



**H-SOURCE HOLDINGS LTD.**

**CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

**FOR THE THREE MONTHS ENDED MARCH 31, 2019 AND 2018**

**(EXPRESSED IN US DOLLARS)**

**H-SOURCE HOLDINGS LTD.**  
**Condensed Consolidated Interim Statements of Financial Position**  
**(Expressed in US Dollars)**

	Notes	As At March 31, 2019 \$ (Unaudited)	As At December 31, 2018 \$ (Audited)
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash		55,189	72,864
Short-term investment	5	14,966	18,655
Prepaid expenses		147,870	221,443
Accounts receivable		192,837	207,676
Inventory		99,189	111,460
<b>Total Current Assets</b>		<b>510,051</b>	<b>632,098</b>
Patents	7	104,247	107,498
Software development costs	7	138,400	184,533
<b>TOTAL ASSETS</b>		<b>752,698</b>	<b>924,129</b>
<b>LIABILITIES</b>			
<b>Current Liabilities</b>			
Accounts payable and accrued liabilities	8	917,322	648,843
Interest and profit sharing payable	9	83,513	62,286
Due to related parties	12	57,925	47,925
Loans payable	9	335,657	200,657
<b>TOTAL LIABILITIES</b>		<b>1,394,417</b>	<b>959,711</b>
<b>SHAREHOLDERS' EQUITY (DEFICIENCY)</b>			
Common shares	10	10,024,162	10,024,162
Common shares to be issued	10	51,912	51,912
Reserves		782,134	774,137
Deficit		(11,533,466)	(10,920,074)
Accumulative other comprehensive income (loss)		33,539	34,281
<b>Total Shareholders' Equity (Deficiency)</b>		<b>(641,719)</b>	<b>(35,582)</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>752,698</b>	<b>924,129</b>

Nature and continuance of operations (Note 2)

On behalf of the board:

“John Kupice” Director  
John Kupice

“Murray Walden” Director  
Murray Walden

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

# H-SOURCE HOLDINGS LTD.

## Condensed Consolidated Interim Statements of Loss and Comprehensive Loss (Unaudited - Expressed in US Dollars)

		Three Months Ended	
	Notes	March 31, 2019	March 31, 2018
		\$	\$
<b>Revenue</b>		253,268	241,361
<b>Cost of Sales</b>		(192,117)	(187,680)
		61,151	53,681
Commission revenue (net)		8,236	53,097
		69,387	106,778
<b>Expenses</b>			
Advertising and promotion		43,193	25,457
Amortization	7	49,384	48,854
Consulting fees		20,309	75,158
General and administration expenses	6	186,035	215,645
Professional fees		52,072	43,446
Salaries and benefits	12	300,905	325,415
Share-based payments	10	7,997	-
		(659,895)	(733,975)
<b>Income Before Other Income (Expenses)</b>		(590,508)	(627,197)
Interest income		52	1,463
Interest and other finance costs, net	9	(22,936)	(419)
<b>Net Loss for the Period</b>		(613,392)	(626,153)
<b>Other Comprehensive Loss</b>			
Foreign exchange gain		(742)	59,407
<b>Net and Comprehensive Loss for the Period</b>		(614,134)	(566,746)
Basic and Diluted Loss Per Share		(0.01)	(0.01)
Weighted Average Number of Common Shares Outstanding		117,640,277	85,166,568

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

## H-SOURCE HOLDINGS LTD.

### Condensed Consolidated Interim Statements of Changes in Shareholders' Equity (Deficiency) (Unaudited - Expressed in US Dollars)

	Common Shares		Reserves	Common Shares to be Issued	Accumulative Other Comprehensive Income (Loss)	Accumulated Deficit	Shareholders' Equity
	Number of Shares	\$					
Balance – December 31, 2017	88,674,705	7,924,721	570,305	-	(23,527)	(7,865,984)	605,515
Shares issued for cash on private placement, net of issuance costs	17,250,000	1,080,046	50,812	-	-	-	1,130,858
Net loss and comprehensive loss for the year	-	-	-	-	59,407	(626,153)	(566,746)
Balance – March 31, 2018	105,924,705	9,004,767	621,117	-	35,880	(8,492,137)	1,169,627
Shares issued for cash on private placement, net of issuance costs	11,666,667	1,006,792	38,953	-	-	-	1,045,745
Shares issued from warrants exercise	48,905	12,603	(5,807)	-	-	-	6,796
Issuance of stock options	-	-	120,758	-	-	-	120,758
Issuance of restricted share units	-	-	59,025	-	-	-	59,025
Shares to be issued from restricted share units exercise	-	-	(51,912)	51,912	-	-	-
Net loss and comprehensive loss for the year	-	-	-	-	(2,341)	(3,041,329)	(3,043,670)
Balance – March 31, 2019	117,640,277	10,024,162	782,134	51,912	33,539	(11,533,466)	(641,719)

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

**H-SOURCE HOLDINGS LTD.**  
**Condensed Consolidated Interim Statements of Cash Flows**  
**(Unaudited - Expressed in US Dollars)**

