

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

For the three months ended December 31, 2024 and 2023

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**MANAGEMENT’S COMMENTS ON UNAUDITED
CONDENSED CONSOLIDATED INTERIM 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 Accounting Standards”) 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 STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

Expressed in Canadian Dollars

	December 31, 2024	September 30, 2024
Assets		
Current assets		
Cash and cash equivalents	\$17,497,607	\$16,746,781
Accounts receivable	5,356,596	3,645,252
Inventories (Note 3)	8,570,914	7,696,084
Prepaid expenses	451,403	686,106
Finance lease receivable (Note 8)	170,503	264,728
Total current assets	32,047,023	29,038,951
Non-current assets		
Property, plant and equipment (Note 5)	1,081,714	1,010,728
Intangible assets (Note 4)	1,519,904	1,439,714
Finance lease receivable (Note 8)	50,284	148,728
Right-of-use assets (Note 6)	117,996	168,453
Total non-current assets	2,769,898	2,767,623
Total assets	\$34,816,921	\$31,806,574
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	\$3,380,618	\$3,323,790
Lease liabilities (Note 7)	568,295	600,485
Deferred revenue	-	72,082
Total current liabilities	3,948,913	3,996,357
Non-current liabilities		
Accounts payable	-	4,423
Lease liabilities (Note 7)	216,377	301,186
Total non-current liabilities	216,377	305,609
Total liabilities	4,165,290	4,301,966
Shareholders' equity		
Share capital (Note 9)	51,748,095	51,748,095
Contributed surplus	8,413,114	8,322,591
Foreign exchange translation reserve	4,980,867	3,130,413
Accumulated deficit	(34,490,445)	(35,696,491)
Total shareholders' equity	30,651,631	27,504,608
Total liabilities and shareholders' equity	\$34,816,921	\$31,806,574

Contingencies and commitments (Note 17)

On behalf of the Board:

(signed) "Amir Boloor"

Director

(signed) "Brent Ashton"

Director

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

Covalon Technologies Ltd.

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

Expressed in Canadian Dollars

	Three months ended December 31,	
	2024	2023
Revenue		
Product	\$8,077,940	\$4,575,767
Development and consulting services	5,826	56,640
Licensing and royalty fees	82,214	30,650
	8,165,980	4,663,057
Total revenue		
	3,171,514	1,814,520
Cost of sales		
	4,994,466	2,848,537
Gross profit		
Operating expenses		
Operations	371,069	630,713
Research and development activities	373,339	311,411
Sales, marketing, and agency fees	1,209,820	1,646,303
General and administrative	1,725,570	1,731,625
	3,679,798	4,320,052
Finance (income)	(41,068)	(9,964)
Loss/(gain) on finance lease receivable (Note 8)	149,690	(610,008)
Net income (loss)	1,206,046	\$(851,543)
Other comprehensive income (loss)		
Amount that may be reclassified to profit or loss		
Foreign currency translation adjustment	1,850,454	(387,273)
Total comprehensive income (loss)	\$3,056,500	\$(1,238,816)
Earnings (loss) per common share		
Basic earnings (loss) per share (Note 15)	\$0.04	\$(0.03)
Diluted earnings (loss) per share (Note 15)	\$0.04	\$(0.03)

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS 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, 2023	24,669,577	\$42,770,879	\$11,436,826	\$(38,366,283)	\$2,951,395	\$18,792,817
Share-based payment expense (Note 10)	-	-	115,929	-	-	115,929
Net loss for the period	-	-	-	(851,543)	-	(851,543)
Foreign currency translation adjustment	-	-	-	-	(387,273)	(387,273)
Balance at December 31, 2023	24,669,577	\$42,770,879	\$11,552,755	\$(39,217,826)	\$2,564,122	\$17,669,930
Balance at October 1, 2024	27,398,077	\$51,748,095	\$8,322,591	\$(35,696,491)	\$3,130,413	\$27,504,608
Share-based payment expense (Note 10)	-	-	90,523	-	-	90,523
Net income for the period	-	-	-	1,206,046	-	1,206,046
Foreign currency translation adjustment	-	-	-	-	1,850,454	1,850,454
Balance at December 31, 2024	27,398,077	\$51,748,095	\$8,413,114	\$(34,490,455)	\$4,980,867	\$30,651,631

