

# **Devonian Health Group Inc.**

Consolidated Financial Statements

**July 31, 2022 and 2021**



## Independent auditor's report

To the Shareholders of Devonian Health Group 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 Devonian Health Group Inc. and its subsidiary (together, the Company) as at July 31, 2022 and 2021, 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 Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at July 31, 2022 and 2021;
- the consolidated statements of comprehensive income for the years then ended;
- the consolidated statements of changes in 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 significant accounting policies and other explanatory information.

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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 Company 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.

PricewaterhouseCoopers LLP/s.r.l./s.e.n.c.r.l.  
1250 René-Lévesque Boulevard West, Suite 2500, Montréal, Quebec, Canada H3B 4Y1  
T: +1 514 205 5000, F: +1 514 876 1502

"PwC" refers to PricewaterhouseCoopers LLP/s.r.l./s.e.n.c.r.l., an Ontario limited liability partnership.



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## **Material uncertainty related to going concern**

We draw attention to note 2 to the consolidated financial statements, which describes events or conditions that indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

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## **Other information**

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

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 Company'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 Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company'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 Company'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 Company'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 Company 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 Company 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 Sébastien Bellemare.

**/s/PricewaterhouseCoopers LLP<sup>1</sup>**

Montréal, Quebec  
November 25, 2022

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<sup>1</sup> CPA auditor, public accountancy permit No. A116819

# Devonian Health Group Inc.

## Consolidated Statements of Financial Position

As at July 31, 2022 and 2021

	2022 \$	2021 \$
<b>Assets</b>		
<b>Current assets</b>		
Cash	2,805,191	344,795
Guaranteed investment certificate	5,000,000	-
Accounts receivable (note 5)	314,738	218,803
Tax credits receivable (note 6)	22,460	16,251
Inventories (note 7)	154,622	28,221
Prepaid expenses	120,218	56,155
	<u>8,417,229</u>	<u>664,225</u>
<b>Property, plant, equipment, and right-of-use asset</b> (note 8)	2,884,656	3,066,547
<b>Intangible assets</b> (note 9)	5,641,102	6,233,889
<b>Goodwill</b> (notes 3 and 9)	4,643,084	4,643,084
	<u>21,586,071</u>	<u>14,607,745</u>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable (note 10)	1,035,177	1,809,418
Current portion of lease liability	6,030	4,598
	<u>1,041,207</u>	<u>1,814,016</u>
<b>Long-term debt</b> (note 11)	3,576,423	3,570,081
<b>Convertible debentures</b> (note 12)	680,165	1,687,532
<b>Lease liability</b>	15,747	12,631
	<u>5,313,542</u>	<u>7,084,260</u>
<b>Shareholders' Equity</b>		
Share capital (note 13)	27,572,182	20,208,600
Stock options (note 14)	1,113,033	765,205
Warrants (note 15)	4,737,154	540,421
Contributed surplus	3,676,907	3,387,704
Deficit	(20,826,747)	(17,378,445)
	<u>16,272,529</u>	<u>7,523,485</u>
	<u>21,586,071</u>	<u>14,607,745</u>

**Material uncertainty related to going concern** (note 2)

### Approved by the Board of Directors

(s) André Boulet, Chief Scientific Officer

(s) Érick Shields, Board Member

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

# Devonian Health Group Inc.

## Consolidated Statements of Net Loss and Comprehensive Loss

For the years ended July 31, 2022 and 2021

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	2022 \$	2021 \$
<b>Distribution revenues</b>	2,305,188	1,474,690
<b>Operating expenses</b>		
Cost of sales	1,744,173	1,715,592
Research and development expenses	778,544	610,252
Administrative expenses	2,695,037	1,454,807
Net financial expenses (note 18)	535,736	1,086,235
	5,753,490	4,866,886
Loss before other item and income taxes	(3,448,302)	(3,392,196)
<b>Other item</b>		
Canada Emergency Business Loan Grant	-	45,816
Net loss and comprehensive loss	(3,448,302)	(3,346,380)
<b>Net loss per share</b> (note 19)		
Basic	(0.029)	(0.038)
Diluted	(0.029)	(0.038)

**Additional information to the consolidated statements of net loss and comprehensive loss** (notes 2, 4, 18 and 20)

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

# Devonian Health Group Inc.

## Consolidated Statements of Changes in Equity

For the years ended July 31, 2022 and 2021

	Number				Amount					
	Shares	Stock options	Warrants	Total	Share capital \$	Stock options \$	Warrants \$	Contributed surplus \$	Deficit \$	Total \$
<b>Balance</b> , as at July 31, 2020	82,522,541	6,228,355	12,689,699	101,440,595	19,021,908	697,085	2,139,324	1,557,978	(14,032,065)	9,384,230
Issuance of shares (note 13)	10,738,147	-	-	10,738,147	1,158,968	-	-	-	-	1,158,968
Share issuance costs:										
In cash	-	-	-	-	(35,671)	-	-	-	-	(35,671)
Stock-based compensation (note 14)	-	861,645	-	861,645	-	82,720	-	-	-	82,720
Issuance of warrants (note 15)	-	-	5,654,315	5,654,315	-	-	229,618	-	-	229,618
Warrants exercised (note 15)	200,000	-	(200,000)	-	63,395	-	(13,395)	-	-	50,000
Warrants expired (note 15)	-	-	(8,403,361)	(8,403,361)	-	-	(1,815,126)	1,815,126	-	-
Options expired (note 14)	-	(150,000)	-	(150,000)	-	(14,600)	-	14,600	-	-
Net loss and comprehensive loss for the year	-	-	-	-	-	-	-	-	(3,346,380)	(3,346,380)
	10,938,147	711,645	(2,949,046)	8,700,746	1,186,692	68,120	(1,598,903)	1,829,726	(3,346,380)	(1,860,745)
<b>Balance</b> , as at July 31, 2021	93,460,688	6,940,000	9,740,653	110,141,341	20,208,600	765,205	540,421	3,387,704	(17,378,445)	7,523,485
Issuance of shares (note 13)	36,977,947	-	-	36,977,947	7,313,265	-	-	-	-	7,313,265
Share issuance costs:										
In cash	-	-	-	-	(171,565)	-	-	-	-	(171,565)
Stock-based compensation (note 14)	-	2,220,000	-	2,220,000	-	532,687	-	-	-	532,687
Issuance of warrants (note 15)	-	-	35,666,394	35,666,394	-	-	4,347,959	-	-	4,347,959
Warrants exercised (note 15)	700,000	-	(700,000)	-	221,882	-	(46,882)	-	-	175,000
Warrants expired (note 15)	-	-	(2,036,722)	(2,036,722)	-	-	(104,344)	104,344	-	-
Options expired (note 14)	-	(1,085,000)	-	(1,085,000)	-	(184,859)	-	184,859	-	-
Net loss and comprehensive loss for the year	-	-	-	-	-	-	-	-	(3,448,302)	(3,448,302)
	37,677,947	1,135,000	32,929,672	71,742,619	7,363,582	347,828	4,196,733	289,203	(3,448,302)	8,749,044
<b>Balance</b> , as at July 31, 2022	131,138,635	8,075,000	42,670,325	181,883,960	27,572,182	1,113,033	4,737,154	3,676,907	(20,826,747)	16,272,529

