



Direct Communication Solutions, Inc.  
Management's Discussion and Analysis  
For the Three Months Ended March 31, 2022

Amounts in United States dollars unless stated otherwise

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis of Direct Communication Solutions, Inc. (the "Company", "DCS", "we" and "our" refer to Direct Communication Solutions, Inc.) provides an analysis of the Company's performance and financial condition for the three months ended March 31, 2022. This management discussion and analysis should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2021 (the "**Financial Statements**"), which were prepared in accordance with International Financial Reporting Standards ("**IFRS**").

All amounts referred to in this management discussion and analysis are prepared in accordance with IFRS and presented in United States dollars (\$ or US\$), unless otherwise indicated. C\$ refers to Canadian dollars.

The following information is prepared as at May 30, 2022.

### **Forward-looking Statements**

This management discussion and analysis contains "forward-looking information" which may include, but is not limited to, statements with respect to the future financial or operating performances of the Company; revenues; the timing and amount of estimated future operating, capital and development expenditures and requirements for additional capital. Often, but not always, forward-looking information can be identified by the use of words such as "plans", "expects", "is expected", "budget", "scheduled", "estimates", "forecasts", "intends", "anticipates", or "believes", or variations (including negative variations) of such words and phrases, or state that certain actions, events or results "may", "could", "would", "might", or "will" be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results to differ from those anticipated, estimated or intended. Forward-looking statements contained herein are made as of the date of this management discussion and analysis based on the opinions and estimates of management, and the Company disclaims any obligation to update any forward-looking statements, whether as a result of new information, estimates or opinions, future events or results or otherwise. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, potential investors should not place undue reliance on forward-looking statements.

## Overview

Direct Communication Solutions, Inc. provides Internet of Things (IoT) products, services, and solutions. The Company has two main focuses to its business: (i) Hardware distribution, where we resell products from CalAmp and ATrack Technology Inc. and (ii) Software as a Service "SaaS" solutions. Our products and solutions enable devices to communicate with each other and with server or cloud-based application infrastructures.

The Company's current SaaS solutions include MiFleet™, which provides fleet and vehicle SaaS telematics, MiSensors™, which provides machine-to-machine device management and service enablement for wireless sensors and MiFailover™, which provides high-speed wireless internet failover to small and medium sized businesses as a redundancy solution to continue to run their business in the event the internet is not available. In addition, we have recently deployed MiConnectivity to provide wireless data connectivity for global connectivity through our fully integrated SIM management platform and MiServices™ to provide engineering support to its distribution customers. These services include software development, hardware integration and logistics support such as SIM card insertion, activation, provisioning, labeling and device readiness checks.

Our corporate headquarters is in San Diego, California.

Incorporated in 2006, the Company traditionally has been a distributor of IoT components and a system integrator that assisted clients in installing such components into their installed systems and applications. The Company has focused on providing hardware items and solutions that have aided in data collection, analysis and management.

The global costs and prices of IoT sensors and products continue to drop in price and margin. As a response to this, and an interest to develop more vertically-integrated, comprehensive solutions, we began to develop software applications and databases that can analyze and manage the data that its IoT hardware has traditionally just collected. This provides us the opportunity to increase its gross and net profit margins by providing more services and software – through the cloud and/or via a SaaS/MaaS (Module as a Service) business model.

The Company has traditionally sold within various hardware-related vertical markets that are tied to the broad IoT market. These areas have included markets such as fleet management, healthcare, retail point-of-sale, industrial, energy & utilities, and safety and security. As the Company transitions to software, SaaS and services it can now address traditional software application markets. In addition, we are planning to launch applications within the beer, transportation and cannabis marketplaces. Both the beer and cannabis markets have very similar needs when it comes to sensors and utilizing the big data from those sensors. Both are temperature sensitive and have a very limited shelf-life, therefore, the logistics data that can be obtained from these sensors makes the operational side of these verticals so critical.

