Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

For the three and nine months ended June 30, 2021, and 2020

Contents

MANAGEMENT'S COMMENTS ON UNAUDITED INTERIM

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the interim financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim financial statements of Covalon Technologies Ltd. (the "Company") have been prepared by and are the responsibility of the Company's management. The unaudited condensed consolidated interim financial statements are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS") and reflect management's best estimates and judgment based on information currently available. The Company's independent auditor has not performed a review of these unaudited condensed consolidated interim financial statements.

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

Expressed in Canadian Dollars

	June 30, 2021	September 30, 2020
Assets		
Current assets		
Cash and cash equivalents	**$3,529,136**	$3,506,991
Accounts receivable	**5,771,593**	3,333,437
Inventories (Note 4)	**5,559,977**	7,199,774
Prepaid expenses	**855,421**	809,404
Total current assets	**15,716,127**	14,849,606
Non-current assets		
Restricted cash	**37,045**	37,309
Property, plant and equipment (Note 6)	**1,542,271**	1,824,959
Intangible assets (Note 5)	**1,846,456**	2,151,274
Right-of-use assets (Note 8)	**2,238,102**	2,815,724
Goodwill (Note 5)	**12,095,836**	13,018,102
Total non-current assets	**17,759,710**	19,847,368
Total assets	**$33,475,837**	$34,696,974
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	**$4,070,560**	$3,899,266
Short-term debt (Note 7)	**7,760,529**	7,649,027
Lease liabilities (Note 9)	**524,207**	516,372
Acquisition note payable (Note 2)	**9,360,321**	10,074,013
Deferred revenue	**314,094**	498,149
Total current liabilities	**22,029,711**	22,636,827
Non-current liabilities		
Deferred revenue	**185,910**	290,123
Lease liabilities (Note 9)	**2,152,440**	2,663,346
Total non-current liabilities	**2,338,350**	2,953,469
Total liabilities	**24,368,061**	25,590,296
Shareholders' equity		
Share capital (Note 10)	**44,607,119**	44,607,119
Contributed surplus (Note 10)	**11,854,216**	11,652,765
Foreign exchange translation reserve	**(741,893)**	565,772
Accumulated deficit	**(46,611,666)**	(47,718,978)
Total shareholders' equity	**9,107,776**	9,106,678
Total liabilities and shareholders' equity	**$33,475,837**	$34,696,974

On behalf of the Board:

(signed) "Abe Schwartz" — *Director*

(signed) "Brian Pedlar" — *Director*

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

Expressed in Canadian Dollars

	Three months ended June 30,		Nine months ended June 30,	
	2021	2020	**2021**	2020
Revenue				
Product	**$8,455,147**	$6,365,839	**$20,217,578**	$18,167,287
Development and consulting services	**312,102**	221,943	**1,168,997**	1,554,964
Licensing and royalty fees	**48,268**	85,612	**158,614**	158,274
Total revenue	**8,815,517**	6,673,394	**21,545,189**	19,880,525
Cost of sales	**3,719,038**	3,628,656	**9,220,792**	9,207,884
Gross profit before operating expenses	**5,096,479**	3,044,738	**12,324,397**	10,672,641
Operating expenses				
Operations	**223,647**	137,156	**741,641**	1,128,236
Research and development activities	**295,716**	205,133	**840,892**	653,784
Sales, marketing, and agency fees	**1,336,165**	919,620	**3,999,970**	6,155,581
General and administrative	**2,059,665**	1,263,082	**5,274,881**	6,847,203
	3,915,193	2,524,991	**10,857,384**	14,784,804
Finance expenses	**123,355**	205,580	**359,701**	657,025
Net income (loss)	**$1,057,931**	$314,167	**$1,107,312**	$(4,769,188)
Other comprehensive income (loss)				
Amount that may be reclassified to profit or loss				
Foreign currency translation adjustment	**(242,427)**	(838,205)	**(1,307,665)**	520,905
Total comprehensive income (loss)	**$815,504**	$(524,038)	**$(200,353)**	$(4,248,283)
Basic earnings (loss) per share (Note 16)	**$0.04**	$0.01	**$0.04**	$(0.18)
Diluted earnings (loss) per share (Note 16)	**$0.04**	$0.01	**$0.04**	$(0.18)