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



# Devonian Health Group Inc.

## Consolidated Statements of Cash Flows

For the years ended July 31, 2022 and 2021

	2022 \$	2021 \$
<b>Cash flows from</b>		
<b>Operating activities</b>		
Net loss	(3,448,302)	(3,346,380)
Items not affecting cash		
Amortization of property, plant, equipment and depreciation of right-of-use asset	271,082	264,597
Amortization of intangible assets	592,787	765,733
Amortization of discount on convertible debentures, net of settlement of original issue discount	(125,178)	242,281
Amortization of discount on emergency business account loan	6,342	2,211
Interest on lease liability	958	-
Unrealized loss (gain) on derivatives	(361,583)	293,177
Interest on convertible debentures	262,000	248,080
Stock-based compensation	532,687	82,720
	<u>(2,269,207)</u>	<u>(1,447,581)</u>
Net change in non-cash working capital items (note 22)	(602,375)	(385,685)
	<u>(2,871,582)</u>	<u>(1,833,266)</u>
<b>Investing activities</b>		
Acquisition of guaranteed investment certificate	(5,000,000)	-
Acquisition of property, plant, and equipment	(73,669)	-
Acquisition of right-of-use asset	(5,775)	(14,101)
	<u>(5,079,444)</u>	<u>(14,101)</u>
<b>Financing activities</b>		
Principal payments on lease liability	(6,154)	(5,199)
Government loan	-	58,015
Convertible debentures	(520,606)	-
Issuance of shares and warrants	10,763,182	1,176,329
Warrants exercised	175,000	50,000
	<u>10,411,422</u>	<u>1,279,145</u>
<b>Increase (decrease) in cash</b>	2,460,396	(568,222)
<b>Cash – Beginning of year</b>	<u>344,795</u>	<u>913,017</u>
<b>Cash – End of year</b>	<u>2,805,191</u>	<u>344,795</u>

For the year ended July 31, 2022, cash flows from operating activities include interest paid of \$309,197 (2021 – \$295,746) and \$479,394 for the discount portion of the convertible debentures (2021 – none), and no taxes paid (2021 – none).

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

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

July 31, 2022 and 2021

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### 1 Statutes of incorporation and nature of activities

Devonian Health Group Inc. (the Company) was incorporated under the Business Corporations Act (Québec) on March 27, 2015. On May 12, 2017, the Company was continued under the Canada Business Corporations Act (CBCA).

Its main activity is the development of botanical drugs. It is also involved in the development of value-added products for dermo-cosmetics and the distribution of pharmaceutical products through its subsidiary. The Company has established a research effort focused towards the anticipation of new solutions in the medical sector as well as in the cosmetic sector. The Company's head office is located at 360 Rue des Entrepreneurs, Montmagny, Québec.

### 2 Material uncertainty related to going concern

These consolidated financial statements have been prepared on a going concern basis, which assumes that assets will be realized and liabilities discharged in the normal course of business for the foreseeable future. Accordingly, these consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or on the discharge or classification of liabilities, should the Company be unable to continue its business in the normal course. It is committed to the development of botanical drugs and will have to obtain necessary funding to continue its operations until the commercialization phase of its products. The Company has incurred losses since its inception and anticipates that losses will continue for the foreseeable future. The Company's liquidities are limited considering its ongoing projects. Consequently, the Company's ability to continue as a going concern depends also on its ability to source from its pharmaceutical suppliers, its ability to distribute its products while generating positive cash flows and to obtain, in a timely matter, further financing to complete research and development projects, and to market its developed products, as to which no assurance can be given.

Management continues to negotiate further financing and different agreements that could create positive cash flows. The success of these negotiations is contingent on many factors outside the Company's control, and its ability to successfully complete such financings and agreements is tinged with material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern.

These consolidated financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial classifications that would be necessary if the Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

### **3 Significant accounting policies**

#### **Declaration of compliance**

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

These consolidated financial statements were approved by the Board of Directors on November 22, 2022.

#### **Basis of measurement**

The consolidated financial statements have been prepared on the historical cost basis.

#### **Functional and presentation currency**

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

#### **Consolidation**

These consolidated financial statements include the accounts of the Company and the accounts of its subsidiary, Altius Healthcare Inc. Intercompany balances, income, expenses and cash flows are fully eliminated upon consolidation. When necessary, adjustments are made to the subsidiary's financial statements to align its accounting policies with those of the Company.

#### **Distribution revenue recognition**

Revenues from the distribution of pharmaceutical and cosmeceutical products are recognized when the terms of a contract with a client are fulfilled, i.e. when:

- the control of the product has been transferred to the client; and
- the product is received by the client or the transfer to the client of the ownership title occurs upon shipment.

After delivery, the client assumes obsolescence and loss risks with respect to such goods. Revenues are recognized according to the prices set in the contracts, less estimated sales rebates or returns.

#### **Use of estimates and judgments**

The preparation of consolidated financial statements in compliance with IFRS requires management to use judgment and make estimates and assumptions that affect the application of accounting policies and the carrying value of assets, liabilities, revenues, and expenses. Actual results could differ from those estimates.

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

### July 31, 2022 and 2021

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The estimates and underlying assumptions are reviewed on an ongoing basis. Any revision to accounting estimates is recognized in the period in which the estimates are revised and in any future periods affected by these revisions.

Information relating to critical judgments in applying accounting policies that have the most significant impact on the amounts recognized in the consolidated financial statements is as follows:

- Impairment of intangible assets

Assessment of impairment of intangible assets at the end of each reporting period requires the use of judgments, assumptions and estimates when addressing whether there are any indicators that could give rise to the requirement to conduct a formal impairment test on the Company's intangible assets. The assessment of fair values requires the use of estimates and assumptions for forecasted revenues, discount rates and operating costs. In addition, the Company may use other approaches in determining fair value. Changes in any of the assumptions and estimates used in determining the fair value of the intangible assets measured at cost, could impact the impairment analysis.

- Payables to wholesalers

Management uses judgment in estimating provisions for sale deductions such as cash discounts, allowances, returns, rebates, chargebacks and distribution fees.

- Fair value of embedded derivative

The convertible debentures issued by the Company include a conversion option, which is considered as a Level 3 financial instrument. The derivative is measured at fair value through profit and loss, and its fair value must be measured at each reporting period, with subsequent changes in fair value recorded in the consolidated statement of net loss and comprehensive loss. A derivative valuation model is used, and includes management's assumptions, to estimate the fair value. Detailed assumptions used in the model to determine the fair value of the embedded derivative as of July 31, 2021 are provided in note 12.

### **Currency translation**

Transactions concluded in foreign currencies are translated into Canadian dollars as follows: monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate in effect at the date of the consolidated statement of financial position, while other assets and liabilities are translated at the exchange rate in effect at the date of transactions. Revenues and expenses denominated in foreign currencies are translated at the average exchange rate, except for amortization which is translated at the historical exchange rate. Exchange gains and losses resulting from this translation are recognized in net loss.

# **Devonian Health Group Inc.**

## **Notes to Consolidated Financial Statements**

### **July 31, 2022 and 2021**

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#### **Income taxes**

The Company provides for income taxes using the asset and liability method of accounting for deferred income taxes. Under this method, deferred tax assets and liabilities are determined based on deductible or taxable temporary differences between the carrying value and tax values of assets and liabilities using enacted or substantively enacted income tax rates in effect for the year in which the differences are expected to be reversed.

