# NEXTLEAF SOLUTIONS LTD.

# MANAGEMENT DISCUSSION AND ANALYSIS

**Three months ended**
**December 31, 2019**

**NEXTLEAF SOLUTIONS LTD.**

(formerly Legion Metals Corp.)

**MANAGEMENT DISCUSSION AND ANALYSIS ("MD&A")**

**Effective March 2, 2020**

The following discussion and analysis of the financial condition and results of operations of Nextleaf Solutions Ltd. (formerly Legion Metals Corp.) ("Legion" or the "Company") for the three months ended December 31, 2019 should be read in conjunction with the Company's annual audited financial statements and related notes for the year ended September 30, 2019. The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). All monetary amounts in the MD&A are expressed in Canadian dollars, or as otherwise indicated.

## FORWARD-LOOKING STATEMENTS

This MD&A includes forward-looking statements that are based upon current expectations, which involve risks and uncertainties associated with our business and the environment in which the business operates. Any statements contained herein that are not statements of historical fact may be deemed to be forward looking statements, including those identified by the expressions "anticipate", "believe", "plan", "estimate", "expect", "intend" and similar expressions to the extent they relate to the Company or its management. Forward-looking statements are not historical facts but reflect management's expectations regarding future events. Forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations.

## DESCRIPTION OF THE BUSINESS

Nextleaf Solutions Ltd. (formerly Legion Metals Corp.) ("Legion", the "Company") was incorporated under the laws of the province of British Columbia on December 8, 2016. The Company changed its name to Nextleaf Solutions Ltd., ("Nextleaf") on March 14, 2019.

Nextleaf is a Canadian cannabis extractor and processor, with a focus on developing intellectual property for the extraction, distillation and formulation of cannabinoids. Nextleaf has developed a portfolio of issued and pending patents pertaining to the company's unique, industrial-scale process of producing purified cannabinoid distillate, a tasteless, odourless cannabis concentrate best suited for infusing premium value-added products, and is actively developing and protecting intellectual property pertaining to the extraction, refinement, and purification of cannabinoids. Nextleaf has completed construction of its dedicated extraction and processing facility in Greater Vancouver, British Columbia. Nextleaf

As of the date of this MD&A, the Company owns a total of 14 issued patents from four international patent offices in the key markets of Canada, the United States of America, Australia, and Colombia. The portfolio of issued patents pertains to the industrial-scale production of high-purity, cannabinoid-rich distillate, the key ingredient used in the manufacturing of standardized THC and CBD based products.

The Company is commercializing its intellectual property portfolio of issued and pending patents through licensing of intellectual property, providing toll processing services to licensed cultivators of cannabis and hemp, and supplying cannabis oil to qualified Canadian and international business-to-business partners under their own brand, see "Overall Performance" below for agreements relating to the commercialization of the Company's intellectual property. The Company's commercialization efforts are through Nextleaf Labs Ltd., a Health Canada licensed Standard Processor in which the Company is in the process of acquiring (see below).

On September 9, 2019, Health Canada issued a Standard Processing Licence to the Company's facility to Nextleaf Labs Ltd. ("Labs") located in Coquitlam, BC. Labs is a private company incorporated in the province of British Columbia and wholly-owned by a consultant of the Company. On October 11, 2019, the Company entered into a Share Purchase Agreement to acquire Labs (see below).

*Share Purchase Agreement – Nextleaf Labs Ltd.*

On October 11, 2019, the Company entered into a Share Purchase Agreement to acquire all of the issued and outstanding shares of Labs. Consideration payable by the Company is $385,000 by way of issuing common shares of the Company. Other than owning the Standard Processing Licence issued by Health Canada on the Company's facility, Labs does not own other material assets or liabilities. The acquisition has not yet closed and is subject to standard approval procedures.

On January 22, 2020, Health Canada granted a Cannabis Research Licence to Nextleaf Labs Ltd., on the Company's Standard Processing Facility.

