



Direct Communication Solutions, Inc.

Management's Discussion and Analysis

For the Three and Six months ended June 30, 2023

Amounts in United States dollars unless stated otherwise

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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 and six months ended June 30, 2023. 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 August 14, 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.

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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.

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Significant Highlights

The following highlights and developments for the six months ended June 30, 2023 and to the date of this management discussion and analysis:

- Successful collaboration between Epson and the Company's MiFleet solution in the fight against cargo theft.
- Signed a five-year agreement with AlSCO Uniforms, the world's largest uniform provider, to offer its AI Video Telematics Solution powered by VisionTrack.
- Partnered with VisionTrack to provide AI Powered Video Telematics and IoT Solutions to the North American Market.
- Partnered with Teltonika to provide IoT Solutions in North America
- Continuously working on NYSE up listing.

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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 17% (2022 – 9%) of total corporate revenue for the six months ended June 30, 2023.

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 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

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IFRS financial measure, for the three and six months ended June 30, 2023 and 2022:

	Three months ended June 30, 2023	Restated Three months ended June 30, 2022	Six months ended June 30, 2023	Restated Six months ended June 30, 2022
	\$	\$	\$	\$
Loss before tax	(1,102,297)	103,095	(2,349,171)	694,925
Accretion	55,759	-	107,277	-
Net changes in fair value	(237,740)	-	(344,434)	-
Amortization of debt issuance costs of credit facility	-	-	-	1,041
Depreciation and amortization	106,749	107,649	214,315	215,988
Finance cost for right of use assets	16,819	20,412	34,588	41,643
Interest expense	46,868	21,465	93,735	51,361
Government assistance	-	-	-	(286,995)
Provision for excess and obsolete inventory	(130,502)	(51,353)	(158,389)	(22,398)
Stock based compensation	18,733	90,947	35,574	198,647
Tax fees	1,700	2,953	4,023	9,410
One-time costs related to up-listing to senior exchange				
One-time professional fees	543,755	65,770	911,106	120,355
D&O	21,000	-	33,000	-
Marketing expenses	57,350	-	138,586	-
Adjusted EBITDA	(601,806)	360,938	(1,279,790)	1,023,977

Revenues decreased by 21% (Gross Profit decreased by 11%) on a year-over-year basis from the corresponding second quarter of 2022 and decreased by 43% (Gross Profit decreased by 39%) on a year-over-year basis for the six months ended June 30, 2023. The decrease in EBITDA for the three months and six months ended June 30, 2023 compared to the same period in 2022 was primarily attributable to decreased revenue due to Covid 19 impacted supply chain issues. Many customers ordered in advance in 2022 and still have inventory on hand for 2023. Also, during the beginning of 2022, there was a spike in revenue due to customers transiting from 3G to 4G devices. For the six months ended June 30, 2023, the Company have 18,625 active subscribers for our SaaS Solutions (16,829 active subscribers for the year ended December 2022) representing a growth of 11% in active subscribers.

Key Business Metrics

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

	<u>As at June 30, 2023</u>
Annual recurring revenue ("ARR")	\$ 2,576,882

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

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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 June 30, 2023

Revenues for the three months ended June 30, 2023 were \$4,584,708 compared to \$5,797,602 for the same period last year. Product revenue of \$3,922,122 was down 25% over the same period as last year as customers stocked up in inventory in 2022 due to supply chains issues caused by COVID-19.

Solutions and other services revenue of \$662,586 was up 13% from the same period as last year.

Cost of revenues for the three months ended June 30, 2023 were \$2,969,956 compared to \$3,974,868 for the same period in 2022. The following tables summarize gross profit and gross margin:

	Gross Profit		Gross Margin	
	Q2 2023	Q2 2022	Q2 2023	Q2 2022
	\$	\$	%	%
Products	1,162,595	1,549,335	29.6%	29.7%
Solutions and other services	452,157	414,524	68.2%	70.8%
Total	1,614,752	1,963,859	35.2%	31.4%

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 June 30, 2023 were \$2,650,928 compared to \$1,818,887 for the same period in 2022. Advertising and marketing expenses and professional fees increased in 2023 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. Compensation and benefits increased in 2023 primarily due to an adjustment of salaries to inflation for employees as a result of the COVID 19 pandemic. Bank fees decreased substantially due to decreased usage of the Company's credit facilities. Increase in other represents increase in corporate activities.

