



Direct Communication Solutions, Inc.  
Management's Discussion and Analysis  
For the Year ended December 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 year ended December 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, 2022 (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 April 19, 2023.

### **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. We deliver enhanced one-stop solutions that connect assets to increase visibility, operational efficiency, and profitability. We provide our solutions and services to a variety of industries including, Supply Chain Logistics, Transportation, Health Care, and Food & Beverages. We are a chosen global partner of service providers, value-added collaborators, system integrators, and enterprises due to our commitment to quality and demonstrated experience. We intend to continue expanding our long-standing relationships and work strategically with our partners, to jointly build leading IoT solutions based on integrated hardware, cloud-based software, and other services.

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 managed services solution that includes all-inclusive device readiness program and engineering support. These services include software development, hardware integration and logistics support from SIM to Shipment, including device preparation, custom labeling, packaging, configuration confirmation, and system-side 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. Currently, the company has three primary business focuses on revenue stream and growth generation.

**Smart Hardware Provider.** The company utilizes smart hardware from an expanding group of suppliers to deploy through our strategic agreements with channel partners including Verizon, AT&T, U.S. Cellular, Ingram Micro, Synnex and Hyperion Partners as the basis to develop our own end-to-end SaaS based intelligent business solutions.

**SaaS Software Solutions Provider.** Our products and services then enable devices to communicate with each other and with server or cloud-based application infrastructures. These software applications address and solve real-world data collection and monitoring problems to best serve our customers and manage their evolving business requirements.

**Industry Technology Innovation.** DCS has sold to customers within various smart 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 and utilities and safety and security. As the company applies its core competencies it can now address a broadening spectrum of software application markets.

DCS is continuing to evolve from our smart hardware distribution base of mobile broadband hardware to providing End-to-End solutions for mobile internet, M2M, and vertical markets. We serve our clients by simplifying IoT technologies, making them less costly, easier to deploy and overall, more efficient. We intend to continue to leverage our long-standing relationships with strategic partners and jointly build unique IoT solutions based on integrated third-party equipment along with our application software. This mixed hardware and software implementation allows 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 year ended December 31, 2022 and to the date of this management discussion and analysis:

#### December 31, 2022

- Launch the first phase of the SMART ESG Program to provide Cloud-Based IoT solutions for ESG Assets and Data market
- Listed on Frankfurt Stock Exchange under the trading symbol “7QU”.
- Collaborated with UScellular to provide 4G LTE Wireless upgrade for Duplin County’s 157 school buses in North Carolina.
- Closed the fully subscribed \$1,500,000 USD unsecured convertible debenture.
- Launch of MiEbike: a Cloud-Based Asset Tracking Solution for the Growing E-Bike Market.
- Filing of registration statement for proposed initial public offering and application for up-listing to NYSE American.
- Launch of IPO for up-listing to NYSE American.
- Reverse stock split/consolidation of its common stock on seven old common shares for one new common shares.
- Partnering with VisionTrack to provide AI powered video telematics to the North American Market.
- Henriksen Concrete Washout Systems selected DCS cloud-based IoT solutions to manage and monitor their high-value assets.
- DCS and Cellcom announced enhanced partnership for IoT solutions on their 4G network.

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

In March 2020, the World Health Organization declared COVID-19 ("COVID-19" or the "pandemic") to be a public health pandemic of international concern, which has led to adverse impacts on the U.S. and global economies and continues to impact our supply chain and operations. More recently, we have experienced supply shortages as a result of global supply imbalances driven by component shortages, disruptions in accessible labor, other freight and logistical challenges and other related macro-economic factors. These supply imbalances negatively impacted all parts of our business during fiscal 2022 and have continued into fiscal 2023. It is difficult to predict the extent to which these factors will continue to impact our future business or operating results, which are highly dependent on uncertain future developments, including the severity of the continuing pandemic, the actions taken or to be taken by governments and private businesses in relation to the resolution of supply chain issues and component shortages. Because our business is dependent on telematics product sales, device installations and related subscription-based services, the ultimate effect of these factors may not be fully reflected in our operating results until future periods.