The Company's head office is located at #304 – 68 Water Street, Vancouver, British Columbia, V6B 1A4 and its registered and records office is located at #600 – 1090 West Georgia Street, Vancouver, British Columbia, V6E 3V7. The Company's common shares trade on the Canadian Securities Exchange under the trading symbol "OILS", on the OTCQB Markets under the trading symbol "OILFF", and on the Frankfurt Stock Exchange under the trading symbol "L0MA".

The Company's facility has been designed with an annual production capacity to process 219,000 kg of dried cannabis biomass. The Company's facility also includes dedicated research and laboratory infrastructure, allowing for the continued and rapid development of new intellectual property related to cannabis processing technologies and formulations

The Company's mission is to develop and deploy large-scale cannabis and hemp extraction technologies and provide turn-key processing solutions to help licensed cultivators maximize the value of every harvest.

The Company owns and continually invests in an intellectual property portfolio of systems, methods, and apparatuses for the extraction and refinement of high-value extracts from cannabis and hemp biomass, as well as formulations for a number of cannabinoid-infused products. The Company's patented technology and market-validated formulations help cultivators increase revenue and profitability through extraction and purification of biomass into tasteless, and odourless cannabinoid distillate oil. Containing a cannabinoid concentration of up to 95%, the resulting distillate is easy to dose, formulate, and develop into innovative, value-added products for medical and adult-use markets.

**OVERALL PERFORMANCE**

The Company's focus for the three months ended December 31, 2019, was preparations to commence cannabis extraction services and the commercialization of its patent portfolio (see below).

The Company's focus for the year ended September 30, 2019, was completing the build-out of its centralized processing facility in Coquitlam, BC, completing an RTO to obtain a public listing on the Canadian Securities Exchange, obtaining licensing for its centralized processing facility (received on September 9, 2019), and entering into agreements to commercialize its intellectual property. Additionally, the Company was active in developing and protecting intellectual property pertaining to the extraction, purification, and formulation of cannabinoids and production of cannabis derived products by obtaining a number of issued patents for its extraction processes and technology (currently 14 issued and over 60 pending patents).

<u>Commercialization of Intellectual Property</u>

*Supply Agreement*

On September 16, 2019, the Company announced a Supply Agreement with BevCanna Enterprises Inc. ("BevCanna"), a company based in British Columbia that trades on the Canadian Securities Exchange. Pursuant to the Supply Agreement, the Company has granted BevCanna an exclusive license for the use of the Company's intellectual property related to water-soluble cannabinoids for the development, manufacturing and sale of BevCanna products. Commencement of this Supply Agreement is subject to BevCanna obtaining a license permitting it to process and sell cannabis.

*Royalty Agreement*

On December 16, 2019, the Company entered into a License and Distribution Royalty Agreement (the "Royalty Agreement") with a private British Columbia company (the "Licensee"). Pursuant to the Royalty Agreement, the Company will grant the Licensee a non-exclusive license for the use of certain issued and pending patents (the "Licensed Patents") in exchange for a 20% royalty on the Licensee's gross revenue, which will be payable to the Company on a quarterly basis. The Royalty Agreement is for an indefinite term.

The Company will also contribute working capital to the Licensee for use in the development of the Licensee's business. This cash contribution is repayable to the Company if the Royalty Agreement terminates on or before December 6, 2024.

During the three months ended December 31, 2019, the Company recognized revenue of $350,000 in licensing (royalty) fees, for the initial month of the Royalty Agreement. This initial traction puts the contract ahead of Management's annual guidance of $3,000,000 in revenue to be generated from the contract in fiscal 2020.

*Share Purchase Agreement – Nextleaf Labs Ltd.*

On October 11, 2019, the Company entered into a Share Purchase Agreement to acquire all of the issued and outstanding shares of Nextleaf Labs Ltd. (see "Description of the Business" above).

