Xebec Adsorption Inc.

Consolidated Financial Statements
December 31, 2018 and 2017
(expressed in Canadian dollars)

Raymond Chabot
Grant Thornton LLP
Suite 2000
National Bank Tower
600 De La Gauchetière Street West
Montréal, Quebec
H3B 4L8

T 514-878-2691

Independent Auditor's Report

To the Shareholders of
Xebec Adsorption Inc.

Opinion

We have audited the consolidated financial statements of Xebec Adsorption Inc. (hereafter "the Company"), which comprise the consolidated statements of financial position as at December 31, 2018 and 2017 and the consolidated statements of income (loss), the consolidated statements of comprehensive loss, the consolidated statements of changes in equity and the consolidated statements of cash flows for the years then ended, and notes to the consolidated financial statements including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

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 are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Material uncertainty related to going concern

We draw attention to Note 1 to the consolidated financial statements, which indicates the existence of a uncertainty that may cast doubt about the the Company’s ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Information other than the consolidated financial statements and the auditor’s report thereon

Management is responsible for the other information. The other information comprises the information, other than the consolidated financial statements and our auditor’s report thereon, included in 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.

We obtained the Management's Discussion and Analysis prior to the date of this auditor's report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in this auditor's report. We have nothing to report in this regard.

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 International Financial Reporting Standards (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.

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 group 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 on our independence, and where applicable, related safeguards.

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

Montreal
April 16, 2019

Raymond Chabot Grant Thornton LLP[1]

[1] CPA auditor, CA public accountancy permit n° A125741

Xebec Adsorption Inc.

Consolidated Statements of Financial Position
As at December 31, 2018 and 2017

(expressed in Canadian dollars)

	December 31, 2018 $	December 31, 2017 $
Assets		
Current assets		
Cash	2,382,146	1,341,121
Restricted Cash (Note 29)	1,540,000	-
Trade and other receivables (Note 5)	6,865,331	4,133,259
Inventories (Note 6)	3,339,542	1,963,392
Investment tax credits receivable	15,943	15,943
Other current assets	260,743	260,157
Total current assets	14,403,705	7,713,872
Non-current assets		
Property, plant and equipment (Note 7)	281,818	208,632
Intangible assets (Note 8)	405,477	418,363
Total non-current assets	687,295	626,995
Total assets	15,091,000	8,340,867
Liabilities		
Current liabilities		
Credit facility (Note 10)	-	1,437,912
Trade, other payables and accrued liabilities (Note 11)	2,682,924	3,585,755
Contract liabilities (Note 12)	4,370,643	720,996
Current portion of long-term debt (Note 13a)	1,777,915	22,236
Current portion of government royalty program obligation (Note 13b)	100,515	86,826
Current portion of provisions (Note 14)	15,275	16,689
Current portion of obligation arising from shares issued by a subsidiary (Note 15)	198,300	-
Total current liabilities	9,145,572	5,870,414
Non-current liabilities		
Long-term debt (Note 13a)	1,902,647	2,223,478
Government royalty program obligation (Note 13b)	436,258	504,546
Obligation arising from shares issued by a subsidiary (Note 15)	3,971,053	3,912,314
Deferred rent	133,531	132,815
Provisions (Note 14)	40,324	5,601
Deferred tax liabilities	81,989	81,989
Total non-current liabilities	6,565,802	6,860,743
Total liabilities	15,711,374	12,731,157
Equity		
Share capital (Note 16)	26,508,168	19,703,836
Contributed surplus	3,691,192	3,339,740
Equity component of convertible debentures	189,645	291,389
Accumulated other comprehensive loss	(1,140,342)	(1,049,455)
Deficit	(29,869,037)	(26,675,800)
Total equity	(620,374)	(4,390,290)
Total liabilities and equity	15,091,000	8,340,867

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

Approved by the Board of Directors

(signed) Kurt Sorschak, Director

(signed) Guy Saint-Jacques, Director

Xebec Adsorption Inc.

Consolidated Statements of Income (loss)
For the years ended December 31, 2018 and 2017
(expressed in Canadian dollars)

	2018 $	2017 $
Revenue (Note 27)	20,208,496	14,745,931
Cost of goods sold	14,520,154	8,977,709
Gross margin	5,688,342	5,768,222
Research and development expenses (Note 19)	92,069	(31,114)
Selling and administrative expenses	7,215,500	5,217,075
Foreign exchange (gain) loss	(152,482)	131,149
Loss (gain) on insurance claim	-	(132,366)
Loss (gain) on conversion of shares issued by a subsidiary (Note 15)	116,090	(2,358)
	7,271,177	5,182,386
Operating income (loss)	(1,582,835)	585,836
Other charge (income)		
Finance income	(1,611)	(122,068)
Finance expenses (Note 20)	1,323,162	611,152
	1,321,551	489,084
Income (loss) before income taxes	(2,904,386)	96,752
Income taxes (Note 22)	-	-
Net income (loss) for the year	(2,904,386)	96,752
Net income (loss) per share		
Basic and diluted net income (loss) per share (Note 16)	(0.07)	0.002

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

Xebec Adsorption Inc.

