

# **EcoSynthetix Inc.**

Consolidated Financial Statements  
**December 31, 2019 and December 31, 2018**  
(expressed in US dollars)



## *Independent auditor's report*

To the Shareholders of EcoSynthetix Inc.

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### *Our opinion*

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of EcoSynthetix Inc. and its subsidiaries (together, the Entity) as at December 31, 2019 and 2018, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

#### **What we have audited**

The Entity's consolidated financial statements comprise:

- the consolidated balance sheets as at December 31, 2019 and 2018;
- the consolidated statements of operations and comprehensive loss for the years then ended;
- the consolidated statements of shareholders' equity for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

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### *Basis for opinion*

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### **Independence**

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

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### *Other information*

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis.

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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### *Responsibilities of management and those charged with governance for the consolidated financial statements*

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

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### *Auditor's responsibilities for the audit of the consolidated financial statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from



error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Entity to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Jennifer Psutka.

*PricewaterhouseCoopers LLP*

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Ontario  
March 2, 2020

# EcoSynthetix Inc.

## Consolidated Balance Sheets

As at December 31, 2019 and December 31, 2018

(expressed in US dollars)

	2019	2018
<b>Assets</b>		
<b>Current assets</b>		
Cash	7,975,713	14,207,342
Short-term investments (note 5)	35,720,548	30,635,400
Accounts receivable (note 6)	1,824,581	2,347,622
Inventory (note 7)	2,268,961	2,722,742
Government grants receivable (note 8)	114,956	140,000
Prepaid expenses	75,973	129,240
	<u>47,980,732</u>	<u>50,182,346</u>
<b>Non-current assets</b>		
Property, plant and equipment (note 9)	<u>6,729,371</u>	<u>6,174,898</u>
<b>Total assets</b>	<u>54,710,103</u>	<u>56,357,244</u>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Trade accounts payable and accrued liabilities (note 10)	1,360,568	2,255,430
<b>Non-current liabilities</b>		
Lease liability (note 11)	<u>1,176,643</u>	<u>-</u>
<b>Total liabilities</b>	<u>2,537,211</u>	<u>2,255,430</u>
<b>Shareholders' Equity</b>		
<b>Common shares</b> (note 14)	490,590,406	491,618,125
<b>Contributed surplus</b>	10,351,658	9,798,803
<b>Accumulated deficit</b>	<u>(448,769,172)</u>	<u>(447,315,114)</u>
<b>Total shareholders' equity</b>	<u>52,172,892</u>	<u>54,101,814</u>
<b>Total liabilities and shareholders' equity</b>	<u>54,710,103</u>	<u>56,357,244</u>

Approved by the Board of Directors

(signed)

Paul Lucas, Chairman

(signed)

Jeff MacDonald, Chief Executive Officer

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

# EcoSynthetix Inc.

## Consolidated Statements of Operations and Comprehensive Loss For the years ended December 31, 2019 and December 31, 2018

(expressed in US dollars)

	2019	2018
<b>Net sales</b>	18,446,922	22,799,329
<b>Cost of sales</b>	14,417,197	18,302,982
<b>Gross profit on sales</b>	4,029,725	4,496,347
<b>Expenses</b>		
Selling, general and administrative	4,849,977	5,511,936
Research and development	1,742,452	2,219,275
Termination benefits	-	222,778
	6,592,429	7,953,989
<b>Loss from operations</b>	(2,562,704)	(3,457,642)
<b>Interest income</b>	1,108,646	926,884
<b>Net loss and comprehensive loss</b>	(1,454,058)	(2,530,758)
<b>Basic and diluted loss per common share</b> (note 19)	(0.02)	(0.04)
<b>Weighted average number of common shares outstanding</b>	58,297,045	59,498,498

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

# EcoSynthetix Inc.

## Consolidated Statements of Shareholders' Equity

For the years ended December 31, 2019 and December 31, 2018

(expressed in US dollars)

	Common shares \$	Contributed surplus \$	Accumulated deficit \$	Total \$
<b>Balance – December 31, 2017</b>	493,631,495	9,550,445	(444,784,356)	58,397,584
Share-based compensation (note 13)	-	780,395	-	780,395
Common share options exercised (note 14)	636,384	(248,808)	-	387,576
Deferred share units converted	110,507	(110,507)	-	-
Restricted share units converted	172,722	(172,722)	-	-
Common shares repurchased	(2,932,983)	-	-	(2,932,983)
Net loss and comprehensive loss	-	-	(2,530,758)	(2,530,758)
<b>Balance – December 31, 2018</b>	491,618,125	9,798,803	(447,315,114)	54,101,814
Share-based compensation (note 13)	-	784,623	-	784,623
Common share options exercised (note 14)	327,661	(111,841)	-	215,820
Restricted share units converted	119,927	(119,927)	-	-
Common shares repurchased	(1,475,307)	-	-	(1,475,307)
Net loss and comprehensive loss	-	-	(1,454,058)	(1,454,058)
<b>Balance – December 31, 2019</b>	490,590,406	10,351,658	(448,769,172)	52,172,892

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

# EcoSynthetix Inc.

## Consolidated Statements of Cash Flows

For the years ended December 31, 2019 and December 31, 2018

(expressed in US dollars)