## **Outlook**

DCS is an emerging provider that offers Internet of Things ("IoT") and connectivity-related business-critical solutions and services. 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 10% (2021 – 14%) of total corporate revenue for the year ended December 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.

## **Non-IFRS Financial Measures – Adjusted EBITDA**

This MD&A references adjusted EBITDA, which is a non-IFRS financial measure. Adjusted EBITDA is not a recognized measure under IFRS, has no standardized meaning prescribed by IFRS and is therefore unlikely to be comparable to adjusted EBITDA presented by other companies. Rather, it is provided as additional information to complement IFRS measures by providing further understanding of the Company's results of operations from management's perspective. Accordingly, adjusted EBITDA should not be considered in isolation nor as a substitute for analysis of our financial information reported under IFRS.

We use non-IFRS financial measures to provide investors with supplemental measures of our operating performance and thus highlight trends in our core business that may not otherwise be apparent when relying solely on IFRS financial measures. We believe that securities analysts, investors, and other interested parties frequently use non-IFRS financial measures in the evaluation of issuers. There are certain limitations related

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to the use of non-IFRS financial measures versus their nearest IFRS equivalents. Investors are encouraged to review our financial statements and disclosures in their entirety and are cautioned not to put undue reliance on any non-IFRS financial measure and view it in conjunction with the most comparable IFRS financial measures. In evaluating non-IFRS financial measures, you should be aware that in the future we will continue to incur expenses similar to those adjusted in non-IFRS financial measures.

Adjusted EBITDA is a non-IFRS financial measure that we calculate as net income (loss) before tax excluding depreciation and amortization expense, share based expense, unrealized gain on inventory, finance expense, other asset impairments, unrealized loss on fair value of deposits and convertible note, and listing expenses. Adjusted EBITDA is used by management to understand and evaluate the performance and trends of the Company's operations. The following table shows a reconciliation of adjusted EBITDA to net income (loss) before tax, the most comparable IFRS financial measure, for the year ended December 31, 2022 and 2021:

	Year ended December 31, 2022	Restated Year ended December 31, 2021	Three months ended December 31, 2022	Restated Three months ended December 31, 2021
	\$	\$	\$	\$
Loss before tax	(2,234,315)	(1,995,114)	(2,067,308)	(786,402)
Accretion	104,467	-	95,837	-
Net changes in fair value	(104,290)		(344,877)	-
Amortization of debt issuance costs of credit facility		13,271	-	3,125
Depreciation	431,974	239,814	265,360	65,765
Finance cost for right of use assets	79,914	25,604	18,698	14,746
Gain on debt extinguishment	-	(856,605)	-	-
Interest expense	180,840	107,774	32,877	36,823
		-		-
Provision for excess and obsolete inventory	97,869	(159,932)	149,920	(219,058)
Share based expense	280,885	629,167	(245,867)	264,347
Tax fees	19,315	10,666	5,532	(3)
One-time costs related to up-listing to senior exchange				
One-time professional fees	1,445,141	-	883,541	-
Marketing expenses	193,302	-	52,682	-
<b>Adjusted EBITDA</b>	<b>495,102</b>	<b>(1,985,355)</b>	<b>(1,153,605)</b>	<b>(620,657)</b>

Revenues decreased by 24% (Gross Profit decreased by 49%) on a year-over-year basis from the corresponding last quarter of 2021. The decrease in EBITDA for the three months ended December 31, 2022 was primarily attributable to increased payroll expenses from hiring two key managers at the beginning of the quarter in the Accounting and Operation department. The Company continues further strengthen its management team and board in preparation for an up-listing to a senior exchange. For the year ended December 31, 2022, we have 16,829 active subscribers for our SaaS Solutions (13,180 active subscribers for the year ended December 2021) representing a growth of 28% in active subscribers.