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

Expressed in Canadian Dollars

	Number of shares	Share capital	Contributed surplus	Accumulated deficit	Foreign exchange translation reserve	Total
Balance at October 1, 2019	25,818,677	$44,607,119	$10,717,141	$(40,766,754)	$372,612	$14,930,118
Share-based payment expense	-	-	845,968	-	-	845,968
Net loss for the period	-	-	-	(4,769,188)	-	(4,769,188)
Foreign currency translation adjustment	-	-	-	-	520,905	520,905
Balance at June 30, 2020	**25,818,677**	**$44,607,119**	**$11,563,109**	**$(45,535,942)**	**$893,517**	**$11,527,803**
Balance at October 1, 2020	25,818,677	$44,607,119	$11,652,765	$(47,718,978)	$565,772	$9,106,678
Share-based payment expense	-	-	201,451	-	-	201,451
Net income for the period	-	-	-	1,107,312	-	1,107,312
Foreign currency translation adjustment	-	-	-	-	(1,307,665)	(1,307,665)
Balance at June 30, 2021	**25,818,677**	**$44,607,119**	**$11,854,216**	**$(46,611,666)**	**$(741,893)**	**$9,107,776**

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS (UNAUDITED)

Expressed in Canadian Dollars

	Nine months ended June 30, 2021	2020
Cash flows from (used in) operating activities		
Net income (loss) for the period	**$1,107,312**	$(4,769,188)
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation of property, plant and equipment	**310,829**	337,727
Amortization of intangible assets	**155,806**	171,631
Depreciation - right of use assets (Note 8)	**374,725**	412,470
Share-based payment expense (Note 11)	**201,451**	845,968
Interest expense and accretion	**359,701**	657,025
Cash generated by operating activities before change in non-cash working capital balances	**2,509,824**	(2,344,367)
Change in non-cash working capital (Note 19)	**(1,537,630)**	(1,619,698)
Total cash flows generated from (used in) operating activities	**972,194**	(3,964,065)
Cash flows from (used in) investing activities		
Purchase of property, plant and equipment	**(139,310)**	(317,484)
Restricted cash	**(2,358)**	336
Total cash flows used in investing activities	**(141,668)**	(317,148)
Cash flows from financing activities		
Interest paid	**(236,454)**	(275,177)
Repayment of debt	**(900,000)**	(1,065,000)
Proceeds from debt	**1,000,000**	570,000
Payment of lease liabilities	**(469,420)**	(403,120)
Total cash flows used in financing activities	**(605,874)**	(1,173,297)
Foreign exchange rate changes on cash	**(202,507)**	79,496
Total cash flows during the period	**22,145**	(5,375,014)
Cash and cash equivalents, beginning of the period	**$3,506,991**	$9,575,149
Cash and cash equivalents, end of the period	**$3,529,136**	$4,200,135

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

1. CORPORATE INFORMATION

Covalon Technologies Ltd. ("the Company") is incorporated under the laws of Ontario and is engaged in the business of developing, licensing, and selling medical technologies and products. The unaudited condensed consolidated interim financial statements of Covalon Technologies Ltd. for the three and nine months ended June 30, 2021, comprise the results of the Company and its wholly owned subsidiaries. The Company has received regulatory approval on numerous products and is currently generating revenue. The Company has adopted a business model that predominantly contracts the manufacturing and distribution of its commercialized products through partners. The Company generates its revenues through development contracts, licensing agreements, distribution contracts, and sales of products.

The Company is listed on the TSX Venture Exchange, having the symbol COV. The Company also trades on the OTCQX Best Market, having the symbol of CVALF.

The address of the Company's corporate office and principal place of business is 1660 Tech Avenue, Unit 5, Mississauga, Ontario, Canada.