The Company recognized \$65,210 of bad debt expense compared to recognizing a bad debt recovery of \$5,588 during the same quarter last year. The increase was due to managements' decision to write off a customer receivable balance due to the likelihood the customer would default on its loan, whereas last year the estimated balance of allowance for doubtful accounts decreased due to successful collections of accounts receivable during the quarter. Bad debt expense and estimated balance of allowance for doubtful accounts are determined by the aging of accounts receivable balance at each quarter end and would move in correlation with the balance of accounts receivable at the point in time.

There were no other significant changes in general and administrative expenses.

Research and development costs for the three months ended June 30, 2023 were \$184,415 compared to \$145,364 for the same period in 2022. The increase was a result of additional testing for new hardware devices in connection with the new agreements signed and partnerships mentioned in the significant highlight section, there were less similar significant events for the same period last year.

Interest expense and accretion for the three months ended June 30, 2023 were \$119,446 compared to \$41,877 for the same period in 2022. The increase was primarily due to the interest expense and accretion of the convertible debentures that were issued subsequent to Q2 2022, there were no such expense for the same period last year.

Net loss for the three months ended June 30, 2023 was \$1,102,297 compared to a net income of \$103,095 for the same period in 2022. The difference in net income or loss was primarily the result of increased advertising and marketing expense and professional fee during the year of 2023 to promote shareholder awareness.

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Results of Operations for the Six Months ended June 30, 2023

Revenues for the six months ended June 30, 2023 were \$7,781,710 compared to \$13,597,515 for the same period last year. Product revenue of \$6,494,834 was down 48% over the same period as last year as customers stocked up in inventory in 2022 due to supply chains issues caused by COVID-19.

Solutions and other services revenue of \$1,286,876 was up 8% from the same period as last year.

Cost of revenues for the six months ended June 30, 2023 were \$5,215,323 compared to \$9,367,766 for the same period in 2022. The following tables summarize gross profit and gross margin:

	Gross Profit		Gross Margin	
	Q2 2023	Q2 2022	Q2 2023	Q2 2022
	\$	\$	%	%
Products	1,686,180	3,390,630	26.0%	27.3%
Solutions and other services	880,207	839,119	68.4%	70.7%
Total	2,566,387	4,229,749	33.0%	31.1%

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 six months ended June 30, 2023 were \$4,659,104 compared to \$3,168,055 for the same period in 2022. Advertising and marketing expenses and professional fees increased in 2023 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. Compensation and benefits increased in 2023 primarily due to an adjustment of salaries to inflation for employees as a result of the COVID 19 pandemic. Bank fees decreased substantially due to decreased usage of the Company's credit facilities. Increase in other represents increase in corporate activities. Included in other expense was a recovery \$286,995 recorded in connection to employee retention tax credit during the six month period ended June 30, 2022, no such event occurred in the current year.

The Company recognized \$99,223 of bad debt expense compared to \$176,033 the same period last year due to two large customers defaulting on their balances. No such event occurred in the current year.

There were no other significant changes in general and administrative expenses.

Research and development costs for the six months ended June 30, 2023 were \$365,288 compared to \$272,724 for the same period in 2022. The increase was a result of additional testing for new hardware devices in connection with the new agreements signed and partnerships mentioned in the significant highlight section, there were less similar significant events for the same period last year.

Interest expense and accretion for the six months ended June 30, 2023 were \$235,600 compared to \$94,045 for the same period in 2022. The increase was primarily due the interest expense and accretion of the convertible debentures that were issued subsequent to Q2 2022, there were no such expense for the same period last year.