	2019	2018
<b>Cash provided by (used in)</b>		
<b>Operating activities</b>		
Net loss and comprehensive loss	(1,454,058)	(2,530,758)
Items not affecting cash		
Depreciation	1,381,061	1,248,946
Share-based compensation (note 13)	784,623	780,395
Other	65,527	227,814
Changes in non-cash working capital		
Accounts receivable	523,041	(51,367)
Inventory	458,881	(211,982)
Government grants receivable (note 8)	25,044	(140,000)
Prepaid expenses	23,585	24,284
Trade accounts payable and accrued liabilities	(1,016,944)	(774,477)
Accrued termination benefits	-	(39,830)
Interest on short-term investments		
Interest received on short-term investments	892,733	187,318
Accrued interest on short-term investments	(977,881)	(651,597)
	<u>705,612</u>	<u>(1,931,254)</u>
<b>Investing activities</b>		
Purchase of property, plant and equipment (note 9)	(458,172)	(218,865)
Receipts on mature short-term investments (note 5)	30,000,000	30,000,000
Purchase of short-term investments (note 5)	(35,000,000)	(30,000,000)
	<u>(5,458,172)</u>	<u>(218,865)</u>
<b>Financing activities</b>		
Principal payments made on lease liability (note 11)	(187,427)	-
Common shares repurchased (note 14)	(1,475,307)	(2,932,983)
Exercise of common share options (note 14)	215,820	387,576
	<u>(1,446,914)</u>	<u>(2,545,407)</u>
<b>Effect of exchange rate changes on cash</b>	<u>(32,155)</u>	<u>(213,960)</u>
<b>Change in cash during the year</b>	(6,231,629)	(4,909,486)
<b>Cash – Beginning of year</b>	<u>14,207,342</u>	<u>19,116,828</u>
<b>Cash – End of year</b>	<u>7,975,713</u>	<u>14,207,342</u>

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



# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

### 1 Business operations

EcoSynthetix Inc. (EcoSynthetix or the Company) is engaged in the development and commercialization of environmentally friendly, bio-based technologies as replacement solutions for synthetic, petrochemical-based adhesives and other related products in the Americas, Europe, Middle East and Africa (EMEA) and Asia Pacific. EcoSynthetix is incorporated and domiciled in Canada. The address of its registered office is 3365 Mainway, Burlington, Ontario, Canada.

### 2 Summary of significant accounting policies

#### Statement of compliance

These consolidated financial statements have been authorized for issuance by the Board of Directors of the Company on March 2, 2020.

#### Basis of preparation

The consolidated financial statements have been prepared under International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), using the historical cost convention.

#### Use of estimates and judgments

The preparation of consolidated financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. These estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future. Actual results could differ from those estimates.

Significant estimates made by the Company include estimates of useful lives of property, plant and equipment, share-based compensation, allowances for expected credit losses (ACL), provisions for inventory that are carried in excess of net realizable value and the realizability of deferred income tax assets.

Property, plant and equipment are tested for impairment at the end of each reporting period or when events or changes in circumstances indicate the carrying amounts may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units or CGUs). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (which is the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. Non-financial assets that have been impaired previously are reviewed for possible reversal of impairment at each reporting date.

The Company has determined it has a single CGU, assessed as the entity as a whole, due to the interdependence of the Company's assets and liabilities in generating cash inflows. The recoverable amount of the CGU is highly dependent on projected revenues, expenses and discount rates used in performing an analysis.

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

### **Basis of consolidation**

The consolidated financial statements of the Company consolidate the accounts of EcoSynthetix and all of its subsidiaries. All intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Subsidiaries are all entities wholly owned and controlled by the Company and include the following entities:

- EcoSynthetix Ltd.
- EcoSynthetix Coporation
- EcoSynthetix B.V.

### **Foreign currency translation**

- i) Functional and presentation currency

Items included in the financial statements of each consolidated entity in the Company's consolidated financial statements are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in US dollars, which is the Company's reporting currency. The functional currency of all entities is US dollars.

- ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign currency exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than the Company's functional currency are recognized in the consolidated statements of operations and comprehensive loss.

### **Cash**

Cash consists of deposits held with banks.

### **Financial instruments**

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the financial instrument. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership. Financial assets and financial liabilities are offset and the net amount is reported in the consolidated balance sheets when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the financial asset and settle the financial liability simultaneously.

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

The Company determines the classification of financial assets and liabilities at initial recognition. The Company's financial assets are classified into one of the following three categories:

- Amortized cost – If the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (held to collect).
- Fair value through other comprehensive income (FVOCI) – If the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.
- Fair value through profit or loss (FVPL) – A financial asset is measured at FVPL unless it is measured at amortized cost or through other comprehensive income.

The Company's financial assets measured at amortized cost include cash, short-term investments, accounts receivable and government grants receivable. The Company does not have any financial assets measured at FVOCI or FVPL. The Company's financial liabilities, trade accounts payable and accrued liabilities and lease liability are measured at amortized cost. Financial assets and liabilities included in this category are initially recognized at fair value (net of transaction costs, if applicable) and are subsequently measured at amortized cost using the effective interest rate method less allowances for losses.

A financial asset is derecognized when its contractual right to the cash flows that compose the financial asset expire or substantially all the risks and rewards of the asset are transferred. A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expired. Gains and losses on derecognition are recognized in net income (loss). If a financial instrument is modified and does not result in derecognition, the gross carrying value of the financial instrument is revised and the modification gain or loss is recognized in net income (loss).

The Company applies a simplified approach to measure an ACL where the loss allowance is always equal to lifetime expected credit losses (ECL). The Company assesses whether there has been a significant increase in credit risk since initial recognition of a financial asset and both the ECL and ACL measurement at each reporting date. Increases or decreases in the ACL are recognized as impairment gains and losses in net income (loss).

### **Inventory**

Inventory is valued at the lower of cost, determined on a first-in, first-out basis, and net realizable value. Inventory costs include the costs of material, contract manufacturing costs, variable overhead and an allocation of fixed manufacturing overhead, including depreciation based on normal production volumes. Net realizable value is the estimated selling price less applicable selling expenses.

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

### Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost can be measured reliably. The carrying amount of a replaced asset is derecognized when replaced. Repairs and maintenance costs are charged to the consolidated statements of operations and comprehensive loss during the year in which they are incurred.

Depreciation is calculated on a straight-line method to reduce the cost of the asset to its residual value over its estimated useful life. The depreciation period applicable to each category of property, plant and equipment is as follows:

Leasehold improvements	remaining lease term
Computer hardware	3 years
Machinery and equipment	2 – 15 years

Useful lives and residual values are reviewed and adjusted, if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of other gains and losses in the consolidated statements of operations and comprehensive loss.