2. AQUAGUARD SALE AND COVID-19

AquaGuard Sale

On July 29, 2021, the Company sold the AquaGuard product line to TIDI Products, LLC ("TIDI"), an arm's length party, for approximately $38 million (US$30 million) subject to post-closing adjustments ("AquaGuard Sale"). Under the terms of the purchase agreement, the Company sold all its interest in Covalon Technologies Holdings (USA), Ltd. and Covalon Technologies AG Ltd. ("Former Subsidiaries") to TIDI. The transaction included the sale of moisture barrier products sold under the AquaGuard brand, certain trademarks and intellectual property, related customer contracts, and the manufacturing assets to support the AquaGuard business. Immediately prior to closing, the Company spun-off all its assets in the Former Subsidiaries other than its AquaGuard product line of business to an existing subsidiary, which will carry on the Company's ongoing business in the United States. The purchase price of US$30 million includes US$2 million placed in escrow for indemnity claims (which escrow amount will be released 50% in 12 months following closing and the remaining 50% in 14 months following closing, assuming no claims). The Company used proceeds of $7,691,797 from the AquaGuard Sale to fully satisfy its indebtedness to its senior lender, HSBC, and the credit facility with HSBC Bank Canada ("HSBC") has now been terminated.

The Company also extinguished US$7,552,300 of secured indebtedness owed to Cenorin, LLC ("Cenorin") under a promissory note dated as of October 1, 2018, as amended, (the "Acquisition Note") by making a cash payment of approximately $5,025,000 (US$4,000,000) to Cenorin and issuing to Cenorin 200,000 warrants for the purchase of common shares in the capital of the Company (the "Warrants"). Each Warrant entitles the holder to acquire a common share of the Company at a price of $4.00 for a period of five years. The issuance of the Warrants was approved by the TSX Venture Exchange. The Warrants and the underlying common shares of the Company are subject to a hold period of four months and one day in accordance with applicable securities laws.

As of July 29, 2021, the Company has no outstanding debt (other than normal-course payables and similar liabilities) and no debt-related restrictions as it relates to operations or actions of the Company.

COVID-19

In March 2020, the World Health Organization characterized the outbreak of the novel strain of coronavirus, specifically identified as COVID-19, as a global pandemic. In response to the outbreak, governmental authorities in Canada and internationally have introduced various recommendations and measures to try to limit the pandemic, including travel restrictions, border closures, non-essential business closures, quarantines, selfisolations, shelters-in-place, and social distancing. The governmental responses have caused material disruption to business globally, economic slowdowns, and shifts in economic markets. The significant uncertainty related to the virus, and the governmental responses, has negatively impacted the Company's suppliers, as well as customers and their demand for our products and services.

During the nine months ended June 30, 2021, the Company applied for and was approved for funding of $535,275 (2020 - $387,276) under the Canadian Emergency Wage Subsidy Program ("CEWS"). During the period, the Company also applied for, and received, US$1,103,860 (2020 – US$1,103,861) in a second draw of the United States Paycheck Protection Program loan ("US PPP Loan") from the US Small Business Administration under the US Paycheck Protection Program. During the three and nine months ended June 30, 2021, the Company recorded $630,818 (2020 - $1,825,202) and $1,976,819 (2020 - $1,825,202) respectively in relation to CEWS and the PPP loan, net against the related operating expenses. The US PPP Loan will be forgiven if certain conditions are met (including the funds being used for eligible payroll and rent expenses during the eligibility period) and a loan forgiveness application is completed. Any ineligible portion of the US PPP Loan will otherwise carry interest of 1%. The Company also received funds from other subsidy programs of $56,963 (2020 - $46,408) during the nine months ended June 30, 2021. The Company recognizes government grants when there is reasonable assurance that it will comply with the conditions required to qualify for the grant, and that the grant will be received. These amounts are recorded as an offset to the corresponding operating expense account.

During the nine months ended June 30, 2021, the Company's first draw of the US PPP Loan, being US$1,103,861 and all related interest, was forgiven by the U.S. Small Business Administration ("SBA") and no repayments were required. Subsequent to June 30, 2021, the Company's second draw of the US PPP Loan, being US$1,103,860 and all related interest, was forgiven by the SBA with no repayments required.

