

**kneat.com, inc.**  
**(formerly Fortune Bay Corp.)**  
**Year ended December 31, 2016**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

*This Management's Discussion and Analysis ("MD&A") provides a review of the performance of kneat.com, inc. ("kneat.com" or the "Company") and should be read in conjunction with the audited consolidated financial statements of kneat.com (the "Financial Statements") for the years ended December 31, 2016 and December 31, 2015, which have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").*

*The information presented in this MD&A is as of April 24, 2017. The reporting currency for kneat.com is the Canadian dollar. All of the financial information presented herein is expressed in Canadian dollars, unless otherwise stated. United States dollars are indicated by the symbol "US\$". Euros are indicated by the symbol "€". This MD&A contains "forward-looking statements" that are subject to risk factors set out in a cautionary note contained herein. The reader is cautioned not to place undue reliance on forward-looking statements.*

## **CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS AND INFORMATION**

This MD&A contains "forward-looking information", as such term is defined in applicable Canadian securities legislation. Forward-looking information is necessarily based on a number of estimates and assumptions that are inherently subject to significant business, economic and competitive uncertainties and contingencies. All statements other than statements which are reporting results as well as statements of historical fact set forth or incorporated herein by reference, are forward looking information that may involve a number of known and unknown risks, uncertainties and other factors, many of which are beyond kneat.com's ability to control or predict. Forward-looking information can be identified by the use of words such as "may," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "intends," "continue," or the negative of such terms, or other comparable terminology.

This information includes, but is not limited to, comments regarding:

- the development plans for the Kneat Gx platform;
- the Company's business strategy;
- the Company's strategy for protecting its intellectual property;
- the Company's ability to obtain necessary funding on favorable terms or at all;
- the Company's plan and ability to secure additional customers and additional revenues;
- the risk of competitors entering the market;
- the Company's hiring and retention of skilled staff;
- the ability to obtain financing to fund future expenditure and capital requirements; and
- the impact of adoption of new accounting standards.

Although kneat.com believes that the plans, intentions and expectations reflected in this forward-looking information are reasonable, kneat.com cannot be certain that these plans, intentions or expectations will be achieved. Actual results, performance or achievements could differ materially from those contemplated, expressed or implied by the forward-looking information contained in this report. Disclosure of important factors that could cause actual results to differ materially from kneat.com's plans, intentions or expectations is included in this report under the heading *Risk Factors*.

Forward-looking information inherently involves risks and uncertainties that could cause actual results to differ materially from the forward-looking information. Factors that could cause or contribute to such differences include, but are not limited to, unexpected changes in business and economic conditions, including the global financial and capital markets; changes in interest and currency exchange rates; changes in operating revenues and costs; political or economic instability, either globally or in the countries in which kneat.com operates; local and community

impacts and issues; labour disputes; environmental costs and risks; competitive factors; availability of external financing at reasonable rates or at all; and the factors discussed in this MD&A under the heading "Risk Factors". Many of these factors are beyond kneat.com's ability to control or predict. These factors are not intended to represent a complete list of the general or specific factors that may affect kneat.com. kneat.com may note additional factors elsewhere in this MD&A. All forward-looking statements and information speak only as of the date made. All subsequent written and oral forward-looking statements attributable to kneat.com, or persons acting on kneat.com's behalf, are expressly qualified in their entirety by these cautionary statements. Readers are cautioned not to put undue reliance on forward-looking information due to the inherent uncertainty therein. kneat.com disclaims any intent or obligation to update publicly any forward-looking statements, whether as a result of new information, future events or results or otherwise.

## COMPANY OVERVIEW

kneat.com, inc. (the "Company" or "kneat.com"), (formerly Fortune Bay Corp.) commenced trading on the TSX Venture Exchange ("TSX-V") as kneat.com on July 5, 2016 under the symbol KSI (TSX-V). The Company is incorporated and domiciled in Canada and its registered office is located at 1969 Upper Water Street, Suite 2001, Halifax, Nova Scotia. The Company's operations are centralized in Limerick, Ireland.

### *Transaction with Kneat Solutions Limited*

On June 27, 2016, kneat.com completed a transaction with Kneat Solutions Limited and 9617337 Canada Limited (now renamed Fortune Bay Corp., herein after referred to as "Spinco"), pursuant to which it: (i) spun-out its resource properties to Spinco by way of a court-approved plan of arrangement in Ontario (the "Arrangement"); and (ii) acquired 100% of the issued and outstanding ordinary shares of Kneat Solutions Limited by way of a concurrent scheme of arrangement in Ireland (the "Merger"), collectively referred to as the "Transaction".

Pursuant to the Transaction, shareholders of kneat.com on the close of business on June 24, 2016 received one (1) new common share of kneat.com (each a "kneat.com share") and one and one half (1.5) of a common share of Spinco (a "Spinco Share") in exchange for each three (3) common shares of kneat.com held by them on June 24, 2016.

Upon completion of the Transaction on June 27, 2016, shareholders of kneat.com on June 24, 2016 held 31.3% of the issued and outstanding kneat.com shares, with the former shareholders of Kneat Solutions Limited holding the remaining 68.7% of the issued and outstanding kneat.com shares. In addition to acquiring all the issued and outstanding shares of Kneat Solutions Limited, kneat.com retained net \$8.0 million of cash.

The shareholders of Kneat Solutions Limited, through owning 68.7% of the outstanding kneat.com shares on completion of the Transaction, control kneat.com. As a consequence of the Transaction, the shareholders of Kneat Solutions Limited acquired control over the combined entity. After its reorganization, kneat.com does not meet the definition of a business, therefore the Transaction is outside the scope of IFRS 3, *Business Combinations*. The Transaction has therefore been accounted for under IFRS 2, *Share-based payment*. Under this basis of accounting, the consolidated entity is considered to be a continuation of Kneat Solutions Limited, with the net identifiable assets of kneat.com deemed to have been acquired by Kneat Solutions Limited. Refer to note 6 of the audited consolidated financial statements of the Company for the year ended December 31, 2016 for further details.

### *Operational overview*

kneat.com designs, develops and supplies software for data and document management within regulated environments. kneat.com's current product is Kneat Gx, a configurable, commercial, off-the-shelf application focused on validation lifecycle management and testing within the life sciences industry (i.e. biotech, pharmaceutical and medical device manufacturing). Complete and comprehensively documented validation of processes, products, equipment and software is a significant and impactful regulatory requirement in the life sciences industry. The Kneat Gx application provides a compliant e-solution that enables life science companies to become efficient and compliant with an automated process that has traditionally been manual, in-efficient and 100% paper-based.

Every manufacturing process, every piece of equipment and every computer system involved in the manufacturing of pharmaceutical, biotechnology and medical device products must be validated in accordance with current Good Manufacturing Practice (“cGMP”) regulations. Validation necessitates extensive signed and time stamped documentary evidence that all aspects of these systems are designed and tested to ensure that they will repeatedly produce products to the approved specifications. This documentation is subject to audit by global regulatory authorities such as the United States of America Food and Drug Administration and the European Medicines Agency.

Traditionally validation and cGMP testing has been a manual, paper intensive activity. Test documents must be developed, printed, approved, executed, post approved and filed away ready for regulatory audit in the future. Everything is done on paper using wet ink to record, apply proof signature and date, etc. It is a data and document minefield that leaves healthcare companies susceptible to delays, high costs and non-compliance. Non-compliance can lead to regulatory fines, recalls, threats to patient safety and delays to market. Non-compliance can cost companies billions of dollars in penalties, lost revenues and remediation.

The solution that Kneat Gx provides to its customers is a complex one that has taken a dedicated professional team of industry experts over nine years of intense research and development to overcome. kneat.com’s customers cite Kneat Gx’s innovation, ease of use, its central and dynamic data management, its configurability and its electronic records and signatures capabilities as the key differentiators that set it apart in the market. In addition, kneat.com’s team of developers, training manuals and customer support are considered best in class by its customers.

kneat.com possesses a best in class quality management system and is certified to ISO 9001. In addition, it adheres to all applicable life science regulations such as all current cGMPs, GAMP5, International Conference on Harmonization ICH Q8, Q9 and Q10, EU Annex 11, FDA CFR Title 21 Part 11 governing Electronic Records and Electronic Signatures. Adhering to these regulations and guidelines is a mandatory requirement in order to supply to this highly regulated market. Potential customers must perform extensive audits to verify compliance prior to purchasing kneat.com’s products.