	<b>Three Months Ended</b>	
	<b>March 31, 2019</b>	<b>March 31, 2018</b>
	<b>\$</b>	<b>\$</b>
<b>Cash provided by (used in):</b>		
<b>Operating activities</b>		
Net loss for the year	(613,392)	(626,153)
Items not involving cash:		
Amortization	49,384	48,854
Share based payments	7,997	-
Changes in non-cash operating working capital:		
Accounts receivable	15,022	(137,270)
Prepaid expenses	74,061	65,753
Inventory	12,271	12,223
Accounts payable and accrued liabilities	266,665	71,626
Interest and profit sharing payable	21,233	-
Due to related parties	10,000	-
<b>Net cash used in operating activities</b>	<b>(156,759)</b>	<b>(564,967)</b>
<b>Cash flows from investing activities:</b>		
Short-term investments	4,100	(319,547)
Patents	-	(2,215)
<b>Net cash provided (used) by investing activities</b>	<b>4,100</b>	<b>(321,762)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from share issuances, net share issuance costs	-	1,080,046
Proceeds from loans	135,000	-
<b>Net cash provided by financing activities</b>	<b>135,000</b>	<b>1,080,046</b>
<b>Effect of foreign exchange</b>	<b>(16)</b>	<b>111,463</b>
<b>Change in cash</b>	<b>(17,675)</b>	<b>193,317</b>
<b>Cash, beginning</b>	<b>72,864</b>	<b>56,426</b>
<b>Cash, ending</b>	<b>55,189</b>	<b>361,206</b>

Supplemental Cash Flow Information (Note 11)

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

# **H-SOURCE HOLDINGS LTD.**

## **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

**For the Three Months Ended March 31, 2019 and 2018**

**(Unaudited - Expressed in US Dollars)**

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### **NOTE 1 - NATURE OF OPERATIONS**

H-Source Holdings Ltd. (the “Company”), was incorporated on November 11, 2014 under the laws of British Columbia, Canada. Its head office is located at 1980-1075 W. Georgia St., Vancouver, BC, V6E 3C9, Canada and registered office is located at 1500-1055 W. Georgia St., Vancouver, BC, V6E 4N7, Canada. The Company is listed on the TSX Venture Exchange under the symbol “HSI” and on the OTCQB in the USA under the symbol “HSCHF”.

The Company has developed a digital platform and network to operate in the healthcare industry and offers a private, hospital-to-hospital marketplace that allows members to buy/sell/transfer supplies and capital equipment with each other. Members can conduct secure transactions within Integrated Delivery Networks (IDNs), Group Purchasing Organizations (GPOs), the complete HSI network, or customize their own group of hospitals using the Company’s built-in filters. This network is designed specifically to reduce health care costs and medical products waste.

These condensed consolidated interim financial statements of the Company were approved and authorized for issue by the Board of Directors on May 29, 2019.

### **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Statement of compliance with International Financial Reporting Standards**

The condensed consolidated interim financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (“IFRS”) and International Accounting Standards (“IAS”) 34, Interim Financial Reporting, as issued by the International Accounting Standards Board (“IASB”) on a basis consistent with the significant accounting policies disclosed in note 2 of the most recent annual financial statements as at and for the year ended December 31, 2018 as filed on SEDAR at [www.sedar.com](http://www.sedar.com). The condensed consolidated interim financial statements do not include all of the information required for full annual financial statements.

#### **Basis of presentation and going concern**

These condensed consolidated interim financial statements have been prepared on a historical cost basis except for financial instruments classified as financial instruments at fair value through profit or loss that have been measured at fair value. In addition, these condensed interim consolidated financial statements have been prepared using the accrual basis of accounting and are presented in United States dollars unless otherwise noted.

The principal accounting policies applied in the preparation of the condensed consolidated interim financial statements are set out below. These policies have been consistently applied to all of the periods presented, unless otherwise stated.

These condensed consolidated interim financial statements include the accounts of H-Source Holdings Ltd., H-Source, Inc. (“HSI”) a Washington State corporation, and H-Source Distribution-US, Inc., a Washington State corporation. Control is achieved when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The subsidiary is fully consolidated from the date on which control is acquired by the Company. Inter-company transactions and balances are eliminated upon consolidation. The subsidiary is de-consolidated from the date that control by the Company ceases. Inter-company balances and transactions and any unrealized income and expenses arising from inter-company transactions are eliminated in preparing the condensed interim consolidated financial statements.

The Company started realizing revenue during the year ended December 31, 2017 and has experienced net losses since inception. As of March 31, 2019, and December 31, 2018, the Company had an accumulated deficit of \$11,533,466 and \$10,920,074, respectively. For the periods ended March 31, 2019 and 2018, the Company had cash outflows from cash used in operating activities of \$156,759 and \$564,967, respectively. The Company expects to continue to incur net losses and have significant cash outflows for the foreseeable future. The Company is subject to a number of risks similar to those of other pre-commercial stage companies, including its dependence on key individuals, generation of revenues, dependence on outside sources of capital, successful protection of intellectual property, competition with larger, better-capitalized companies, and successful completion of the Company’s development programs. Ultimately, the attainment of profitable operations is dependent on future events, including obtaining adequate financing to fulfill its development activities and generating a level of revenues adequate to support the Company’s cost structure.