## SUMMARY OF QUARTERLY RESULTS

The following table shows results from the last eight quarters:

| Period Ending | Revenue $ | Loss and comprehensive loss $ | Basic and Diluted Loss Per Share $ |
|---|---|---|---|
| December 31, 2019 | 350,000 | (1,320,462) | (0.01) |
| September 30, 2019 | - | (2,050,650) | (0.02) |
| June 30, 2019 | - | (1,489,458) | (0.04) |
| March 31, 2019 | - | (4,473,406) | (0.11) |
| December 31, 2018 | - | (732,121) | (0.01) |
| September 30, 2018 | 182,000 | (769,437) | (0.01) |
| June 30, 2018 | 90,172 | (428,424) | (0.01) |
| March 31, 2018 | 221,002 | (614,305) | (0.01) |

## RESULTS OF OPERATIONS

Three months ended December 31, 2019, compared to the three months ended September 30, 2019:

On a quarter to quarter basis, loss and comprehensive loss decreased by approximately 36% or $738,000 during the three months December 31, 2019, compared to the three months September 30, 2019.

Contributing to the decrease in loss and comprehensive loss was the Company recognizing revenue of $350,000 in licensing (royalty) fees, for the initial month of the Royalty Agreement the Company entered into on December 16, 2019, (see above). The Company did not recognize any revenue during the three months ended September 30, 2019.

Additionally, more notable fluctuations on a quarter to quarter basis included: (i) administrative expenses decreasing approximately $184,000; (ii) depreciation increasing approximately $124,000 due to the transition to IFRS 16 – *Leases*; (iii) investor relations and advertising, management fees, and professional fees and consulting decreasing in aggregate by approximately $550,000, and government assistance income decreasing approximately $195,000 as the Company received a refund from the Government of Canada relating to its 2017 and 2018 SR&ED claims during the three months ended September 30, 2019, whereas no such refund was received during the three months ended December 31, 2019.

The overall reduction of quarterly losses and improvement in the Company's net cash flow position is consistent with Management's expectations as the Company's facility is substantially complete and the focus shifts towards scaling revenues and moving towards profitability.

Three months ended December 31, 2019, compared to the three months ended December 31, 2018:

On a year over year basis, loss and comprehensive loss increased by approximately $588,000 during the three months December 31, 2019, compared to the three months December 31, 2018. Notably, the Company recognized revenue of $350,000 during the three months ended December 31, 2019, whereas no revenue was recognized for the comparative period.

Contributing to the increase in loss and comprehensive loss were increases in several components of expense. This is mainly attributable to the Company increasing operations since completing the RTO with Legion Metals and becoming a reporting issuer which drives increases in overhead and professional fees in general. Subsequent to completion of the RTO effective March 14, 2019, the Company also undertook advertising initiatives which increased investor relations and advertising. Notably, during the comparative three months ended December 31, 2018, the Company had not completed the RTO and was not as active in operations in general.

Specific contributors to the increase in loss and comprehensive loss during the three months ended December 31, 2019, compared to the three months ended December 31, 2018, included the following:

- Share-based payment expense of $431,980 comprises the fair value of stock options vested during the period. There was no share-based payments expense recognized during the comparative three month period. Share-based payment expense is a non-cash expense.
- Depreciation expense of $242,944 increased by approximately $163,000. This is attributable to an increase in property and equipment subject to depreciation during the period, as well as the transition to IFRS 16 relating to the Company's facility lease which causes the recognition of the facility lease as a right-of-use asset and the related depreciation of the right-of-use asset over the term of the lease.
- Investor relations and advertising increased by approximately $83,000 to $193,982 due to increased advertising campaigns and the Company scales revenue. Professional fees and consulting increased by approximately $121,000 to $296,692 comprising of third-party consulting fees for various matters.
- Wages and salaries increased by approximately $127,000 to $261,664 as the Company hired additional staffing at its facility and head office in various departments to facilitate growth efforts.

## LIQUIDITY AND CAPITAL RESOURCES

The Company's objectives when managing its liquidity and capital are to support further advancement of the Company's business objectives, as well as to ensure that the Company is able to meet its financial obligations as they come due.