## **BUSINESS OBJECTIVES**

With the completion of the Transaction, kneat.com now has the ability to use its financial resources for the following key business objectives:

- development of new features and functionality of Kneat Gx based on customer feedback;
- product advancements to enhance the user experience;
- further development and deployment of its SaaS model to small and medium size customers;
- securing contracts with key customers and targets; and
- expansion of the operational management team in order to reach these and other key future objectives.

### *Recent developments*

On April 4, 2017, kneat.com announced the appointment of Mr. Derek Hughes as the United States Sales Director. Mr. Hughes will be responsible for sales of the Kneat Gx software platform throughout the United States.

On February 22, 2017, the Company announced that the Journal of Validation Technology published the article 'Case Study: Implementation of an Electronic Life Cycle Management System for Validation ...and Beyond' which outlines the value of the Kneat Gx software. The case study concludes that Kneat's software assisted a multi-national biotech company to create best practices across its global network, providing productivity gains in excess of 100% and cycle time improvements of more than 50% in validation, with the prospect of leveraging the technology across many other testing processes.

On January 4, 2017, kneat.com announced that a large multi-national pharmaceutical company deployed the Kneat Gx platform to replace many of its paper-based validation and GxP testing processes within their highly regulated manufacturing facilities worldwide. This customer is reporting significant productivity and cycle time improvements; all supporting a faster time to market goal. This initial contract is for a period of three years and is valued at a minimum of \$1.1 million CAD.

On November 3, 2016, the Company announced the appointment of Mr. Mark Geldard as its European Sales Director. Mr. Geldard will lead the Company's sales and marketing activities throughout Europe.

During the year ended December 31, 2016, the focus of the Company has been: i) the completion of the Transaction; ii) the progress towards key improvements in the functionality of the Kneat Gx platform; iii) the further development of the software as a service (SaaS) model; and iv) the advancement of discussions with key customers and targets.

- Management's priority from a business perspective was to complete the Transaction, whereby cash was secured to fund ongoing growth and to increase the liquidity of the stock by meeting the requirements for listing on the TSX-V.
- During the year ended December 31, 2016, key software developers and testers have been hired to further advance and develop the Kneat Gx platform. The functionality and performance of the Kneat Gx platform has been and continues to be improved based on the technical feedback from early customers and new prospects.
- One of the key initiatives for the Company is to deploy a SaaS model which will allow the Company to service small to mid-size customers. During the year ended December 31, 2016, development of the SaaS model has progressed significantly and will continue to be a focus into 2017.
- Management has spent 2016 focusing on building relationships with new or potential customers. In addition, discussions with current customers are ongoing and have focused on sustainable long term growth based on expansion of the Company's technology within their operations. Significant time has also been spent on developing a marketing plan and hiring of key sales team members.

## SELECTED ANNUAL INFORMATION

Expressed in thousands of Canadian dollars, except for per common share amounts, and prepared in accordance with IFRS:

	2016	2015	2014
	\$	\$	\$
Total revenue	820	986	293
Total expenses	(7,836)	(1,995)	(1,474)
Total loss	(7,016)	(1,009)	(1,181)
Total loss per common share	(0.21)	(0.04)	(0.05)
Cash dividends per common share	N/A	N/A	N/A
Total assets	9,571	4,251	2,236
Total non-current financial liabilities	1,115	1,159	1,057

## SELECTED QUARTERLY INFORMATION

Expressed in thousands of Canadian dollars, except for per common share amounts, and prepared in accordance with IFRS:

	Q4 2016	Q3 2016	Q2 2016	Q1 2016	Q4 2015	Q3 2015	Q2 2015	Q1 2015
	\$	\$	\$	\$	\$	\$	\$	\$
Total revenue	707	82	19	18	345	299	201	147
Total expenses	(1,100)	(814)	(5,230)	(725)	(675)	(457)	(416)	(451)
Total loss	(392)	(732)	(5,211)	(707)	(330)	(158)	(215)	(304)
Total loss per common share	(0.01)	(0.02)	(0.19)	(0.03)	(0.01)	(0.01)	(0.01)	(0.01)
Cash dividends per common share	N/A							

\* Cumulative totals vary nominally as a result of foreign exchange differences between quarters.

kneat.com expects to record losses until such time as it further develops the Kneat Gx platform and secures additional customer contracts. The Company estimates that the funding received on completion of the Transaction will provide kneat.com with the ability to make an investment in staffing and further development of the Kneat Gx

platform which may result in positive cash flows from operations within the next three to five years. See the *Risk Factors* section of this MD&A and note 1, *Nature of operations and going concern*, of the annual consolidated financial statements for the year-ended December 31, 2016 for further details.

*Other historical information*

Financial year ended December 31, 2016

kneat.com financed its operations in 2016 through the completion of the Transaction, as outlined above, and through revenue from customers of approximately \$0.8 million. Refer to *Recent developments* for further details of operations throughout fiscal year 2016.

Financial year ended December 31, 2015

Kneat Solutions Limited raised approximately \$2.5 million through the issuance of common shares. These funds were used to further develop the Kneat Gx platform, extend sales reach throughout Europe and the United States and service current and newly acquired customers. Costs of approximately \$1.0 million were incurred and capitalized specifically to further develop the Kneat Gx platform. Customers were secured through the execution of license, maintenance and service agreements. Revenue totalling approximately \$1.0 million was recognized during the year.

Financial year ended December 31, 2014

As Kneat Solutions Limited progressed with customers in the United States, a presence in the United States was required. Thus, Kneat Solutions, Inc., a 100% wholly-owned subsidiary of Kneat Solutions Limited, was incorporated in Pennsylvania, United States. Kneat Solutions Limited raised in excess of \$0.8 million through the issuance of common shares. These funds were used to further develop the Kneat Gx platform. Costs of approximately \$1.0 million were incurred and capitalized specifically to further develop the Kneat Gx platform.

The financial year ended December 31, 2014 was the first year in which Kneat was able to execute contracts with customers and recognize revenue. Kneat secured two multi-national biotech and diagnostics customers and recognized their first revenue from operations of approximately \$0.3 million.

**RESULTS OF OPERATIONS**

**Year-ended December 31, 2016**

*Revenues for the year ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
License fees	\$690,892	\$102,197	\$588,695	576.0%
Maintenance fees	\$63,498	\$144,519	(\$81,021)	(56.1%)
Professional services and other	\$65,970	\$739,512	(\$673,542)	(91.1%)
<b>Total revenues</b>	<b>\$820,360</b>	<b>\$986,228</b>	<b>(\$165,868)</b>	<b>(16.8%)</b>

Licenses entitle a customer to use the Kneat Gx platform for a set number of users. License fee revenue for the year ended December 31, 2016 was \$690,892 as compared to \$102,197 for the year ended December 31, 2015. The increase in license fee revenue was primarily the result of a significant customer contract signed in the fourth quarter of 2016.

Maintenance fees are established annually. Maintenance entitles the customer to front line support and software upgrades. Maintenance fee revenues for the year ended December 31, 2016 were \$63,498 as compared to \$144,519 for the year ended December 31, 2015. The decrease of \$81,021 or 56.1% was due the timing of the maintenance contract commencement and ending dates.

Professional services and other revenues vary by customer depending on the customer specific needs. Service fees may include such services as special training, development of tailored functionality, pilots to potential customers, implementation and deployment services. Professional services and other revenue for the year ended December 31, 2016 was \$65,970 as compared to \$739,512 for the year ended December 31, 2015. The decrease in professional services and other revenue was primarily due to the Company's focus on service milestones that were not yet met as of quarter end and fewer ongoing service assignments in the year ended December 31, 2016.

*Amortization of the intangible asset for the year ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Amortization of the intangible asset	(\$702,765)	(\$526,087)	176,678	33.6%

The intangible asset, which represents the costs associated with the development of the Kneat Gx platform, is amortized over a five-year period on a straight-line basis. The expense for the year ended December 31, 2016 was \$702,765 compared to \$526,087 for the year ended December 31, 2015. The increase of \$176,678 or 33.6% was primarily due to additions to the intangible asset, consisting mainly of the salaries and benefits of the development team, made throughout the year ended December 31, 2016 which increased the carrying value of the intangible asset and thus the amortization charged to the statement of loss. This was offset by a change in estimate whereby the half-year rule was implemented for additions (see note 3 (j) of the December 31, 2016 consolidated financial statements).