## Key Business Metrics

The following table shows a summary of our key business metrics as of the periods presented:

	December 31, 2022
	\$
Annual recurring revenue (“ARR”)	2,123,019

## ARR

We believe that ARR is a key indicator of the trajectory of our business performance, enables measurement of the progress of our business initiatives, and serves as an indicator of future growth. We define ARR as the annualized value of subscription contracts that have commenced revenue recognition as of the measurement date. ARR highlights trends that may be less visible from the face of our financial statements due to ratable revenue recognition. ARR does not have a standardized meaning and is not necessarily comparable to similarly titled measures presented by other companies. ARR should be viewed independently of revenue and is not intended to be combined with or to replace it. ARR is not a forecast and the active contracts at the date used in calculating ARR may or may not be extended or renewed.

## Results of Operations for the Three Months ended December 31, 2022

Revenues for the three months ended December 31, 2022 were \$4,298,055 compared to \$5,679,136 for the same period last year. Product revenue of \$3,776,934 was down 27% over the same period as last year as customers were delaying orders into 2023.

Solutions and other services revenue of \$521,121 was up 3% from the same period as last year.

Cost of revenues for the three months ended December 31, 2022 were \$3,604,431 compared to \$4,323,330 for the same period in 2021. The following tables summarize gross profit and gross margin:

	<b>Gross Profit</b>		<b>Gross Margin</b>	
	Q4 2022	Q4 2021	Q4 2022	Q4 2021
	\$	\$	%	%
Products	323,517	1,043,430	8.6%	20.2%
Solutions and other services	370,107	312,376	71.0%	61.6%
Total	693,624	1,355,806	16.1%	23.9%

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 December 31, 2022 were \$3,445,842 compared to \$1,918,307 for the same period in 2021. Advertising and marketing expenses and professional fees increased in Q4 2022 vs same period in last year due to efforts to increase awareness within the investor community across the globe in preparation of the Company’s ongoing IPO process. Increase in depreciation and amortization of \$ 53,080 is mainly due to the commencement of intangible asset amortization. Facilities expense increased due to increased common area maintenance expense compared to the prior year.

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Compensation and benefits increased due to additional members on the team compared to the same quarter last year and a reclassification of research and development expense to compensation and benefits. Increase in other represents increase in corporate activities. The Company recognized \$134,669 of bad debt expense compared to \$95,288 the same quarter last year due to adjustment in management estimate in accordance to IFRS guidance.

Research and development costs for the three months ended December 31, 2022 were a downward adjustment of \$468,749 compared to \$187,078 for the same period in 2021. R&D activities were reclassified to compensation and benefits to better reflect the nature of the expenses.

Net loss for the three months ended December 31, 2022 was \$2,067,308 compared to \$786,402 for the same period in 2021. The increase in net loss was primarily the result of \$1,533,892 increases in loss from operations.

**Results of Operations for the Year Ended December 31, 2022**

Revenues for the year ended December 31, 2022 were \$22,586,306 compared to \$16,525,523 for the year ended December 31, 2021. Product revenue of \$20,300,579 was up 40% over the same period as last year.

Solutions and other services revenue of \$2,285,727 was up 15% from the same period as last year.

Cost of revenues for the year ended December 31, 2022 were \$15,556,883 compared to \$11,492,853 for the same period in 2021. The following tables summarize gross profit and gross margin:

	<b>Gross Profit</b>		<b>Gross Margin</b>	
	<b>YTD 2022</b>	<b>YTD 2021</b>	<b>YTD 2022</b>	<b>YTD 2021</b>
	\$	\$	%	%
Products	4,743,696	3,050,892	23.4%	21.0%
Solutions and other services	1,624,363	1,330,595	71.1%	67.1%
<b>Total</b>	<b>6,368,059</b>	<b>4,381,487</b>	<b>28.2%</b>	<b>26.5%</b>