We intend to continue to leverage our long-standing relationship with its strategic partners and jointly build unique IoT solutions based on its integrated third party equipment along with new application software. This mixed hardware and software implementation will allow us to build new, more robust, solutions that address multiple customer problems operating on a single Company platform.

## **Significant Highlights**

The following highlights and developments for the three months ended March 31, 2022 and to the date of this management discussion and analysis:

- Announced partnership with Simetric to deliver a global cross-carrier, single pane of glass IoT device management platform to consolidate wireless connectivity providers and optimize IoT rate plan utilization and business processes.
- Announced listing on the Frankfurt Stock Exchange (FSE:7QU)
- Announced strategic partnership with Telenor Group, one of the world's major mobile operators to provide global wireless connectivity to our customers and expand our market reach for IoT solutions.
- Announced our intention to pursue an uplisting to the NASDAQ Stock Exchange.
- Announced strategic partnership with Streamline Transportation Technologies in Canada to kick-off our international expansion strategy for SaaS by delivering next-generation video telematics solutions.
- Upgraded firmware updates over-the-air for approximately 200k devices that are deployed in the field to comply with the AT&T 3G sunset to ensure continued operation in the field and comply with AT&T 4G network requirements.
- Onboarded 4 new resellers to promote and sell all DCS related SaaS solution offerings.
- Achieved positive EBIDTA and Net Profit in a quarter and increased overall gross margin by continuing to focus and invest in our SaaS solution strategy.

## **COVID-19 Impact on Operations and Financial Position**

In March 2020 the World Health Organization declared coronavirus COVID-19 a global pandemic. The outbreak led governments and other authorities around the world, including federal, state and local authorities in the United States, to impose measures intended to control its spread, including restrictions on freedom of movement and business operations such as travel bans, border closings, business closures, quarantines and shelter-in-place orders. The outbreak and preventative or protective actions that governments have taken in respect of this coronavirus have resulted in a period of business disruption, reduced customer traffic, negative impact on our order fulfillment, reduced operations, and has adversely affected workforces, economies, and financial markets globally. Furthermore, several of our key products are manufactured in Asia in locations subject to quarantines and factory closures. The magnitude of the impact of COVID-19 outbreak on our business and operations remains uncertain. In addition, we may experience disruptions to our business operations resulting from quarantines, or other movement and restrictions on the ability of our employees to perform their jobs that may impact our ability to develop and design our products and solutions in a timely manner or meet required customer commitments.

## **Outlook**

DCS is a value-added reseller of IoT telematics devices, and a developer of our own end-to-end SaaS based intelligent business solutions. Our customers include technology distributors, cellular operators fleet service providers and any business that needs to monitor or draw data from their machine-based assets. We serve our clients by simplifying IoT Technologies, making them less costly, easier to deploy and overall, more efficient. Since 2018 we started to transition from a hardware reseller to a SaaS based, recurring revenue, customized solutions provider, offering turnkey IoT solutions for new and existing customers. SaaS and other services revenue accounted for approximately 8% of total corporate revenue for the three months ended March 31, 2022.

We continue to expand the industries we serve which now include property management, restaurants, healthcare, cold chain management, retail, offices, fleet management, public safety, and construction.

The large cellular providers are moving towards a technology sunset on their legacy 2G networks. This will affect all 2G devices deployed on their networks and force a transition to solutions with 4G technologies. We believe our relationships with the cellular providers along with our product and service offerings, will allow us significant sales opportunities.

Total backlog for our products as of March 31, 2022 and March 31, 2021 was \$11.6 million and \$12.7 million, respectively. Our backlog for products increased year-over-year as we continue to experience significant supply shortages primarily caused by the lingering impact of the COVID-19 pandemic. As a result of the ongoing supply shortages, we reduced our workforce by 9 employees in September 2021. We continue to face delays in receiving products from key vendors and do not know at this time when these delays will be resolved. We are working closely with key vendors to reduce the delays and continue to meet our customers demands.