*Administrative expenses for the year ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Administrative expenses	(\$2,736,489)	(\$1,441,915)	\$1,294,574	89.8%

Administrative expenses for the year ended December 31, 2016 totalled \$2,736,489 which was an increase of \$1,294,574 or 89.8% over the administrative expenses of \$1,441,915 for the year ended December 31, 2015. This increase can be attributed mainly to the following items:

- Professional fees incurred for the year ended December 31, 2016 were \$501,549 as compared to the year ended December 31, 2015 of \$290,182. The increase in professional fees of \$211,367 was due primarily to legal fees associated with the completion of the Transaction.
- The directors and key management salaries increased by \$276,786 due to increases in the annual salaries of the Chief Executive Officer, Director of Research and Development and Director of Quality. In addition, the Chief Financial Officer was added to the key management team on June 27, 2016 and Directors' fees began to accrue as of the quarter ended September 30, 2016.
- Other administrative costs increased by \$94,533 due primarily to an increase in recruitment costs.
- Cloud hosting and other services costs totalling \$204,849 for the year ended December 31, 2016 had increased by \$71,640 from the year ended December 31, 2015 related primarily to the acquisition of increased cloud back up and monitoring services and other software services.
- Audit and accounting fees increased by \$62,002 for the year ended December 31, 2016 as compared to the year ended December 31, 2015 due primarily to an increase in costs associated with the completion of the Transaction and increased audit requirements for a public company.
- Securities and regulatory fees of \$46,668 relate to costs associated with operating a public company.
- The net recovery in the statement of loss from the research and development tax credit has decreased by a net amount of \$72,798 (2015 amounts are shown gross within the employee salaries and benefit line items and the research and development tax credit line items in the statement of loss). The recovery in the statement of loss for the year ended December 31, 2016 relates to the eligible costs associated with the research and development tax credits that were not eligible for capitalization to the intangible asset and thus are expensed through the statement of loss.
- Share-based compensation increased by \$224,244 primarily due to the incremental fair value associated with the modification to stock options held by Kneat Solutions Limited options holders and the issuance of new options during the year ended December 31, 2016.
- The increases in the expenses were partially offset by a decrease in employee salaries, wages and benefits expense of \$154,604 bringing the expense down to \$442,265 for the year ended December 31, 2016. This was due primarily to the increase in employee costs which were capitalized to the intangible asset as a result of the time employees spent on development activities and the fact that the 2015 amounts were shown gross of research and development tax credits as noted above.

*Other expenses for the year ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Finance costs, net	(\$175,739)	(\$27,302)	\$148,437	543.7%
Listing expense	(\$3,795,887)	-	(\$3,795,887)	100.0%
Disbursement connected to the Transaction	(\$425,285)	-	(\$425,285)	100.0%

Net finance costs increased primarily due to unrealized foreign currency losses of \$127,536 which arose in the current year due to the impact of changes in exchange rates on financial assets and financial liabilities denominated in currencies other than the functional currency of the entity in which they are held.

Under IFRS 2, the Transaction is measured at the fair value of the shares deemed to have been issued by Kneat Solutions Limited such that the kneat.com shareholders held 31.3% of the combined entity. The fair value of the deemed shares of Kneat Solutions Limited issued to kneat.com shareholders is based on the fair value of Kneat Solutions Limited on the effective date of the Transaction and is estimated to be \$11,518,443 and has been allocated as follows:

	\$
Net assets of kneat.com on the Transaction date (consisting of approximately \$8.2 million in cash and \$0.2 million in accounts payable)	8,040,457
Fair value of 31.3% of the equity of the combined entity based on the estimated fair value	(11,518,443)
Fair value of warrants	(67,424)
Fair value of options	(250,477)
Listing expense	<u>(3,795,887)</u>

The listing expense is expensed through the statement of loss. The consideration and allocation reflects the best estimates and assumptions of the management of the Company after taking in to account all available information. As at December 31, 2016, it was determined that the cost that will be incurred in relation to certain former Kneat Solutions Limited shareholders who took part in the employment and investment incentive scheme (“EIIS”) proposal (“EIIS proposal”), as outlined in the Management Information Circular of Fortune Bay Corp. dated May 13, 2016, is \$425,285. This amount is expected to be settled during 2017.

**Three-month period ended December 31, 2016**

*Revenues for the three-month periods ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
License fees	\$695,720	\$105,354	\$590,366	560.4%
Maintenance fees	\$11,323	\$95,891	(\$84,568)	(88.2%)
Professional service and other	-	\$144,507	(\$144,507)	(100.0%)
<b>Total revenues</b>	<b>\$707,043</b>	<b>\$345,752</b>	<b>(\$361,291)</b>	<b>104.5%</b>

Licenses entitle a customer to use the Kneat Gx platform for a specific number of users. License fee revenue for the period ended December 31, 2016 was \$695,720 as compared to \$105,354 for the period ended December 31, 2015. The increase in license fee revenue was primarily as a result of a customer contract signed in the fourth quarter of 2016.

Maintenance fees are established annually. Maintenance entitles the customer to front line support and software upgrades. Maintenance fee revenues for the three-month period ended December 31, 2016 were \$11,323 as compared to \$95,891 for the three-month period ended December 31, 2015. The decrease of \$84,568 or 88.2% was due the timing of the maintenance contract commencement and ending dates.

Professional services and other revenues vary by customer depending on the customer specific needs. Service fees may include such services as special training, development of tailored functionality, pilots for potential customers, implementation and deployment services. Professional services and other revenue for the three-month period ended December 31, 2016 was \$nil as compared to \$144,507 for the three-month period ended December 31, 2015. The service fee revenue decrease was primarily as a result of the Company’s focus on service milestones that were not yet met as of quarter end and fewer ongoing service agreements during the three-month period ended December 31, 2016.

*Amortization of the intangible asset for the three-month periods ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Amortization of the intangible asset	(\$219,632)	(\$178,910)	\$40,722	22.8%

The intangible asset, which represents the costs associated with the development of the Kneat Gx platform, is amortized straight-line over a five-year period. The expense for the three-month period ended December 31, 2016 was \$219,632 compared to \$178,910 for the three-month period ended December 31, 2015. The increase of \$40,722 or 22.8% was primarily due to additions to the intangible asset, consisting mainly of the salaries and benefits of the development team, made throughout the year ended December 31, 2016 which increased the carrying value of the intangible asset and thus the amortization charged to the statement of loss. This was offset by a change in estimate whereby the half-year rule was implemented for additions (see note 3 (j) of the December 31, 2016 consolidated financial statements).

*Administrative expenses for the three-month periods ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Administrative expenses	(\$677,467)	(\$488,830)	\$188,637	38.6%

Administrative expenses for the three-month period ended December 31, 2016 totalled \$677,467 which was an increase of \$188,637 or 38.6% over the administrative expenses of \$488,830 for the three-month period ended December 31, 2015. This increase can be attributed mainly to the following items:

- Professional fees for the three-month period ended December 31, 2016 decreased by \$92,670. The decrease in professional fees was due primarily to legal fees accrued in the quarter ended December 31, 2015 relating to the Transaction.
- The directors and key management salaries increased by \$155,865 due to increases in annual salaries of the Chief Executive Officer, Director of Research and Development and Director of Quality. In addition, the Chief Financial Officer was added to the key management team and Directors' fees began to be accrued as of the quarter ended September 30, 2016.
- Cloud hosting and other services costs totalling \$60,355 for the three-month period ended December 31, 2016 had increased by \$47,583 from the three-month period ended December 31, 2015 related primarily to the acquisition of increased cloud back up and monitoring services and other services.
- The net recovery in the statement of loss from the research and development tax credit has decreased by a net amount of \$21,291 (2015 amounts are included within the employee salaries and benefit line items and the research and development tax credit line items in the statement of loss). The expense in the statement of loss for the three-month period ended December 31, 2016 relates to the eligible costs associated with the research and development tax credits that were not eligible for capitalization to the intangible asset. During the fourth quarter of 2016, this amount has been adjusted based on the final research and development tax credit calculations for the year 2016 which are expected to be filed with the relevant tax authorities.
- Share-based compensation increased by \$56,191 primarily due to the issuance of new stock options during the fourth quarter of 2016.
- Regulatory fees of \$18,953 relate to costs associated with operating a public company.
- An increase in consultancy fees of \$55,678 for the three-month period ended December 31, 2016 was due mainly to the fact that a consultant was engaged in 2016 to service customers in the United States.
- The increases in the expenses were partially offset by a decrease in employee salaries, wages and benefits expense of \$179,612 for the three-month period ended December 31, 2016. This was due primarily to the increase in employee costs which were capitalized to intangible assets as a result of the time employees spent on development activities and the fact that the 2015 amounts were shown gross of research and development tax credits as noted above.