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

	Three months ended December 31,	
	2024	2023
Cash flows from (used in) operating activities		
Net income (loss) for the period	\$1,206,046	\$(851,543)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation of property, plant and equipment (Note 5)	101,636	114,212
Amortization of intangible assets (Note 4)	95,138	69,291
Depreciation of right of use assets (Note 6)	60,351	56,691
Share-based payment expense (Note 10)	90,523	115,929
Impairment of intangible assets	-	74,448
Interest expense and accretion	9,740	25,781
(Gain)/loss on finance lease receivables (Note 8)	149,690	(610,008)
Cash flows from (used in) operating activities before change in non-cash working capital and other balances	1,713,124	(1,005,199)
Net changes in non-cash working capital and other balances:		
Accounts receivable	(1,500,680)	2,707,881
Prepaid expenses	262,005	(197,091)
Inventories	(490,795)	(110,936)
Accounts payable and accrued liabilities	211,143	(1,239,757)
Deferred revenue	(70,266)	(59,857)
Total net changes in non-cash working capital balances	(1,588,593)	1,100,240
Total cash flows from operating activities	124,531	95,041
Cash flows from (used in) investing activities		
Purchase of property, plant and equipment (Note 5)	(108,947)	(74,215)
Purchase of intangible assets (Note 4)	(83,175)	(18,364)
Restricted cash	-	2,940
Total cash flows used in investing activities	(192,122)	(89,639)
Cash flows from (used in) financing activities		
Finance lease receivable	65,700	29,097
Payment of lease liabilities	(181,745)	(179,144)
Total cash flows used in financing activities	(116,045)	(150,047)
Foreign exchange rate changes on cash	934,462	(357,525)
Total cash flows during the period	750,826	(502,170)
Cash and cash equivalents, beginning of the period	\$16,746,781	\$8,794,650
Cash and cash equivalents, end of the period	\$17,497,607	\$8,292,480

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

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

1. CORPORATE INFORMATION

Covalon Technologies Ltd. (“the Company”) is incorporated under the laws of Ontario and is engaged in the business of researching, developing, manufacturing, and marketing of patent-protected medical products that improve patient outcomes and save lives in the areas of infection management, advanced wound care, and surgical procedures. The unaudited condensed consolidated interim financial statements of Covalon Technologies Ltd. for the three months ended December 31, 2024 comprise the results of the Company and its wholly owned subsidiaries. The Company leverages its patented medical technology platforms and expertise in two ways: (i) by developing products that are sold under the Company’s name; and (ii) by developing and commercializing medical products for other medical companies under development and license contracts. The Company has received regulatory approval on numerous products and leverages contract manufacturers to make its products and distribution contracts to sell its commercialized products to medical customers. 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. 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 Accounting Standards”) applicable to the preparation of interim financial statements, under 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, 2024, which were prepared in accordance with IFRS Accounting Standards.

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

The unaudited condensed consolidated interim financial statements were authorized for issue by the Board of Directors on February 20, 2025.

Accounting pronouncements issued but not yet effective

The IASB has issued classification, measurement and disclosure amendments to IFRS 9, Financial Instruments and IFRS 7, Financial Instruments: Disclosures with an effective date for annual reporting periods beginning on or after January 1, 2026. The amendments clarify the date of recognition and derecognition of some financial assets and liabilities and introduce a new exception for some financial liabilities settled through an electronic payment system. Other changes include a clarification of the requirements when assessing whether a financial asset meets the solely payments of principal and interest criteria and new disclosures for certain instruments with contractual terms that can change cash flows (including instruments where cash flows changes are linked to environment, social or governance targets).