The Company establishes a valuation allowance against deferred tax assets if, based on available information, it is likely that some or all of the deferred tax assets will not be realized.

#### **Government subsidy**

On March 27, 2020, the Canadian government announced the Canada Emergency Wage Subsidy (CEWS) program, in effect from March 15 to June 30, 2021, and extended thereafter, enabling Canadian businesses to meet the challenges of the pandemic. Certain eligibility criteria must be met in order to be eligible for the CEWS. The Company can only recognize the amounts of subsidy when collection is reasonably assured. The Company opted to recognize the government subsidy as a reduction of the expenses to which it relates. The Company did not recognize any subsidy in its consolidated results for the year ended July 31, 2022 (2021 – \$127,210).

#### **Financial instruments**

##### **Classification and measurement**

Classification and measurement of financial assets include the following categories: amortized cost, fair value through profit or loss (FVTPL) and fair value through other comprehensive income (FVOCI). The classification of financial assets is generally based on the business model for which a financial asset is managed and the characteristics of the contractual cash flows. Financial liabilities are classified and measured in two categories: amortized cost and FVTPL.

##### **Financial assets measured at amortized cost**

Financial assets measured at amortized cost, i.e. cash and accounts receivable, are measured at fair value at the date on which the Company becomes a party to the contractual provisions of the instrument. They are subsequently measured at amortized cost using the effective interest rate method, net of impairment losses.

##### **Financial liabilities measured at amortized cost**

Financial liabilities measured at amortized cost, i.e. accounts payable, long-term debt and convertible debentures (debt host), are initially measured at fair value. They are subsequently measured at amortized cost using the effective interest rate method.

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

### July 31, 2022 and 2021

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#### Fair value

The fair value of a financial instrument generally corresponds to the consideration for which the instrument would be exchanged in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. This measurement is carried out at a definite time and could be modified over the future presentation periods due to market conditions and other factors.

Fair value is established using the quoted prices of the most advantageous active market for that instrument to which the Company has immediate access. If there is no active market, fair value is established on internal or external valuation methods, such as discounted cash flow models. The fair value established using these valuation models requires the use of assumptions in regard to the amount and timing of the estimated future cash flows, as well as for many other variables. To determine these assumptions, readily observable market data are used when available. Otherwise, the Company uses the best possible estimates. Since they are based on estimates, fair values may not be realized in the event of an actual sale or immediate settlement of these instruments.

#### Impairment of financial assets

Financial assets recognized at amortized cost are subject to an impairment test at each reporting date. The Company estimates the expected credit losses based on the history of its credit losses and the credit risk assessment of its customers, and, if applicable, the net change in expected credit losses on accounts receivable is recognized in net loss.

The amount of the impairment loss is equal to the difference between the carrying amount of the asset and the present value of the estimated future cash flows, discounted at the original effective interest rate of the financial asset. The Company uses historical trends of the probability of default, the timing of recovery and its judgment in estimating future cash flows.

The Company applies the IFRS 9 simplified approach to measuring expected credit losses using a lifetime expected credit loss allowance for trade receivables. The expected loss rates are based on the Company's historical credit losses experienced over the three-year period prior to the period-end. The historical loss rates are then adjusted for current and forward-looking information on macroeconomic factors affecting the Company's customers. The Company assumes that there is no significant increase in credit risk for instruments that have a low credit risk.

#### **Research and development expenses and tax credits**

Research and development expenses are expensed as incurred. However, development expenses are deferred when they meet the accepted criteria for deferral up to the amount that is reasonably certain to be recovered. As at July 31, 2022 and 2021, no development costs were deferred.

Tax credits for research and development are recognized in loss or deferred as a reduction of related expenses. Tax credits are recognized when there is reasonable assurance that the Company has met the requirements and that the credits will be received.

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

### July 31, 2022 and 2021

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#### **Inventories**

Inventories of raw materials and finished products are valued at the lower of cost and net realizable value, the cost being determined using the first in, first out method.

The net realizable value is the estimated selling price in the ordinary course of business less variable selling expenses that apply.

#### **Share issuance costs**

Costs directly identifiable with the issuance of shares are deferred as an asset until the issuance of the shares. At issuance, these costs are recorded as a reduction of share capital. In case of abandonment, these costs are recognized in net loss.

#### **Property, plant and equipment**

Property, plant and equipment are initially recorded at cost and, subsequently, at cost less amortization and accumulated impairment losses.

Amortization is based on the estimated useful life of each component of property, plant and equipment using the straight-line method and the following periods:

Building	
Structure and shell	40 years
Improvements, mechanical and plumbing systems	20 years
Leasehold improvements	5 years
Production and laboratory equipment	10 years
Computer equipment	3 years
Furniture and equipment	5 years

The residual value, the estimated useful life and the amortization method are reviewed at the end of each reporting date, and any changes in estimates are accounted for on a prospective basis. Amortization is recorded when the asset is ready to be used.

#### **Right-of-use asset and lease liability**

Leases are recognized as a right-of-use asset and a corresponding lease liability at the commencement date. Each lease payment is allocated between a reduction of the liability and finance cost. The finance cost is recognized in "Financial expenses" in the consolidated statements of net loss and comprehensive loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The lease liability is measured at the value of lease payments to be made, discounted using the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily available. The period over which the lease payments are discounted is the period for which the lessee has the right to use the underlying asset.

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

### July 31, 2022 and 2021

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Right-of-use asset is measured at cost, which is calculated as the amount of the initial measurement of lease liability plus any lease payments made at or before the lease commencement date, any initial direct costs and related restoration costs. The right-of-use asset is depreciated over the lease term on a straight-line basis. The depreciation starts at the commencement date of the lease.

Costs associated with short-term leases and leases of low-value assets are included in the consolidated statements of net loss and comprehensive loss.

#### **Intangible assets**

Intangible assets, comprising intellectual property, website development costs and patents related to cosmeceuticals, are recorded at cost and, subsequently, at cost less amortization and accumulated impairment losses.

Intangible assets acquired in the business combination, being licenses, trademarks and distribution rights, are initially recognized at fair value at the acquisition date. After initial recognition, they are recorded at cost less accumulated amortization and accumulated impairment losses, using the same method used for intangible assets acquired separately.

Amortization is based on the estimated useful life using the straight-line method and the following periods:

Patents	2 to 13 years
Website	4 years
Licenses, trademarks and distribution rights	4 to 12 years

No amortization for the intellectual property has been recognized, since it is still under development. The amortization method and estimated useful life will have to be reviewed at each reporting date.

#### **Business combinations and goodwill**

Business combinations are accounted for by using the acquisition method. The consideration transferred in a business combination is measured at the fair value, at the acquisition date, of the assets transferred by the acquirer. The Company recognizes the fair value of the consideration at the acquisition date as part of the consideration transferred in exchange for the acquiree. Related costs related to business combinations are recognized as expenses when incurred. At the acquisition date, the identifiable assets acquired, and the liabilities assumed, as well as the identifiable contingent liabilities, are recognized at their fair value at that date. Deferred tax assets and liabilities are measured in accordance with IAS 12, Income Taxes. The result of the acquiree is included in the consolidated loss of the Company from the date of acquisition. Goodwill is measured as the excess of the total consideration transferred over the fair value of all identified assets and liabilities. If, at the date of acquisition, the net balance of the amounts of the identifiable assets acquired and liabilities assumed is greater than the consideration transferred, the excess is recognized immediately in loss as a profit on a business combination on advantageous terms and conditions.