Consolidated Statements of Comprehensive Loss
For the years ended December 31, 2018 and 2017

(expressed in Canadian dollars)

	2018 $	2017 $
Net income (loss) for the year	(2,904,386)	96,752
Other comprehensive loss		
Cumulative translation adjustment	(90,887)	(109,239)
Comprehensive loss for the year	(2,995,273)	(12,487)

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

Xebec Adsorption Inc.

Consolidated Statements of Changes in Equity

For the years ended December 31, 2018 and 2017

(expressed in Canadian dollars)

	Number							Amount
	Common shares	Warrants	Share capital – Common shares $	Contributed surplus $	Accumulated other comprehensive income (loss) $	Deficit $	Equity Component of convertible debentures $	Total $
Balance – January 1, 2017	39,363,867	-	19,318,856	2,996,621	(940,216)	(26,772,552)	150,304	(5,246,987)
Net income for the year	-	-	-	-	-	96,752	-	96,752
Other comprehensive loss	-	-	-	-	(109,239)	-	-	(109,239)
Comprehensive loss for the year	-	-	-	-	(109,239)	96,752	-	(12,487)
Stock-based compensation expense (Note 17)	-	-	-	372,603	-	-	-	372,603
Issuance of convertible debentures (net of deferred tax liability of $ 81,989 (Note 22)	-	-	-	-	-	-	186,177	186,177
Share issued from the exercise of options	1,140,500	-	88,535	(29,484)	-	-	-	59,051
Conversion of convertible debentures	2,000,000	-	296,445	-	-	-	(45,092)	251,353
Balance – December 31, 2017	42,504,367	-	19,703,836	3,339,740	(1,049,455)	(26,675,800)	291,389	(4,390,290)
Balance – January 1, 2018	42,504,367	-	19,703,836	3,339,740	(1,049,455)	(26,675,800)	291,389	(4,390,290)
Adjustment from the adoption of IFRS 15 (Note 3)	-	-	-	-	-	(288,851)	-	(288,851)
Balance – January 1, 2018 Adjusted	42,504,367	-	19,703,836	3,339,740	(1,049,455)	(26,964,651)	291,389	(4,679,141)
Net loss for the year	-	-	-	-	-	(2,904,386)	-	(2,904,386)
Other comprehensive loss	-	-	-	-	(90,887)	-	-	(90,887)
Comprehensive loss for the year	-	-	-	-	(90,887)	(2,904,386)	-	(2,995,273)
Share issued from conversion of debentures	4,766,665	-	765,000	-	-	-	(101,744)	663,256
Share issued from the exercise of options	307,272	-	79,271	(26,071)	-	-	-	53,200
Stock-based compensation (Note 17)	-	-	-	352,897	-	-	-	352,897
Share issued from public offering	9,439,966	-	5,984,687	-	-	-	-	5,984,687
Warrants issued from public offering		5,286,381	(24,626)	24,626	-	-	-	-
Balance –December 31, 2018	57,018,270	5,286,381	26,508,168	3,691,192	(1,140,342)	(29,869,037)	189,645	(620,374)

Accumulated other comprehensive income (loss) relates solely to cumulative translation adjustments.

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

Xebec Adsorption Inc.

Consolidated Statements of Cash Flows
For the years ended December 31, 2018 and 2017
(expressed in Canadian dollars)

	2018 $	2017 $
Cash flows from		
Operating activities		
Net income (loss) for the year	(2,904,386)	96,752
Items not affecting cash		
Depreciation of property, plant and equipment (Note 7)	78,689	87,584
Amortization of intangible assets (Note 8)	139,079	80,325
Reversal of inventory write-down	(144,442)	(189,065)
Government grant	-	(2,083)
Accretion finance expenses and gain on revaluation of government royalty program obligation (Note 13b)	27,401	(91,168)
Accretion of the obligation arising from shares issued by a subsidiary (Note 15)	339,249	332,537
Exchange gain/loss on the obligation arising from shares issued by a subsidiary	116,090	(2,358)
Accretion of convertible debentures (Note 13a)	220,763	86,549
Stock-based compensation expense (Note 17)	352,897	372,603
Reversal of trade payables	-	(697,659)
Reversal of allowance for doubtful accounts (Note 18)	-	(315,145)
Deferred rent	716	(5,701)
	(1,773,994)	(244,471)
Change in non-cash working capital balances related to operations (Note 23)	(1,184,241)	(1,610,526)
	(2,958,185)	(1,854,997)
Investing activities		
Acquisition of property, plant and equipment	(146,953)	(26,110)
Acquisition of intangible assets	(139,290)	(308,702)
Receipt of R&D tax credit (Note 8)	13,634	-
	(272,609)	(334,812)
Financing activities		
Increase (decrease) of bank loan	-	(755,000)
Increase (decrease) of credit facility (Note 10)	(1,437,912)	1,437,912
Obligation arising from preferred shares issued by a subsidiary	(198,300)	-
Proceeds from debenture units	-	2,024,149
Increase from obligation under a capital lease	-	11,327
Debenture issue costs	-	(129,390)
Proceeds from issuance of share capital (Notes 16 et 17)	6,037,887	59,051
Long-term debt	1,899,578	-
Repayment of long-term debt	(22,236)	(24,303)
Repayment of government royalty program obligation (Note 13b)	(82,000)	(75,000)
	6,197,017	2,548,746
Net increase in cash and cash equivalent during the year	2,966,223	358,937
Cash – Beginning of the year	1,341,121	1,088,592
Effect of exchange rate changes on cash	(385,198)	(106,408)
Cash and cash restricted – End of the year	3,922,146	1,341,121
Additional information		
Interest paid	739,811	378,098