IFRS 18, Presentation and Disclosure in Financial Statements (IFRS 18) is a new standard that will provide new presentation and disclosure requirements, and which will replace IAS 1, Presentation of Financial Statements (IAS 1). IFRS 18 introduces changes to the structure of the income statement; provides required disclosures in financial statements for certain profit or loss performance measures that are reported outside an entity’s financial statements; and provides enhanced principles on aggregation and disaggregation in financial statements. Many

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

other existing principles in IAS 1 have been maintained. IFRS 18 is effective for years beginning on or after January 1, 2027.

The impact of the adoption of these pronouncements is currently being assessed.

3. INVENTORIES

Inventories consist of the following:

	December 31, 2024	September 30, 2024
Raw materials	4,297,098	\$3,520,835
Finished goods	5,999,330	6,372,772
Inventory provision	(1,725,514)	(2,197,523)
	8,570,914	\$7,696,084

Cost of sales for the three months ended December 31, 2024, included \$3,101,889 (2023 - \$1,761,972), in inventoried materials. The company reduced the inventory provision for the three-month period ended December 31, 2024, totalling \$357,36 (2023 - \$422,107). A reduction in the inventory provision related to net realizable value for the three months ended December 31, 2024, amounted to \$114,645 (2023 - \$192,771) and is included in cost of sales in the condensed consolidated interim statements of operations and comprehensive income (loss).

4. INTANGIBLE ASSETS

Intangible assets are comprised of the following amounts:

	Deferred Development Costs (\$)	Patents (\$)	Trademarks (\$)	Computer Software (\$)	Total (\$)
Balance at September 30, 2024	2,251,667	1,064,510	81,111	1,087,866	4,485,154
Additions	83,175	-	-	-	83,175
Foreign exchange	137,180	70,186	5,349	82,995	295,710
Balance at December 31, 2024	2,472,022	1,134,696	86,460	1,170,861	4,864,039
Accumulated amortization					
Balance at September 30, 2024	2,190,907	643,908	-	210,625	3,045,440
Depreciation	29,153	10,229	-	55,756	95,138
Foreign exchange	145,297	42,752	-	15,508	203,557
Balance at December 31, 2024	2,365,357	696,889	-	281,889	3,344,135
Carrying amounts					
At September 30, 2024	60,760	420,602	81,111	877,241	1,439,714
At December 31, 2024	106,665	437,807	86,460	888,972	1,519,904

As at December 31, 2024, included in computer software is an amount of \$92,456 (September 30, 2024 - \$11,272) which primarily relates to new information systems where amortization has not yet commenced as it had not yet been placed into service.

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

5. PROPERTY, PLANT AND EQUIPMENT

	Computer Hardware, Furniture and Fixtures (\$)	Production and Lab Equipment (\$)	Leasehold Improvements (\$)	Total (\$)
Balance at September 30, 2024	485,114	2,682,794	382,755	3,550,663
Additions	-	108,947	-	108,947
Foreign exchange	31,981	176,878	25,235	234,094
Balance at December 31, 2024	517,095	2,968,619	407,990	3,893,704
Accumulated depreciation				
Balance at September 30, 2024	393,399	1,769,700	376,836	2,539,935
Depreciation	16,911	82,098	2,627	101,636
Foreign exchange	26,428	119,068	24,923	170,419
Balance at December 31, 2024	436,738	1,970,866	404,386	2,811,990
Carrying amounts				
At September 30, 2024	91,715	913,094	5,919	1,010,728
At December 31, 2024	80,357	997,753	3,604	1,081,714

As at December 31, 2024, included in production and lab equipment is an amount of \$354,132 (September 30, 2024 - \$242,397) which primarily relates to new production equipment where amortization has not yet commenced as they had not yet been placed into service.

6. RIGHT-OF-USE ASSETS

	Right-of-use assets (\$)
Balance at October 1, 2024	168,453
Depreciation	(60,351)
Foreign exchange	9,894
Balance at December 31, 2024	117,996

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

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

7. LEASE LIABILITIES

Lease liabilities are comprised of the following amounts:

	Lease liabilities (\$)
Balance at October 1, 2024	901,671
Interest	9,559
Payments	(181,745)
Foreign exchange	55,187
Balance at December 31, 2024	784,672
Less: Current portion	568,295
Long-term portion	216,377

Following the impairment of the right of use asset related to the Company's Seattle lease agreement, an onerous contract liability at December 31, 2024 of \$213,534 (September 30, 2024 - \$223,020) has been recognized in accounts payable and accrued liabilities related to future variable lease payments that are not included in the lease liability.