### Leases

The Company assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Company assesses whether:

- the contract involves the use of an identified asset. This may be specified explicitly or implicitly and should be physically distinct or represent substantially all the capacity of a physically distinct asset. If the supplier has a substantive substitution right, then the asset is not identified; and
- the Company has the right to direct the use of the asset. The Company has the right when it has the decision-making rights that are most relevant to changing how and for what purpose the asset is used. In rare cases where the decision about how and for what purpose the asset is used is predetermined, the Company has the right to direct the use of the asset if either:
  - the Company has the right to operate the asset; or
  - the Company designed the asset in a way that predetermines how and for what purpose it will be used.

# **EcoSynthetix Inc.**

## **Notes to Consolidated Financial Statements**

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(expressed in US dollars, unless otherwise noted)

The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received. The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property, plant and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. The Company uses its incremental borrowing rate as the discount rate. Lease payments include fixed payments, variable payments, amounts expected to be payable under a residual guarantee and payments under a purchase option, extension option and termination penalties if the Company is reasonably certain it will exercise those options or terminate the lease early.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Company's estimate of the amount expected to be payable under a residual value guarantee, or if the Company changes its assessment of whether it will exercise a purchase, extension or termination option.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

### **Provisions**

Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period and are discounted to present value where the effect is material. The Company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

### **Research and product development costs**

Expenditures during the research phase are expensed as incurred. Expenditures during the development phase are expensed as incurred, unless it is probable that future economic benefits that are attributable to the asset will flow to the Company and the cost of the asset can be measured reliably. No development costs have been capitalized to date.

### **Government grants**

Government grants include funding for government research and product development support. Research and product development funding is recognized when there is reasonable assurance the Company has complied

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## **Notes to Consolidated Financial Statements**

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(expressed in US dollars, unless otherwise noted)

with the conditions attached to the funding arrangement and is recognized as the applicable costs are incurred. Research and product development funding is presented as a reduction in research and product development expenses, unless it is for the reimbursement of an asset, in which case it is accounted for as a reduction in the carrying amount of the applicable asset.

### **Revenue recognition**

Revenue is recognized when the Company has satisfied its performance obligation as set out in the contract with the customer, the contract has commercial substance and it is probable that the Company will collect the consideration it is entitled to on performance of its obligations in the contract.

These criteria are met when transfer of control of goods has occurred, which is generally on shipment or delivery of goods to the customer, where they have legal title to and possession of the goods, and are therefore able to use and obtain substantially all of the benefits of the goods.

Revenue is measured as the transaction price that is allocated to the performance obligation as stipulated in the contract with the customer. Historical experience is used to estimate and provide for discounts and returns. Costs to fulfill or obtain contracts are not directly attributable to specific contracts or are not recoverable and are expensed as incurred.

### **Cost of sales and gross profit**

Gross profit is derived from net sales, less cost of sales. Cost of sales includes raw material costs, contract manufacturing costs, freight costs and depreciation related to manufacturing equipment. Raw materials consist of the costs of natural feedstock and process chemicals.

### **Share capital**

Common shares are classified as equity. The Company has classified all outstanding exchangeable shares of its subsidiaries as issued and outstanding of the parent company.

### **Share-based compensation**

- Long-term incentive program (LTIP)

The Company's LTIP is a variable element of compensation that will allow executive officers and certain senior managers to be recognized and rewarded for their sustained contributions to the Company's financial performance and growth. The Company's long-term incentive program is composed of stock options and restricted share units (RSUs), each of which may be subject to performance and time-based vesting conditions.

Stock options provide a right, but not an obligation, to purchase common shares of the Company at a stated price for a given period of time, subject to performance and/or time based vesting conditions. The issuance of stock options are governed by the 2011 plan, which allows for the grant of stock options to the Company's employees, directors, senior officers and consultants with vesting of those stock options subject

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to the terms of the plan, any performance conditions imposed by the Board upon recommendation of the Compensation Committee and the optionees continued employment with the Company. Each tranche of a share option award is considered a separate award with its own vesting period and recorded at fair value on the date of grant. The fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche's vesting period based on the number of awards expected to vest by increasing contributed surplus. The number of awards expected to vest is reviewed periodically with any impact being recognized in the consolidated statements of operations and comprehensive loss. Any contribution paid by an employee or director on the exercise of share options is credited to common shares with any previously recognized compensation expense.

The restricted share unit plan (RSU Plan) provides that restricted share unit awards (the RSUAs) may be granted by a committee that administers the RSU Plan to full-time employees, officers and eligible contractors of the Company or an affiliate in a calendar year as a bonus for services rendered to the Company as determined at the sole discretion of the Board. The number of RSUs awarded will be credited to the participants' accounts effective on the grant date of the RSUs. Each RSU entitles the holder to receive common shares issued from the treasury of the Company. RSUs awarded cliff vest at the end of a three-year vesting period subject to continued employment with the Company. Compensation cost is calculated on a straight-line basis over the vesting period with a corresponding increase to contributed surplus. Forfeitures are estimated at the grant date and are revised to reflect a change in expected or actual forfeitures.

- Stock Options and RSUs with Performance Conditions

Performance stock options (PSOs) are awards of stock options that provide a right, but not an obligation, to purchase common shares of the Company at a stated price for a given period of time, subject to performance and time based vesting conditions. Performance restricted share units (PRSUs) entitle the holder to receive common shares issued from treasury of the Company subject to performance and time based vesting conditions.

PSOs and PRSUs vest at a rate of 33.33% per year following the date of grant subject to the achievement of certain performance conditions. The Board establishes a minimum level of performance below which no vesting will occur at the time of the grant. PSOs and PRSUs can only be settled in common shares issued from treasury. In the event that performance exceeds targeted performance conditions for a particular year, 33.33% of the PSO or PRSU will vest in that year. The Board may, at its discretion at the time of grant or after, accelerate the vesting schedule to beyond one third of the grant in a year actual performance exceeds the LTIP target; however, in no event can the cumulative vesting exceed 100%. The Company has estimated the length of the expected vesting period at the grant date based on the most likely outcome of the performance conditions. The fair values of PSOs and PRSUs are recorded over the expected vesting period, subject to management's estimate of the achievement of the performance conditions. The fair values of the PSOs and PRSUs are recognized as compensation expense over the vesting period with a corresponding increase to contributed surplus.