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Goodwill is allocated to the group of cash-generating units benefiting from the synergy of the business combination. Goodwill is initially recognized at cost as an asset and is subsequently measured at cost less accumulated impairment losses. Goodwill is not amortized but is subject to annual impairment testing or more frequently when events or circumstances indicate that there may be impairment. The Company determines whether there is impairment by assessing whether the carrying amount to which the goodwill relates exceeds its recoverable amount. In such a case, the loss of value is initially attributed to goodwill and any excess is allocated to the carrying amount of assets proportionately. Any impairment of goodwill is recognized in loss in the period in which it is recognized as a loss. Impairment losses on goodwill are not reversed in subsequent periods.

### **Impairment of non-financial assets**

The carrying value of property, plant and equipment and intangible assets is tested for impairment at each reporting date, in order to determine if there is any indication that an asset has experienced a loss of value. If any such evidence exists, the recoverable value of the asset is estimated.

The recoverable value of an asset or cash-generating unit (CGU) is the higher between its value in use and its fair value less costs of sale. To determine the value in use, the estimated future cash flows are discounted to their present value by applying a discount rate that reflects current market assessments, the time value of money and risks specific to the asset. For the purpose of impairment testing, assets are grouped to form the smallest groups of assets that generates cash flows that are largely independent of cash flows from other assets or groups of assets (CGU).

An impairment loss is recognized whenever the carrying value of an asset or a CGU exceeds its estimated recoverable value. Impairment losses are recognized in loss.

Impairment losses recognized in previous years are assessed at the reporting date to determine whether there are indications that confirm that the loss has decreased or if it still exists. An impairment loss is reversed if there has been a change in estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the carrying value of assets does not exceed the carrying value that would have been determined, after depreciation, if no impairment loss had been recognized.

### **Convertible debentures**

Convertible debentures are compound financial instruments within the meaning of IAS 32, Financial Instruments: Presentation, and have a liability component and an embedded derivative component.

#### Embedded derivatives

An embedded derivative is a component of a hybrid contract that also includes a non-derivative host, with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative.

# **Devonian Health Group Inc.**

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If a hybrid contract contains a host that is an asset, the entire hybrid contract is measured at fair value through net loss. If a hybrid contract contains a host that is not an asset, embedded derivatives are recorded at fair value separately from the host contract when their economic characteristics and risks are not clearly and closely related to those of the host contract. Subsequent changes in fair value are recorded in the consolidated statements of net loss and comprehensive loss.

The convertible debentures issued by the Company are a hybrid financial instrument that can be converted into units composed of common shares and warrants of the Company at the option of the holder. The hybrid financial instrument is recognized as a liability, with the initial carrying value of the convertible debentures (host) being the residual amount of the proceeds after separating the derivative component, which is recognized at fair value. Any directly attributable transaction costs are allocated to the host and derivative components in proportion to their initial carrying amounts. Subsequent to initial recognition, the host component of the hybrid financial instrument is measured at amortized cost using the effective interest method. The derivative component of the hybrid financial instrument is measured at FVTPL. Subsequent changes in fair value are recorded in the consolidated statements of net loss and comprehensive loss.

### **Fair value of warrants**

The proceeds from the issuance of units are distributed between shares and warrants issued based on their relative fair values using the proportional distribution method. At the time the warrants are exercised, their value is reclassified to share capital. The value of warrants that have not been exercised at maturity is reclassified to contributed surplus.

### **Cash**

Cash comprises cash and highly liquid financial instruments, with an initial term of three months or less, when applicable.

### **Stock-based compensation**

The Company has a stock option plan under which directors, executives, employees and consultants can be granted stock options of the Company.

Each grant is treated separately with its proper vesting period and its own fair value at the grant date, determined by the Black & Scholes option-pricing model. Compensation expense is recognized over the vesting period of each grant according to the number of options granted that are estimated to ultimately vest. Any revision of estimate is immediately recognized. Any consideration paid by the employees on exercise or purchase of stock options is credited to share capital. The value attributed to stock options is transferred to share capital at the issuance of shares.

In the normal course of business, the Company grants options in exchange for goods or services to parties other than staff members. For these transactions, the Company evaluates the fair value of goods or services received and, in counterpart, increases the equity by the same amount unless the fair value cannot be reliably estimated. In this case, the fair value is the value of options issued on the market at the date the goods or services are received.

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### Net loss per share

Basic loss per share is calculated by dividing net loss attributable to common shareholders by the weighted average number of shares outstanding during the year. Diluted loss per share is calculated by taking into account the potential dilution that could occur in the event that the warrants, stock options and the convertible debt conversion options to issue shares are exercised at the beginning of the year or at the date of their issuance, if later. The treasury stock method makes it possible to determine the dilution effect of the warrants and options.

### Provision

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and if it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are not recognized for future operating losses.

If the effect of time value of money is material, provisions are measured at the present value of cash flows expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation.

## 4 Additional information to the consolidated statements of net loss and comprehensive loss

The consolidated statements of net loss and comprehensive loss include the following items:

	2022 \$	2021 \$
Research and development – Amortization of property, plant, equipment and depreciation of right-of-use asset	271,082	264,597
Cost of sales – Amortization of intangible assets	592,787	765,733
Administrative expenses – Salaries and employer's contributions <sup>(2)</sup>	587,883	263,446
Administrative expenses – Stock-based compensation	532,687	82,720
Research and development expenses – Salaries and employer's contributions <sup>(1)</sup>	110,267	57,784
Cost of sales – Cost of inventories	540,101	514,100
Cost of sales – Inventory obsolescence	-	4,236

<sup>(1)</sup> The Company is eligible for refundable tax credits for research and development from the Government of Quebec for an amount of \$22,460, which has been credited for research and development costs (2021 – \$16,251).

<sup>(2)</sup> During the year, the Company didn't benefit from the wage subsidy (2021 – the amount of \$127,210 was credited to payroll expenses).

# Devonian Health Group Inc.

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### 5 Accounts receivable

	2022 \$	2021 \$
Trade	219,952	175,874
Sales taxes	65,444	42,929
Interest receivable	29,342	-
	<hr/> 314,738	<hr/> 218,803

### 6 Tax credits receivable

	2022 \$	2021 \$
Balance, beginning of year	16,251	164,773
Tax credits for research and development accounted for	22,460	16,251
Tax credits for research and development received	<hr/> (16,251)	<hr/> (164,773)
Balance, end of year	<hr/> 22,460	<hr/> 16,251

Tax credits receivable consist of tax credits for research and development receivable from the Government of Quebec, which relates to eligible research and development expenses under applicable tax legislation. The amounts in the receivable are subject to a tax audit by the governments, and the final amounts received may be different from those recorded.