Net loss for the six months ended June 30, 2023 was \$2,349,171 compared to a net income of \$694,925 for the same period in 2022. The difference in net income or loss was primarily the result of less sales for the year of 2023.

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.

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	Q2 2023	Q1 2023	Q4 2022	Q3 2022
	\$	\$	\$	\$
Revenue				
Products	3,922,122	2,572,712	3,776,934	4,112,623
Solutions & other services	662,586	624,290	521,121	578,113
	<u>4,584,708</u>	<u>3,197,002</u>	<u>4,298,055</u>	<u>4,690,736</u>
Operating Expenses	2,835,343	2,189,049	2,977,094	2,009,488
Net income (loss)	(1,102,297)	(1,246,874)	(2,067,306)	(914,377)
Basic income (loss) per share	(0.48)	(0.54)	(0.90)	(0.40)
Fully-diluted income (loss) per share	(0.48)	(0.54)	(0.90)	(0.40)
Weighted average number shares outstanding - basic	2,305,079	2,305,079	2,305,091	2,305,091
Weighted average number shares outstanding – diluted	2,305,079	2,305,079	2,305,091	2,305,091
Total fully diluted shares	<u>2,305,079</u>	<u>2,305,079</u>	<u>2,305,091</u>	<u>2,305,091</u>
	Restated Q2 2022	Restated Q1 2022	Q4 2021	Q3 2021
	\$	\$	\$	\$
Revenue				
Products	5,212,313	7,198,709	5,172,283	2,303,477
Solutions & other services	585,289	601,204	506,853	524,181
	<u>5,797,602</u>	<u>7,799,913</u>	<u>5,679,136</u>	<u>2,827,658</u>
Operating Expenses	1,818,887	1,621,892	2,105,385	1,510,635
Net income (loss)	103,095	732,955	(786,402)	(240,662)
Basic income (loss) per share	0.04	0.32	(0.35)	(0.11)
Fully-diluted income (loss) per share	0.04	0.32	(0.35)	(0.11)
Weighted average number shares outstanding - basic	2,305,091	2,271,126	2,233,532	2,233,532
Weighted average number shares outstanding – diluted	2,305,091	2,271,126	2,233,532	2,233,532
Total fully diluted shares	<u>2,375,091</u>	<u>2,375,091</u>	<u>2,233,532</u>	<u>2,233,532</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 June 30, 2023, the Company is not subject to any externally imposed capital requirements or debt covenants.

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.

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.

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.

At June 30, 2023 and December 31, 2022, the outstanding balance on the credit facility was \$1,499,180 and \$Nil, respectively.

Cash flows used in operating activities during the six months ended June 30, 2023 were \$3,281,457 compared to \$2,543,736 provided during the same period last year.

Cash flows used in investing activities during the six months ended June 30, 2023 were \$5,214 versus \$Nil during the same period last year. The difference is primarily the purchase of property and equipment in the current year compared to no purchases during the same period last year.

Cash flows provided in financing activities during the six months ended June 30, 2023 were \$1,388,180 compared to used \$1,478,233 during the same period last year. Net repayments on credit facility were \$1,670,833 during the six months ended June 30, 2022 compared to borrowing \$1,499,180 this year. During the six months ended June 30, 2022,

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the Company received \$300,000 proceeds from note payable, and there were no such transactions in the current year.

At June 30, 2023, the Company had working capital deficiency of \$2,139,455 (December 31, 2022 - \$1,137,657 working capital).

Capital Resources

As of June 30, 2023, 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.

There were no transactions affecting share capital during the six months ended June 30, 2023.

At June 30, 2023, the Company had 2,305,079 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 January 2022, 15,183 warrants 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 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.

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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
Outstanding, December 31, 2021	620,270	\$ 5.84
Granted	171,429	5.35
Exercised	-	-
Expired	(47,270)	6.01
Forfeited	(202,143)	10.23
Outstanding, December 31, 2022 and June 30, 2023	542,286	\$ 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	13,714	\$ 6.79
February 4, 2032	25,000	14,955	\$ 2.87
February 24, 2032	14,286	10,119	\$ 2.87
March 14, 2032	62,143	37,024	\$ 4.13
May 9, 2027	14,286	14,286	\$ 5.53
May 9, 2027	55,714	55,714	\$ 8.40

On May 9, 2022, the Company granted 55,714 and 14,286 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.