The Company has estimated the length of expected vesting period at the grant date based on the most likely outcome of the performance conditions. The Company will revise its estimate of the length of the vesting period, if necessary, if subsequent information indicates that the length of the vesting period differs

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## Notes to Consolidated Financial Statements

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(expressed in US dollars, unless otherwise noted)

from previous estimates and any change to compensation cost will be recognized in the period in which the revised estimate is made with a corresponding change to contributed surplus. Forfeitures are estimated at the grant date and are revised to reflect a change in expected or actual forfeitures.

All PSOs have an expiry between seven and ten years from the grant date. The exercise price is determined based on the average closing price of common shares on the Toronto Stock Exchange (TSX) five trading days immediately prior to the date as of which fair value is determined.

- **Deferred Share Units (DSUs)**

The deferred share unit plan (DSU Plan) provides for awards of DSUs to non-employee directors of the Company. Under the DSU Plan, non-executive directors may receive a grant of DSUs in satisfaction of their annual retainer. Each DSU is equivalent to one common share and vests on a quarterly vesting schedule, with 25% of each award vesting consecutive quarter. DSUs must be retained until the director leaves the Board, at which time the DSUs will be settled through common shares. In the event dividends are declared and paid, additional DSUs would be credited to reflect dividends paid on common shares. The number of DSUs to be awarded is determined based on the average closing price of the common shares on the TSX five trading days immediately prior to the date fair value is determined.

The fair values of the DSUs are recognized as compensation expense over the vesting period with a corresponding increase to contributed surplus.

### **Income taxes**

Income taxes comprise current and deferred income taxes. Income taxes are recognized in the consolidated statements of operations and comprehensive loss, except to the extent that they relate to items recognized directly in shareholders' equity, in which case the income taxes are also recognized directly in shareholders' equity.

Current income taxes are the expected income taxes payable on the taxable income for the year, using income tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustment to income taxes payable in respect of previous years.

In general, deferred income taxes are recognized in respect of temporary differences arising between the income tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income taxes are determined on a non-discounted basis using income tax rates and laws that have been enacted or substantively enacted at the consolidated balance sheet dates and are expected to apply when the deferred income tax asset or liability is settled. Deferred income tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income taxes are provided on temporary differences arising on investments in subsidiaries and associates, except, in the case of subsidiaries, where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.



# EcoSynthetix Inc.

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Deferred income tax assets and liabilities are presented as non-current.

### Loss per share

Basic loss per common share is calculated based on the weighted average number of common shares outstanding for the year. Diluted loss per common share is calculated using the weighted average number of common shares outstanding for the year for basic net loss per common share plus the weighted average number of potential dilutive common shares that would have been outstanding during the year had potentially all common shares been issued at the beginning of the year or when the underlying share options or warrants were granted, if later, unless they were anti-dilutive.

### Operating segments

The Company operates in one operating segment that is reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (CODM). The chief executive officer has authority for resource allocation and assessment of the Company's performance and is, therefore, the CODM.

### New accounting policies adopted

#### New accounting policies

- IFRS 16 - Leases

On January 1, 2019, the Company adopted IFRS 16, which establishes the principles that should be used to determine the recognition, measurement, presentation and disclosure of leases for both parties to a contract: the customer (lessee) and the supplier (lessor). The standard removes the distinction between operating and finance leases and requires the recognition of a right-of-use asset and lease liability at the lease commencement for all leases, except for short-term leases and leases of low value assets. The requirements for lessor accounting have remained largely unchanged. IFRS 16 replaces the previous leases standard, IAS 17, Leases, and related interpretations. The Company has adopted IFRS 16 on a modified retrospective basis recognizing the corresponding asset and liability as at January 1, 2019 with no adjustment to opening retained earnings or restatement of prior period figures.

The lease associated with the Company's corporate headquarters located in the Centre of Innovation in Burlington, Ontario was impacted by the adoption of IFRS 16. Previously, the Company recognized the lease charge associated with this facility as an operating lease expense on a straight-line basis over the term of the lease. The corresponding right-of-use asset and lease liability are measured by discounting the lease payments over the remaining lease term of seven years using the Company's incremental borrowing rate of 6.2%. There were no other lease agreements that were impacted by the adoption of this standard.

## 3 Risk management and financial instruments

The Company has classified its financial instruments into one of the following categories: amortized cost, FVOCI and FVPL.

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

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The Company's financial instruments were classified as follows at December 31, 2019:

	Amortized cost \$	FVOCI	FVPL	Total
Cash	7,975,713	-	-	7,975,713
Short-term investments	35,720,548	-	-	35,720,548
Accounts receivable	1,824,581	-	-	1,824,581
Government grants receivable	114,956	-	-	114,956
Trade accounts payable and accrued liabilities	(1,360,568)	-	-	(1,360,568)
Lease liability	(1,176,643)	-	-	(1,176,643)
	<u>43,098,587</u>	<u>-</u>	<u>-</u>	<u>43,098,587</u>

The Company's financial instruments were classified as follows at December 31, 2018:

	Amortized cost \$	FVOCI	FVPL	Total
Cash	14,207,342	-	-	14,207,342
Short-term investments	30,635,400	-	-	30,635,400
Accounts receivable	2,347,622	-	-	2,347,622
Government grants receivable	140,000	-	-	140,000
Trade accounts payable and accrued liabilities	(2,255,430)	-	-	(2,255,430)
	<u>45,074,934</u>	<u>-</u>	<u>-</u>	<u>45,074,934</u>

The carrying amount of financial assets and financial liabilities at amortized cost approximates their fair values.

### Liquidity risk

The Company has sustained annual losses and negative cash flows since its inception. Liquidity risk is the risk the Company will encounter difficulty in meeting its financial obligations associated with financial liabilities that are settled by delivering cash or another financial asset. The Company is exposed to liquidity risk as it continues to have net cash outflows. The Company's approach to managing liquidity risk is to ensure it will have sufficient liquidity to meet liabilities when due. The Company achieves this by maintaining sufficient cash. The Company monitors its financial position on a monthly basis and updates its expected use of cash resources based on the latest available data. The Company's trade accounts payable and accrued liabilities will be paid within the next 12 months.