Operationally, the Company has been negatively impacted by the COVID-19 pandemic, and the efforts to mitigate the pandemic, as have many of the Company's employees, customers, and vendors regardless of geographic location. The Company's direct sales staff have been limited in their ability to call on customers in the United States and the United Kingdom. There have also been increased costs associated with shipping products, and a slow-down in receiving regulatory approvals. As a result of this uncertainty there is a higher level of estimation uncertainty as it relates to the assessment of impairment for intangibles, provisions for inventory and receivables, and general future cash flows. Our distribution relationships with several companies in North America and internationally have been impacted due to the material disruption to business globally, economic slowdowns, and shifts in economic markets caused by governmental responses to the COVID-19 pandemic. Demand for some of the Company's products also temporarily decreased as facilities adjust to patient demand and procedure types.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

The Company's unaudited condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS") applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. These condensed consolidated interim financial statements are presented in Canadian dollars and should be read in conjunction with the Company's annual financial statements for the year ended September 30, 2020, which were prepared in accordance with IFRS.

The Company's unaudited condensed consolidated interim financial statements have been prepared on a going concern basis which presumes that the Company will continue in operation for the foreseeable future and will be able to realize assets and discharge liabilities in the normal course of its operations.

The accounting policies adopted are consistent with those of the previous financial year end.

Expressed in Canadian Dollars

On October 31, 2018, amendments to IAS 1 and IAS 8 to clarify and align the definition of material information and provide guidance to help improve consistency in the application of materiality when used in other IFRS standards. These amendments were effective for years beginning on or after January 1, 2020 and are to be applied prospectively. The Company adopted the amendments on October 1, 2020 and there was no impact on the unaudited condensed consolidated interim financial statements.

The unaudited condensed consolidated interim financial statements were authorized for issue by the Board of Directors on August 27, 2021.

4. INVENTORIES

Inventories consist of the following:

	June 30, 2020	September 30, 2020
Raw materials	**$2,727,284**	$2,983,418
Finished goods	**4,804,731**	6,300,288
Inventory provision	**(1,972,038)**	(2,083,932)
	$5,559,977	$7,199,774

Cost of product sales for the three and nine month period ended June 30, 2021 includes $3,320,758 (2020 - $3,397,552) and $8,293,213 (2020 - $7,751,412), respectively in inventoried materials.

5. INTANGIBLE ASSETS AND GOODWILL

Goodwill is comprised of the following amounts:

	Goodwill ($)
Balance at October 1, 2020	13,018,102
Foreign exchange	(922,266)
Balance at June 30, 2021	**12,095,836**

Intangible assets are comprised of the following amounts:

	Deferred Development Costs ($)	**Brand ($)**	**Patents ($)**	**Trademarks ($)**	**Computer Software ($)**	**Total ($)**
Cost						
Balance at September 30, 2020	2,224,978	1,133,815	971,638	83,704	177,994	4,592,129
Foreign exchange	(157,628)	(80,325)	(68,836)	(5,930)	(12,610)	(325,329)
Balance at June 30, 2021	2,067,350	1,053,490	902,802	77,774	165,384	4,266,800
Accumulated amortization						
Balance at September 30, 2020	1,719,944	113,382	448,313	-	159,216	2,440,855
Amortization	74,121	40,346	37,400	-	3,939	155,806
Foreign exchange	(123,543)	(8,873)	(32,540)	-	(11,361)	(176,317)
Balance at June 30, 2021	1,670,522	144,855	453,173	-	151,794	2,420,344
Carrying amounts						
At September 30, 2020	505,034	1,020,433	523,325	83,704	18,778	2,151,274
At June 30, 2021	**396,828**	**908,635**	**449,629**	**77,774**	**13,590**	**1,846,456**