### Cash and working capital

As at December 31, 2019, the Company had cash of approximately $2,012,000 and working capital of approximately $1,636,000.

### Cash flow activity

For three months ended December 31, 2019, cash decreased by approximately $2,284,000, which was driven by the following:

- Cash used in operating activities of approximately $1,039,000, driven by cash-based expenditures and fluctuations in working capital items; and
- Cash used in investing activities of approximately $1,245,000, driven by purchases of extraction equipment and leasehold improvements totaling approximately $1,146,000.

## SHARE CAPITAL INFORMATION

**Authorized:** Unlimited number of common shares with no par value.

### Issued and Outstanding

As at the date of this MD&A, total issued, and outstanding common shares consists of 109,060,544 common shares.

- There were no transactions for the issue of share capital during the three months ended December 31, 2019.

**Stock options**

As at the date of this MD&A, the Company has 14,439,287 stock options outstanding.

A summary of the status of the Company's stock options as at December 31, 2019 and changes during the three months then ended is as follows:

| | Three months ended December 31, 2019 | |
|---|---|---|
| | Options # | Weighted average exercise price $ |
| Options outstanding, beginning of period/year | 13,989,287 | 0.35 |
| Granted | 450,000 | 0.50 |
| Granted - Performance stock options | - | - |
| Replaced on RTO | - | - |
| Exercised | - | - |
| **Options outstanding, end of period/year** | **14,439,287** | **0.36** |

As at December 31, 2019, the Company has stock options outstanding and exercisable as follows:

| | Options outstanding # | Options exercisable # | Weighted average Exercise price $ | Expiry date | Weighted average remaining life (years) |
|---|---|---|---|---|---|
| | 114,287 | 114,287 | 0.35 | May 1, 2022 | 2.33 |
| (1) | 13,725,000 | 7,550,000 | 0.35 | March 15, 2024 | 4.21 |
| | 150,000 | 150,000 | 0.50 | July 8, 2024 | 4.52 |
| | 300,000 | - | 0.50 | October 15, 2024 | 4.79 |
| | 150,000 | - | 0.50 | October 16, 2024 | 4.80 |
| | **14,439,287** | **7,814,287** | **0.35** | | **4.21** |

(1) Includes 7,500,000 performance stock options held by officers and directors of the Company.

**Warrants**

At the date of this MD&A, the Company had 25,470,305 warrants outstanding. There were no changes in the Company's share purchase warrants during the three months ended December 31, 2019.

The following table summarizes information about the warrants outstanding at December 31, 2019:

| Warrants # | Weighted average exercise price $ | Expiry Date | Weighted average remaining life (years) |
|---|---|---|---|
| 14,285,711 | 0.70 | March 14, 2021 | 1.20 |
| 485,969 | 0.35 | March 21, 2021 | 1.22 |
| 298,625 | 0.40 | May 15, 2021 | 1.37 |
| 10,400,000 | 0.70 | May 15, 2021 | 1.37 |
| **25,470,305** | **0.69** | | **1.27** |

**OFF-BALANCE SHEET ARRANGEMENTS**

Nextleaf does not utilize off-balance-sheet arrangements.

**PROPOSED TRANSACTIONS**

There are no proposed transaction as of the date of this MD&A.

## TRANSACTIONS WITH RELATED PARTIES

The remuneration of key management for the three months ended December 31, 2019 and December 31, 2018 are as follows:

| | **December 31, 2019** | December 31, 2018 |
|---|---|---|
| | **$** | $ |
| Directors' fees | 17,500 | - |
| Management fees | 110,400 | 110,400 |
| Share-based payments | 288,369 | - |
| | **416,269** | 110,400 |

Management fees and share-based payments comprise amounts paid/accrued to the officers and directors of the Company either directly, or to companies controlled by them for their services as executive officers and/or directors of the Company which includes the CEO, CFO, CTO and other directors. Legal fees comprise amounts paid to a former director until the date which the individual ceased to be a director.