### Credit risk

Credit risk arises from the potential that a counterparty will fail to perform its obligations. The Company is exposed to credit risk from customers. As at December 31, 2019, the Company's two largest customers accounted for 56% (2018 - two customers at 56%) of trade accounts receivable. In order to minimize the risk of loss for accounts receivable, the Company's extension of credit to customers involves a review and approval by senior management. The majority of the Company's sales are invoiced with payment terms up to 60 days. The

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Company's objective is to minimize its exposure to credit risk from customers in order to prevent losses on financial assets by performing regular monitoring of overdue balances and to provide an ACL.

The Company's trade accounts receivable have a carrying amount of \$1,610,427 at December 31, 2019 (2018 – \$2,111,366), representing the maximum exposure to credit risk of those financial assets, exclusive of the ACL. The Company's exposure to credit risk for trade accounts receivable by geographic area at December 31 was as follows:

	2019 %	2018 %
Americas	44	33
EMEA	12	23
Asia Pacific	44	44
	<hr/>	<hr/>
	100	100

The Company may also have credit risk relating to cash, which it manages by dealing with large chartered banks. The Company's objective is to minimize its exposure to credit risk in order to prevent losses on financial assets by placing its investments in lower risk deposits of these chartered banks. The Company's cash carrying amount is \$7,975,713 as at December 31, 2019 (2018 – \$14,207,342), representing the maximum exposure to credit risk of these financial assets. Approximately 93% (2018 – 94%) of the Company's cash at December 31, 2019 was held with one financial institution. The Company's exposure to credit risk relating to cash segmented by geographic area at December 31 was as follows:

	2019 %	2018 %
Canada	93.1	94.4
United States of America	4.3	3.7
The Netherlands	2.6	1.9
	<hr/>	<hr/>
	100.0	100.0

The Company may also have credit risk relating to short-term investments, which it manages by dealing with a large chartered Canadian bank. The short-term investments are short-term in nature and are low risk investments. The Company's short-term investment carrying amount is \$35,720,548 as at December 31, 2019 (2018 – \$30,635,400), representing the maximum exposure to credit risk of these financial assets.

### Foreign currency risk

Foreign currency risk arises because of fluctuations in foreign currency exchange rates. The Company conducts a portion of its business activities in currencies other than the functional currency of the parent company (US dollars). This primarily includes Canadian dollar and euro denominated transactions. The Company's objective in managing its foreign currency risk is to minimize its net exposure to foreign currency cash flows by converting foreign denominated financial assets into US dollars to the extent practical to match the obligations of its financial liabilities. Financial assets and financial liabilities denominated in foreign currencies will be

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affected by changes in the exchange rate between the functional currency and these foreign currencies. This primarily includes cash, accounts receivable, government grants receivable, trade accounts payable and accrued liabilities and lease liability, which are denominated in foreign currencies. The Company realized foreign currency exchange gains in the year ended December 31, 2019 of \$60,171 (2018 – loss of \$88,700). The Company has unrealized foreign exchange gains in the year ended December 31, 2019 of \$29,626 (2018 – loss of \$199,154).

If a shift in the Canadian dollar relative to the US dollar of 10% were to occur, the foreign currency exchange gain or loss on the net financial assets would be \$36,779 (2018 – \$390,663) and this amount would be recorded in the consolidated statements of operations and comprehensive loss.

If a shift in the euro relative to the US dollar of 10% were to occur, the exchange gain or loss on the net financial assets would be \$30,431 (2018 – \$55,063).

### **Interest rate risk**

Interest rate risk arises because of the fluctuation in market interest rates. The Company's objective in managing interest rate risk is to maximize the return on its cash. The Company is subject to interest rate risk on its cash. If a shift in interest rates of 10% were to occur, the impact on the consolidated statements of operations and comprehensive loss for the year would be a gain or loss of \$14,402 (2018 – \$32,999). The Company is not subject to interest rate risk on its fixed rate short-term investments.

## **4 Capital management**

The Company's objective in managing capital is to ensure sufficient liquidity to pursue its growth strategy and fund research and product development, while at the same time taking a conservative approach toward financial leverage and management of financial risk. The Company's capital is composed of total shareholders' equity. The total capital at December 31, 2019 is \$52,172,892 (2018 – \$54,101,814). The Company's primary uses of capital are financing operations, non-cash working capital and capital expenditures. The Company currently funds these requirements from existing cash resources. The Company's objectives when managing capital are to ensure the Company will continue to have enough liquidity so that it can provide its products and services to its customers and returns to its shareholders. The Company monitors its capital on the basis of the adequacy of its cash resources to fund its business plan. In order to maximize the capacity to finance the Company's ongoing growth, the Company does not currently pay a dividend to holders of its common shares.

## **5 Short-term investments**

During the year ended December 31, 2019, the Company purchased \$35,000,000 of short-term investment certificates maturing in January 2020 at an annual interest rate between 2.8% and 3%. All short-term investments are held with one large chartered Canadian bank. The carrying value of the short-term investments include accrued interest and is recorded at amortized cost using the effective interest method.

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## Notes to Consolidated Financial Statements

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	2019	2018
Short-term investment certificates	25,671,233	-
Term deposits	10,049,315	30,635,400
	<u>35,720,548</u>	<u>30,635,400</u>

### 6 Accounts receivable

	2019	2018
Trade accounts receivable	1,610,427	2,111,366
Commodity taxes receivable and other	214,154	236,256
	<u>1,824,581</u>	<u>2,347,622</u>

The aging of trade accounts receivable at each reporting date was as follows:

	2019	2018
Current	1,454,186	1,987,045
Past due 1 – 30 days	156,241	124,321
Past due 31 – 60 days	-	-
Past due 61 – 90 days	-	-
Past due greater than 91 days	-	-
	<u>1,610,427</u>	<u>2,111,366</u>

### 7 Inventory

	2019	2018
Raw materials	321,702	218,290
Finished goods	1,947,259	2,504,452
	<u>2,268,961</u>	<u>2,722,742</u>

The Company has a recorded provision of \$14,222 (2018 – \$20,000) against finished goods and raw materials inventory.