*Other expenses for the three-month periods ended December 31,*

	<b>2016</b>	<b>2015</b>	<b>\$ change in 2016</b>	<b>% change in 2016</b>
Finance costs, net	(\$184,662)	(\$8,074)	\$176,588	2187.3%
Listing expense	(\$16,077)	-	\$16,077	100.0%
Disbursement connected to the Transaction	(\$1,693)	-	\$1,693	100.0%

Finance costs increased primarily due to unrealized foreign currency losses of \$184,513 which arose in the current quarter due to the impact of changes in exchange rates on financial assets and financial liabilities denominated in currencies other than the functional currency of the entity in which they are held.

Under IFRS 2, the Transaction is measured at the fair value of the shares deemed to have been issued by Kneat Solutions Limited such that the kneat.com shareholders held 31.3% of the combined entity. Refer to the calculation outlined above. The amount recorded during the quarter ended December 31, 2016 was due to final adjustments to the fair value of the assets of kneat.com.

As at December 31, 2016, it was determined that the cost that will be incurred in relation to certain former Kneat Solutions Limited shareholders who took part in the employment and EIIIS proposal, as outlined in the Management Information Circular of Fortune Bay Corp. dated May 13, 2016, is \$425,285, which is \$1,693 above the estimate made in the quarter ended September 30, 2016. This amount is expected to be settled during 2017.

## **LIQUIDITY AND CAPITAL RESOURCES**

kneat.com's liquidity depends on existing cash reserves, supplemented as necessary by asset dispositions, equity and/or debt financings and revenue generated from customers. As of December 31, 2016, kneat.com had cash of \$4,988,601 compared to \$1,063,524 as at December 31, 2015. kneat.com's long term debt relates to the loan payable held by Enterprise Ireland which is due on June 27, 2019. The working capital balance at December 31, 2016 was \$5,113,947 as compared to \$848,645 at December 31, 2015 due primarily to the cash received on completion of the Transaction.

During the year ended December 31, 2016, kneat.com used cash of \$2,429,123 to fund operating activities. In addition, kneat.com raised funds through financing activities of \$8,254,809 during the year ended December 31, 2016 through the completion of the Transaction. Investing activities focused mainly on development of the intangible asset resulting in net cash outflow from investing activities of \$1,815,218 for the year ended December 31, 2016.

kneat.com's business to date has been the development of the Kneat Gx platform which has generated limited revenues. kneat.com has historically relied primarily on funding through the issuance of common shares and debt.

Liquidity risk is the risk that the Company will not meet its financial obligations as they become due. The Company has a planning and budgeting process to monitor operating cash requirements, including amounts projected for capital expenditures, which are adjusted as input variables change. These variables include, but are not limited to, the ability of the Company to generate revenue from current and prospective customers, general and administrative requirements of the Company and the availability of capital markets. As these variables change, liquidity risks may necessitate the need for the Company to issue equity or obtain debt financing.

The Company is currently negotiating contracts with several customers and is pursuing financing alternatives. There can be no assurance that additional customer revenues will be generated or additional future financings will be available on acceptable terms or at all. If the Company is unable to obtain additional financing when required, the Company may have to substantially reduce or eliminate planned expenditures. Refer to note 1, *Nature of operations and going concern* in the audited consolidated financial statements for the year ended December 31, 2016.

## COMMITMENTS AND CONTINGENCIES

In the normal course of business, kneat.com enters into contracts that give rise to commitments for future minimum payments. The following table summarizes the remaining contractual maturities of the financial liabilities. The amounts included in this table may not result in an actual obligation of kneat.com as the requirement to settle certain of these amounts is contingent on the occurrence of certain events that may or may not transpire:

	Payments due by period as of December 31, 2016				Total
	Within 1 year	2-3 years	4-5 years	Over 5 years	
Accounts payable and accrued liabilities	\$ 1,117,577	\$ -	\$ -	\$ -	\$ 1,117,577
Operating leases and other	115,264	120,375	-	-	235,639
Loan payable	-	922,608	-	-	922,608
	<u>1,232,841</u>	<u>1,042,983</u>	<u>-</u>	<u>-</u>	<u>2,275,824</u>

## OFF-BALANCE SHEET ARRANGEMENTS

kneat.com has no off-balance sheet arrangements such as guarantee contracts, contingent interest in assets transferred to an entity, derivative instruments obligations or any obligations that trigger financing, liquidity, market, or credit risk to kneat.com.

## OUTSTANDING SHARE INFORMATION

The Company has authorized an unlimited number of common shares without par value. As of December 31, 2016 and April 24, 2017, the Company had 39,563,684 common shares outstanding. Of the common shares issued and outstanding, 17,048,720 are subject to an escrow agreement as at December 31, 2016 and April 24, 2017.

As of April 24, 2017, the Company has 2,323,485 (December 31, 2016 – 1,985,859) stock options outstanding at an average exercise price of \$0.80 per common share with varying expiry dates. In addition, as of December 31, 2016, 267,857 common share purchase warrants are outstanding, exercisable into common shares of the Company at an exercise price of \$0.90 per common share. These warrants expired on April 1, 2017.

## RELATED PARTY TRANSACTIONS

Amounts receivable from officers and directors were \$8,513 as at December 31, 2016 (Amounts payable for the year-ended December 31, 2015 – \$259,146). During the year ended December 31, 2016, the Company repaid directors' current account balances of \$250,855 (year-ended December 31, 2015 - \$75,866).

During the year ended December 31, 2015, a director of Kneat Solutions Limited was granted 2,727 shares of Kneat Solutions Limited valued at \$56,151 as compensation for consulting fees.

Key management of the Company previously included the Board of Directors, the Chief Executive Officer, Director of Research and Development and the Director of Quality. Effective June 27, 2016, key management also includes the Chief Financial Officer.

During the year-ended December 31, 2016, the Company incurred costs for management services from a related party, Numus Financial Inc. ("Numus"), a company controlled by a director of kneat.com in the amount of \$18,000 (December 31, 2015 - \$nil) and incurred rent and office costs from Numus in the amount of \$14,848 (December 31, 2015 - \$nil).

During the year-ended December 31, 2016, the Company paid professional fees on behalf of a related party, Beek Investments Limited. ("Beek"), a company controlled by directors and officers of kneat.com, in the amount of \$16,104 (December 31, 2015 - \$nil). As at December 31, 2016, the amount due from Beek was \$16,104.

## FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

### Market Risk

#### *Currency risk*

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Currency risk exposure arises from kneat.com entering into transactions which are denominated in currencies other than its functional currency.

The Company is exposed to currency risk on its cash balances, loan payable, intercompany balances, and accounts payable and accrued liabilities that are held in currencies that are not in the transacting entity's functional currency. For the year ended December 31, 2016, a 5% decrease in the exchange rate between the functional currency and foreign currencies would decrease the net loss by approximately \$318,000; a 5% increase would increase the net loss by approximately \$318,000. The Company currently does not hedge its currency risk.

#### *Interest rate risk*

Interest rate risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market interest rates. An immaterial amount of interest rate exposure exists in respect of cash balances and the loan payable on the consolidated statement of financial position. The Company holds a loan payable with a fixed interest rate. The loan is privately issued, with no secondary market. It is measured at amortized cost and bears a fixed interest rate and as a result kneat.com is not exposed to cash flow interest rate risk on the loan payable.

#### *Credit risk*

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with kneat.com. The carrying amounts of financial assets best represent the maximum credit risk exposure at the reporting date. At December 31, 2016 and December 31, 2015, kneat.com's financial assets exposed to credit risk amounted to the following:

	December 31, 2016	December 31, 2015
	\$	\$
Cash and cash equivalents	4,988,601	1,063,524
Accounts receivable and other	1,771,030	1,023,014

During the years ended December 31, 2016 and December 31, 2015, the Company did not hold any financial assets that were past due or impaired. Trade debtors of \$726,745 are included in accounts receivable as at December 31, 2016 (2015 - \$230,280). Trade debtors are monitored on a regular basis in order to minimize material aging and to ensure adequate collection.