### Amounts payable to related parties

The following amounts are payable to related parties and included in accounts payable and accrued liabilities as at December 31, 2019 and September 30, 2019:

| | **December 31, 2019** | September 30, 2019 |
|---|---|---|
| | **$** | $ |
| Amounts due to Officers/Directors | 101,900 | 50,345 |
| | **101,900** | 50,345 |

Amounts are due to CEO, CFO, and CTO, and certain directors relating to management fees and/or directors' fees presented above.

### Amounts receivable from/prepaid to related parties

The following amounts are prepaid to related parties as at December 31, 2019 and September 30, 2019:

| | **December 31, 2019** | September 30, 2019 |
|---|---|---|
| | **$** | $ |
| Prepaid management fees and expenses | 61,728 | 68,573 |
| | **61,728** | 68,573 |

Prepaid management fees and expenses are amounts involving the Company's CTO.

Facility lease

The Company has an agreement to lease its centralized processing facility and corporate office. The lease is for the period from July 1, 2018 to June 30, 2023. The Company's minimum annual commitments are as follows:

| **Fiscal Year** | **Total Commitment** |
|---|---|
| | **$** |
| 2020 (remaining) | 48,180 |
| 2021 | 66,012 |
| 2022 | 69,120 |
| 2023 | 52,763 |
| **Undiscounted amount of lease liability** | **236,075** |
| Future finance charges | (45,833) |
| **Total** | **190,242** |

## NEW ACCOUNTING STANDARDS

### New accounting policies

The Company adopted the following accounting standards that were effective for the Company beginning on October 1, 2019.

*New standard IFRS 16 - Leases*

IFRS 16 - *Leases* ("IFRS 16") replaced IAS 17, *Leases*. It became effective for the Company on October 1, 2019 (Q1 2020). IFRS 16 eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, IFRS 16 requires a single, on-balance sheet accounting model that is similar to current finance lease accounting. Leases become an on-balance sheet liability that attract interest, together with a new asset.

The most significant effect of the new standard is the lessee's recognition of the initial present value of unavoidable future lease payments as right-of-use ("ROU") assets and lease liabilities on the statement of financial position, including those for most leases that would have formerly been accounted for as operating leases.

The Company has a lease on its processing facility including corporate offices. In the context of IFRS 16, a ROU asset of $188,316 and a lease liability of $201,278 were recognized as at October 1, 2019, in accordance with the modified retrospective approach. The lease liability was measured at the present value of the remaining lease payments, discounted using the Company's weighted average incremental borrowing rate of approximately 10% on October 1, 2019. The ROU asset (recognized within property and equipment) was measured at an amount equal to the corresponding initial lease liability.

Refer to Note 2 within the Company's financial statements for more details on IFRS 16, and the Company's significant accounting policy in connection therewith.

*New Interpretation IFRIC 23 - Uncertainty over Income Tax Treatments*

On June 7, 2017, the IASB issued IFRIC Interpretation 23 - Uncertainty over Income Tax Treatments. The Interpretation provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. The Interpretation is applicable for annual periods beginning on or after January 1, 2019.

There were no reporting changes as a result of adopting the new Interpretation.

## FINANCIAL RISK MANAGEMENT

The Company's financial instruments consist of the following:

| Financial assets: | Classification: | Subsequent measurement: |
|---|---|---|
| Cash | FVTPL | Fair value |
| Receivables | Amortized cost | Amortized cost |
| Deposit | Amortized cost | Amortized cost |
| Loans receivable | Amortized cost | Amortized cost |

| Financial liabilities: | Classification: | Subsequent measurement: |
|---|---|---|
| Accounts payable and accrued liabilities | Other financial liabilities | Amortized cost |
| Lease liability | Other financial liabilities | Amortized cost |

The Company's financial instruments with the exception of cash approximate their fair values. Cash, under the fair value hierarchy is based on Level 1 quoted prices in active markets for identical assets or liabilities.

