street in Eugene, Oregon. The lease agreement is for a base term of ten years (see note below) and a monthly rent obligation of \$13,800, subject to annual increases of 3% per year, plus an amount for additional rent based on final buildout costs incurred by the Company. The lease is a double net lease with maintenance and real property taxes to be paid by the Tenant and insurance costs paid by the Company.

Upon the expiration of the term of ten years, the Lessee has the option to renew the lease agreement for one five-year term, on the same terms as provided in the lease agreement.

### Springfield Suites

In July 2017, the Company entered into a lease agreement for its property and warehouse building located at 800 N 42<sup>nd</sup> street in Springfield, Oregon. The lease agreement is for a term of ten years (see note below) and a monthly rent obligation of \$64,640, subject to annual increases of 3% per year plus an amount for additional rent based on final buildout costs incurred by the Company. The lease is a double net lease with maintenance and real property taxes to be paid by the Tenant and insurance costs paid by the Company. Rent will begin to accrue on the date plant growing commences on the property and rental payments will begin after first harvest. The Company expects to treat such period as a free rental period for accounting purposes. At the time rental payments begin, the total of base rent and additional rent will not be less than \$1.00 per foot for light assisted greenhouse and \$.25 per usable square foot for un-light assisted greenhouse or outdoor grow space.

Upon the expiration of the term of ten years, the Lessee has the option to renew the lease agreement for five-year term, on the same terms as provided in the lease agreement.

### 14336 S. Union Hall Road Mulino

In July 2017, the Company entered into a lease agreement for its property located at 14336 South Union Hall Road in Mulino, Oregon. The lease agreement is for a term of ten years (see note below) and a monthly rent obligation of \$18,750, subject to annual increases of 3% per year plus an amount for additional rent based on final buildout costs incurred by the Company. The lease is a double net lease with maintenance and real property taxes shall be paid by the Tenant and insurance costs paid by the Company. Rent will begin to accrue on the date plant growing commences on the property and rental payments will begin after first harvest. The Company expects to treat such period as a free rental period for accounting purposes. At the time rental payments begin, the total of base rent and additional rent will not be less than \$1.00 per foot for light assisted greenhouse and \$.25 per usable square foot for un-light assisted greenhouse or outdoor grow space.

Upon the expiration of the term of ten years, the Lessee has the option to renew the lease agreement for five year term, on the same terms as provided in the lease agreement.

### 7827 SE Powell

In July 2017, the Company entered into a lease agreement for its acquired property located at 7827 SE Powell Blvd. in Portland, Oregon. The lease agreement is for a term of ten years and a monthly rent obligation of \$6,523, subject to annual increases of 3% per year. Maintenance and real property taxes shall be paid by the Tenant and insurance paid by the Company. Additional rents will be added to pay landlord back for tenant improvements by the end of the first term of the lease, payments will include annual interest at 12% compounded monthly.

Upon the expiration of the term of ten years, the Lessee has the option to renew the lease agreement for five-year term, on the same terms as provided in the lease agreement.