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.

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 on the consolidated

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interim statement of operations associated with CFO Connect's services for \$Nil (June 30, 2022 - \$83,850) for the six months ended June 30, 2023. As of June 30, 2023 and December 31, 2022, the Company owed \$Nil and \$Nil, respectively to CFO Connect.

John Hubler, a member of the Company's Board of Directors, is a partner of BH IoT Group. On July 28, 2022, John Hubler resigned as a director, and rejoined the Company as a director in April 2023. In November 2020, the Company entered into an agreement with BH 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. For the six months ended June 30, 2023, John Hubler was considered as a related party starting April 2023 for the fiscal year 2023. The Company recorded \$60,000 (2022 - \$67,500) professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2023.

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. Since fiscal year end 2022, the Company incurred additional professional fees in connection to its plans for NYSE up-listing, and MYZ Corporate Relations also contributed additionally to the event. The Company recorded \$58,800 of professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2023 (June 30, 2022 - \$29,400). As at June 30, 2023, \$8,400 of expenses included in accounts payable were owed to MYZ Corporate Relations, Ltd.

Mr. Lichtenwald, a member of the Company's Board of Directors, is a principal at Zeus Capital Ltd. In April 2022, Mr. Lichtenwald was appointed the new CFO of the Company, and on June 30, 2022, Mr. Lichtenwald resigned as a director. In November 2021, 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 \$90,000 of professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2023 (June 30, 2022 - \$199,080). Of the \$199,080 professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2022, \$109,080 was a portion of the \$218,158 paid by issuing 71,428 in shares to Zeus Capital Ltd. for corporate development.

Also, Mr. Lichtenwald is a principal of Lichtenwald Professional Corp ("LPC"). The Company entered into an agreement with LPC to provide CFO service fees of \$12,500 monthly, effective April 2022. The Company recorded \$75,000 of professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2023 (June 30, 2022 - \$51,500). As at June 30, 2023, \$3,892 of expenses included in accounts payable were owed to Mr. Lichtenwald.

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 fees of \$2,500 monthly. Since April 2023, Mr. Diamond provided additional service to the Company in connection to its plans for NYSE up-listing, The Company recorded \$22,500 of professional fees on the consolidated condensed interim statement of operations for the six months ended June 30, 2023 (June 30, 2022 - \$Nil).

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

	Six months ended June 30,	
	2023	2022 (restated)
	\$	\$
Salary ¹⁾	642,160	505,931
Consulting fees ¹⁾	306,300	376,789
Share-based compensation ¹⁾	1,754	125,534

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Total	950,214	1,008,254
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- 1) Including commission fee of \$12,913, consulting fee of \$83,850, and share-based compensation of \$33,498 paid to former officer of the Company during the six months ended June 30, 2022.

During the six months ended June 30, 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 June 30, 2023, \$12,292 (2022 – \$Nil) was included in accounts payable for fees and expenses owed to related parties.

Remuneration to key management personnel for the six months ended June 30, 2023 was \$950,214 compared to \$1,008,254 for the same period in 2022. Salaries increased due to adjustment to inflation resulted from COVID 19 pandemic. Consulting fees decreased compared to the same period in 2022 primarily due to the fees paid to the former CFO whose relationship terminated as of March 31, 2022. Share-based compensation decreased in the current year compared to same period in the prior year because there were no options granted in the current year whereas there were 84,285 options granted to officers in the prior year.