# **H-SOURCE HOLDINGS LTD.**

## **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

**For the Three Months Ended March 31, 2019 and 2018**

**(Unaudited - Expressed in US Dollars)**

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### **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T**

The Company requires additional cash resources to support infrastructure, network infrastructure, and sales and marketing efforts of its software platform. These conditions, among others, raise substantial doubt about the Company's ability to continue as a going concern. The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. This basis of accounting contemplates the recovery of the Company's assets and the satisfaction of liabilities in the normal course of business. A successful transition to attaining profitable operations is dependent upon achieving a level of positive cash flows adequate to support the Company's cost structure.

The future viability of the Company is dependent on its ability to generate cash from operating activities, and to raise additional capital to finance its operations. The Company's failure to raise capital as and when needed could have a negative impact on its financial condition and ability to pursue its business strategies.

The condensed consolidated interim financial statements do not include any adjustments due to this uncertainty relating to the recoverability and classification of recorded asset amounts and classification of liabilities.

#### **Foreign currency translation**

The functional currency of an entity is the currency of the primary economic environment in which the entity operates. The functional currency of H-Source Holdings Ltd. is the Canadian dollar ("C\$") and of HSI and H-Source Distribution-US Inc. is the United States dollar. The reporting currency of the Company is the United States dollar. The functional currency determinations were conducted through an analysis of the consideration factors identified in IAS 21, "The Effects of Changes in Foreign Exchange Rates".

Transactions denominated in foreign currencies are converted to their functional currencies at exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to their functional currencies at the exchange rate prevailing at the reporting date. Non-monetary assets and liabilities are translated at historical exchange rates prevailing at each transaction date. Revenues and expenses are translated at exchange rates prevailing on the date of transactions. Exchange differences arising on the translation of monetary items or on settlement of monetary items are recognized in the statement of comprehensive loss in the period in which they arise, except where deferred in equity as a qualifying cash flow or net investment hedge.

The financial statements of each entity are prepared under their functional currencies and are translated into United States dollars for consolidation purposes as follows: assets and liabilities are translated using the exchange rate prevailing at the reporting date; expenses are translated using the average rates of exchange for the period. Gains and losses resulting from translation adjustments are recorded as other comprehensive income (loss).

#### **Reclassification**

Certain amounts in the prior period financial statements have been reclassified to conform to the presentation of the current period financial statements. These reclassifications had no effect on the previously reported net loss or net and comprehensive loss for the period.

#### **Patents**

Patents are capitalized if it is probable that the future economic benefits that are attributable to the patent will flow to the Company and the cost of the patent can be measured reliably. Patents have finite lives and are measured at cost less accumulated amortization and accumulated impairment losses over their useful lives. Patents are assessed for impairment whenever there is an indication that they may be impaired. If any such indication exists, the recoverable amount is estimated and an impairment loss is recognized whenever the carrying amount exceed their recoverable amount. At March 31, 2019, the patents were in service and amortized using the straight-line method over a 10-year period.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

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### NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

#### **Deferred software development costs**

Research costs are expensed as incurred. Costs related to the development of software are expensed as incurred unless such costs meet the criteria for deferral and amortization under IFRS. The criteria include identifiable costs attributable to a clearly defined product, the establishment of technical feasibility, identification of a market for the software, the Company's intent to market the software, and the existence of adequate resources to complete the project. Directly attributable costs that are capitalized as part of the software application include internal costs. Software development costs are amortized over an estimated useful life of three years. Capitalized software development is evaluated in each reporting period to determine whether it continues to meet the criteria for continued deferral and amortization.

#### **Inventory**

Inventory is stated at the lower of cost and net realizable value. Cost is determined on an average cost basis. Inventory costs include the purchase price and other costs directly related to the acquisition on of materials, and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less selling expenses.

#### **Loss per share**

Basic loss per share is calculated by dividing the loss attributable to common shareholders by the weighted average number of common shares outstanding in the period. For all periods presented, the loss attributable to common shareholders equals the reported loss attributable to owners of the Company. Diluted loss per share is calculated using the treasury stock method. Under the treasury stock method, the weighted average number of common shares outstanding for the calculation of diluted loss per share assumes that the proceeds to be received on the exercise of dilutive share options and warrants are used to repurchase common shares at the average market price during the period. Diluted loss per share is not presented as there are no dilutive securities outstanding.

#### **Impairment of assets**

The carrying amount of long-lived assets, specifically intangible assets, is reviewed at each reporting date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. Long-lived assets under construction are evaluated for impairment annually. An impairment loss is recognized whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognized in the statement of comprehensive loss.

The recoverable amount of assets is the greater of an asset's fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. There were no impairments recognized in the three months ended March 31, 2019 and 2018.

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Any reversal of impairment cannot increase the carrying value of the asset to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized in previous years.