The Company is exposed to varying levels and degrees of risk, including credit risk, liquidity risk, and market risk as detailed in Note 11 to the financial statements.

## SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

Nextleaf prepares its financial statements in conformity with IFRS which requires management to make judgments estimates and assumptions that affect the report amounts of assets, liabilities and contingent liabilities at each reporting date and the reporting amounts of income and expenses during each reporting period. Nextleaf details its significant areas of estimation uncertainty, and significant areas of judgment within its significant accounting policies in Note 3 to its annual audited financial statements for the year ended September 30, 2019.

## RISKS AND UNCERTAINTIES

The Company operates in rapidly changing environment that involves risks and uncertainties and as a result management expectation may not be realized for a number of reasons. An investment in Nextleaf common shares is speculative and involves a high degree of risk and uncertainty. The current regulatory uncertainty poses additional risks and uncertainties which may materially affect management's expectations.

### Regulatory Risks

The operations of the Company will be subject to various laws governing the production and distribution of cannabis oil, taxes, labour standards and occupational health, toxic substances, land use, water use, and other matters.

The *Cannabis Act* is a new regime and as such, revisions to the regime could be implemented which could have an impact on operations.

Furthermore, although the operations of each of Nextleaf are currently carried out in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner which could limit or curtail the ability to produce cannabis oil and related products. Amendments to current laws and regulations governing the distribution, transportation and/or production of cannabis oil or related products, or more stringent implementation thereof could have a substantial adverse impact.

### Ongoing Need for Financing

As the Company has recently commenced generating revenues, its ability to continue operations will be largely reliant on its continued attractiveness to equity investors. The Company is expected to incur operating losses as it continues to expend funds to develop its business operations. Even if its financial resources are sufficient to fund its current operations, there is no guarantee that the Company will be able to achieve its business objectives. The continued development of Nextleaf is expected to require additional financing to fund further growth. The failure to raise such capital could result in the delay or indefinite postponement of current business objectives or the going out of business. The primary source of funding available to the Company will consist of equity financing. There can be no assurance that additional capital or other types of financing will be available if needed or that, if available, the terms of such financing will be favourable. In addition, from time to time, the Company may enter into transactions to acquire assets or the shares of other corporations. These transactions may be financed wholly or partially with debt, which may temporarily increase the Company's debt levels above industry standards.

### Requirement for Licences

The Company's facility received Health Canada licensing (Standard Processing Licence) on September 9, 2019. The licence holder is Nextleaf Labs Ltd. (see pending acquisition of Nextleaf Labs Ltd. by the Company, "Share Purchase Agreement – Nextleaf Labs Ltd." within "Description of the Business"). The Company is required to remain in compliance with current and evolving Health Canada Regulations and City of Coquitlam requirements to ensure it operates in compliance with licensing and regulatory requirements for the duration of the licence period and subsequent thereto in order to remain ongoing licensing and renewal. The Company's commercial operations and the ability to continue as a going concern are dependent on the Company acquiring the licence from Nextleaf Labs Ltd., and remaining compliant.

### Competition

The cannabis production industry is competitive in all of its phases. The Company will face strong competition from other companies in connection with such matters. Many of these companies have greater financial resources, operational experience and technical capabilities than Nextleaf. As a result of this competition, the Company may be unable to maintain its operations or develop them as currently proposed, on terms it considers acceptable or at all. Consequently, the revenues, operations and financial condition of the Company could be materially adversely affected.

Because of early stage of the industry in which Nextleaf operates, the Company may face additional competition from new entrants. If the number of users of cannabis in Canada increases, the demand for products will increase and expects that competition will become more intense, as current and future competitors begin to offer an increasing number of diversified products. To remain competitive, the Company will require a continued high level of investment in research and development, marketing, sales and client support. The Company may not have sufficient resources to maintain research and development, marketing, sales and client support efforts on a competitive basis which could materially and adversely affect the business, financial condition and results of operations.

## APPROVAL

The Board of Directors of Nextleaf have approved the disclosures in this MD&A.