8. FINANCE LEASE RECEIVABLES

During the first quarter, the Company entered into two sublease agreements for a total of 10,451 square feet out of a total of 18,246 square feet that comprises its Seattle facility. Both subleases are considered finance leases as it is reasonably certain that the sublease term will match that of the Company's existing lease agreements to April 2026. As a result of this transaction the company has recognized a finance lease receivable at the inception of the subleases in the amount of \$610,008 with an offsetting gain recognized in the condensed consolidated interim statements of operations and comprehensive income (loss).

On December 19, 2024, one sublease tenant notified us of their intention to terminate their sublease early, providing a 60-day notice. The tenant will be vacating the premises on February 28, 2025. This has resulted in a loss on the finance lease receivable of \$149,690 for the three months ended December 31, 2024.

The movement in finance lease receivables during the period is as follows:

	Finance lease receivables (\$)
Balance at October 1, 2024	413,456
Loss on finance lease receivable	(149,690)
Interest income	4,746
Brokerage fees	(4,927)
Payments received	(65,700)
Foreign exchange	22,902
Balance at December 31, 2024	220,787
Current portion	170,503
Non-current portion	50,284

A maturity analysis of the lease payments receivable is as follows:

2025	128,239
2026	82,461
Total future minimum payments receivable	210,700
Imputed interest	10,087
Finance lease receivable	220,787

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NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

9. 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.

Warrants

The following is a summary of all warrants:

	Number of Warrants	Weighted average exercise Price	Weighted Average Expiry (years)
Balance at September 30, 2024	200,000	\$4.00	1.83
Exercised during the period	-	-	-
Balance at December 31, 2024	200,000	\$4.00	1.58

10. SHARE-BASED PAYMENTS

Long-Term Incentive Plan

On March 8, 2023, the shareholders approved the Long-Term Incentive Plan (the Plan).

Stock Options

Stock options outstanding are non-transferable options to purchase common shares of the Company which may be granted to Directors, officers, employees, or service providers of the Company. The terms of the stock options 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 ten years. No amounts are paid or payable by the recipient on receipt of the stock option. All stock options issued to date 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. Future grants of stock options may vest over alternative periods as authorized by the Directors.

Issuance of RSUs and DSUs

RSUs and DSUs vest over a period of three years on each anniversary of the grant date unless a different vesting schedule is approved by the Board of Directors. DSUs are only eligible to be converted into common shares of the Company when the holder ceases its relationship with the Company.

The maximum number of common shares which may be issued under the Plan cannot exceed 10% of the common shares issued and outstanding at any given time, calculated on a non-diluted basis. Grants held by non-employee directors of the Company are at all times limited to no more than 1% of the common shares issued and outstanding, calculated on a non-diluted basis, and the total annual grant to any one non-employee director under the Plan cannot exceed a grant value of \$150,000 in total equity.

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

The following is a summary of changes in stock options from October 1, 2024 to December 31, 2024:

Grant Date	Expiry Date	Exercise Price	Opening Balance	Granted	Forfeited/Expired	Closing Balance	Vested	Unvested	Weighted Average Expiry (years)
28-Mar-22	28-Mar-27	\$2.19	382,500	-	(2,500)	380,000	125,400	254,600	2.24
06-Sep-22	06-Sep-27	\$2.50	145,000	-	(2,500)	142,500	47,025	95,475	2.68
10-Jan-24	10-Jan-29	\$1.50	800,000	-	-	800,000	-	800,000	4.03
			1,327,500	-	(5,000)	1,322,500	172,425	1,150,075	3.37
Weighted Average Exercise Price			\$1.81	\$0.00	\$2.35	\$1.81	\$2.27	\$1.74	