### Results of Operations for the Three Months Ended March 31, 2022

Revenues for the three months ended March 31, 2022 were \$7,799,913 compared to \$4,311,597 for the same period last year. Product revenue of \$7,198,709 was up 88% over the same period as last year as customers were delaying orders in 2021 due to the pandemic.

Solutions and other services revenue of \$601,204 was up 26% from the same period as last year.

Cost of revenues for the three months ended March 31, 2022 were \$5,392,898 compared to \$3,138,461 for the same period in 2021. The following tables summarize gross profit and gross margin:

	<b>Gross Profit</b>		<b>Gross Margin</b>	
	Q1 2022	Q1 2021	Q1 2022	Q1 2021
Products	\$ 1,982,420	\$ 843,596	27.5%	22.0%
Solutions and other services	424,595	329,540	70.6%	69.3%
Total	\$ 2,407,015	\$ 1,173,136	30.9%	27.2%

The Company went through and aggressively reworked the pricing models to achieve healthier margins. The Company also expanded the portfolio of product offerings which permitted higher margin sales.

General and administrative expenses for the three months ended March 31, 2022 were \$1,533,578 compared to \$1,430,332 for the same period in 2021. Compensation was slightly lower in Q1 2022 vs same period in last year. Increase in professional fees is mainly due to consulting fees for building complete IoT bundled solutions, services to raise public awareness of the Company and other corporate development. Decrease in other is mainly due to a decrease in the provision for bad debts.

Research and development costs for the three months ended March 31, 2022 were \$191,149 compared to \$343,569 for the same period in 2021.

Net income for the three months ended March 31, 2022 was \$630,120 compared to loss of \$196,988 for the same period in 2021. The increase in net income was primarily the result of \$3,362,909 and 1,233,879 increases in revenue and gross profit, respectively.

## Summary of Quarterly Results

The following table is based on the Company's financial statements prepared in accordance with IFRS. Amounts are in US\$ except share numbers.

	Q1 2022	Q4 2021	Q3 2021	Q2 2021
	\$	\$	\$	\$
Revenue				
Products	7,198,709	5,172,283	2,303,477	3,232,185
Solutions & other services	601,204	506,853	524,181	474,947
	<u>7,799,913</u>	<u>5,679,136</u>	<u>2,827,658</u>	<u>3,707,132</u>
Operating Expenses	1,724,727	2,105,385	1,510,635	1,759,758
Net income (loss)	682,288	(563,602)	(240,662)	(771,062)
Basic income (loss) per share	0.04	(0.03)	(0.02)	(0.05)
Fully-diluted income (loss) per share	0.04	(0.03)	(0.02)	(0.05)
Weighted average number shares outstanding - basic	16,135,640	15,634,727	15,634,727	15,631,640
Weighted average number shares outstanding – diluted	16,135,640	15,634,727	15,634,727	15,631,640
Total fully diluted shares	<u>20,659,587</u>	<u>20,159,587</u>	<u>20,159,587</u>	<u>20,184,587</u>
	Q1 2021	Q4 2020	Q3 2020	Q2 2020
	\$	\$	\$	\$
Revenue				
Products	3,835,800	3,860,012	2,696,150	2,669,412
Solutions & other services	475,797	554,597	508,058	527,889
	<u>4,311,597</u>	<u>4,414,609</u>	<u>3,204,208</u>	<u>3,197,301</u>
Operating Expenses	1,773,901	1,706,328	1,203,228	1,439,993
Net income (loss)	(196,988)	(537,970)	(245,673)	(494,580)
Basic income (loss) per share	(0.01)	(0.04)	(0.02)	(0.04)
Fully-diluted income (loss) per share	(0.01)	(0.04)	(0.02)	(0.04)
Weighted average number shares outstanding - basic	15,208,916	13,924,261	13,403,300	13,403,300
Weighted average number shares outstanding – diluted	15,208,916	13,924,261	13,403,300	13,403,300
Total fully diluted shares	<u>20,558,444</u>	<u>19,923,444</u>	<u>17,229,580</u>	<u>17,254,580</u>

The Company's business typically undergoes seasonal variation in the fiscal quarter ended March 31 due to disruptions in the manufacturing of hardware components in Asia driven primarily by the observance of the lunar new year holidays during that period and in the fiscal quarter ended September 30 due to summer vacations of the industrial buyers representing business or government customers.