### 7 Inventories

	2022 \$	2021 \$
Raw materials	75,264	-
Finished goods	<hr/> 79,358	<hr/> 28,221
	<hr/> 154,622	<hr/> 28,221

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**8 Property, plant and equipment and right-of-use assets**

								2022
	Building \$	Land \$	Leasehold improvements \$	Production and laboratory equipment \$	Computer equipment \$	Furniture and equipment \$	Right- of-use asset \$	Total \$
<b>Cost</b>								
Balance, beginning of year	2,537,676	562,324	2,100	1,543,990	20,568	62,100	32,523	4,761,281
Variation	-	-	-	63,409	6,760	3,500	7,415	81,084
Balance, end of year	2,537,676	562,324	2,100	1,607,399	27,328	65,600	39,938	4,842,365
<b>Accumulated amortization</b>								
Balance, beginning of year	641,830	-	2,100	964,071	20,568	62,100	4,065	1,694,734
Variation	-	-	-	-	-	-	(8,107)	(8,107)
Amortization	102,614	-	-	157,933	1,127	350	9,058	271,082
Balance, end of year	744,444	-	2,100	1,122,004	21,695	62,450	5,016	1,957,709
Carrying value, end of year	1,793,232	562,324	-	485,395	5,633	3,150	34,922	2,884,656
								2021
	Building \$	Land \$	Leasehold improvements \$	Production and laboratory equipment \$	Computer equipment \$	Furniture and equipment \$	Right- of-use asset \$	Total \$
<b>Cost</b>								
Balance, beginning of year	2,537,676	562,324	2,100	1,543,990	20,568	62,100	29,474	4,758,232
Variation	-	-	-	-	-	-	3,049	3,049
Balance, end of year	2,537,676	562,324	2,100	1,543,990	20,568	62,100	32,523	4,761,281
<b>Accumulated amortization</b>								
Balance, beginning of year	539,216	-	2,100	809,837	20,568	62,100	7,368	1,441,189
Variation	-	-	-	-	-	-	(11,052)	(11,052)
Amortization	102,614	-	-	154,234	-	-	7,749	264,597
Balance, end of year	641,830	-	2,100	964,071	20,568	62,100	4,065	1,694,734
Carrying value, end of year	1,895,846	562,324	-	579,919	-	-	28,458	3,066,547

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### 9 Intangible assets and goodwill

					<b>2022</b>
	<b>Intellectual property \$</b>	<b>Patents \$</b>	<b>Website \$</b>	<b>Licenses, trademark and distribution rights \$</b>	<b>Total \$</b>
<b>Cost</b>					
Balance, beginning of year	4,888,000	136,693	49,833	3,812,822	8,887,348
Balance, end of year	4,888,000	136,693	49,833	3,812,822	8,887,348
<b>Accumulated amortization</b>					
Balance, beginning of year	-	90,906	34,865	2,527,688	2,653,459
Amortization	-	9,270	12,460	571,057	592,787
Balance, end of year	-	100,176	47,325	3,098,745	3,246,246
Carrying value, end of year	4,888,000	36,517	2,508	714,077	5,641,102
					<b>2021</b>
	<b>Intellectual property \$</b>	<b>Patents \$</b>	<b>Website \$</b>	<b>Licenses, trademark and distribution rights \$</b>	<b>Total \$</b>
<b>Cost</b>					
Balance, beginning of year	4,888,000	136,693	49,833	3,812,822	8,887,348
Balance, end of year	4,888,000	136,693	49,833	3,812,822	8,887,348
<b>Accumulated amortization</b>					
Balance, beginning of year	-	59,830	22,405	1,805,491	1,887,726
Amortization	-	31,076	12,460	722,197	765,733
Balance, end of year	-	90,906	34,865	2,527,688	2,653,459
Carrying value, end of year	4,888,000	45,787	14,968	1,285,134	6,233,889

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

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### Licenses, trademarks, and distribution rights

The licenses, trademarks and distribution rights valued in the consolidated statements of financial position are Pantoprazole, Cléo-35 and PurGenesis.

### Impairment test

Goodwill arising from the business combination is allocated to groups of CGUs likely to benefit from the business combination. For the goodwill, there is one CGU and the impairment assessment was performed by comparing the Company's net assets to the market capitalization as at July 31, 2022, which is considered a Level 1 measurement.

## 10 Accounts payable

	2022 \$	2021 \$
Suppliers	410,443	555,498
Accrued expenses <sup>(1)</sup>	591,894	1,238,210
Salaries, payroll deductions and contributions	32,840	15,710
	<u>1,035,177</u>	<u>1,809,418</u>

<sup>(1)</sup> Subsequent to the date of financial statements 2021 and effective from May 2022, the management agreed with one of the wholesalers that no fees are due for their Pharmacy Programs. As a consequence of this recent available information, the management concluded to revise accruals previously recorded for this wholesaler of an amount \$305,802 against reduction of distribution revenues.

## 11 Long-term debt

	2022 \$	2021 \$
Loan, secured by the universality of movable and immovable property, tangible and intangible, present and future of the Company, for a carrying value of \$8,490,836, interest payable monthly at the Toronto Dominion Bank's prime rate plus 6% (10.70%; 2021 – 8.45%), principal repayable at maturity in January 2024*	3,500,000	3,500,000
Canada Emergency Business Account Loan	76,423	70,081
	<u>3,576,423</u>	<u>3,570,081</u>

\* In the event of a change of control by acquisition or dilution at 50%, the principal and the interest payable until maturity of the term are payable within 30 days of the date of the change of control.

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**12 Convertible debentures**

	<b>2022</b>		
	<b>Host \$</b>	<b>Derivative \$</b>	<b>Total \$</b>
Balance, as at July 31, 2021	1,325,949	361,583	1,687,532
Accretion	354,216	-	354,216
Matured	(1,000,000)	-	(1,000,000)
Change in fair value of derivative	-	(361,583)	(361,583)
Balance, as at July 31, 2022	<u>680,165</u>	<u>-</u>	<u>680,165</u>
			<b>2021</b>
	<b>Host \$</b>	<b>Derivative \$</b>	<b>Total \$</b>
Balance, as at July 31, 2020	1,083,668	68,407	1,152,075
Accretion	242,281	-	242,281
Change in fair value of derivative	-	293,176	293,176
Balance, as at July 31, 2021	<u>1,325,949</u>	<u>361,583</u>	<u>1,687,532</u>

The principal amount of the debentures (\$697,000 as at July 31, 2022 and \$1,697,000 as at July 2021) was convertible into units of the Company at a price of \$0.75 per unit and matured in August 2022. Each unit consists of one subordinate voting share in the capital of the Company and one subordinate voting share purchase warrant. Each warrant was to entitle the holder to acquire one subordinate voting share in the capital of the Company at a price of \$0.95 until 48 months after the closing date.

Interest on the convertible debentures was payable in units semi-annually based on an annual rate of 10%. Each unit was to comprise one common share and one share purchase warrant having a four-year contractual life. The number of units to be issued was to be calculated as follows according to the situation:

- If the subordinate voting shares comprising the units were not subject to resale restrictions by a recognized stock exchange immediately following the issuance, the five-day average of the VWAP (volume-weighted average share price) immediately prior to the interest payment date was applicable and was to be used to settle the 10% interest. The exercise price of the warrants included in the units will be equal to the one obtained for the price of the shares used to settle the interest plus 30%.
- If the subordinate voting shares were subject to resale restrictions after they were issued, 90% of the five-day average of the VWAP immediately prior to the interest payment date was to be applicable and the exercise price of the warrants was equal to the one obtained for the price of the shares based on the conversion rate of interest plus 30%.