Deferred Share Units

The following is a summary of changes in Deferred Share Units from October 1, 2024 to December 31, 2024:

Grant Date	Exercise Price	Opening Balance	Granted	Exercised	Forfeited/Expired	Closing Balance	Vested	Unvested
20-Oct-23	\$1.44	280,000	-	-	-	280,000	226,667	53,333
		280,000	-	-	-	280,000	226,667	53,333
Weighted Average Exercise Price		\$1.44	\$0.00	-	-	\$1.44	1.44	\$1.44

Share Based Payment Expense

Total share-based payment expense recognized during the three months ended December 31, 2024, was \$90,523 (2023 - \$115,929).

11. 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 and finance lease 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 accounts receivables. To measure the expected credit losses, accounts receivables are grouped based on shared credit risk characteristics and the days past due. On this basis, the loss allowance as at December 31, 2024 and September 30, 2024 is nominal as the Company only transacts with hospitals, distributors and private clinics and has not incurred a sustained trend

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Expressed in Canadian Dollars

of any credit losses. The Company's cash management policies include ensuring cash and cash equivalents are deposited in Canadian chartered banks.

Accounts receivables 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 receivables 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 December 31, 2024, five customers accounted for 90% (September 30, 2024 – five customers for 75%) 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:

	December 31, 2024	September 30, 2024
Current	\$5,356,596	\$3,628,070
30-60 days past due	-	17,182
	<u>5,356,596</u>	<u>3,645,252</u>

Interest Rate Risk

The Company is subject to interest rate risk on its cash and cash equivalents. The Company believes that interest rate risk is low due to market based variable interest rates.

Currency Risk

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

	<u>December 31, 2024</u>				<u>September 30, 2024</u>			
	<u>Canadian</u>	<u>USD</u>	<u>GBP</u>	<u>Total</u>	<u>CAD</u>	<u>USD</u>	<u>GBP</u>	<u>Total</u>
Cash and cash equivalents	\$3,115,914	\$14,381,693	-	\$17,497,607	\$5,549,162	\$11,197,619	-	\$16,746,781
Accounts receivable	\$59,662	\$5,229,916	\$67,018	\$5,356,596	\$396,849	\$3,185,530	\$62,873	\$3,645,252
Finance lease receivable	-	\$220,787	-	\$220,787	-	\$413,456	-	\$413,456
Accounts payable and accrued liabilities	\$193,144	\$3,169,135	\$18,339	\$3,380,618	\$337,881	\$2,973,128	\$17,204	\$3,328,213
Lease liabilities	\$160,169	\$624,503	-	\$784,672	\$225,094	\$676,577	-	\$901,671

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

If exchange rates were to change by 5% at December 31, 2024 total comprehensive income (loss) would change by \$804,372 (September 30, 2024 - \$559,628).

Fair Value

The fair values of cash and cash equivalents, accounts receivable, finance lease receivable, accounts payable and accrued liabilities and lease liabilities approximate their carrying values, due to their relatively short periods to maturity.

Liquidity risk

The Company continually monitors working capital to ensure sufficient cash is available to meet operational and capital expenditure requirements. The Company has contractual obligations related to lease liabilities and accounts payable and accrued liabilities that are due as reflected in the following table:

	Carrying amount (\$)	Future cash flows (\$)	Less than 1 year (\$)	Between 1 and 5 years (\$)	Greater than 5 years (\$)
Accounts payable and accrued liabilities	3,380,618	3,380,618	3,380,618	-	-
Lease liabilities	784,672	653,287	434,715	218,572	-
Total	4,165,290	4,033,905	3,815,333	218,572	-

12. CAPITAL MANAGEMENT

The Company defines capital that it manages as its shareholders' equity comprising share capital, contributed surplus, foreign exchange translation reserve and accumulated deficit. 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 December 31, 2024 is \$30,651,631 (September 30, 2024 – \$27,504,608).

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.