## **Liquidity and Capital Resources**

The Company defines capital as consisting of issued share capital, reserves and accumulated deficit. We expect to fund the operating costs of the Company over the next twelve months from expanding sales of our current products and solutions that support the growth of the Company and raising additional capital as necessary. The Company's continuing operations and its financial viability is dependent upon the extent to which it can successfully raise the capital to implement its future plans and ultimately on generating sufficient revenue to attain profitable operations. These factors indicate the existence of an uncertainty that may cast doubt about the Company's ability to continue as a going concern. At March 31, 2022, the Company is not subject to any externally imposed capital requirements or debt covenants.

On February 19, 2021, the Company was granted a second loan (the "Second Loan") from TAB Bank ("TAB") in the aggregate amount of \$434,105 pursuant to the Paycheck Protection Program (the "PPP") established as part of the Coronavirus Aid, Relief and Economic Security Act ("CARES Act") in the United States. The Second Loan, which was in the form of a Note dated February 19, 2021 matures February 19, 2026 and bears interest at a rate of 1.00% per annum, payable in 44 equal monthly payments commencing on June 19, 2022. The Second Loan may be prepaid at any time prior to maturity with no prepayment penalties. The Second Loan and accrued interest are forgivable after twenty-four weeks as long as the borrower uses the proceeds for eligible purposes, including payroll, benefits, rent and utilities, and maintains its payroll levels. The Company intends to use the entire Second Loan amount for eligible purposes.

On March 5, 2021, the Company received notice from the U.S. Small Business Administration a loan (the "Loan") dated April 10, 2020 from TAB in the aggregate amount of \$422,500 pursuant to the PPP was forgiven in full.

In February and March 2021, the Company issued 553,140 shares due to the exercise of warrants for proceeds of \$426,512.

In July 2021, the Company issued 4,000 shares due to the exercise of options for proceeds of \$3,880.

On August 5, 2021, the Company received notice from TAB that the Second Loan was forgiven in full.

In November and December 2021, the Company had issued convertible promissory debentures totalling \$275,000. The debentures accrued interest at a rate of 10% per annum and was payable semi-annually unless the holder elected to defer payment. All unpaid principal and accrued interest are due two years from date of issuance. The holder of the debenture at any time could convert in whole or any part principal and interest into common shares of the Company at a conversion price of \$1.00 per share. In the event of default, all principal and interest due shall become immediately due and payable.

At March 31, 2022 and December 31, 2021, the outstanding balance on the credit facility was \$483,856 and \$1,670,833, respectively.

The Company has a credit facility with TAB whereby it advances funds to the Company up to 90% of the Company's domestic receivables less than 90 days from invoice date and not subject to offset up to \$2,000,000. TAB charges monthly interest at a rate greater of (a) 90-Day LIBOR rate plus 4.50% and (b) 6.41%. In addition, there is an administration fee equal to 0.008% per diem of the outstanding daily obligations. The credit facility is secured by a lien on substantially all the assets of the Company.



Cash flows provided in operating activities during the three months ended March 31, 2022 were \$1,013,485 compared to \$1,488,925 used during the same period last year.

Cash flows used in investing activities during the three months ended March 31, 2022 were \$Nil versus \$3,399 during the same period last year. The difference is primarily the purchase of property and equipment during the same period last year.