Expressed in Canadian Dollars

6. PROPERTY, PLANT AND EQUIPMENT

	Furniture and Fixtures ($)	Lab Equipment ($)	Leasehold Improvements ($)	Total ($)
Cost				
Balance at September 30, 2020	901,046	2,751,986	484,315	4,137,347
Additions	46,028	87,605	5,677	139,310
Foreign exchange	(64,483)	(197,145)	(34,433)	(296,061)
Balance at June 30, 2021	882,591	2,642,446	455,559	3,980,596
Accumulated depreciation				
Balance at September 30, 2020	552,852	1,523,979	235,557	2,312,388
Depreciation	73,287	183,583	53,959	310,829
Foreign exchange	(55,370)	(111,715)	(17,807)	(184,892)
Balance at June 30, 2021	570,769	1,595,847	271,709	2,438,325
Carrying amounts				
At September 30, 2020	348,194	1,228,007	248,758	1,824,959
At June 30, 2021	**311,822**	**1,046,599**	**183,850**	**1,542,271**

7. DEBT

During the year ended September 30, 2018, the Company entered into the Facility with HSBC. This Facility was amended during the year ended September 30, 2020, to allow for an additional borrowing line supported by the Business Credit Availability Program ("BCAP") with the Business Development Bank of Canada ("BDC"), in the amount of $1,000,000. The Facility includes an Acquisition Line, Operating line, and other credit facilities.

During the nine months ended June 30, 2021, the Company drew $1,000,000 against the BCAP facility through HSBC. This facility is interest-only until July 2021 and then is repayable over a four-year term by equal monthly payments.

The Facility is secured by a General Security Agreement which also includes the wholly owned subsidiaries. The Company is also subject to financial covenant and certain reporting requirements. These covenants include: 1) funded debt to adjusted EBITDA; 2) fixed charged coverage ratio; 3) current ratio; and 4) maintaining a cash balance of $1,500,000 as well as other reporting requirements. As of June 30, 2021, the Company was not able to fulfill all financial covenants as stipulated under the Facility, for the Acquisition Line, which constituted an event of default. Since the Company did not have an unconditional right to defer the settlement of the debt for at least 12 months, IFRS requires the liability to be classified as current as at June 30, 2021. The carrying amount of the acquisition line is $2,805,529 as of June 30, 2021.

A reconciliation of the operating line is as follows:

	June 30, 2021 ($)
Balance – October 1, 2020	3,955,000
Interest accrued during the period	130,636
Interest paid during the period	(130,636)
Balance – Ending	3,955,000
Less: Current portion	3,955,000

This facility is repayable on demand by HSBC which could occur if there was a deficiency in the borrowing base of assets used to support this line. The interest rate associated with the operating line is Prime Rate plus 1.5%.

Expressed in Canadian Dollars

A reconciliation of the Acquisition Line is as follows:

	June 30, 2021 ($)
Balance – October 1, 2020	3,694,027
Repayments of principal	(900,000)
Interest accrued during the period	103,056
Interest paid during the period	(91,554)
Balance – Ending	2,805,529
Less: Current portion	2,805,529
Non-current portion	-

This facility is repayable on demand by HSBC which could occur if there was a default on the financial covenants and the event of default was not waived by HSBC.

A reconciliation of the BCAP facility is as follows:

	June 30, 2021 ($)
Balance – October 1, 2020	-
Proceeds received	1,000,000
Interest accrued during the period	14,264
Interest paid during the period	(14,264)
Balance – Ending	1,000,000
Less: Current portion	1,000,000
Non-current portion	-

This facility is interest-only until July 2021, and then is repayable over a four-year term.

Subsequent to June 30, 2021, the Company fully repaid all outstanding debt, including the BCAP facility, with HSBC (see Note 2).

8. RIGHT-OF-USE ASSETS

	Right-of-use assets ($)
Balance at October 1, 2020	2,815,724
Depreciation	(374,725)
Foreign exchange	(202,897)
Balance at June 30, 2021	**2,238,102**

The Company leases office space in Mississauga, Canada and Seattle, USA.