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Convertible debentures are compound financial instruments within the meaning of IAS 32 and have a liability component and an embedded derivative component. The derivative is measured at FVTPL, and its fair value must be measured at each consolidated statement of financial position date. Subsequent changes in fair value are recognized in the consolidated statement of net loss and comprehensive loss. The change in fair value is included in finance costs (note 18).

The fair market value of the derivative component of the debentures was established according to the discounted cash flow method, and using the following average assumptions:

	<b>2022</b>	<b>2021</b>
Expected life	0.08 years	1 to 1.75 years
Risk-free interest rate	1.50%	0.43%
Expected volatility	45%	85%

### **13 Share capital**

#### **Description of authorized share capital**

An unlimited number of subordinate voting shares, exchangeable subordinate voting shares and multiple voting shares, participating, without par value, have a non-cumulative dividend.

The subordinate voting shares, exchangeable subordinate voting shares and multiple voting shares are handled as if they were of one and the same category.

The holders of subordinate voting shares and exchangeable subordinate voting shares are entitled to receive notice, and to attend and vote at all meetings of the shareholders, except those at which holders of a specific class are entitled to vote separately as a class under the CBCA. Each subordinate voting share and each exchangeable subordinate voting share confers the right to one vote per share.

The holders of multiple voting shares were entitled to receive notice and to attend and vote, at all meetings of the shareholders, except those at which holders of a specific class were entitled to vote separately as a class under the CBCA. Each multiple voting share conferred the right to six votes per share. Each multiple voting share could, at any time, be exchanged for one subordinate voting share. In May 2027, ten years after the qualifying transaction, the authorized holder, without any further action, should automatically be deemed to have exercised their right to exchange all of the multiple voting shares held by such holder, into fully paid and non-assessable subordinate voting shares of the Company on a share-for-share basis.

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	2022 \$	2021 \$
<b>Share capital issued</b>		
131,138,635 shares (2021 – 93,460,688)	27,572,182	20,208,600

The 131,138,635 shares outstanding as at July 31, 2022 are all subordinate voting shares. As part of the December 2021 financing agreement, the 19,966,523 multiple voting shares were converted into subordinate voting shares (2021 – 73,494,165 subordinate voting shares and 19,966,523 multiple voting shares).

**Issuance**

a) Interest on convertible debentures

During fiscal 2022, the Company issued 353,642 units to holders of debentures issued on July 19, 2018, and August 31, 2018, at a unit price ranging from \$0.45 to \$0.50. These units and shares were issued in consideration for the interest owed to them for a total amount of \$169,700. Each unit is composed of one subordinate voting share and one warrant. Each warrant grants its holder the right to subscribe for one subordinate voting share of the share capital of the Company at a price ranging from \$0.59 to \$0.65 for a period of 48 months.

The fair values of the 353,642 shares and 353,642 warrants were estimated at \$169,700 and \$97,917, respectively, according to the following weighted average assumptions:

Risk-free interest rate	0.43%
Average expected duration	4 years
Expected volatility	85%
Share price	\$0.44
Expected dividend	Nil

During fiscal 2021, the Company issued 604,315 units and 33,832 shares to holders of debentures issued on July 19, 2018, and August 31, 2018 at a unit price ranging from \$0.15 to \$0.23. These units and shares were issued in consideration for the interest owed to them for a total amount of \$120,111. Each unit is composed of one subordinate voting share and one warrant. Each warrant grants its holder the right to subscribe for one subordinate voting share of the share capital of the Company at a price ranging from \$0.19 to \$0.30 for a period of 48 months.

The 33,832 shares were issued to a director, who is a holder of debentures issued during the second tranche of the private placement closed on August 31, 2018.

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The fair values of the 638,147 shares and 604,315 warrants were estimated at \$120,111 and \$56,475, respectively, according to the following weighted average assumptions:

Risk-free interest rate	0.43%
Average expected duration	1.5 years
Expected volatility	85%
Share price	\$0.188
Expected dividend	Nil

b) Private financing

On September 13, 2021, the Company completed a private financing by issuing 2,415,090 units at a price of \$0.44 per unit for gross proceeds of \$1,062,640. Each unit consists of one subordinate voting share and one share purchase warrant. Each warrant entitles its holder to acquire one subordinate voting share at a price of \$50 per share, until September 2023. Related costs of \$49,506 for this share issuance were recorded as a reduction of share capital.

The fair value of the 2,415,090 shares issued and the 2,415,090 warrants issued was estimated at \$793,711 and \$268,929, respectively, according to the Black-Scholes valuation model and using the following assumptions:

Risk-free interest rate	0.43%
Average expected duration	2.5 years
Expected volatility	85%
Share price	\$0.44
Expected dividend	Nil

On November 12, 2021, and November 26, 2021, the Company completed a private financing, through the issuance of a total of 32,897,662 units at a price of \$0.30 per unit, for gross proceeds of \$9,869,299. Each unit consists of one subordinate voting share and one share purchase warrant. Each warrant entitles its holder to acquire one subordinate voting share at a price of \$0.40 per share until November 2023.

Related costs of \$119,251 for this share issuance were recorded as reduction of share capital.

The fair value of the 32,897,662 shares issued and the 32,897,662 warrants issued was estimated at \$5,888,187 and \$3,981,112, respectively, according to the Black-Scholes valuation model and using the following assumptions:

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Risk-free interest rate	1%
Average expected duration	2 years
Expected volatility	85%
Share price	\$0.40
Expected dividend	Nil

On December 29, 2020, the Company completed a private financing, by issuing 10,100,000 units at a price of \$0.12 per unit, for gross proceeds of \$1,212,000. Each unit is made up of one subordinate voting share and one-half share purchase warrant. Each warrant confers on its holder the right to acquire one subordinate voting share at a price of \$0.15 until December 29, 2022.

The Company paid finder's fees for a cash amount of \$22,100 and related costs for an amount of \$13,571.

The fair value of the 10,100,000 shares issued and the 5,050,000 warrants issued was estimated at \$1,038,857 and \$173,143, respectively, according to the Black and Scholes valuation model and using the following assumptions:

Risk-free interest rate	0.43%
Average expected life	1.5 years
Expected volatility	85%
Share price	\$0.12
Expected dividend	Nil

c) Exercise of warrants

On May 4, 2022, the Company issued 700,000 subordinate voting shares, at a unit price of \$0.25 per share, for gross proceeds of \$175,000, following the exercise of 700,000 warrants. The value of \$46,882 that had been assigned to these warrants was reclassified to share capital.

On May 31, 2021, the Company issued 200,000 subordinate voting shares, at a unit price of \$0.25 per unit, for gross proceeds of \$50,000, following the exercise of 200,000 warrants. The value of \$13,395 which had been attributed to these warrants was reclassified to share capital.

d) Settlement of a debt

On March 10, 2022, a total of 1,311,553 subordinate voting shares were issued at a price of \$0.352 per unit, for a consideration of \$461,667. These shares were issued in settlement of the total amount of \$461,667 due to a consultant of the Company's wholly owned subsidiary, Altius Healthcare Inc., which was assumed by the Company.