Cash flows used in financing activities during the three months ended March 31, 2022 were \$1,000,677 compared to \$1,146,087 provided during the same period last year. The Company received \$300,000 during the March 31, 2022 compared to \$434,105 for the same period in 2021 from the Paycheck Protection Program. During March 31, 2021, the Company received \$426,512 from the exercise of 533,140 warrants while there was \$Nil received during the March 31, 2022. Net repayments on credit facility were \$1,186,977 during the three months ended March 31, 2022 while net borrowings under our credit facility were \$341,911 during the same period in 2021.

At March 31, 2022, the Company had working capital of \$1,314,788 (December 31, 2021 – deficiency of \$32,630).

## **Capital Resources**

### Share Capital

The Company has authorized 40,000,000 shares with a par value of \$0.00001 per share.

On January 7, 2020, the Company completed its initial public offering and sold 1,328,500 shares of common stock for net proceeds of \$1,773,063 after underwriter's commission and offering expenses of \$248,085 of which \$47,102 were paid during the year ended December 31, 2019.

On December 15, 2020, the Company completed an offering and sold 1,695,200 shares of common stock at C\$1.05 per share for net proceeds of \$1,209,226 after share issuance costs of \$123,061.

In March 2021, 533,140 common shares were issued due to the exercising of 533,140 warrants for proceeds of \$426,512.

In July 2021, 4,000 common shares were issued due to the exercising of 4,000 options for proceeds of \$3,880.

At December 31, 2021, the Company had 15,635,640 shares issued and outstanding with a par value of \$0.00001.

In January 2022, 500,000 common shares of common stocks were issued at CAD\$0.55 in exchange for non-arm's length consulting fee for corporate development.

### Warrants

In January 2020 in conjunction with the Company's initial public offering, the Company issued warrants to the underwriter to purchase 106,280 shares of common stock with an exercise price of C\$2.00 per share and

a term of two years.

In November 2020 in a private offering, the Company issued warrants to purchase 880,000 shares of common stock with an exercise price of \$0.80 per share and a term of six months for proceeds of \$30,556.

In November and December 2020, in conjunction with an offering, the Company issued warrants to placement agents to purchase 118,664 shares of common stock with an exercise price of \$0.80 per share and a term of six months.

In February and March 2021, 533,140 shares were issued due to the exercise of warrants for proceeds of \$426,512.

In May and June 2021, 465,524 warrants expired and were forfeited.

In January 2022, all outstanding warrants were expired.

### Stock Options

In October 2017, the Company's board of directors and stockholders approved the 2017 Stock Plan under which 3,500,000 shares of common stock are reserved for the granting of incentive stock options, non-statutory stock options, stock appreciation rights, restricted stock and performance awards to employees, directors and consultants. Recipients of stock option awards are eligible to purchase shares of the Company's common stock at an exercise price equal to no less than the estimated fair market value of such stock on the date of grant. The maximum term of awards granted under the 2017 Plan is ten years and vesting is determined by the board of directors. Stock awards are generally not exercisable prior to the applicable vesting date, unless otherwise accelerated under the terms of the applicable stock plan agreement. Unvested shares of the Company's common stock issued in connection with an early exercise allowed by the Company may be repurchased by the Company upon termination of the optionee's service with the Company. The vesting terms of each option grant are at the discretion of the Board of Directors

In June 2019, the Board of Directors and Stockholders of the Company agreed to increase the number of authorized shares reserved for issuance under the Company's 2017 Stock Plan from 3,500,000 to 4,100,000 shares and add an annual evergreen feature that will adjust the number of authorized shares reserved to an amount equal to 29.99% of the Company's issued capital stock (other than the maximum number of shares that may be issued through Incentive Stock Options, which is fixed at 4,100,000 shares). As a result of the evergreen feature, the number of authorized shares for issuance increased to 4,528,040 effective January 1, 2021.