13. RELATED PARTY TRANSACTIONS

Key management personnel include 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 December 31	
	2024	2023
Compensation and short-term employee benefits	\$395,293	\$315,035
Share based payment expense	73,343	56,191
	468,636	371,226

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The Company had previously accrued \$667,969 for termination benefits related to a former senior management team member during the 2023 fiscal year. The amount continues to represent management's best estimate of the termination benefits owed. On April 5, 2024, this former senior executive filed a claim for wrongful dismissal. An additional amount of \$1,832,031 has been claimed, which the Company has not accrued for and believes to be unwarranted. There can be no assurance as to the final outcome of the claim and termination benefits owed.

During the year end September 30, 2013, a non-interest-bearing loan of \$50,000 was made to a key employee. As of December 31, 2024, \$10,000 of this loan remained outstanding.

14. EXPENSES BY NATURE

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

	Three months ended December 31,	
	2024	2023
Inventoried materials	\$3,101,889	\$1,761,972
Wages, benefits, consulting fees, director compensation	2,340,624	2,265,518
Share based payments	90,523	115,929
Depreciation and amortization	257,125	240,194
Facility	86,455	57,604
Patent and trademark maintenance	75,792	31,343
Insurance	101,162	102,946
Information technology system costs	202,169	188,606
Professional fees	243,182	234,230
Impairment of intangible assets	-	74,448
Other expenses	352,391	1,061,782
Total	\$6,851,312	\$6,134,572

Depreciation and amortization

	Three months ended December 31,	
	2024	2023
Cost of product sales	\$69,625	\$52,548
Operations	22,676	-
Research and development activities	22,703	47,480
General and administrative	142,121	140,166
Total depreciation and amortization	\$257,125	\$240,194

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

15. EARNINGS (LOSS) PER SHARE

Details of the basic and diluted weighted average common shares outstanding for the respective periods are the following:

	Three months ended December 31	
	2024	2023
Weighted average number of common shares outstanding – basic	27,398,077	24,669,577
Dilutive effect of securities outstanding Stock Options/DSU's	645,342	-
Weighted average number of common shares outstanding – diluted	28,043,419	24,669,577

For the three month period ended December 31, 2023, diluted loss per share is equal to the basic loss per share due to the anti dilutive effect of the stock options, DSUs and warrants.

16. SEGMENT REPORTING

During the three months ended December 31, 2024, the Company generated revenue of \$7,137,832 (2023 – \$4,133,801) in the United States, \$977,977 (2023 – \$378,788) in the Middle East, \$8,477 (2023 – \$14,085) in Canada, and \$40,694 (2023 – \$136,383) in the rest of the world.

As of December 31, 2024, the Company had \$2,712,052 (September 30, 2023 - \$2,606,782) of its property, plant, and equipment, right-of-use assets and intangible assets located in Canada and \$7,562 (September 30, 2024 - \$12,113) in the United States.

17. CONTINGENCIES AND COMMITMENTS

The following are commitments of the Company beyond December 31, 2024:

	September 30,		
	2025	2026	2027
Telecommunications and office equipment leases	36,606	38,196	23,006
	\$36,606	\$38,196	\$23,006

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.

Covalon Technologies Ltd.

NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

Expressed in Canadian Dollars

18. SUBSEQUENT EVENT

Potential Impact of Tariffs on Operations

On February 1, 2025, President Trump signed an executive order imposing a 25% tariff on goods imported from Canada and Mexico, effective February 4, 2025. In response, the Government of Canada announced retaliatory tariffs on certain US goods, which will be implemented in phases starting February 4, 2025. Mexico has also indicated it may impose retaliatory tariffs but has not yet announced specific measures. Additionally, the US has imposed a separate 10% tariff on imports from China. To allow time for negotiations, all three North American governments have agreed to a temporary 30-day pause on the tariffs.

The Company's operations may be impacted by tariffs, potentially affecting pricing and demand dynamics. The overall economic impact remains uncertain and will depend on the severity and duration of the tariffs. The Company is actively monitoring the situation and has identified strategies to mitigate risks, with several options available to minimize the impact of any potential future tariffs.