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 year ended December 31, 2022 were \$8,154,887 compared to \$5,991,390 for the same period in 2021. Compensation was 10% higher vs last year due to additional members being added to the team. Advertising and marketing increased in the current year due to efforts to increase awareness within the investor community across the globe in preparation of the Company's ongoing IPO process. Increase in professional fees is mainly due to consulting fees incurred in connection to preparation of up-listing to NYSE. Increase in other represents the increase in corporate activities. Increase in depreciation and amortization is mainly due to the commencement of intangible asset amortization. The Company recognize \$224,795 of bad debt expense in the current year compared to \$95,288 last year due to adjustment in management estimate in accordance to IFRS guidance.

Research and development costs for the year ended December 31, 2022 were \$553,465 compared to \$1,158,289 for the year of 2021.



Net loss for the year ended December 31, 2022 was \$2,234,315 compared to \$1,995,114 for the same period in 2021. The increase in net loss was primarily due to no gain on debt extinguishment was recognized in the current year compared to \$856,605 being recognized in 2021.

### 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.

	Q4 2022	Q3 2022	Q2 2022	Q1 2022
	\$	\$	\$	\$
Revenue				
Products	3,776,934	4,112,623	5,212,313	7,198,709
Solutions & other services	521,121	578,113	585,289	601,204
	<u>4,298,055</u>	<u>4,690,736</u>	<u>5,797,602</u>	<u>7,799,913</u>
Operating Expenses	2,977,094	2,009,488	1,906,918	1,724,727
Net income (loss)	(2,067,306)	(914,377)	117,248	682,288
Basic income (loss) per share	(0.90)	(0.40)	0.05	0.30
Fully-diluted income (loss) per share	(0.90)	(0.40)	0.05	0.30
Weighted average number shares outstanding - basic	2,305,091	2,305,091	2,305,091	2,305,091
Weighted average number shares outstanding – diluted	2,305,091	2,305,091	2,305,091	2,305,091
Total fully diluted shares	<u>2,954,518</u>	<u>2,954,518</u>	<u>2,954,518</u>	<u>2,954,518</u>
	Q4 2021	Q3 2021	Q2 2021	Q1 2021
	\$	\$	\$	\$
Revenue				
Products	5,172,283	2,303,477	3,232,185	3,835,800
Solutions & other services	506,853	524,181	474,947	475,797
	<u>5,679,136</u>	<u>2,827,658</u>	<u>3,707,132</u>	<u>4,311,597</u>
Operating Expenses	2,105,385	1,510,635	1,759,758	1,773,901
Net income (loss)	(786,402)	(240,662)	(771,062)	(196,988)
Basic income (loss) per share	(0.35)	(0.11)	(0.35)	(0.09)
Fully-diluted income (loss) per share	(0.35)	(0.11)	(0.35)	(0.09)
Weighted average number shares outstanding - basic	2,233,532	2,233,532	2,233,091	2,172,702
Weighted average number shares outstanding – diluted	2,233,532	2,233,532	2,233,091	2,172,702
Total fully diluted shares	<u>2,879,941</u>	<u>2,879,941</u>	<u>2,883,512</u>	<u>2,936,920</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 December 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 76,163 shares due to the exercise of warrants for proceeds of \$426,507.

In July 2021, the Company issued 571 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 \$7.00 per share. In the event of default, all principal and interest due shall become immediately due and payable.

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

During the year ended December 31, 2022, the Company received convertible debenture financing for the aggregate amount of \$100,000. 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 \$8.33 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.

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The units comprise a share and one-half of one warrant, where a whole warrant shall be exercisable at \$2.80 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.