At March 31, 2022, 3,636,885 options were outstanding of which 2,668,090 are vested and are exercisable at \$0.47 per option; 102,605 are vested and exercisable at \$1.53 per option; 6,875 are vested and exercisable at \$0.79 per option; 36,000 are vested and exercisable at \$0.42 per option; 29,688 are vested and exercisable at \$0.41 per option; 4,167 are vested and exercisable at \$0.41 per option; 59,557 are vested and exercisable at \$0.59 per option. The Company recognized stock-based compensation expense for the three months ended March 31, 2022 of \$263,048.

On March 14, 2022, the Company granted 435,000 stock options to officers with an exercise price of \$0.59 which was the fair market value of a share of stock on the date of the grant.

On February 28, 2022, the Company cancelled 980,000 stock options. of which 100,000 were exercisable at US\$0.79, 485,000 were exercisable at \$1.53, 375,000 were exercisable at \$1.59, and 20,000 were exercisable at \$1.68.

On February 24, 2022, the Company granted 100,000 stock options to officers with an exercise price of \$0.41 which was the fair market value of a share of stock on the date of the grant.

On February 9, 2022, the Company cancelled 435,000 stock options. of which 85,000 were exercisable at \$0.79, 50,000 exercisable at \$1.53, and 300,000 exercisable at \$1.59.

On February 4, 2022, the Company granted 175,000 options with an exercise price of \$0.41 which was the fair market value of a share of stock on the date of the grant.

On June 1, 2021, the Company granted 125,000 options of which 100,000 to a director. The options are exercisable at \$0.97 which was the fair market value of a share of stock on the date of the grant.

In June 2021, the Company modified an option for a former Board of Director to extend the period to exercise 66,667 vested options from 90 days to one year (the "Modification"). The Company recognized an additional \$1,694 in stock-based compensation associated with the Modification, included within total stock-based compensation of \$629,167.

On March 19, 2021, the Company granted 675,000 options of which 375,000 were to certain officers. The options are exercisable at \$1.59 which was the fair market value of a share of stock on the date of the grant.

On May 20, 2020, the Company granted 290,000 options of which 100,000 to a director. The options are exercisable at \$0.79 which was the fair market value of a share of stock on the date of the grant.

On January 7, 2020, the Company granted 755,000 options to certain of its directors and officers. 735,000 of the options are exercisable at \$1.53 (\$2.00 CAD equivalent) and 20,000 of the options are exercisable at \$1.68 per share (\$2.20 CAD equivalent). As our CEO is more than a 10% shareholder, per incentive stock option rules in the U.S., his exercise price is 110% of the fair market value of a share of stock on the effective date of grant of the option.

### **Related Party Transactions**

Key management personnel include those persons having authority and responsibility for planning, directing and controlling the activities of the Company as a whole. The Company has determined that key management personnel consist of executive and non-executive members of the Company's Board of Directors and corporate officers.

Rich Gomberg, the Company's former CFO is also a former employee of CFO Connect. Ed O'Sullivan, a former member of the Company's Board of Directors, is managing partner of CFO Connect.

The Company is a party to a Business Services Agreement with CFO Connect whereby CFO Connect provides CFO services. The Company recorded professional fees the consolidated statement of operations associated with this agreement \$83,850 for the three months ended March 31, 2022. As of March 31, 2022 and December 31, 2021, the Company owed \$19,500 and \$9,325 under this agreement, respectively.

John Hubler, a member of the Company's Board of Directors, is a partner of BH IoT Group.

In January 2022, the Company entered into an agreement with BH IoT Group to provide consulting services to launch MiConnectivity. The agreement is month-to-month.

Mike Zhou, a member of the Company's Board of Directors, is the owner of MYZ Corporate Relations, Ltd.

In May 2021, the Company entered into an agreement with MYZ Corporate Relations, Ltd. To provide consulting services on strategic matters related to business development opportunities, product development and marketing strategies for a monthly fee of \$8,000. The agreement is effective for one year and will automatically renew annually unless terminated by either party. The Company recorded \$21,000 of professional fees on the consolidated statement of operations for the three months ended March 31, 2022.