Related costs of \$2,808 related to this transaction were recorded as reduction of share capital.

## **14 Stock option plan**

Under the stock option plan put in place in May 2017, the members of the Board of Directors can attribute stock options allowing the directors, executives, employees, and consultants of the Company to acquire shares of the Company. The maximum number of options that can be granted according to the stock option plan is equal to a maximum of 10% of the outstanding subordinate voting shares.

The options to be granted according to the stock option plan will not exceed a duration of 10 years and will be granted at the price and conditions that the directors will consider necessary to reach the goal of the stock option plan, and according to the applicable regulations. The exercise price of the option cannot be lower than the market price.

During the year, the Company granted 1,695,000 stock options to consultants and directors of the Company as well as 525,000 stock options to employees and members of the management of the Company. These options can be exercised at a price ranging from \$0.40 to \$0.50, for a period of 10 years from the date of grant. These options are exercisable on the grant date. The fair value of these options was estimated at \$532,585 based on the Black-Scholes valuation model and using the following weighted average assumptions:

Risk-free interest rate	1%
Average expected life	3 years
Expected volatility	95%
Share price	\$0.45
Expected dividend	Nil

During fiscal year 2021, the Company granted 60,000 stock purchase options to a director of the Company as well as 801,645 stock purchase options to a member of management. These options are exercisable at a price of \$0.20 and \$0.12, respectively, for a period of 10 years from the date of grant. These options are exercisable on the grant date. The fair value of these options was estimated at \$59,509 based on the Black-Scholes valuation model and using the following weighted average assumptions:

Risk-free interest rate	0.43%
Average expected life	2.5 years
Expected volatility	95%
Share price	\$0.12
Expected dividend	Nil

The Company recorded an expense of \$532,687 during the year (2021 – \$82,720).

The determination of the volatility assumption of stock options is based on a historical volatility analysis over a period equal to the expected life of the options.

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The following table summarizes the situation of the Company's stock option plan and the changes incurred during the years ended July 31, 2022 and 2021:

	2022		2021	
	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$
Outstanding, beginning of year	6,940,000	0.33	6,228,355	0.37
Options expired	(1,085,000)	0.49	(150,000)	0.80
Options granted to directors and consultants	1,695,000	0.45	60,000	0.20
Options granted to members of management and employees	525,000	0.40	801,645	0.12
Outstanding, end of year	8,075,000	0.34	6,940,000	0.33
Options exercisable, end of year	8,075,000	0.34	6,935,000	0.33
Weighted average fair value of the options granted during the year		0.24		0.07

The following table summarizes information about the options outstanding and exercisable as at July 31, 2022:

Exercise price \$	Options outstanding and exercisable	
	Number of options outstanding	Weighted average remaining contractual life
0.12	801,645	8.41 years
0.15	2,658,355	7.90 years
0.20	60,000	8.64 years
0.21	625,000	7.73 years
0.40	1,345,000	9.3 years
0.44	150,000	9.15 years
0.50	725,000	9.47 years
0.60	1,510,000	4.07 years
1.20	200,000	0.62 years

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### 15 Warrants

The following table summarizes information about the Company's warrants and the changes during the years:

	2022		2021	
	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$
Outstanding, beginning of year	9,740,653	0.23	12,689,699	0.89
Issued	35,666,394	0.41	5,654,315	0.16
Expired	(2,036,722)	0.38	(8,403,361)	1.19
Exercised	(700,000)	0.25	(200,000)	0.25
Outstanding, end of year	42,670,325	0.37	9,740,653	0.23

The following table summarizes information about warrants outstanding as at July 31, 2022:

Exercise price \$	Warrants outstanding	
	Number of warrants outstanding	Average remaining contractual life
0.15	5,050,000	0.41 years
0.194	201,982	2.50 years
0.218	179,137	1.50 years
0.225	291,393	1.50 years
0.237	272,467	2.00 years
0.26	252,055	2.51 years
0.263	146,561	1.75 years
0.30	150,278	2.63 years
0.338	190,727	1.50 years
0.38	173,831	0.73 years
0.40	32,993,162	1.32 years
0.50	2,415,090	1.12 years
0.59	78,078	3.14 years
0.61	73,540	3.60 years
0.64	101,202	3.26 years
0.65	100,822	3.51 years

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### 16 Capital management

The Company includes all components of equity in its capital definition: share capital, stock options, warrants, contributed surplus and deficit. In terms of capital management, the Company's objectives are to preserve its ability to continue as a going concern to ensure its sustainability by obtaining the necessary funding to realize its development activities and to provide in the future an adequate return to its shareholders. The Company finances its operations by issuing shares and debentures as well as operating income.

The Company's objectives and policies in terms of capital management have not changed since July 31, 2021. The Company has committed to the lender not to redeem preferred or common shares without its prior written consent.

### 17 Commitments

The Company has committed to pay a total amount of \$80,000 over a four-year period to a research project entitled "The Next Generation Agriculture: Botanical Extracts and Essential Oils as the New Antimicrobials against Microbial Contaminants and Diseases of Cannabis." As at July 31, 2022, the balance of this commitment was \$10,000.

### 18 Financial expenses

Financial expenses are as follows:

	2022	2021
	\$	\$
Interest expenses and bank charges	4,258	3,988
Interest on long-term debt	309,197	295,746
Interest on lease liability	958	752
Interest on deposit certificate	(39,652)	-
Amortization of discount on convertible debentures	354,216	242,281
Amortization of discount on Canada Emergency Business Account Loan	6,342	2,211
Embedded derivative convertible debentures – Change in fair value	(361,583)	293,177
Interest expense on convertible debentures	262,000	248,080
	<u>535,736</u>	<u>1,086,235</u>



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### 19 Net loss per share

The following table provides the weighted average number of shares used to calculate the basic loss per share:

	2022 \$	2021 \$
Weighted average number of shares used to calculate the basic loss per share	119,027,954	88,842,565
Items excluded from the calculation of diluted loss per share:		
Stock options	8,075,000	6,940,000
Warrants	42,670,325	9,740,653
Convertible debentures	1,858,667	4,525,334

For the years ended July 31, 2022 and 2021, the impacts of the warrants, stock options and the convertible debentures were excluded from the calculation of diluted loss per share as they would have an anti-dilutive effect.

### 20 Income taxes

The presented recovery of income taxes differs from the amount of the income tax expense calculated using the Canadian statutory tax rates, mainly due to the following:

	2022 \$	2021 \$
Canadian statutory tax rate	26.50%	26.50%
Recovery calculated using the statutory tax rates	(871,290)	(886,791)
Increase (decrease) in income tax expense from:		
Stock-based compensation	141,162	21,921
Variation of potential tax assets not recognized	768,588	871,645
Non-deductible fees	1,478	727
Other individually insignificant items	(39,938)	(7,502)
	-	-

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The significant components of the deferred tax assets (liabilities) of the Company are as follows:

	<b>2022</b>	<b>2021</b>
	\$	\$
Deferred long-term tax assets:		
Tax losses	4,126,734	3,580,427
Financing fees	49,608	73,599
Research and development expenses	1,001,403	905,799
Lease liability	5,771	4,565
	<u>5,183,516</u>	<u>4,564,390</u>
Deferred long-term tax liabilities:		
Fixed assets and intangible assets	899,841	1,106,229
Right-of-use asset	9,254	7,541
Debentures	4,462	2,509
	<u>913,557</u>	<u>1,116,279</u>
	4,269,959	3,448,111
Potential tax assets not recognized	<u>(4,269,959)</u>	<u>(3,448,111)</u>
	<u>-</u>	<u>-</u>

The Company's non-capital losses that may be used to reduce taxes in future years total \$15.3 million at the federal level and \$15.6 million at the provincial level and expire at various dates between 2034 and 2042.