Cash is held with reputable banks in Ireland and Canada. The long-term credit rating, as determined by Standard and Poor's was BBB and AA-, respectively. This reduces concentration risk.

### RISK FACTORS

#### *kneat.com has a limited operating history and its future profitability is uncertain*

kneat.com has a limited operating history and its business is subject to all of the risks inherent in the establishment of a new business enterprise. Our likelihood of success must be considered in light of the problems, expenses, difficulties, complications and delays frequently encountered in connection with establishing a new software development company. If kneat.com continues to incur operating losses and fails to become a profitable company, it may be unable to continue its operations. kneat.com expects to continue to operate at a net loss for the next several years, as it continues its software development efforts and continues to further develop its sales, marketing and distribution capabilities.

#### *kneat.com needs to raise additional capital to operate its business*

kneat.com is an early commercial-stage company focused on product development and commercialization and has generated only limited product revenues to date. For the foreseeable future, kneat.com will have to fund all of its operations and capital expenditures primarily from the net proceeds of future offerings and grants of securities.

kneat.com's actual capital requirements will depend on many factors. If kneat.com experiences unanticipated cash requirements, it may need to seek additional sources of financing, which may not be available on favorable terms, if at all. If kneat.com does not succeed in raising additional funds on acceptable terms, it may be forced to discontinue product development and/or commercialization, reduce or forego sales and marketing efforts and attractive business opportunities or discontinue operations.

*kneat.com has a history of losses and we may never achieve or sustain profitability*

kneat.com has incurred substantial losses since its inception, and it may not achieve profitability in the foreseeable future, if at all. kneat.com expects to incur net losses and negative cash flows for the foreseeable future due in part to increasing research and development expenses, marketing expenses and hiring additional personnel. As a result, kneat.com will need to generate significant revenues in order to achieve and maintain profitability. kneat.com may not be able to generate these revenues or achieve profitability in the future. Even if kneat.com does achieve profitability, it may not be able to sustain or increase profitability.

*kneat.com has limited access to the capital markets, and, even if it can raise additional funding, it may be required to do so on terms that are dilutive to shareholders*

kneat.com has limited access to the capital markets to raise capital. The capital markets have been unpredictable in the recent past for other software development companies and unprofitable companies such as kneat.com. In addition, it is generally difficult for early commercial-stage companies to raise capital. The amount of capital that a company such as kneat.com is able to raise often depends on variables that are beyond its control. As a result, kneat.com may not be able to secure financing on terms attractive to it, or at all. If kneat.com is able to consummate a financing arrangement, the amount raised may not be sufficient to meet its future needs. If adequate funds are not available on acceptable terms, or at all, kneat.com's business, results of operations, financial condition and its continued viability will be materially adversely affected.

*The length of kneat.com's sales cycle can fluctuate significantly which could result in significant fluctuations in license revenues being recognized from quarter to quarter*

The decision by a customer to license kneat.com's software products or purchase its services often involves a comprehensive implementation process across the customer's network or networks. As a result, the licensing and implementation of kneat.com's software products and any related services may entail a significant commitment of resources by prospective customers, accompanied by the attendant risks and delays frequently associated with significant technology implementation projects. Given the significant investment and commitment of resources required by an organization to implement kneat.com's software products, its sales cycle may be longer compared to other companies within kneat.com's own industry, as well as companies in other industries. Also because of changes in customer spending habits, it may be difficult for kneat.com to budget, forecast and allocate its resources properly. In weak economic environments, it is not uncommon to see reduced information technology spending. It may take several months, or even several quarters, for marketing opportunities to materialize. If a customer's decision to license kneat.com's software is delayed or if the implementation of these software products takes longer than originally anticipated, the date on which kneat.com may recognize revenues from these licenses would be delayed. Such delays and fluctuations could cause kneat.com's revenues to be lower than expected in a particular period and kneat.com may not be able to adjust its costs quickly enough to offset such lower revenues, potentially negatively impacting its business, operating results and financial condition.

*If kneat.com does not continue to develop technologically advanced products, future revenues and its operating results may be negatively affected*

kneat.com's success depends upon its ability to design, develop, test, market, license and support new software products, services and enhancements of current products and services on a timely basis in response to both competitive threats and marketplace demands. Examples of significant trends in the software industry include cloud computing, mobility, social media and other SaaS. In addition, kneat.com's software products, services and enhancements must remain compatible with standard platforms and file formats. Moreover, if new industry standards emerge that kneat.com does not anticipate or adapt to, or with rapid technological change occurring, if alternatives to its services and solutions are developed by its competitors, kneat.com's software products and services could be rendered obsolete, causing kneat.com to lose market share and, as a result, harm its business and operating results and its ability to compete in the marketplace.

*If kneat.com's software products and services do not gain market acceptance, its operating results may be negatively affected*

kneat.com intends to pursue the goal for Kneat Gx to be the global standard for regulated data and documentation management across all industries, where good data management, good documentation practices and regulatory compliance are keys to success. kneat.com intends to pursue its strategy through, among other things, its proprietary research and the development of new software product and service offerings, as well as through acquisitions. In response to customer demand, it is important to kneat.com's success that it continues to enhance its software products and services and to seek to set the standard for Kneat Gx capabilities. The primary market for its software products and services is rapidly evolving, which means that the level of acceptance of products and services that have been released recently or that are planned for future release by the marketplace is not certain. If the markets for kneat.com's software products and services fail to develop, develop more slowly than expected or become subject to increased competition, its business may suffer. As a result, kneat.com may be unable to: (i) successfully market its current products and services; (ii) develop new software products and services and enhancements to current software products and services; (iii) complete customer implementations on a timely basis; or (iv) complete software products and services currently under development. In addition, increased competition could put significant pricing pressures on kneat.com's products which could negatively impact its margins and profitability. If kneat.com's software products and services are not accepted by its customers or by other businesses in the marketplace, kneat.com's business, operating results and financial condition will be materially affected.

*kneat.com's investment in its current research and development efforts may not provide a sufficient, timely return*

The development of Kneat Gx is a costly, complex and time-consuming process and the investment in kneat.com's software product development often involves a long wait until a return is achieved on such an investment. kneat.com is making, and will continue to make, significant investments in software research and development and related product opportunities. Investments in new technology and processes are inherently speculative. Commercial success depends on many factors, including the degree of innovation of the software products and services developed through kneat.com's research and development efforts, sufficient support from its strategic partners and effective distribution and marketing. Accelerated software product introductions and short product life cycles require high levels of expenditures for research and development. These expenditures may adversely affect kneat.com's operating results if they are not offset by revenue increases. kneat.com believes that it must continue to dedicate a significant amount of resources to its research and development efforts in order to maintain its competitive position. However, significant revenues from new software product and service investments may not be achieved for a number of years, if at all. Moreover, new software products and services may not be profitable, and even if they are profitable, operating margins for new software products and services may not be as high as projected.

*Failure to protect kneat.com's intellectual property could harm its ability to compete effectively*

kneat.com is highly dependent on our ability to protect our proprietary technology. We rely on a combination of trade secret laws, as well as non-disclosure agreements and other contractual provisions to establish and maintain its proprietary rights. kneat.com currently does not own any patents or have any patents pending. kneat.com intends to protect its intellectual property rights vigorously; however, there can be no assurance that these measures will, in all cases, be successful. Software piracy has been, and is expected to be, a persistent problem for the software industry and piracy of its software products represents a loss of revenue to kneat.com. Where applicable, certain of kneat.com's license arrangements have required it to make a limited confidential disclosure of portions of the source code for its software products or to place such source code into escrow for the protection of another party. Despite the precautions kneat.com has taken, unauthorized third parties, including its competitors, may be able to copy certain portions of kneat.com's software products or reverse engineer or obtain and use information that kneat.com regards as proprietary. Also, kneat.com's competitors could independently develop technologies that are perceived to be substantially equivalent or superior to its technologies. kneat.com's competitive position may be adversely affected by its possible inability to effectively protect kneat.com's intellectual property. In addition, certain of its products contain open source software. Licensees of open source software may be required to make public certain source code or to make certain derivative works available to others. While kneat.com monitors and controls the use of open source software in its products and in any third party software that is incorporated into its products, and kneat.com tries to ensure that no open source software is used in such a way as to require it to disclose the source code to the related product or service, there can be no guarantee that such use could not inadvertently occur. If this

happened it could harm kneat.com intellectual property position and have a material adverse effect on its business, results of operations and financial condition.