#### **Share capital**

Common shares issued for non-cash consideration are recorded at the fair value of the shares at the time, or if the fair value of shares is not measurable, then the fair value of the services provided.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

### NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

#### **Share-based payment transactions**

The stock option and restricted stock unit plans allow Company directors, officers, employees and consultants to acquire shares of the Company. The fair value of share purchase options or restricted stock units granted are recognized as an employee or consultant expense with a corresponding increase in equity. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee. The fair value is measured at grant date and the share-based compensation is expensed based on graded vesting. When the value of goods or services received in exchange for the share-based payment cannot be reliably estimated, the fair value of the share purchase options granted is measured using the Black-Scholes Option Pricing Model taking into account the terms and conditions upon which the share purchase options were granted. Forfeiture rates are estimated in advance and are used in the estimate of the share-based expense for the financial statement period. Equity-settled share-based payment transactions with non-employees are measured at the fair value of the goods or services received. However, if the fair value cannot be estimated reliably, the share-based payment transaction is measured at the fair value of the equity instruments granted at the date the Company receives the goods or the services.

#### **Warrants**

Proceeds from issuances by the Company of units consisting of shares and warrants are allocated based on the residual method, whereby the carrying amount of the warrants is determined based on any difference between gross proceeds and the estimated fair market value of the shares. If the proceeds from the offering are less than or equal to the estimated fair market value of shares issued, a nil carrying amount is assigned to the warrants.

#### **Financial instruments**

The Company adopted all of the requirements of IFRS 9 Financial Instruments on January 1, 2018. IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 utilizes a revised model for recognition and measurement of financial instruments in a single, forward-looking “expected loss” impairment model. The following is the Company’s accounting policy for financial instruments under IFRS 9:

##### (i) Classification

The Company classifies its financial instruments in the following categories: financial assets at fair value through profit or loss (“FVTPL”), at fair value through other comprehensive income (loss) (“FVTOCI”) or at amortized cost. The Company determines the classification of its financial assets at initial recognition. The classification of debt instruments is driven by the Company’s business model for managing the financial assets and their contractual cash flow characteristics. Equity instruments that are held for trading are classified as FVTPL. For other equity instruments, on the day of acquisition the Company can make an irrevocable election (on an instrument-by-instrument basis) to designate them as at FVTOCI. Financial liabilities are measured at amortized cost, unless they are required to be measured at FVTPL (such as instruments held for trading or derivatives) or if the Company has opted to measure them at FVTPL.

The Company completed a detailed assessment of its financial assets and liabilities as at January 1, 2018. The following table shows the original classification under IAS 39 and the new classification under IFRS 9:

<u>Financial assets/liabilities</u>	<u>Original Classification IAS 39</u>	<u>New Classification IFRS 9</u>
Cash	FVTPL	FVTPL
Short-term investments	FVTPL	FVTPL
Accounts receivable	Amortized cost	Amortized cost
Accounts and loans payable	Amortized cost	Amortized cost
Due to related parties	Amortized cost	Amortized cost

The adoption of IFRS 9 resulted in no impact to the opening accumulated deficit nor to the opening balance of accumulated comprehensive income on January 1, 2018.

##### (ii) Measurement

Financial assets and liabilities at amortized cost are initially recognized at fair value plus or minus transaction costs, respectively, and subsequently carried at amortized cost less any impairment.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

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### NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

Financial assets and liabilities carried at FVTPL are initially recorded at fair value and transaction costs are expensed in the statements of loss. Realized and unrealized gains and losses arising from changes in the fair value of the financial assets and liabilities held at FVTPL are included in the statements of loss in the period in which they arise.

Debt investments at FVTOCI are subsequently measured at fair value. Interest income calculated using the effective interest method, foreign exchange gains and losses and impairment are recognized in profit or loss. Other net gains and losses are recognized in other comprehensive income ("OCI"). On derecognition, gains and losses accumulated in OCI are reclassified to profit or loss.

Equity investments at FVTOCI are subsequently measured at fair value. Dividends are recognized as income in profit or loss unless the dividend clearly represents a recovery of part of the cost of the investment. Other net gains and losses are recognized in OCI and are never reclassified to profit or loss.

#### (iii) Impairment of financial assets at amortized cost

The Company recognizes a loss allowance for expected credit losses on financial assets that are measured at amortized cost. At each reporting date, the Company measures the loss allowance for the financial asset at an amount equal to the lifetime expected credit losses if the credit risk on the financial asset has increased significantly since initial recognition. If at the reporting date, the financial asset has not increased significantly since initial recognition, the Company measures the loss allowance for the financial asset at an amount equal to the twelve month expected credit losses. The Company shall recognize in the statements of loss and comprehensive loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognized.

#### (iv) Derecognition

The Company derecognizes financial assets only when the contractual rights to cash flows from the financial assets expire, or when it transfers the financial assets and substantially all of the associated risks and rewards of ownership to another entity.

The Company derecognizes a financial liability when its contractual obligations are discharged or cancelled, or expire. The Company also derecognizes a financial liability when the terms of the liability are modified such that the terms and/or cash flows of the modified instrument are substantially different, in which case a new financial liability based on the modified terms is recognized at fair value.

Gains and losses on derecognition are generally recognized in profit or loss.

### **Revenue**

The Company adopted all of the requirements of IFRS 15 Revenue from Contracts with Customers ("IFRS 15") as of January 1, 2018. IFRS 15 utilizes a methodical framework for entities to follow in order to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Revenue is recognized based on a five-step model:

1. Identify the contract(s) with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when (or as) the performance obligations are satisfied.