The balance of the research and development expenses that may be used to reduce taxes in future years is \$3.8 million. The Company may take advantage of the tax benefit related to these expenses for an indefinite period.

A deferred tax asset of \$1,001,403 (2021 – \$905,799) is recorded relative to the items listed above, being an amount equal to the deferred tax liability recorded.

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### 21 Related party transactions

The principal executives are the President of the Company, the President of the subsidiary, the interim Chief Financial Officer and the Directors. During the year ended July 31, 2022, the Company has paid them a total remuneration of \$1,238,751 (2021 – \$480,955), which has been recognized in administrative expenses and of which the main components are:

	2022 \$	2021 \$
Salaries and benefits	599,275	299,408
Consultant fees	160,416	-
Management fees	200,000	100,000
Stock-based compensation	279,060	81,547

### 22 Details of consolidated statements of cash flows

#### Changes in non-cash working capital

The changes in non-cash working capital items for the years ended July 31, 2022 and 2021 are as follows:

	2022 \$	2021 \$
Accounts receivable	(95,935)	291,581
Tax credits receivable	(6,209)	148,522
Inventories	(126,401)	58,354
Prepaid expenses	(64,063)	5,594
Accounts payable	(309,767)	(889,736)
	<u>(602,375)</u>	<u>(385,685)</u>

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### 23 Reconciliation of liabilities from financing activities

The table below shows the changes in liabilities arising from the Company's financing activities, which includes changes in cash flows and changes without cash consideration:

	Balance, as at July 31, 2021 \$	Net cash flows from financing activities \$	Other changes <sup>(1)</sup> \$	Balance, as at July 31, 2022 \$
			Changes without cash consideration	
Convertible debentures (note 12)	1,687,532	(1,000,000) <sup>(2)</sup>	(7,367)	680,165
Long-term debt (note 11)	3,570,081	-	6,342	3,576,423
	5,257,613	(1,000,000)	(1,025)	4,256,588

<sup>(1)</sup> Other changes include amortization of the discount on convertible debentures and the long-term debt and changes in fair value of the embedded derivative of convertible debentures.

<sup>(2)</sup> Including \$479,394, classified as operating activities representing the initial issue discount.

	Balance, as at July 31, 2020 \$	Net cash flows from financing activities \$	Other changes <sup>(1)</sup> \$	Balance, as at July 31, 2021 \$
			Changes without cash consideration	
Convertible debentures (note 12)	1,152,075	-	535,457	1,687,532
Long-term debt (note 11)	3,509,855	60,226	-	3,570,081
	4,661,930	60,226	535,457	5,257,613

<sup>(1)</sup> Other changes include amortization of the discount on convertible debentures and the long-term debt and changes in fair value of the embedded derivative of convertible debentures.

## **24 Economic dependence**

During the year, the Company realized 30% (2021 – 32%) of its revenues from one client and 88% (2021 – 91%) of its purchases of inventories from one supplier.

## **25 Financial instruments**

In the normal course of business, the Company is exposed to risks, the most significant of which are market risk, credit risk and liquidity risk.

### **Market risk**

Market risk is the risk that the fair value or cash flows of a financial instrument will fluctuate due to changes in market factors. Market risk comprises three types of risk: interest rate risk, currency risk and price risk. The Company is exposed to one of these risks: interest rate risk.

#### **Interest rate risk**

The Company has a long-term borrowing bearing interest at variable rate. Consequently, the Company is exposed to interest rate risk based on changes in the prime rate. Based on the balance as at July 31, 2022, a 1% increase in the prime rate would increase interest expense by \$35,000 over a 12-month horizon.

### **Credit risk**

The Company's cash is maintained at major financial institutions; therefore, the Company considers the risk of non-performance of this instrument to be remote.

The Company is exposed to credit risk on the loss associated with a counterparty's inability to fulfill its payment obligations. The maximum credit risk is equal to the carrying value of accounts receivable. The Company does not expect to be exposed to a higher-than-normal credit risk.

As at July 31, 2022, approximately 43% (2021 – 65%) of receivables were due from a single client.

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### Liquidity risk

Liquidity risk is the risk that the Company has difficulty meeting its commitments associated with financial liabilities. As at July 31, 2022, the Company has current debts of \$874,761 (2021 – \$1,809,418). The maturity dates of the long-term debt and the convertible debentures are presented in notes 11 and 12.

The Company monitors its cash resources. If the Company believes that it does not have sufficient liquidity to meet its obligations, management will consider the possibility of obtaining additional funds through the issuance of shares or debentures (note 2).

The tables below categorize the Company's financial liabilities (including interest) into relevant maturity groupings based on the remaining periods at the consolidated statement of financial position dates to the contractual maturity dates.

	Less than 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
	\$	\$	\$	\$	\$
Long-term debt	94,395	280,105	3,656,982	-	4,031,482
Convertible debentures	667,000	-	-	-	667,000
Accounts payable and accrued liabilities	876,625	-	-	-	876,625

### Fair value

The fair value of long-term debt is comparable to its carrying value, due to its variable rate. Interest based on variable rates is determined using the rate in effect at the end of the year.

For the debentures, the fair value is comparable to the carrying value due to imminent maturity.

## 26 Segment information

The Company is currently operating in a single reportable operating segment in Canada, which is the pharmaceutical sector.

# Devonian Health Group Inc.

## Notes to Consolidated Financial Statements

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### 27 Subsequent events

On August 24, 2022, the Company granted 300,000 stock options to employees as well as 675,000 stock options to a consultant and members of the Board of Directors, exercisable at a price of \$0.50 per subordinate voting share. Of these 975,000 options, 350,000 are exercisable immediately, for a period of five years, while 375,000 are exercisable immediately for a period of 10 years and finally, 250,000 options will be exercisable from February 26, 2023, for a period of 10 years.

On September 14, 2022, the Company issued 39,999 units following the conversion of debentures that had been issued on August 31, 2018, for a total consideration of \$30,000.

Each unit includes a subordinate voting share issued at a price of \$0.75 and a warrant exercisable at a price of \$0.95, for a period of four years following the date of their issuance. As of October 7, 2022, the entire remaining balance of \$667,000 of convertible debentures had been repaid to holders.

On September 19, 2022, the Company issued 87,840 units to holders of debentures issued on August 31, 2018, at a unit price of \$0.40. These units were issued in consideration for the interest due to them as of August 31, 2022, for a total amount of \$35,136. Each unit consists of one subordinate voting share and one warrant. Each warrant entitles its holder to subscribe for one subordinate voting share of the share capital of the Company at a price of \$0.52 for a period of 48 months following their date of issue.