Expressed in Canadian Dollars

9. LEASE LIABILITIES

Lease liabilities are comprised of the following amounts:

	Lease liabilities ($)
Balance at October 1, 2020	3,179,718
Interest	111,745
Payments	(469,420)
Foreign exchange	(145,396)
Balance at June 30, 2021	**2,676,647**
Less: Current portion	524,207
Long-term portion	2,152,440

10. SHAREHOLDERS' EQUITY

Common Shares

The Company is authorized to issue an unlimited number of common shares with no par value. All shares are fully paid.

On October 1, 2018, Covalon acquired AquaGuard, a division of Cenorin LLC., and issued 75,136 common shares of the Company in escrow with release dates of 12 months, 18 months and 24 months after the acquisition date. During the nine months ended June 30, 2021 25,045 (2020 - 25,045) shares were released from escrow leaving a balance of nil.

Warrants

The following is a summary of all warrants:

	Number of Warrants	**Weighted average exercise Price**	**Weighted Average Expiry (years)**
Balance at September 30, 2020	**2,750,000**	**$2.00**	**3.97**
Exercised during the period	-	-	
Balance at June 30, 2021	**2,750,000**	**$2.00**	**3.22**

11. SHARE-BASED PAYMENTS

Option Plan Details

The Company has a Stock Option Plan ("the Plan") under which non-transferable options to purchase common shares of the Company may be granted to directors, officers, employees, or service providers of the Company. The terms of the Plan provide that the Directors have the right to grant options to acquire common shares of the Company at not less than the closing market price of the shares on the day preceding the grant at terms of up to five years. No amounts are paid or payable by the recipient on receipt of the option, and the options granted are not dependent on any performance-based criteria. Unless the board of directors decides otherwise, options granted under the plan will vest as follows: 34% of the options vest in one year, with a further 33% vesting in each of the subsequent two years on the anniversary of the initial grant date.

Expressed in Canadian Dollars

The following is a summary of changes in stock options from October 1, 2020 to June 30, 2021:

Grant Date	Expiry Date	Exercise Price	Opening Balance	Forfeited/ Expired	Closing Balance	Vested	Unvested	Weighted Average Expiry (years)
7-Mar-16	7-Mar-21	$1.13	100,000	(100,000)	-	-	-	-
23-Jun-16	23-Jun-21	$1.29	110,834	(5,000)	105,834	105,834	-	-
14-Sep-16	14-Sep-21	$2.29	20,000	-	20,000	20,000	-	0.21
8-Feb-17	8-Feb-22	$2.20	168,333	(35,000)	133,333	133,333	-	0.61
20-Jun-17	20-Jun-22	$2.47	348,333	(2,500)	345,833	345,833	-	0.97
25-Oct-17	25-Oct-22	$3.80	60,000	-	60,000	60,000	-	1.32
21-Dec-17	21-Dec-22	$4.65	137,500	(10,000)	127,500	127,500	-	1.48
24-Jan-18	24-Jan-23	$6.02	60,000	-	60,000	60,000	-	1.57
27-Sep-18	27-Sep-23	$8.50	130,000	(24,168)	105,832	70,555	35,277	2.24
22-Dec-18	22-Dec-23	$4.28	322,501	(31,667)	290,834	95,975	194,859	2.48
15-Mar-19	15-Mar-24	$5.03	150,000	(15,000)	135,000	44,550	90,450	2.71
			1,607,501	**(223,335)**	**1,384,166**	**1,063,580**	**320,586**	**1.52**
Weighted Average Exercise Price			**$3.73**	**$2.98**	**$3.85**	**$3.52**	**$4.96**	

Share Based Payment Expense

Total expense arising from share-based payment transactions recognized during the three and nine months ended June 30, 2021, as part of employee benefit expense were $(3,111) (2020 - $227,092) and $201,451 (2020 - $845,968).

12. FINANCIAL RISK MANAGEMENT

The following is a discussion of market, credit, and liquidity risks and related mitigation strategies that have been identified.