In September 2022, the Company issued additional convertible promissory debentures totalling \$1,500,000, bearing interest at 10% per annum (accruing annually and payable at maturity), on September 9, 2022 and maturing on September 9, 2024, or a period of 24-months. The Debentures are convertible, at the option of the holder, to common shares of DCS at a price of \$8.33 or a price equal to the price of the shares of the next financing carried out before the second anniversary of the closing date less a 25% discount. Upon issuance of the debentures, the Company also issued 107,142 share purchase warrants. Each warrant entitles the holder to purchase one common share at a price of \$6.02 per share for a period of 24 months from the date of issuance of the debentures. The Company records the fair value of the conversion features with variable exercise prices as an embedded derivative separate from the host contract. The fair value of the derivative liabilities is revalued on each balance sheet date with corresponding gains and losses recorded in the consolidated statements of operations. The Company uses a derivative valuation technique to fair value the components of the hybrid contract on initial recognition, including the debt component, the embedded derivative, and the warrants.

During the year ended December 31, 2022, the Company received unsecured promissory note in the principal amount of \$200,000. The note is interest bearing at 5.00% per annum and any payments made by the Company will first be applied to accrued interest and then to principal. The note matures December 31, 2022, and had been paid back in full as at December 31, 2022.

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 year ended December 31, 2022 were \$1,352,554 compared to \$1,032,394 used during the same period last year.

Cash flows used in investing activities during the year ended December 31, 2022 were \$4,040 versus \$12,249 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 year ended December 31, 2022 were \$287,875 compared to \$2,077,529 provided during the same period last year. The Company received \$1,600,000 from convertible debenture and note payables during the year ended December 31, 2022 compared to \$709,105 for the same period in 2021 from the Paycheck Protection Program. During the year ended December 31, 2021, the Company received \$426,512 from the exercise of 533,140 warrants while there was \$Nil received during the year ended December 31, 2022. Net repayments on credit facility were \$1,671,875 during the year ended December 31, 2022 while net borrowings under our credit facility were \$1,166,960 during the same period in 2021.

At December 31, 2022, the Company had working capital of \$1,137,657 (December 31, 2021 - \$1,431,066).

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### **Capital Resources**

As of December 31, 2022, the Company has committed approximately \$600K to complete the development of BrewSee®. The Company has sufficient capital resources to meet this commitment. The Company has no other sources of financing which have been arranged but are as yet unused.

#### Share Capital

Effective February 9, 2023, the Company consolidated 7 common shares for 1 common share (the "Stock Consolidation"). The Stock Consolidation was effected in the form of cancelling 6 common shares for each common share owned by shareholders of record at the close of business on February 9, 2023. All share data and stock-based compensation plans presented herein have been retroactively adjusted to give effect to the Stock Consolidation.

The Company has authorized 5,714,286 shares with a par value of \$0.00001 per share.

In March 2021, 76,163 common shares were issued due to the exercising of 76,163 warrants for proceeds of \$426,507.

In July 2021, 571 common shares were issued due to the exercising of 571 options for proceeds of \$3,880.

At December 31, 2022, the Company had 2,305,091 shares issued and outstanding with a par value of \$0.00001.

In January 2022, 71,428 common shares of common stocks were issued at \$3.05 in exchange for non-arm's length consulting fee for corporate development.

#### Warrants

In February and March 2021, 76,163 shares were issued due to the exercise of warrants for proceeds of \$426,507.

In May and June 2021, 66,503 warrants expired and were forfeited.

In January 2022, 15,183 warrants were expired.

In September 2022, upon issuance of the debentures, the company also issued 107,143 share purchase warrants. Each warrant entitles the holder to purchase one common share at a price of \$6.02 per share for a period of 24 months from the date of issuance of the debentures. The Company determined the warrants represent an embedded derivative and has accounted for the warrants in derivative liability.

#### Stock Options

In October 2017, the Company's board of directors and stockholders approved the 2017 Stock Plan under which 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

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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 a majority of the stockholders approved the following amendments to the 2017 Stock Plan: (a) increase in the number of authorized shares for issuance to 585,714 and (b) add an annual evergreen provision that will adjust the number of authorized shares reserved for issuance to an amount equal to 29.99% of the Company's issued common stock. As a result of the evergreen provision, the number of authorized shares for issuance increased to 646,862 effective January 2021.