Inventories recognized as an expense during the year amounted to \$11,699,058 (2018 – \$15,053,066).

### 8 Government grants

The Company has a funding agreement of up to CA\$2,072,207 with Bioindustrial Innovation Canada, which is funded by the Federal Government. The investment was provided to develop new green resins for adhesive binders in wood products and covers reimbursement of eligible expenditures from April 2018 to April 2023. The investment is non-repayable unless the Company defaults on conditions contained in the funding agreement. The Company has met the conditions of the investment in fiscal 2019 and 2018 and has accordingly recognized \$154,076 (2018 – \$140,000) in its operating results.

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During the year ended December 31, 2019, the Company collected cash of \$183,732 (2018 – \$nil) relating to claims under the investment.

### 9 Property, plant and equipment

The composition of the net carrying amount of the Company's property, plant and equipment is presented in the following table:

	<b>Machinery and equipment</b>	<b>Leasehold improvements</b>	<b>Right-of use asset</b>	<b>Computer hardware</b>	<b>Total</b>
Cost					
January 1, 2018	15,806,251	831,843	-	90,091	16,728,185
Additions	297,552	-	-	-	297,552
Disposals	(258,604)	(3,838)	-	-	(262,442)
December 31, 2018	15,845,199	828,005	-	90,091	16,763,295
Additions	379,485	-	-	-	379,485
IFRS 16 implementation	-	-	1,561,149	-	1,561,149
December 31, 2019	16,224,684	828,005	1,561,149	90,091	18,703,929
Accumulated depreciation					
January 1, 2018	(8,711,435)	(831,843)	-	(69,235)	(9,612,513)
Depreciation expense	(1,221,948)	-	-	(2,525)	(1,224,473)
Accumulated depreciation on disposals	244,751	3,838	-	-	248,589
December 31, 2018	(9,688,632)	(828,005)	-	(71,760)	(10,588,397)
Depreciation expense	(1,145,458)	-	(222,372)	(18,331)	(1,386,161)
December 31, 2019	(10,834,090)	(828,005)	(222,372)	(90,091)	(11,974,558)
Net carrying amount					
December 31, 2018	6,156,567	-	-	18,331	6,174,898
December 31, 2019	5,390,594	-	1,338,777	-	6,729,371

The Company invested \$379,485 (2018 – \$297,552) in capital asset additions for the year ended December 31, 2019. The additions primarily relate to machinery and equipment for production. There were no capital asset additions included in trade accounts payable and accrued liabilities as at December 31, 2019 (2018 – \$78,687).

During the year ended December 31, 2019, depreciation expense of \$769,672 (2018 – \$829,438) has been charged to cost of goods sold, \$611,389 (2018 – \$419,508) has been charged to research and development, and depreciation expense of \$5,100 was capitalized into inventory (2018 – expensed from inventory \$24,473).

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

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### 10 Trade accounts payable and accrued liabilities

	2019	2018
Trade accounts payable	536,023	1,306,645
Short-term lease liability	200,769	-
Accrued liabilities	623,776	948,785
	<u>1,360,568</u>	<u>2,255,430</u>

### 11 Lease liability

The Company has one right-of-use asset under property, plant and equipment and corresponding lease liability for the lease associated with the Company's corporate headquarters located in the Centre of Innovation in Burlington, Ontario. The lease liability is measured at amortized cost by discounting the lease payments over the remaining term of the lease at the Company's incremental borrowing rate of 6.2%.

	2019	2018
Lease liability		
Short-term	200,769	-
Long-term	1,176,643	-
	<u>1,377,412</u>	<u>-</u>

During the year ended December 31, 2019, total cash payments of \$269,600 were made on the lease liability, which includes interest expense of \$82,173 that is recognized in net interest income on the consolidated statements of operations and comprehensive loss.

Previously, the Company recognized the lease charge associated with this facility as an operating lease expense on a straight-line basis over the term of the lease. There were no other lease agreements that were impacted by the adoption of this standard. The impact of the adoption of IFRS 16 on the consolidated balance sheet as at January 1, 2019 is as follows:

	December 31, 2018 \$	Impact of IFRS 16 \$	January 1, 2019 \$
Current assets			
Prepaid expenses	129,240	(29,682)	99,558
Non-current assets			
Property, plant and equipment	6,174,898	1,561,149	7,736,047
Current liabilities			
Trade accounts payable and accrued liabilities	2,255,430	182,139	2,437,569
Non-current liabilities			
Lease liability	-	1,349,328	1,349,328

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### 12 Key management compensation

Key management personnel include those individuals having authority and responsibility for planning, directing and controlling the activities of the Company directly or indirectly. Key management personnel include the directors, chief executive officer, chief financial officer and other key members of the executive team. The compensation paid or payable to key management personnel for employee services is shown below:

	2019	2018
Salaries and other short-term employee benefits	1,240,492	1,070,831
Share-based payments	712,039	704,816
	<u>1,952,531</u>	<u>1,775,647</u>

### 13 Share-based compensation

At December 31, 2019, the Company had outstanding share options to purchase 4,780,644 common shares of the Company. The share options expire at various dates through December 20, 2026.

	Number of share options outstanding	Weighted average exercise price (CA\$)
Outstanding – December 31, 2017	4,925,647	1.66
Share options granted	381,877	2.16
Share options forfeitures	(361,132)	2.51
Share options exercised	<u>(510,899)</u>	0.98
Outstanding – December 31, 2018	4,435,493	1.72
Share options granted	858,826	2.21
Share options forfeitures	(277,836)	2.16
Share options exercised	<u>(235,839)</u>	1.23
Outstanding – December 31, 2019	<u>4,780,644</u>	1.80

The weighted average contractual life of the outstanding share options at December 31, 2019 is 3.46 years (2018 – 3.92 years). The total number of share options exercisable at December 31, 2019 is 3,924,227 (2018 – 2,379,901), which have a weighted average exercise price of CA\$1.71 (2018 – CA\$1.33) per share.