*Other companies may claim that kneat.com infringes their intellectual property, which could materially increase costs and materially harm its ability to generate future revenues and profits*

Claims of infringement are becoming increasingly common as the software industry develops and as related legal protections, including patents, are applied to software products. Although kneat.com does not believe that its products infringe on the rights of third parties, third parties have and will continue to assert infringement claims against it in the future. Although most of kneat.com's technology is proprietary in nature, kneat.com does include certain third party and open source software in its software products. In the case of third party software, kneat.com believes this software is licensed from the entity holding the intellectual property rights. Although kneat.com believes that it has secured proper licenses for all third-party intellectual property that is integrated into its products, third parties may continue to assert infringement claims against kneat.com in the future, including the sometimes aggressive and opportunistic actions of non-practicing entities whose business model is to obtain patent-licensing revenues from operating companies such as us. Any such assertion, regardless of merit, may result in litigation or may require kneat.com to obtain a license for the intellectual property rights of third parties. Such licenses may not be available or they may not be available on commercially reasonable terms. In addition, as kneat.com continues to develop software products and expand its portfolio using new technology and innovation, kneat.com's exposure to threats of infringement may increase. Any infringement claims and related litigation could be time-consuming, disruptive to kneat.com's ability to generate revenues or enter into new market opportunities and may result in significantly increased costs as a result of kneat.com's defense against those claims or its attempt to license the intellectual property rights or rework kneat.com's products to avoid infringement of third party rights. Typically kneat.com's agreements with our partners and customers contain provisions which require kneat.com to indemnify them for damages sustained by them as a result of any infringement claims involving kneat.com's products. Any of the foregoing infringement claims and related litigation could have a significant adverse impact on kneat.com's business and operating results as well as its ability to generate future revenues and profits.

*Impact of laws*

kneat.com operates offices in Canada and Ireland, and continues to offer its products and services in the European Union, Canada, the United States and eventually in other countries. kneat.com is and will be subject to a variety of laws in the European Union, Canada, the United States and abroad, including laws regarding consumer protection, privacy, intellectual property, taxation and content suitability, distribution and antitrust, that are continuously evolving and developing. The scope, enforcement and interpretation of the laws that are or may be applicable to kneat.com and its subsidiaries are often uncertain and may be conflicting, particularly laws outside of Canada and the United States. It is also likely that as business grows and evolves to a greater number of countries, kneat.com will become subject to laws and regulations in additional jurisdictions. Compliance with applicable laws or regulations could be very difficult or liability could arise under these laws or regulations, including due to amendments to or evolving interpretation and enforcement of such laws and regulations. As a result, kneat.com could be directly harmed, and may be forced to implement new measures to reduce the exposure to this liability. This may require substantial resources to be expended or a modification of its products and services, which would harm the business, financial condition and results of operations of kneat.com.

*Foreign currency and exchange rate risk*

kneat.com currently reports its results in the Canadian dollar. Fluctuations in the cross exchange rates between the European Euro, United States dollar and Canadian dollar may have a material adverse effect on the business, financial condition and operating results of the Company. To date, kneat.com has not engaged in exchange rate hedging activities and may not do so in the foreseeable future.

*Current and future competitors could have a significant impact on kneat.com's ability to generate future revenues and profits*

The markets for kneat.com's software products and services are intensely competitive and are subject to rapid technological change and other pressures created by changes in its industry. The convergence of many technologies has resulted in unforeseen competitors arising from companies that were traditionally not viewed as threats to kneat.com's marketplace. kneat.com expects competition to increase and intensify in the future as the pace of

technological change and adaptation quickens and as additional companies enter its markets, including those competitors who offer similar solutions as kneat.com does, but offer it through a different form of delivery. We could lose market share if our current or prospective competitors: (i) introduce new competitive products or services, (ii) add new functionality to existing products and services, (iii) acquire competitive products and services, (iv) reduce prices, or (v) form strategic alliances with other companies. If other businesses were to engage in aggressive pricing policies with respect to competing products, or if the dynamics in kneat.com's marketplace resulted in increasing bargaining power by the consumers of kneat.com's software products and services, kneat.com would need to lower the prices it charges for the products and services kneat.com offers. This could result in lower revenues or reduced margins, either of which may materially and adversely affect kneat.com's business and operating results. Additionally, if prospective consumers choose other methods of data and document management within regulated environments, different from that which we offer, kneat.com business and operating results could also be materially and adversely affected.

*kneat.com must continue to manage its internal resources during periods of company growth or its operating results could be adversely affected*

kneat.com's growth, coupled with the rapid evolution of its markets, may place, significant strains on kneat.com's administrative and operational resources and increased demands on its internal systems, procedures and controls. kneat.com's administrative infrastructure, systems, procedures and controls may not adequately support its operations. In addition, kneat.com's management may not be able to achieve the rapid, effective execution of the product and business initiatives necessary to successfully implement kneat.com's operational and competitive strategy. If kneat.com is unable to manage growth effectively, its operating results will likely suffer which may, in turn, adversely affect its business.

*If kneat.com loses the services of our executive officers or other key employees or if it is not able to attract or retain top employees, kneat.com's business could be significantly harmed*

kneat.com's performance is substantially dependent on the performance of its executive officers and key employees. kneat.com does not maintain "key person" life insurance policies on any of its employees. kneat.com's success is also highly dependent on its continuing ability to identify, hire, train, retain and motivate highly qualified management, technical, sales and marketing personnel. In particular, the recruitment of top research developers and experienced salespeople remains critical to its success. Competition for such people is intense, substantial and continuous, and kneat.com may not be able to attract, integrate or retain highly qualified technical, sales or managerial personnel in the future. In addition, in its effort to attract and retain critical personnel, kneat.com may experience increased compensation costs that are not offset by either improved productivity or higher prices for its software products or services.

*Unexpected events may materially harm kneat.com's ability to align incurred expenses with recognized revenues*

kneat.com incurs operating expenses based upon anticipated revenue trends. Since a high percentage of these expenses are relatively fixed, a delay in recognizing revenues from transactions related to these expenses (such a delay may be due to the factors described elsewhere in this risk factor section or it may be due to other factors) could cause significant variations in operating results from quarter to quarter, and such a delay could materially reduce operating income. If these expenses are not subsequently matched by revenues, kneat.com's business, financial condition, or results of operations could be materially and adversely affected.

*kneat.com may fail to achieve its financial forecasts due to inaccurate sales forecasts or other factors*

kneat.com's revenues and particularly its software license revenues are difficult to forecast, and, as a result its quarterly operating results can fluctuate substantially. kneat.com uses a "pipeline" system, a common industry practice, to forecast sales and trends in its business. By reviewing the status of outstanding sales proposals to its customers and potential customers, kneat.com makes an estimate as to when a customer will make a purchasing decision involving its software products. These estimates are aggregated periodically to make an estimate of kneat.com's sales pipeline, which kneat.com uses as a guide to plan its activities and make financial forecasts. kneat.com's sales pipeline is only an estimate and may be an unreliable predictor of actual sales activity, both in a particular quarter and over a longer period of time. Many factors may affect actual sales activity, such as weakened economic conditions, which may cause kneat.com's customers and potential customers to delay, reduce or cancel IT related purchasing decisions and the tendency of some of kneat.com's customers to wait until the end of a fiscal

period in the hope of obtaining more favourable terms from kneat.com. If actual sales activity differs from kneat.com's pipeline estimate, then kneat.com may have planned its activities and budgeted incorrectly and this may adversely affect its business, operating results and financial condition.