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, the Company is eligible for refundable employee retention credits subject to certain criteria. In connection with the CARES Act, the

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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 \$Nil (2022 - \$286,995) employee retention tax credit during the six months ending June 30, 2023, 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 condensed consolidated interim 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. During the six months ended June 30, 2023, approximately 38% of the Company's revenue (2022 - 37%) 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:

	June 30, 2023	December 31, 2022
Accounts receivables	\$ 3,451,529	\$ 3,642,594
Other receivables	72,404	46,343
Allowance for doubtful accounts	(275,204)	(315,199)
Total	\$ 3,248,729	\$ 3,373,738

During the six months ended June 30, 2023, \$99,223 (2022 - \$176,033) of bad debt expense had been recognized in the consolidated interim statement of operating loss and comprehensive loss.

Aged trade receivable listing:

Days outstanding	June 30, 2023	December 31, 2022
Current	\$ 1,281,564	\$ 1,779,778
1 – 30	1,717,295	1,062,174
31 – 60	130,338	235,638
61 - 90	133,506	201,673
> 90	188,826	363,331
Total	\$ 3,451,529	\$ 3,642,594

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 is exposed to liquidity risk due to low working capital as of June 30, 2023. Future liquidity may depend upon the Company's ability to arrange debt or additional equity financings.

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 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 year ended December 31, 2022, 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 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 the December 31, 2022 financial report by adjusting the balance of related accounts. The impact of the adjustment has also impacted June 30, 2022 statement of changes in shareholder's equity (deficiency).

Summary impact on the equity position as at June 30, 2022:

	Originally reported December 31, 2021	Adjustment Increase (decrease)	Restated December 31, 2021
Accumulated deficit	7,029,401	600,784	7,630,185
Total Equity (deficiency)	(227,356)	(600,784)	(828,140)

During the year ended December 31, 2022, management identified an error in connection with the restatement of the 2022 year end financials in the valuation of inventory and accounts payable as at June 30, 2022, which resulted in an understatement of \$243,309 in cost of revenue and \$72,352 in inventory, and \$315,661 in accounts payable. Management also identified an error relating to the available for use date of the intangible, an error in calculating share-based compensation, and an error relating to the incorrect classification of compensation and benefits as research and development, which resulted in an understatement of \$105,026 in depreciation and amortization, \$133,035 in compensation and benefits, and an overstatement in research and development expense of \$428,927 respectively.

Summary impact on statement of operating loss and comprehensive loss for the six months ended June 30, 2022:

Profit and Loss	Originally reported June 30, 2022	Adjustment Increase (decrease)	Restated June 30, 2022
Cost of revenues – Products	8,777,083	243,309	9,020,392
Gross Profit	4,473,058	(243,309)	4,229,749
Research and development	701,651	(428,927)	272,724
Compensation and benefits	1,317,846	133,035	1,450,881
Depreciation and amortization	110,962	105,026	215,988
Loss from Operations	841,413	(52,443)	788,970
Net Income	747,368	(52,443)	694,925

Summary impact on statement of Cash flow for the six months ended June 30, 2022:

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Cash Flow	Originally reported June 30, 2022	Adjustment Increase (decrease)	Restated June 30, 2022
Net Income	747,368	(52,443)	694,925
Depreciation	110,962	105,026	215,988
Stock-based compensation	494,539	(295,892)	198,647
Inventory	1,583,257	(72,352)	1,510,905
Accounts Payable	(817,923)	315,661	(502,262)
Prepaid Expense	(145,759)	(80,675)	(226,434)
Deferred offering costs	(80,675)	80,675	-
Net cash provided in operating activities	2,624,411	(80,675)	2,543,736
Net Cash used in financing activities	(1,558,908)	80,675	(1,478,233)

Summary impact on the equity position for the six months ended June 30, 2022:

	Originally reported June 30, 2022	Adjustment Increase (decrease)	Restated June 30, 2022
Stock-based compensation expense	494,539	(295,892)	198,647
Net income for the period	747,368	(52,443)	694,925
Reserves	7,514,681	(295,892)	7,218,789
Accumulated deficit	6,282,033	653,227	6,935,260
Total Equity (deficiency)	1,232,709	(949,119)	283,590
Basic Earnings per share	\$0.32	(\$0.02)	\$0.30
Diluted Earnings Loss per share	\$0.31	(\$0.02)	\$0.29