# **H-SOURCE HOLDINGS LTD.**

## **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

**For the Three Months Ended March 31, 2019 and 2018**

**(Unaudited - Expressed in US Dollars)**

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### **NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T**

The Company evaluates whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as commissions. When the Company is primarily obligated in a transaction, is subject to inventory risk, has latitude in establishing prices and selecting suppliers, or has several but not all of these indicators, revenue is recorded at the gross sale price at the time of shipping. The Company records the net amounts as commissions earned if it is not primarily obligated and does not have latitude in establishing prices. Such amounts earned are determined using a percentage of seller revenues.

Revenue from product sales are recognized when the risks and rewards of ownership pass to the buyer, collection is reasonably assured and the price is reasonably determinable. Product sales and related shipping revenues are generally recorded when the products are shipped and title passes to customers.

Service sales represent commissions earned and are recognized when service has been rendered. Once products are delivered to the Company's customers, the risks of obsolescence and loss have been transferred to the customer, and either the customer has accepted the products in accordance with the sales order or the acceptance provisions have lapsed.

#### **Provisions**

The Company recognizes provisions for liabilities of uncertain timing or amount including those for legal disputes. If applicable, the provision is measured at the best estimate of the expenditure required to settle the obligation at the reporting date, discounted at a pre-tax rate reflecting current market assessments of the time value of money and risks specific to the liability. There were no provisions recognized as of March 31, 2019 and December 31, 2018.

#### **Recent Accounting Pronouncements**

The following is a summary of recent accounting pronouncements the Company reasonably expects to be applicable at a future date. The Company adopted the following standard as of the effective date.

#### **IFRS 16 – Leases (“IFRS 16”)**

IFRS 16 replaces IAS 17 “Leases” and the related interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting is not substantially changed. The standard is effective for annual periods beginning on or after January 1, 2019, with early adoption permitted for entities that have adopted IFRS 15. As the Company currently does not have any leases, this standard is not expected to impact the financial statements.

### **NOTE 3 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS**

#### **Estimates and assumptions**

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and contingent assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Estimates and assumptions are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcomes can differ significantly from these estimates.

Areas requiring a significant degree of estimation relate to the determination of the life of patents and software development costs, the recoverability of carrying value of long-term assets, fair value measurements for financial instruments and stock-based compensation and other equity-based payments, and the recoverability and measurement of deferred tax assets and liabilities. Actual results may differ from those estimates and judgments.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

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### **NOTE 3 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS-CON'T**

#### **Significant judgments**

The preparation of financial statements in accordance with IFRS requires management to make judgments, apart from those involving estimates, in applying accounting policies. The most significant judgments applying to the Company's financial statements include:

- Continuing feasibility of internally developed software;
- Whether there are indications of impairment of the Company's non-current assets; and
- The assessment of the Company's ability to continue as a going concern and whether there are events or conditions that may give rise to significant uncertainty.

#### **Fair value measurements**

A number of assets and liabilities included in the Company's financial statements require measurement at, and/or disclosure of, fair value.

The fair value measurement of the Company's financial and non-financial assets and liabilities utilizes market observable inputs and data as far as possible. Inputs used in determining fair value measurements are categorized into different levels based on how observable the inputs used in the valuation technique utilized are (the 'fair value hierarchy'):

- *Level 1:* Quoted prices in active markets for identical items (unadjusted)
- *Level 2:* Observable direct or indirect inputs other than Level 1 inputs
- *Level 3:* Unobservable inputs (i.e. not derived from market data).

The classification of an item into the above levels is based on the lowest level of the inputs used that has a significant effect on the fair value measurement of the item. Transfers of items between levels are recognized in the period they occur.

The Company measures below market rate debt at fair value at inception and amortized cost over the remaining life of the notes.

#### **Recoverability of long-lived assets**

The recoverable amount of assets is the greater of an asset's fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

### **NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT**

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board of Directors approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures.

The principal financial instruments used by the Company, from which financial instrument risk arises, are cash, accounts receivable, short-term investments, accounts payable and other accrued liabilities, due to related parties, and loans payable.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

### NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT-CON'T

	March 31, 2019	December 31, 2018
<b>Financial Assets</b>		
Cash	\$ 55,189	\$ 72,864
Accounts receivable	192,837	207,676
Short-term investments	14,966	18,655
<b>Total financial assets</b>	<b>\$ 262,992</b>	<b>\$ 299,194</b>
<b>Financial Liabilities</b>		
Accounts payable and other accrued liabilities	\$ 917,322	\$ 648,843
Due to related parties	57,925	47,925
Loans payable	335,657	200,657
<b>Total financial liabilities</b>	<b>\$ 1,310,904</b>	<b>\$ 897,425</b>

The type of risk exposure and the way in which such exposure is managed is provided as follows:

**a) Credit risk**

Credit risk is the risk of loss associated with a counter party's inability to fulfill its payment obligations. The Company's primary exposure to credit risk is on its cash accounts. Cash accounts are held with a major bank in the United States. The Company has deposited the cash with its bank from which management believes the risk of loss is remote.