Credit Risk

The Company is exposed to credit risk associated with its cash and cash equivalents and accounts receivable. The risk is reduced by having accounts receivables insured or obtaining letters of credit when the Company determines that it is warranted. The Company applies the simplified approach to providing for expected credit losses, which allows the use of a lifetime expected loss for all receivables. Receivables have been grouped based on shared credit risk characteristics and the days outstanding to measure the expected credit loss. On this basis the loss allowance at June 30, 2021 and September 30, 2020 is nominal.

Accounts receivable are written off when there is no reasonable expectation of recovery which may be supported by failure to make contractual payments for more than 180 days as well as other factors.

Accounts receivable are subject to normal industry risks in each geographic region in which the Company operates. The Company attempts to manage these risks by dealing with creditworthy customers; however, due to the limited number of potential customers in each market this is not always possible. As at June 30, 2021, three customers accounted for 60% (2020 – three customers for 53%) of the accounts receivable balance. These customers, who are distributors and strategic partners of the Company, represent a large portion of the Company's sales. Credit risk exposure is mitigated by strong credit granting policies, the use of Letters of Credit, and due diligence procedures for new customers.

The aging of accounts receivable is as follows:

	June 30, 2021	September 30, 2020
Current	**$5,713,938**	$3,283,144
30-60 days past due	**9,582**	22,053
Over 60 days past due	**48,073**	28,240
	5,771,593	3,333,437

Interest Rate Risk

The Company is subject to interest rate risk on its cash, cash equivalents and debt. The Company believes that interest rate risk is low due to market based variable interest rates. During fiscal 2019, the Company took on floating rate debt to fund an acquisition and working capital. At June 30, 2021, if interest rates had been 1% higher or lower then the interest expense would have been $58,204 higher or lower, respectively, during the period.

Currency Risk

The Company's exposure to foreign currency risk at the end of the reporting period, expressed in Canadian dollars, was as follows:

	June 30, 2021				**September 30, 2020**			
	Canadian	USD	GBP	**Total**	CAD	USD	GBP	**Total**
Cash and cash equivalents	$58,836	$3,405,626	$64,674	**$3,529,136**	$199,176	$3,267,280	$40,535	**$3,506,991**
Accounts Receivable	$2,693	$5,604,739	$164,161	**$5,771,593**	$2,283	$3,324,634	$6,520	**$3,333,437**
Acquisition note payable	-	$9,360,321	-	**$9,360,321**	-	$10,074,013	-	**$10,074,013**
Accounts payable and accrued liabilities	$527,963	$3,380,844	$161,753	**$4,070,560**	$609,370	$3,122,046	$167,850	**$3,899,266**
Lease liabilities	$1,110,396	$1,566,251	-	**$2,676,647**	$1,296,801	$1,882,917	-	**$3,179,718**

Fair Value

The fair values of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, acquisition note payable and lease liabilities approximate their carrying values, due to their relatively short periods to maturity. The fair value of debt approximates the carrying amount as it has a floating interest rate.

13. CAPITAL MANAGEMENT

The Company defines capital that it manages as its shareholders' equity comprising share capital, contributed surplus, foreign exchange translation reserve, accumulated deficit, and short-term debt. Its objectives when managing capital are to ensure that the Company will continue as a going concern, so that it can provide services to its customers and returns to its shareholders. The capital at June 30, 2021 is $16,868,305 (September 30, 2020 – $16,755,705).

Expressed in Canadian Dollars

The Company manages its capital structure and adjusts it in light of economic conditions. The Company, upon approval from its Board of Directors, will make changes to its capital structure as deemed appropriate under the specific circumstances.

14. RELATED PARTY TRANSACTIONS

Key management personnel includes the Company's directors and senior management team. These individuals are responsible for planning, directing and controlling the activities of an entity. Key management personnel compensation comprised:

	Three months ended June 30		**Nine months ended June 30,**	
	2021	2020	**2021**	2020
Compensation and short-term employee benefits	**$239,442**	$299,654	**$718,326**	$874,327
Share based payment expense	**24,902**	93,395	**87,308**	348,595
	$264,344	$393,049	**$805,634**	$1,222,922

During the year end September 30, 2013, a non-interest bearing loan of $50,000 was made to a key employee. As of June 30, 2021, $10,000 of this loan remained outstanding.