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## Notes to Consolidated Financial Statements December 31, 2019 and December 31, 2018

(expressed in US dollars, unless otherwise noted)

	Number of share options outstanding	
	2019	2018
Range of exercise prices		
\$0.01 – \$0.50	-	-
\$0.51 – \$1.00	-	46,867
\$1.00 – \$1.50	2,547,159	2,745,492
\$1.50 – \$2.00	723,085	253,978
\$2.00 – \$2.50	633,981	824,595
\$2.50 – \$3.00	667,924	353,498
\$3.00 – \$3.50	157,348	146,245
\$3.50 – \$4.00	-	12,671
\$4.00 – \$4.50	-	-
\$4.50 – \$5.00	-	-
\$5.00 – \$5.50	17,500	18,500
\$5.50 – \$6.00	-	-
\$6.00 – \$6.50	-	-
\$6.50 – \$7.00	-	-
\$7.00 – \$7.50	33,647	33,647
	<u>4,780,644</u>	<u>4,435,493</u>

For the years ended December 31, the Company determined the fair values of share options using the Black-Scholes option pricing model with the following assumptions for share option grants:

	2019	2018
Expected dividend yield	-%	-%
Risk-free interest rate	1.67% to 1.76%	1.86%
Expected share option life (in years)	5 to 6	5
Volatility	49% to 55%	55%

The aggregate fair value of share options granted during the year is CA\$899,010 (2018 – CA\$401,640). The weighted average fair value of the share options is CA\$0.86 (2018 – CA\$0.82) per share. During the fiscal year ended December 31, 2019, the Company recognized a share-based compensation expense of \$387,856 (2018 – \$405,102) related to share options with a corresponding increase in contributed surplus.

For the year ended December 31, 2019, expected volatility is based on a review of historical volatilities for the Company.

The expected share option life is based on the employees' historical exercise behaviour.

The risk-free interest rate used for each grant is equal to the Canadian treasury bill rates in effect at the date of grant for instruments with a term similar to the expected life of the related share option.

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## Notes to Consolidated Financial Statements

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(expressed in US dollars, unless otherwise noted)

a) Share options

i) Share options

During the current fiscal year, the Company issued 858,826 (2018 – 381,877) share options in accordance with the provisions of the LTIP resulting in a total of 3,327,417 (2018 – 2,640,627) share options outstanding at December 31, 2019. For the year ended December 31, 2019, the Company recognized a share-based compensation expense of \$406,518 (2018 – \$212,609).

ii) Performance share options (PSOs)

During the current fiscal year, the Company did not issue any PSOs (2018 – nil), resulting in 1,453,227 PSOs outstanding as at December 31, 2019 (2018 – 1,794,866). For the year ended December 31, 2019, the Company recorded a share-based compensation expense of \$nil (2018 – \$190,622). The Company determined that the performance hurdles related to PSOs were not achieved in the current fiscal year. A credit to the share based compensation expense was recognized for \$18,662 relating to forfeitures of former employees.

b) Restricted share units (RSUs)

i) Restricted share units

During the current fiscal year, the Company issued 15,000 RSUs (2018 – 220,000) resulting in 301,666 RSUs outstanding at December 31, 2019 (2018 – 419,102). For the year ended December 31, 2019, the Company recorded a share-based compensation expense of \$151,706 (2018 – \$68,047) related to RSUs, which cliff vest after three years with no performance conditions.

ii) Performance restricted share units (PRSUs)

During the current fiscal year, the Company issued 241,393 PRSUs (2018 – 178,390) resulting in 401,332 PRSUs outstanding as at December 31, 2019 (2018 – 178,390). For the year ended December 31, 2019, the Company recorded a share-based compensation expense of \$nil (2018 – \$73,312). The Company determined that the performance hurdles related to PRSUs were not achieved in the current fiscal year.

c) Deferred share unit plan

During the fiscal year ended December 31, 2019, 128,458 DSUs (2018 – 179,162) were issued to non-employee directors of the Company. During the fiscal year ended December 31, 2019, the Company recognized a share-based compensation expense of \$245,061 (2018 – \$235,805) related to DSUs with a corresponding increase in contributed surplus. At December 31, 2019, 545,753 DSUs were outstanding (2018 – 417,295).

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements December 31, 2019 and December 31, 2018

(expressed in US dollars, unless otherwise noted)

### 14 Common shares

The authorized share capital of the Company consists of an unlimited number of common shares.

	Number of common shares	Share capital
Balance – December 31, 2017	59,573,558	493,631,495
Common share options exercised	510,899	636,384
Restricted share units converted	133,325	172,722
Deferred share units converted	80,454	110,507
Common shares repurchased	(2,045,500)	(2,932,983)
Balance – December 31, 2018	58,252,736	491,618,125
Common share options exercised	235,839	327,661
Restricted share units converted	124,234	119,927
Common shares repurchased	(710,368)	(1,475,307)
Balance – December 31, 2019	57,902,441	490,590,406

### Share exchange

During the year ended December 31, 2019, the Company held a normal course issuer bid (the Bid) to repurchase a certain number of its outstanding common shares through the facilities of the Toronto Stock Exchange. The Company repurchased and cancelled 710,368 (2018 – 2,045,500) common shares for total consideration of \$1,475,307 (2018 – 2,932,983).

### 15 Income taxes

The difference between income tax expense and the income taxes as computed based on the statutory rate is as follows:

	2019	2018
Net loss before income taxes	(1,454,058)	(2,530,758)
Income tax benefit at statutory rate	(385,325)	(666,676)
Cost (benefit) resulting from		
Research and development credit	(65,213)	(107,958)
Deferred income tax assets expired	10,264	8,037
Change in tax rate	269,862	-
Deferred income tax assets not recognized and other	170,412	766,597
	-	-

The reduction of the corporation tax rate in the Netherlands from 19% in 2019 to 15% in 2021, on income under €200,000, and 25% in 2019 to 21.7% in 2021, on income greater than €200,000, was substantively enacted on September 17, 2019 and will be effective from January 1, 2021. As a result, the relevant deferred tax balances in the Netherlands have been remeasured. The impact of the change in tax rate in the Netherlands is a reduction in tax assets of \$269,862.