**b) Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach to managing liquidity is to ensure that it will have sufficient liquid assets to meet liabilities when they become due. The Company is exposed to liquidity risk as it does not have sufficient cash to settle its current liabilities, refer to Note 2 and the going concern discussion for further information about the Company's plans to manage liquidity risk.

**c) Market risk**

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates will affect the Company's value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

*Interest rate risk*

The Company has cash and cash equivalents balances and interest-bearing debt. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. All debt bears fixed interest rates.

*Foreign currency risk*

Currency risk refers to the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchanges rates. The Company has certain expenditures that are denominated in US dollars and other operating expenses that are in Canadian dollars. The Company's exposure to foreign currency risk arises primarily on fluctuations between the Canadian dollar and the US dollar.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

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### NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT-CON'T

#### d) Capital management

The Company considers its cash and share capital as capital. The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue new debt, acquire or dispose of assets or adjust the amount of cash. There was no change in the Company's approach to capital management during the period ended March 31, 2019.

### NOTE 5 - SHORT TERM INVESTMENT

As at March 31, 2019, the Company has a short-term investment of \$14,966 (2018 - \$18,655) with a major financial institution and \$150 interest receivable, included in accounts receivable, due on July 11, 2019. The short-term investment has an annual yield of prime minus 2.60%.

### NOTE 6 – GENERAL AND ADMINISTRIVE EXPENSES

	March 31, 2019	March 31, 2018
Office	\$ 27,960	\$ 60,938
Rent	15,449	15,449
Software expense	112,209	97,168
Transfer agent and regulatory fees	8,083	11,811
Travel	22,334	30,279
	<u>\$ 186,035</u>	<u>\$ 215,645</u>

### NOTE 7 – INTANGIBLE ASSETS

Cost	Patents	Software Development Costs
At December 31, 2017	\$ 95,964	\$ 380,043
Additions	23,412	-
Amortization	(11,878)	(195,510)
At December 31, 2018	107,498	184,533
Amortization	(3,251)	(46,133)
At March 31, 2019	<u>\$ 104,247</u>	<u>\$ 138,400</u>

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

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### NOTE 8 – ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	March 31, 2019	December 31, 2018
Accounts payable	\$ 861,644	\$ 604,659
Accrued payroll and taxes	55,678	37,504
Unearned revenue	-	6,680
	<u>\$ 917,322</u>	<u>\$ 648,843</u>

### NOTE 9 – LOANS PAYABLE

On April 16, 2018, the Company entered into a term sheet whereby certain non-arm's length parties (the "Lenders") advanced \$174,304 to the Company as a loan (the "Loan"). The Loan bears an interest rate of 3% per month (36% per annum), calculated and payable monthly in arrears. The term of the Loan is 120 days commencing on the date on which the principal amount is advanced to the Company.

On April 16, 2018, the Company entered into a memorandum of understanding with the same Lenders as the Loan whereby the Loan is to be used by the Company to purchase certain assets. If the sale of the assets occurs on or before 60 days after the purchase, 15% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder. If the sale of the assets occurs 60 days after, 20% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder.

During the third quarter of 2018, the Company repaid the principal amount of \$86,665 and interest of \$9,226. As at March 31, 2019, \$87,639 of the principal amount still remains outstanding, \$35,110 was accrued as interest payable and \$30,661 was accrued as profit sharing payable.

On November 30, 2018, the Company entered into a term sheet whereby certain non-arm's length parties (the "Lenders") advanced \$113,018 to the Company as a loan (the "Loan"). The Loan bears an interest rate of 2% per month (24% per annum), calculated and payable monthly in arrears. The term of the Loan is 120 days commencing on the date on which the principal amount is advanced to the Company.

On November 29, 2018, the Company entered into a memorandum of understanding with the same Lenders as the Loan whereby the Loan is to be used by the Company to purchase certain assets. If the sale of the assets occurs on or before 120 days after the date of the memorandum, 10% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder. If the sale of the assets occurs 120 days after, 20% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder.

As at March 31, 2018, the Company repaid \$nil of the principal amount, \$9,399 was accrued as interest and \$6,956 was accrued as profit sharing during the period.

On February 25, 2019, the Company issued \$135,000 of unsecured promissory notes, including a \$35,000 promissory note payable to the president of the Company. The promissory notes bear interest at a rate of 10% and mature on February 25, 2020. As at March 31, 2019, the Company repaid \$nil of the principal amount and \$1,237 was accrued as interest payable.