*kneat.com's software products and services may contain defects that could harm its reputation, be costly to correct, delay revenues, and expose kneat.com to litigation*

kneat.com's software products and services are highly complex and sophisticated and, from time to time, may contain design defects, software errors, hardware failures or other computer system failures that are difficult to detect and correct. Errors may be found in new software products or services or improvements to existing products or services after delivery to kneat.com's customers. If these defects are discovered, kneat.com may not be able to successfully correct such errors in a timely manner. In addition, despite the extensive tests kneat.com conducts on all its software products or services, kneat.com may not be able to fully simulate the environment in which its products or services will operate and, as a result, kneat.com may be unable to adequately detect the design defects or software or hardware errors which may become apparent only after the products are installed in an end-user's network, and users have transitioned to kneat.com's services. The occurrence of errors and failures in kneat.com's software products or services could result in the delay or the denial of market acceptance of its products and alleviating such errors and failures may require kneat.com to make significant expenditure of its resources. Customers often use kneat.com services and solutions for critical business processes and as a result, any defect or disruption in kneat.com's solutions, any data breaches or misappropriation of proprietary information, or any error in execution, including human error or intentional third-party activity such as denial of service attacks or hacking, may cause customers to reconsider renewing their contract with kneat.com. The errors in or failure of kneat.com's software products and services could also result in kneat.com losing customer transaction documents and other customer files, causing significant customer dissatisfaction and possibly giving rise to claims for monetary damages. The harm to kneat.com's reputation resulting from product and service errors and failures may be materially damaging. Since kneat.com regularly provides a warranty with its software products, the financial impact of fulfilling warranty obligations may be significant in the future. kneat.com's agreements with its strategic partners and end-users typically contain provisions designed to limit its exposure to claims. These agreements regularly contain terms such as the exclusion of all implied warranties and the limitation of the availability of consequential or incidental damages. However, such provisions may not effectively protect kneat.com against claims and the attendant liabilities and costs associated with such claims. Any claims for actual or alleged losses to kneat.com's customers' businesses may require kneat.com to spend significant time and money in litigation or arbitration or to pay significant settlements or damages. Defending a lawsuit, regardless of merit, can be costly and would divert management's attention and resources. Although kneat.com maintain errors and omissions insurance coverage and comprehensive liability insurance coverage, such coverage may not be adequate to cover all such claims. Accordingly, any such claim could negatively affect its business, operating results or financial condition.

*Unauthorized disclosures and breaches of security data may adversely affect kneat.com's operations*

kneat.com have strict measures to protect its information systems against unauthorized access and disclosure of personal information and of kneat.com's confidential information and confidential information belonging to its customers. kneat.com has policies and procedures in place dealing with data security and records retention. However, there is no assurance that the security measures kneat.com has put in place will be effective in every case. Breaches in security could result in a negative impact for kneat.com and for its customers, affecting kneat.com's and its customers' businesses, assets, revenues, brands and reputations and resulting in penalties, fines, litigation and other potential liabilities, in each case depending on the nature of the information disclosed. Security breaches could also affect kneat.com's relations with its customers, injure kneat.com's reputation and harm its ability to keep existing customers and to attract new customers. These risks to kneat.com's business may increase as it expands the number of web-based and cloud-based products and services kneat.com offers.

*kneat.com may become involved in litigation that may materially adversely affect it*

From time to time in the ordinary course of kneat.com's business, it may become involved in various legal proceedings, including commercial, product liability, employment, class action and other litigation and claims, as well as governmental and other regulatory investigations and proceedings. Such matters can be time-consuming, divert management's attention and resources and cause kneat.com to incur significant expenses. Furthermore,

because litigation is inherently unpredictable, the results of any such actions may have a material adverse effect on kneat.com's business, operating results or financial condition.

*kneat.com's operating results could be adversely affected by any weakening of economic conditions*

kneat.com's overall performance depends in part on worldwide economic conditions. Certain economies have experienced periods of downturn as a result of a multitude of factors, including, but not limited to, turmoil in the credit and financial markets, concerns regarding the stability and viability of major financial institutions, declines in gross domestic product, increases in unemployment and volatility in commodity prices and worldwide stock markets, and excessive government debt. The severity and length of time that a downturn in economic and financial market conditions may persist, as well as the timing, strength and sustainability of any recovery, are unknown and are beyond kneat.com's control. Moreover, any instability in the global economy affects countries in different ways, at different times and with varying severity, which makes the impact to kneat.com's business complex and unpredictable. During such downturns, many customers may delay or reduce technology purchases. Contract negotiations may become more protracted or conditions could result in reductions in the licensing of kneat.com's software products and the sale of cloud and other services, longer sales cycles, pressure on kneat.com's margins, difficulties in collection of accounts receivable or delayed payments, increased default risks associated with kneat.com's accounts receivables, slower adoption of new technologies and increased price competition. In addition, deterioration of the global credit markets could adversely impact kneat.com's ability to complete licensing transactions and services transactions, including maintenance and support renewals. Any of these events, as well as a general weakening of, or declining corporate confidence in, the global economy, or a curtailment in government or corporate spending could delay or decrease kneat.com's revenues, and therefore have a material adverse effect on its business, operating results and financial condition.

*Stress in the global financial system may adversely affect kneat.com's finances and operations in ways that may be hard to predict or to defend against*

Financial developments seemingly unrelated to kneat.com or to its industry may adversely affect kneat.com over the course of time. For example, material increases in any applicable interest rate benchmarks may increase the debt payment costs for kneat.com's credit facilities. Credit contraction in financial markets may hurt its ability to access credit in the event that kneat.com identifies an acquisition opportunity or require significant access to credit for other reasons. A reduction in credit, combined with reduced economic activity, may adversely affect businesses and industries that collectively constitute a significant portion of kneat.com's customer base. As a result, these customers may need to reduce their licensing of kneat.com's software products or their purchases of kneat.com's services, or kneat.com may experience greater difficulty in receiving payment for the licenses and services that these customers purchase from it. Any of these events, or any other events caused by turmoil in world financial markets, may have a material adverse effect on kneat.com's business, operating results, and financial condition.

## **DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING**

### **Disclosure Controls and Procedures**

Disclosure controls and procedures (as such term is defined in Multilateral Instrument 52-109 – *Certification of Disclosure in Issuers' Annual and Interim Filings*) have been designed by the Company to provide reasonable assurance that

- (a) material information relating to the Company is made known to the Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”) by others, particularly during the period in which the annual filings are being prepared; and
- (b) information required to be disclosed by the Company in its annual filings, interim filings or other reports that it files or submits under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation and is accumulated and communicated to management, including the CEO and CFO, to allow timely decisions regarding required disclosures.

The CEO and CFO have concluded that, as of December 31, 2016, the design and operation of the disclosure controls and procedures are effective to ensure that information required to be disclosed in reports that it files or submits to regulatory authorities is recorded, processed, summarized and reported within the time periods specified

by regulation and is accumulated and communicated to management, including our CEO and CFO, to allow timely decisions regarding required disclosures.

### **Internal Control over Financial Reporting**

The Company's management, with the participation of its CEO and CFO, has designed, established and is maintaining a system of internal control over financial reporting. Under the supervision of the CFO, as at December 31, 2016, the Company's internal control over financial reporting is a process designed to provide reasonable assurance that the financial information prepared by the Company for external purposes is reliable and has been recorded, processed and reported in an accurate and timely manner and in accordance with IFRS.

Management, with the participation of its CEO and CFO, has used the Internal Control—Integrated Framework to evaluate the effectiveness of internal control over financial reporting, which is a recognized and suitable framework issued by the Committee of Sponsoring Organizations (COSO Framework) published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's controls include policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with IFRS; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the annual financial statements or interim financial statements.

There have been no changes to the controls during the year that materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

### **Limitations of Controls and Procedures**

The Company's management, including the CEO and CFO, believe that any disclosure controls and procedures or internal controls over financial reporting, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, they cannot provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been prevented or detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by unauthorized override of the control. The design of any systems of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Accordingly, because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

### **CRITICAL ACCOUNTING POLICIES**

kneat.com's significant accounting policies are disclosed in note 5, *Summary of Significant Accounting Policies*, of the annual consolidated financial statements for the year-ended December 31, 2016. kneat.com has identified certain accounting policies that it believes are most critical in understanding the judgments that are involved in producing the consolidated financial statements and the estimates made that could impact results of the operations, which are discussed below.