The following table summarizes stock option transactions under the 2017 Plan as of the date of this report:

	Number of Options	Weighted average exercise price
<b>Outstanding, December 31, 2020</b>	531,429	4.9
Granted	114,286	10.43
Exercised	(571)	6.79
Forfeited	(24,874)	6.02
<b>Outstanding, December 31, 2021</b>	620,270	\$ 5.81
Granted	171,428	5.35
Exercised	-	-
Expired	(47,270)	6.01
Forfeited	(202,143)	10.23
<b>Outstanding, December 31, 2022</b>	542,285	\$ 4.03

At the date of this report, the Company had outstanding and exercisable stock options as follows:

Date of Expiry	Number of Options Outstanding	Number of Options Exercisable	Exercise Price
October 5, 2027	357,143	357,143	\$ 3.29
June 1, 2031	13,714	10,739	\$ 6.79
February 4, 2032	25,000	10,938	\$ 2.87
February 24, 2032	14,286	6,548	\$ 2.87
March 14, 2032	62,143	25,618	\$ 4.13
May 9, 2027	14,285	14,285	\$ 5.53
May 9, 2027	55,714	55,714	\$ 8.40

On May 9, 2022, the Company granted 55,714 and 14,285 stock options to directors with an exercise price of \$8.40 and \$5.53 respectively.

On March 14, 2022, the Company granted 62,143 stock options to officers with an exercise price of \$4.13 which was the fair market value of a share of stock on the date of the grant.

On February 28, 2022, the Company cancelled 140,000 stock options. of which 14,286 were exercisable at \$5.53, 69,286 were exercisable at \$10.71, 53,571 were exercisable at \$11.13, and 2,857 were exercisable at \$11.76.

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On February 24, 2022, the Company granted 14,286 stock options to officers with an exercise price of \$2.87 which was the fair market value of a share of stock on the date of the grant.

On February 9, 2022, the Company cancelled 62,143 stock options. of which 12,143 were exercisable at \$5.53, 7,143 exercisable at \$10.71, and 42,857 exercisable at \$11.13.

On February 4, 2022, the Company granted 25,000 options with an exercise price of \$2.87 which was the fair market value of a share of stock on the date of the grant.

On June 1, 2021, the Company granted 17,857 options of which 14,286 to a director. The options are exercisable at \$6.79 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 9,524 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 96,429 options of which 53,571 were to certain officers. The options are exercisable at \$11.13 which was the fair market value of a share of stock on the date of the grant.

On May 20, 2020, the Company granted 41,429 options of which 14,286 to a director. The options are exercisable at \$5.53 which was the fair market value of a share of stock on the date of the grant.

On January 7, 2020, the Company granted 107,857 options to certain of its directors and officers. 105,000 of the options are exercisable at \$10.71(\$14.00 CAD equivalent) and 20,000 of the options are exercisable at \$11.76 per share (\$15.40 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 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 relationship with the Company was terminated during the year ended December 31, 2022. The Company recorded professional fees in the consolidated statement of operations associated with CFO services for \$83,850 for the year ended December 31, 2022 (December 31, 2021 - \$277,885). As of December 31, 2022 and 2021, the Company owed \$Nil and \$9,325, respectively.

John Hubler, a former member of the Company's Board of Directors, is a partner of BH IoT Group. Subsequently on July 28, 2022, John Hubler tendered his resignation as a director of the Company to take on the role of chair of the technology advisory board, effective July 28, 2022. Mr. Hubler rejoined the Company effective March 20, 2023. In November 2020, the Company entered into an agreement with BH

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IoT Group to assist in building complete IoT bundled solutions. The Company entered into an initial Phase 1 project expected to last 3 months. At the end of Phase 1, both parties agreed to continue the relationship on a month-to-month basis. The Company recorded \$121,000 professional fees on the consolidated statement of operations for the year ended December 31, 2022 (December 31, 2021 - \$122,825). As of December 31, 2022 and 2021, no balance was due with respect to this agreement.