### NOTE 10 – SHARE CAPITAL

#### **Authorized common shares**

The authorized share capital of the Company is unlimited number of common shares without par value.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

### NOTE 10 – SHARE CAPITAL-CON'T

#### Issued shares

- a) On January 4, 2018, the Company completed a brokered private placement of 17,250,000 common shares at a price of C\$0.10 per share for gross proceeds of \$1,286,850 (C\$1,725,000). The Company paid the agent a cash commission of \$95,814 and issued 1,284,376 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.10 for a period of 18 months from the closing of the offering. The fair value of the options was determined to be \$50,812. The Company paid legal fees and other share issuance costs of \$53,235.
- b) On July 12, 2018, the Company completed a brokered private placement of 7,666,667 common shares at a price of C\$0.15 per share for gross proceeds of \$873,908 (C\$1,150,000). The Company paid the agent a cash commission of \$65,543 (C\$86,250) and issued 575,000 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.15 for a period of 18 months from the closing of the offering. The fair value of the options was determined to be \$38,953. The Company paid legal fees and other share issuance costs of \$61,776.
- c) On August 31, 2018, 48,905 agent compensation options were exercised at C\$0.18 each for proceeds of \$6,796.
- d) On December 17, 2018, the Company completed a non-brokered private placement of 4,000,000 common shares at a price of C\$0.10 per share for aggregate gross proceeds of \$293,643 (C\$400,000). The Company paid legal fees of \$1,430.

#### Share purchase option compensation plan

The Company has adopted a Stock Option Plan (the “Plan”) pursuant to which options may be granted to directors, officers, employees and consultants of the Company. Under the terms of the Plan, the Company can issue a maximum of 10% of the issued and outstanding common shares at the time of the grant, and the exercise price of each option is equal to or above the market price of the common shares on the grant date. Options granted under the Plan including vesting and the term, are determined by, and at the discretion of, the Board of Directors.

The continuity of stock options for the period ended March 31, 2019 and year ended December 31, 2018 is as follows:

	March 31, 2019		December 31, 2018	
	Number of	Weighted Average	Number of	Weighted Average
	Options	Exercise Price	Options	Exercise Price
		C\$		C\$
Options outstanding, beginning of the period	5,672,500	\$0.17	3,902,500	\$0.18
Issued	-	-	1,770,000	\$0.16
Exercised	-	-	-	-
Expired	(665,000)	\$0.16	-	-
Options outstanding, end of the period	5,007,500	\$0.17	5,672,500	\$0.17
Options exercisable, end of the period	4,592,500	\$0.18	5,202,500	\$0.17

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

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### NOTE 10 – SHARE CAPITAL-CON’T

The options outstanding at March 31, 2019 are as follows:

Number Outstanding	Weighted Average Remaining Contractual Life	Expiry Date
1,520,000	1.42 years	August 31, 2020
200,000	1.76 years	January 1, 2021
300,000	2.36 years	August 9, 2021
1,122,500	0.59 years	October 31, 2019
250,000	0.59 years	October 31, 2019
1,615,000	2.34 years	August 1, 2021
5,007,500	1.56 years	

On August 1, 2018, the Company granted 1,300,000 stock options to directors and officers, 445,000 stock options to employees, and 25,000 stock options to a consultant of the Company. The options are exercisable at C\$0.16 and expire on August 1, 2021. The 1,300,000 options to directors and officers are vested immediately. The 445,000 options to employees and 25,000 options to a consultant vest 33.33% on August 1, 2019, 33.33% on August 1, 2020, and 33.34% on August 1, 2021. The Company valued the options to directors and officers, employees, and consultant at \$106,082, \$36,313 and \$942 respectively using the Black-Scholes Option Pricing Model to estimate the fair value of the options using the following assumptions: risk free interest rate of 2.22%; dividend yield of 0%; expected volatility of 109.95%; and expected option life of 3 years. The Company recorded a share-based payment for vesting options in the amount of \$5,487 and \$nil for the periods ending March 31, 2019 and 2018, respectively. As at March 31, 2019, there was \$22,579 (2018-\$nil) of unrecognized share-based payments related to nonvested stock options granted under the Plan.

Option pricing models require the use of highly subjective estimates and assumptions including the expected stock price volatility. Changes in the underlying assumptions can materially affect the fair value estimates and therefore, in management’s opinion, existing models do not necessarily provide reliable measure of the fair value of the Company’s stock options.

#### **Restricted stock unit plan**

The Company has adopted a Restricted Stock Unit (“RSU”) plan. The RSU Plan was designed to provide certain directors, officers, other key employees and consultants of the Company (“Participants”) and its related entities with the opportunity to acquire RSUs of the Company in order to enable them to participate in the long-term success of the Company and to promote a greater alignment of their interests with the interests of the shareholders. Under the terms of the plan, RSU’s are granted to Participants and the shares issued vest over a period of up to three years from the date of grant. Each RSU gives the Participant the right to receive one common share of the Company. The Company has reserved a maximum of 1,401,770 common shares for issuance under this plan. As at March 31, 2019, the Company has 351,770 RSU’s available to be issued under the RSU plan.

The Company uses the fair value method to recognize the obligation and compensation expense associated with the RSU’s. The fair value of RSU’s issued is determined on the grant date based on the market price of the common shares on the grant date multiplied by the number of RSUs granted and taking into account market conditions. The fair value is expensed over the vesting term. Upon conversion of the RSU, the carrying amount is recorded as an increase in common share capital and a reduction in the share-based payment reserve.