In March 2022, the Company entered into an agreement with Zeus Capital Ltd. to assist the company with corporate finance and strategic initiatives for a monthly fee of \$15,000. The agreement is effective for one year and will automatically renew annually unless terminated by either party. The Company recorded \$45,000 of professional fees on the consolidated statement of operations for the three months ended March 31, 2022. Also in April 2022, the Company appointed Mr. Lichtenwald as the new CFO and Mr. Lichtenwald is a principal of Zeus Capital. In January 2022, 500,000 common shares of common stocks were issued at CAD\$0.55 in exchange for consulting fee for corporate development.

Remuneration attributed to key management personnel can be summarized as follows:

	<b>Three Months Ended March 31, 2022</b>	<b>Three Months Ended March 31, 2021</b>
	\$	\$
Salary	400,197	242,859
Consulting fees	219,389	111,370
Share-based compensation	63,684	42,837
<b>Totals</b>	<b>683,270</b>	<b>397,066</b>

As of March 31, 2021, \$51,084 (December 31, 2021 – \$46,503) was included in accounts payable and accrued liabilities for fees owed to related parties.

### **Critical Accounting Estimates**

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. Information about critical estimates in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated interim financial statements are, but not limited to the following:

- Allowance for doubtful accounts receivable - The Company makes allowances for doubtful accounts based on its best estimate of the amount of probable credit losses in existing accounts receivable. These are determined based on analyzing known uncollectible accounts, aged

receivables, economic conditions, historical losses, and changes in customer payment cycles and the customers' credit-worthiness.

- Provision for excess and obsolete inventory - Inventory is valued at the lower of cost and net realizable value. Net realizable value for inventories is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. All of these estimates involve uncertainty relating to future pricing, demand and market conditions. Provisions are made in profit or loss of the current period on any difference between book value and net realizable value.
- Fair value of stock options and warrants - Determining the fair value of warrants and stock options requires judgements related to the choice of a pricing model, the estimation of stock price volatility, the expected forfeiture rate and the expected term of the underlying instruments. Any changes in the estimates or inputs utilized to determine fair value could have a significant impact on the Company's future operating results or on other components of shareholders' equity (deficiency).
- Income taxes - Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in profit or loss both in the period of change, which would include any impact on cumulative provisions, and future periods. Deferred tax assets, if any, are recognized to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse.
- Estimated product returns - Revenue from product sales is recognized net of estimated sales discounts, credits, returns, rebates and allowances. The return allowance is determined based on an analysis of the historical rate of returns, industry return data, and current market conditions, which is applied directly against sales. The Company recognizes product returns when incurred due to the infrequent occurrence of returns.
- Employee retention tax credits – Under the provisions of the CARES Act (Note 9), the Company is eligible for refundable employee retention credits subject to certain criteria. In connection with the CARES Act, the Company adopted a policy to recognize the employee retention credit when received given the uncertainty of when the credit will be received. The Company recorded \$24,247 employee retention tax credit during the year ending December 31, 2021, which is included in other income in the consolidated statements of operating loss.

### **Critical Accounting Judgements**

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are, but are not limited to, the following:

- Deferred income taxes – judgements are made by management to determine the likelihood of whether deferred income tax assets at the end of the reporting period will be realized from future taxable earnings. To the extent that assumptions regarding future profitability change, there can be an increase or decrease in the amounts recognized in respect of deferred tax assets as well as the amounts recognized in profit or loss in the period in which the change occurs.
- Going concern – As disclosed in Note 1 to the consolidated financial statements.

## Financial Instruments

The Company's financial assets include cash and amounts receivable. The carrying value of cash and amounts receivable approximates their fair value due to their short term to maturity.

The Company's financial liabilities include accounts payables, the Second Loan, credit facility, and customer deposits. The carrying value of these items approximates their fair value due to their immediate or short term to maturity.