#### **Revenue recognition**

The Company derives its revenues under license agreements from the sale of proprietary software licenses and provides software-related services including training, installation, upgrades, consulting and maintenance, which include product support services. Software licenses sold by the Company are generally perpetual in nature and the arrangements generally comprise various services. Revenues generated by the Company include the following:

(i) *License fees*

Revenues from perpetual licenses are recognized when an agreement has been signed, the product has been delivered, there are no uncertainties surrounding product acceptance, the fees are fixed or determinable and the amount of revenue and costs can be measured reliably and collection is considered probable such that economic benefits associated with the transaction will flow to the Company. Delivery generally occurs at the point where title and risk of loss have passed to the customer and the Company no longer retains continuing involvement or effective control over the products sold.

(ii) *Maintenance agreements*

Maintenance agreements for proprietary software licenses generally call for the Company to provide technical support and unspecified software updates to customers. Maintenance revenues for technical support and unspecified software update rights are recognized rateably over the term of the maintenance agreement.

(iii) *Consulting and training services*

The Company provides consulting and training services to its customers. Revenues from such services are recognized as the services are performed.

(iv) *Multiple-element arrangements*

Some of the Company's sales involve multiple-element arrangements that include software licenses, maintenance and various professional services. The Company evaluates each deliverable in an arrangement to determine whether such deliverable would represent a separate element. Most of the Company's products and services qualify as separate elements and revenue is recognized when the applicable revenue recognition criteria, as described above, are met.

In multiple-element arrangements, the Company separately accounts for each product or service according to the methods described when the following conditions are met:

- the delivered product or service has value to the customer on a stand-alone basis; and
- there is objective and reliable evidence of fair value of any undelivered product or service.

If there is objective and reliable evidence of fair value for all products and services in a sale, the total price of the arrangements is allocated to each product and service based on relative fair value. Otherwise, the Company first allocates a portion of the total price to any undelivered products and services based on their fair value and the remainder to the products and services that have been delivered.

**Intangible asset**

Expenditure on research activities undertaken with the prospect of gaining new technical knowledge and understanding is recognised in the consolidated statement of comprehensive loss as an expense as incurred.

The intangible asset consists of the internally generated software product, Kneat Gx. The development costs of the software product, net of research and development tax credit, are capitalized as they can be measured reliably, the product is technically and commercially feasible, future economic benefits are probable and the Company intends to, and has sufficient resources to, complete development and to use or sell the product. Expenditures capitalized include the cost of labour and other costs that are directly attributable to preparing the asset for its intended use.

The estimated useful lives, residual value and amortization rates are reviewed on a regular basis. During the review of the amortization rates, management determined that amortization in the year of addition will be calculated using a half year rule. This results in a change in the depreciation rate from 20% to 10% per annum in the year of addition. The reduced amortization rate in the year of addition resulted in a decrease in the amortization expense of \$158,795 for the year ended December 31, 2016.

The intangible asset is amortized based on the cost of the asset less its residual value. Amortization is charged to the consolidated statement of comprehensive loss on a straight-line basis over the estimated useful economic life, from the date the asset is available for use, at an annual rate of 20%.

## **CHANGE IN ACCOUNTING POLICIES**

### **Change in presentation currency**

Effective January 1, 2016 the Company changed its presentation currency from the Euro to the Canadian dollar. The change in presentation currency is to better reflect the Company's business activities and to improve investors' ability to compare the Company's financial results with other publicly traded businesses in the industry. The Company has applied the change retrospectively as if the new presentation currency had always been the Company's presentation currency. In accordance with IAS 21, *The effects of changes in foreign exchange rates*, the financial statements for all periods presented have been translated to the new Canadian dollar presentation currency.

For comparative balances, assets and liabilities have been translated into the presentation currency at the rate of exchange prevailing at the reporting date. Revenues and expenses were translated at the annual average exchange rates for the reporting period as these approximated the actual exchange rates at the dates of the underlying transactions. Common share amounts were translated at the historical spot rates on the date of the related transaction. Retained earnings and contributed surplus were translated at average rates for each year as if the Canadian dollar had always been the presentation currency. Exchange differences arising on translation were taken to the translation reserve in shareholders' equity. See note 3, *Change in presentation currency*, in the audited consolidated financial statements for the year end December 31, 2016 for further details.

### **Share conversion**

The legal capital of kneat.com has been restated at an exchange ratio of 34.2186 common shares of kneat.com as described in note 6 to the consolidated financial statements for the year ended December 31, 2016. The effect of the share conversion has been applied retrospectively in line with IAS 33, *Earnings per share*. Accordingly, the number of common shares outstanding has been amended to 23,314,877 as at January 1, 2015 and 27,178,260 as at December 31, 2015 and the weighted average common shares outstanding for the purpose of determining loss per share has been amended to 25,628,012 for the year ended December 31, 2015. As a result of these amendments, the loss per share has been amended to \$0.04 for the year ended December 31, 2015.

## **SIGNIFICANT ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY**

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments and estimates that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results could differ from these estimates. Estimates are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Information about critical accounting judgments and estimates in applying accounting policies that have the most significant impact on the amounts recognized in the consolidated financial statements are outlined below.

### *Accounting for the Transaction*

In order to account for the Transaction, management has made estimates related to the valuation of Kneat Solutions Limited on the effective date of the Transaction which impact the calculation of the listing fee recognized in the statement of loss and comprehensive loss and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016. The main estimate used in the valuation of Kneat Solutions Limited is the trading price of kneat.com on the Transaction date. A change in this estimate could have a significant impact on the listing expense and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 whereby a ten percent decrease in the valuation of Kneat Solutions Limited would decrease the listing expense and decrease the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 by approximately \$1,200,000. Conversely, if the valuation of Kneat Solutions Limited was increased by ten percent, the listing expense and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 would increase by approximately \$1,200,000.

### *Valuation and amortization of internally generated intangible asset*

The Company capitalizes certain costs incurred for the development of its Kneat Gx computer software platform. Estimates are used in order to determine the point in time whereby the recognition criteria are met and the allocation and nature of costs to capitalize in accordance with IAS 38, *Intangible Assets*. The capitalized costs include the cost of direct labour and other costs directly attributable to preparing the intangible asset for its intended use.

Management then estimates the expected term over which the Company will receive benefits from the software application, which is estimated to be five years. A change in these estimates would have a significant impact on the carrying value of the intangible asset and the amortization and expenses recognized in the statement of loss and comprehensive loss.

#### *Recovery of research and development tax credits*

Amounts recorded for research and development tax credits are calculated based on the expected eligibility and tax treatment of qualifying research and experimental development expenditures recorded in the Company's consolidated financial statements. Estimates are used in determining the eligibility of expenditures incurred and may be subject to audit and further analysis by the tax authorities. A change in the estimates would have a significant impact on the carrying value of the research and development tax credit receivable balance, the research and development tax credit recovery in the statement of loss and comprehensive loss and the carrying value of the intangible asset.

#### *Valuation of stock options*

The fair value of the stock options granted by the Company is estimated by management using the Black- Scholes pricing model which incorporates several assumptions including the grant date, exercise price, share price on the grant date, volatility of the underlying stock and the expected term of the stock options. The Company uses historical price data of comparable entities in the estimate of future volatilities. Changes in the assumptions can materially affect the fair value estimates and, therefore, may not necessarily provide a reliable estimate of the fair value of the related stock options.

#### *Recognition of revenue*

Revenue recognition is subject to critical judgment, particularly in multiple-element arrangements where judgment is required in allocating revenue to each component, including licenses, professional services, software upgrades and maintenance services, based on the relative fair value of each component. As the Company does not have a significant history of generating revenue, management uses judgement, based on customer specific contracts and comparable sales to determine the appropriate fair value of each component. In addition, as certain of these components have a term of more than one year, the identification of each deliverable and the allocation of the consideration related to the components impacts the timing of revenue recognition. A change in the fair value allocated to each component could materially impact the current and future years recognized revenue and deferred revenue balances at period end.

### **MANAGEMENT CHANGES AND OTHER INFORMATION**

On June 27, 2016, the Company completed the Transaction, at which point Edmund Ryan was appointed the Company's Chief Executive Officer, Sarah Oliver was appointed Chief Financial Officer, Kevin Fitzgerald was appointed the Director of Research and Development and Brian Ahearne was appointed the Director of Quality. Edmund Ryan, Kevin Fitzgerald, Paul Breen, James Osborne, Ian Ainsworth, and Wade Dawe were appointed as directors of the Company.

Additional information regarding the Company is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company's website at [www.kneat.com](http://www.kneat.com)