On August 1, 2018, the Company granted 1,050,000 RSUs to officers and an employee of the Company, in which 40%, 40% and 20% can be converted into common shares upon achieving certain performance conditions, which are as follows: the Company’s share price reaching C\$0.20 based on 10 consecutive trading day weighted average; C\$0.25 based on 10 consecutive trading day weighted average; and C\$0.35 based on 10 consecutive trading day weighted average. The RSUs will expire on December 31, 2021. As at March 31, 2019, there were 990,000 RSUs issued and outstanding. The Company recorded a share-based payment of \$2,510 and \$nil for the periods ending March 31, 2019 and 2018, respectively, for vesting RSUs.

# H-SOURCE HOLDINGS LTD.

## NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Three Months Ended March 31, 2019 and 2018

(Unaudited - Expressed in US Dollars)

### NOTE 10 – SHARE CAPITAL-CON'T

During the year ended December 31, 2018, the first performance condition was met and 420,000 RSUs can be converted into 420,000 common shares. As at March 31, 2019, these RSUs have not been converted to common shares of the Company.

#### **Compensation options**

On January 4, 2018, the Company issued 1,284,375 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.10 to July 4, 2019. The fair value of the compensation options of \$50,812 included in share issuance cost was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 1.68%; dividend yield of 0%; expected volatility of 49.15%; and expected life of 1.5 years.

On July 12, 2018, the Company issued 575,000 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.15 for a period of 18 months from the closing of the offering. The fair value of the compensation options of \$38,953 included in share issuance cost was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 1.93%; dividend yield of 0%; expected volatility of 100.8%; and expected life of 1.5 years.

	March 31, 2019		December 31, 2018	
	Number of options	Weighted Average Exercise Price C\$	Number of options	Weighted Average Exercise Price C\$
Options outstanding, beginning of the period	1,859,375	\$0.12	1,304,141	\$0.18
Issued	-	-	1,859,375	\$0.12
Exercised	-	-	(48,905)	\$0.18
Expired	-	-	(1,255,235)	\$0.18
Options outstanding, end of the period	1,859,375	\$0.12	1,859,375	\$0.12

### NOTE 11 – SUPPLEMENTAL CASH FLOW INFORMATION

	March 31, 2019	March 31, 2018
Interest paid in cash	\$ -	\$ -
Income taxes paid in cash	\$ -	\$ -

#### **Investing and financing non-cash transactions**

	March 31, 2019	March 31, 2018
Agent compensation options issued as share issuance cost	\$ -	\$ 50,812
Share-based payments	\$ 7,997	\$ -

### NOTE 12 – RELATED PARTY TRANSACTIONS

Related party transactions are as follows:

Key management (officers and directors) personnel compensation including share-based payments for the three months ended March 31, 2019 was \$88,760 (2017 - \$75,000).

As at March 31, 2019, \$41,950 (2018 - \$nil) and \$15,975 (2018 - \$nil) were due to related parties for bonuses and other amounts payable to the Company's CEO and President respectively.

# **H-SOURCE HOLDINGS LTD.**

## **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

**For the Three Months Ended March 31, 2019 and 2018**

**(Unaudited - Expressed in US Dollars)**

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### **NOTE 12 – RELATED PARTY TRANSACTIONS-CONT**

On February 25, 2019, the Company issued a \$35,000 unsecured promissory note payable to the president of the Company. The promissory note bears interest at a rate of 10% and matures on February 25, 2020. As at March 31, 2019, the Company repaid \$nil of the principal amount and \$321 was accrued as interest payable.

As at March 31, 2019, the Company owed \$39,990 (2017 - \$nil) for a loan payable to a director and \$5,551 (2018 - \$nil) in related interest and profit sharing payable. The loan bears an interest rate of 2% per month (24% per annum) and has a term of 120 days commencing on the date on which the principal amount was advanced to the Company. The loan was utilized to purchase certain assets and if the sale of those assets occurs on or before 120 days, 10% of the net proceeds shall be paid to the director. If the sale of the assets occurs after 120 days, 20% of the net proceeds shall be paid to the director.

### **NOTE 13 – SUBSEQUENT EVENTS**

On May 10, 2019, the Company announced a non-brokered financing of unsecured convertible debentures in the principal amount of up to \$2,500,000 (before OID as defined below). The debentures will mature on the date that is twelve months from the date of issuance and bear interest at a rate of 12% per annum, calculated and paid monthly in arrears commencing on the day that is 30 days from the issue date, on the earlier of (i) the maturity date or (ii) at the election of the holder and will have an original issuer discount equal to 10% of the principal amount (the “OID”).

The principal amount and any accrued and unpaid interest on the debenture may be convertible into common shares in the capital of the Company, in whole or in part, at any time following the issue date but on or before the maturity date at a conversion price of \$0.06 per share. The debentures and the shares issuable upon the conversion of the debentures will be subject to a statutory resale restriction for four months and one day from the date of closing. The Company may pay finder’s fees in accordance with TSX Venture Exchange policies and intends to use the proceeds of the financing for general corporate purposes. The offering of the debentures is subject to the receipt of all necessary approvals, including the final approval of the TSX Venture Exchange. The debentures will not be listed or posted for trading on any exchange.

On May 29, 2019, H-Source formed a new Washington Limited Liability Corporation, HSI Sales, LLC, comprised of a sales lead implementing an independent sales representative network. The Company expects activity to start in June of 2019.