## Financial Risk Factors

### *Credit risk*

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company places its cash with institutions of high credit worthiness. Management has assessed there to be a low level of credit risk associated with its cash balances.

The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the demographics of the Company's customer base, including the default risk of the industry and country in which customers operate, as these factors may have an influence on credit risk. Approximately 30% of the Company's revenue (2021 - 39%) is attributable to sales transactions with one customer.

The Company has established a credit policy under which each major new customer is analyzed individually for creditworthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes external ratings, when available, and in some cases bank references. Purchase limits and terms are established for each customer and reviewed periodically. Customers that fail to meet the Company's benchmark creditworthiness may transact with the Company only on a prepayment basis.

In monitoring customer credit risk, customers are grouped according to their credit characteristics, including whether they are an individual or legal entity, whether they are a wholesale, retail or end-user customer, geographic location, industry, aging profile, maturity and existence of previous financial difficulties. Trade and other receivables relate mainly to the Company's wholesale and retail customers.

Trade and other receivables consist of:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Accounts Receivable	\$ 4,126,185	\$ 4,024,625
Allowance for doubtful accounts	(303,839)	(121,319)
<b>Total</b>	<b>\$ 3,822,346</b>	<b>\$ 3,903,306</b>

Aged trade receivable listing:

<b>Days outstanding</b>	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Current	\$ 2,664,453	\$ 3,046,604
1 – 30	718,991	690,882

31 – 60	572,140	174,211
61 – 90	12,338	32,824
> 90	158,263	80,104
<b>Total</b>	<b>\$ 4,126,185</b>	<b>\$ 4,024,625</b>

### *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.

The Company examines current forecasts of its liquidity requirements so as to make certain that there is sufficient cash for its operating needs. These forecasts take into consideration matters such as the Company's plan to use debt for financing its activity, compliance with any required financial covenants and liquidity ratios, and compliance with external requirements such as laws or regulation.

The Company has a factoring agreement with external funding. The Company's accounts payable and accrued liabilities have contractual terms of 30 to 90 days, with the exception of one vendor where payment terms of 36 months have been granted. The Company is exposed to liquidity risk.

### *Market risk*

#### a) Currency Risk

The Company is located in the United States and virtually all transactions including the company's sales and debt are negotiated in US dollars.

#### b) Interest Rate Risk

The Company's debt has fixed interest rates and are not exposed to interest rate risk until maturity. The Company's credit facility is variable based on the 90 day LIBOR rate. A 1% increase in the 90 day LIBOR rate in 2020 would result in approximately \$115 additional interest expense for the three months ended March 31, 2022.

#### c) Price Risk

Price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices other than those arising from interest rate risk, financial market risk or currency risk. The Company is not exposed to significant price risk.

### **Off-Balance Sheet Arrangements**

The Company has not entered into any off-balance sheet arrangements.

### **SUBSEQUENT EVENTS**

The Company evaluated subsequent events through the date the consolidated financial statements are

available for issuance.

***Issuance of Stock Options***

In May 2022, the Company granted 490,000 stock options. Of those, 100,000 options are exercisable at a price of \$0.79 per share, and 390,000 are exercisable at a price of \$1.20. All the options are exercisable for a term of five years. All the options were granted in accordance with the Company's stock option plan and are subject to vesting provisions.

***Convertible Debenture Offering***

In April 13, 2022, the Company closed convertible debenture financing for the aggregate amount of \$100,000 (U.S.). Subscribers may convert all or part of the principal amount outstanding under the debentures into shares of common stock of the company. The debentures are convertible into units at the higher of \$1.19 or a price equal to the price of the shares or units of the next financing carried out before the second anniversary of the closing date less a 30-per-cent discount.

The units comprise a share and one-half of one warrant, where a whole warrant shall be exercisable at \$0.40 per common share for a two-year term. The debentures have a maturity date of the second anniversary of the closing date and bear an interest rate of 10 per cent per annum, payable semi-annually.