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(expressed in US dollars, unless otherwise noted)

Estimated temporary differences in the timing of recognition of expenses for accounting and income tax purposes at December 31 result in deferred income taxes as follows:

	2019	2018
Estimated deferred income tax assets attributable to		
Net operating loss carry-forwards	24,282,819	22,897,013
Research and development credits	2,971,913	2,794,554
Other deferred income tax assets	3,075,988	2,749,585
	<hr/>	<hr/>
Deferred income tax assets	30,330,720	28,441,152
Deferred income tax assets not recognized and other	(30,330,720)	(28,441,152)
	<hr/>	<hr/>
Net deferred income tax assets	-	-

The estimated net operating loss carry-forwards and estimated research and development credits expire as follows:

	<u>United States of America</u>		<u>Canada and the Netherlands</u>	<u>Canada</u>
	Net operating loss carry- forwards	Research and development credits	Net operating loss carry- forwards	Research and development credits
2020	1,330,044	42,132	415,416	-
2021	2,564,511	55,822	1,100,443	-
2022	1,338,594	52,731	358,595	-
2023	1,321,285	44,965	2,021,740	-
2024	1,532,264	46,333	453,603	-
2025	1,629,456	47,245	232,026	-
2026	1,562,856	41,905	798,393	-
2027	2,011,361	35,351	22,760	-
2028	2,717,038	69,118	2,303	-
2029	2,854,334	63,226	-	-
2030	1,207,399	96,302	-	41,736
2031	3,927,982	-	892,117	334,892
2032	1,127,104	-	3,812,742	528,693
2033	10,855,248	-	7,539,273	618,793
2034	1,333,972	-	11,223,353	540,949
2035	1,058,892	-	17,188,129	358,351
2036	1,275,377	-	6,707,619	188,311
2037	-	-	-	205,447
2038	-	-	7,533,441	94,293
2039	-	-	2,256,872	83,725
	<hr/>	<hr/>	<hr/>	<hr/>
	39,647,717	595,130	62,558,825	2,995,190

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

### 16 Commitments

The Company has entered into the following financial commitments in the normal course of operations that were not recognized as liabilities as at December 31, 2019:

	\$
2020	2,811,201
2021	-
2022	-
Thereafter	-
	<hr/>
	2,811,201
	<hr/>

During the normal course of operations, the Company may enter into feedstock contracts to secure raw material availability over a 12-month period based on market pricing at the time of purchase. At December 31, 2019, the Company was committed to purchases of feedstock of approximately \$2,300,371. In addition to feedstock the Company is also committed to purchasing \$478,005 of other raw material and production related costs through the normal course of operations as well as \$32,825 of property, plant and equipment relating to production.

### 17 Segmented information and enterprise wide disclosures

#### Segmented reporting

The Company operates in one reportable segment and generates revenue primarily from its biopolymer nanosphere technology platform. Revenue is recognized when the transfer of control of goods has occurred, which is generally on shipment or delivery of goods to the customer.

#### Sales by geographic location

The Company is domiciled in Canada. During the year ended December 31, 2019, revenue from external customers located in Canada was \$3,183,517 (2018 – \$3,527,566). The total revenue from external customers in the following regions is as follows:

	2019	2018
Americas	9,349,936	11,149,712
EMEA	4,135,353	5,729,219
Asia Pacific	4,961,633	5,920,398
	<hr/>	<hr/>
	18,446,922	22,799,329
	<hr/>	<hr/>

The revenue has been assigned to each jurisdiction, based on the location of the customer. In situations where a sale is made through a reseller, revenue associated with that sale is attributed to the geographic region of the end customer. During the year ended December 31, 2019, revenue attributable to individual countries representing greater than 10% of total revenues included United States, Japan, Canada and Germany, which represented 27%, 26%, 17% and 14%, respectively.

# EcoSynthetix Inc.

## Notes to Consolidated Financial Statements

December 31, 2019 and December 31, 2018

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(expressed in US dollars, unless otherwise noted)

During the year ended December 31, 2018, revenue attributable to individual countries representing greater than 10% of total revenues included United States, Japan, Canada and Germany, which represented 29%, 24%, 15% and 14%, respectively.

### Sales to major customers

The Company derives a significant portion of its revenues from certain customers. Three customers represented 26%, 17% and 16%, respectively, of total revenue for the year ended December 31, 2019 (2018 – three customers represented 24%, 21% and 15%, respectively). The concentrations listed do not necessarily apply to the same customer year over year.

### Property, plant and equipment

The Company's property, plant and equipment, reported at their net carrying amount, are located in the following countries:

	2019	2018
Canada	2,326,050	1,364,697
United States of America	2,129,048	2,348,867
The Netherlands	2,274,273	2,461,334
	<u>6,729,371</u>	<u>6,174,898</u>

## 18 Expenses by nature

Additional information on the nature of amounts included in cost of sales, selling, general and administrative and research and development is as follows:

	2019	2018
Wages and salaries, including benefits	3,092,295	3,500,243
Termination benefits	-	222,778
Share-based compensation	784,623	780,395
Depreciation	1,381,061	1,248,946
Foreign exchange (gain) loss	(89,797)	287,854

Foreign exchange gains and losses represent the revaluation of monetary assets and liabilities denominated in foreign currencies. The change in foreign exchange revaluation gains and losses is primarily due to foreign exchange rate fluctuations between the US dollar (the Company's functional currency) and foreign currencies and the related impact on the net monetary position in those respective currencies. The foreign exchange gains for the year ended December 31, 2019 primarily relate to monetary assets and liabilities denominated in Canadian dollars.

# **EcoSynthetix Inc.**

## **Notes to Consolidated Financial Statements**

**December 31, 2019 and December 31, 2018**

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(expressed in US dollars, unless otherwise noted)

### **19 Loss per share**

Basic loss per share is calculated by dividing the profit attributable to equity holders of the Company by the weighted average number of common shares in issue during the year.

Diluted loss per share is equivalent to basic loss per share, as the consideration of potentially dilutive securities would be anti-dilutive.

### **20 Comparative figures**

Certain comparative figures have been restated to conform with the current year's presentation.