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 \$4,000. The agreement is effective for one year and will automatically renew annually unless terminated by either party. The Company recorded \$88,200 of professional fees on the consolidated statement of operations for the year ended December 31, 2022 (December 31, 2021 - \$28,124).

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 \$361,798 of professional fees on the consolidated statement of operations for the year ended December 31, 2022 (December 31, 2021 - \$Nil). In January 2022, 71,428 common shares of common stocks were issued at CAD\$3.85 in exchange for consulting fee for corporate development.

Also in April 2022, the Company appointed Mr. Lichtenwald as the new CFO and Mr. Lichtenwald is a principal of Lichtenwald Professional Corp ("LPC"). The Company entered into an agreement with LPC to provide CFO service fee of \$12,500 monthly. The Company recorded \$139,000 of professional fees on the consolidated statement of operations for the year ended December 31, 2022 (December 31, 2021 - \$Nil).

In July 2022, the Company appointed David Diamond as a new director and Chair of the Audit Committee. Mr. Diamond provides services and is compensated via director fee of \$2,500 monthly. The Company recorded \$12,500 of professional fees on the consolidated statement of operations for the year ended December 31, 2022 (December 31, 2021 - \$Nil). Remuneration attributed to key management personnel can be summarized as follows:

	Years ended December 31,	
	2022	2021
	\$	\$
Salary	1,255,144	914,622
Consulting fees	766,348	448,746
Share-based compensation	160,025	401,253
Total	2,181,517	1,764,621

During the year ended December 31, 2022, 71,428 common shares of common stocks were issued at \$3.05 in exchange for non-arm's length consulting fee to current officer of the Company for corporate development.

As at December 31, 2022, \$Nil (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 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, and derivative liability - 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 10), 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, derivative liability, 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 38% of the Company's revenue (2021 - 31%) 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>December 31, 2022</b>	<b>December 31, 2021</b>
Accounts receivables	\$ 3,642,594	\$ 4,024,625
Other receivables	46,343	-
Allowance for doubtful accounts	(315,199)	(121,319)
<b>Total</b>	<b>\$ 3,373,738</b>	<b>\$ 3,903,306</b>

During the year ended December 31, 2022, \$224,795 (2021 - \$95,288) of bad debt expense had been recognized in the consolidated statement of operating loss and comprehensive loss.

Aged trade receivable listing:

<b>Days outstanding</b>	<b>December 31, 2022</b>	<b>December 31, 2021</b>
Current	\$ 1,779,778	\$ 3,046,604
1 - 30	1,062,174	690,882
31 - 60	235,638	174,211
61 - 90	201,673	32,824
> 90	363,331	80,104
<b>Total</b>	<b>\$ 3,642,594</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.

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The Company's credit facility is variable based on the 90 day LIBOR rate. A 1% increase in the 90 day LIBOR rate would not have a significant impact on profit and loss.

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.

**Correction of Error in prior year**

During the current year, management identified that an error was made in the accounting of Inventory and accounts payable as at December 31, 2021, which resulted in an understatement of \$222,800 in Cost of Revenue, \$152,047 in Inventory, and \$752,831 in accounts payable in the financial report for the year ended December 31, 2021. The error also impacted the classification between current and long-term payables as at December 31, 2021. The error has been corrected in this financial report by adjusting the balance of related accounts.

**SUBSEQUENT EVENTS**

Subsequent to year ended December 31, 2022, the Company added two new board members with extensive experience in the Internet of Things industry. On March 20, 2023, John Hubler and Michael Ueland were appointed to the Direct Communication board of directors.