15. EXPENSES BY NATURE

The consolidated statements of operations and comprehensive income (loss) include the following expenses by nature:

	Three months ended June 30,		**Nine months ended June 30,**	
	2021	2020	**2021**	2020
Inventoried materials	$3,320,758	$3,397,552	$8,293,213	$7,778,412
Wages, benefits, consulting fees, director compensation	2,684,643	3,322,753	8,606,146	10,365,492
Government subsidies	(630,818)	(1,825,202)	(1,976,819)	(1,825,202)
Share based payments	(3,111)	227,092	201,451	845,968
Depreciation and amortization	267,857	346,174	841,360	921,828
Professional fees	860,152	333,362	1,680,175	1,366,147
Other expenses	1,134,750	351,916	2,432,650	4,540,043
Total	**$7,634,231**	$6,153,647	**$20,078,176**	$23,992,688

Depreciation and amortization

	For the three months ended June 30,		**For the nine months ended June 30,**	
	2021	2020	**2021**	2020
Cost of product sales	**$73,043**	$91,905	**$233,373**	$259,890
Operations	**710**	877	**2,011**	2,565
Research and development activities	**7,270**	9,256	**22,320**	26,840
General and administrative	**186,834**	244,136	**583,656**	632,533
Total depreciation and amortization	**$267,857**	$346,174	**$841,360**	$921,828

Expressed in Canadian Dollars

16. EARNINGS (LOSS) PER SHARE

The weighted average number of shares outstanding during the three and nine months ended June 30, 2021, was 25,818,677 and 25,818,677, respectively (June 30, 2020 – 25,818,677 and 25,818,677).

Details of dilutive securities outstanding are as follows:

Potentially dilutive securities	Three months ended June 30, 2021	Three months ended June 30, 2020	Nine months ended June 30, 2021	Nine months ended June 30, 2020
Common shares potentially dilutive				
- all stock options	**12,939**	73,286	**7,630**	84,631
- all warrants	**-**	-	**-**	-
Total potentially dilutive shares	**12,939**	73,286	**7,630**	84,631
Diluted earnings (loss) per share	**$0.04**	$0.01	**$0.04**	$(0.18)

17. CONTINGENCIES AND COMMITMENTS

From time to time, the Company is party to legal proceedings arising out of the normal course of business. The results of these litigations cannot be predicted with certainty, and management is of the opinion that the outcome of these types of proceedings is generally not determinable. Any loss resulting from these proceedings will be charged to operations in the period that a loss becomes probable.

18. SEGMENT REPORTING

During the three months ended June 30, 2021, the Company generated revenue of $6,866,108 (2020 – $4,664,501) in the US, $1,020,825 (2020 – $977,324) in the Middle East, $183,729 (2020 – $19,393) in Canada, and $744,855 (2020 – $1,012,176) in the rest of the world.

During the nine months ended June 30, 2021, the Company generated revenue of $16,679,849 (2020 – $15,738,966) in the US, $2,901,971 (2020 – $2,088,270) in the Middle East, $221,992 (2020 – $78,296) in Canada, and $1,741,377 (2020 – $1,974,993) in the rest of the world.

As of June 30, 2021, the Company had $3,679,920 of its property, plant, and equipment, right-of-use assets and intangible assets located in Canada and $1,946,909 in the USA. Goodwill in the amount of $12,095,836 is attributed to the US.

19. CHANGES IN NON-CASH WORKING CAPITAL ITEMS

Net changes in non-cash working capital balances are as follows:

	Nine months ended June 30, 2021	Nine months ended June 30, 2020
Accounts receivable	**$(2,650,146)**	$216,200
Prepaid expenses	**(102,425)**	(344,256)
Inventories	**1,119,521**	(333,320)
Accounts payable and accrued liabilities	**443,493**	(1,654,247)
Deferred revenue	**(348,073)**	495,925
	$(1,537,630)	$(1,619,698)