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

1 Nature of business and liquidity risk

a) Nature of business

Xebec Adsorption Inc. ("Xebec" or the "Company") is a global provider which specializes in the design and manufacture of cost-effective and environmentally responsible purification, separation, dehydration and filtration equipment for gases and compressed air. Xebec's main product lines are: biogas plants for the purification of biogas from agricultural digesters, landfill sites and waste water treatment plants, natural gas dryers for natural gas refuelling stations, associated gas purification systems which enable diesel displacement on drilling sites, and hydrogen purification systems for fuel cell and industrial applications. The Company is incorporated and domiciled in Canada and is listed on the TSX Venture (TSXV) Exchange under the symbol XBC-V. The address of its registered office is 730 Industriel Boulevard, Blainville, Quebec, Canada. The Company's web site address is www.xebec.com.

b) Going concern

The consolidated financial statements have been prepared on the basis of the going concern assumption, meaning that the Company will be able to realize its assets and discharge its liabilities in the normal course of operations. The Company has realized, an operating loss of $1,582,835 in 2018 (an operating income of $585,836 in 2017), had cash outflows from operations of $2,958,185 for the year ended December 31, 2018 ($1,854,997 in 2017), finished the year with cash amounting to $2,382,146 ($1,341,121 in 2017) and a working capital of $5,258,133 ($1,843,458 in 2017). The company has access to credit facilities totalling $2,000,000 of which $ NIL has been used ($ NIL in 2017) (see Note 9). During the year, management undertook various initiatives and developed a plan to manage its operating and liquidity risks in light of prevailing economic conditions. Management is also currently seeking alternative financings for its operations. The Company has prepared a budget for 2019 for which management believes the assumptions are reasonable. Achieving budgeted results is dependent on improving the volume of revenues, delivering on sales and contract schedules, meeting expected overall operating margin levels and controlling general and administrative costs.

The Company is thus faced with uncertainties that may have an impact on future operating results and liquidity. These uncertainties include fluctuations in foreign currency rates and achieving the Company's business plan goals as mentioned in the previous paragraph. While management believes it has developed planned courses of action to mitigate operating and liquidity risks, there is no assurance that management will be able to achieve its business plan and maintain the necessary liquidity level including accessing liquidities from China if events or conditions develop that are not consistent with management's expectations, key budget assumptions for 2019 and planned courses of action. Therefore, the Company may require additional external funding, and there is no assurance that it would be successful. Future changes in capital markets conditions could result in such funding not being available when required or at acceptable costs. The Company is unable to predict the possible effects, if any; of such uncertainties and the potential adjustments to

the carrying values of assets and liabilities that could be needed should the Company have insufficient liquidity. Such adjustments could be material.

2 Basis of compliance and basis of preparation

These consolidated financial statements, have been prepared in accordance with International Financial Reporting Standards ("IFSR")

These consolidated financial statements were approved for issue by the Board of Directors of the Company on April 16, 2019

The consolidated financial statements have been prepared on the historical cost convention, except for where IFRS requires recognition at fair value.

These consolidated financial statements are based on the accounting policies as described below. These policies have been consistently applied to all the periods, unless otherwise stated.

3 Significant accounting policies

New standards adopted as at January 1st, 2018

Financial Instruments

On January 1st, 2018, the Company adopted IFRS 9 Financial Instruments ("IFRS 9"), which replaces IAS 39 Financial Instruments: Recognition and Measurement ("IAS 39'). The Company elected to use the exemption to not restate comparative information for prior periods. IFRS 9 provides a revised model for classification and measurement of financial assets, including a new expected credit loss ("ECL") impairment model. The revised model for classifying financial assets results in classification according to their contractual approach to hedge accounting. IFRS 9 also largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

As a result of the adoption of IRFS9, the Company has changed its accounting policy with respect to financial instruments. Under IFRS9, the Company's financial assets are accounted for as follows when compares to the Company's previous policy in accordance with IAS39:

Financial Assets	**IAS 39**	**IFRS 9**
Cash	Loans and receivables	Amortized cost
Trade and other receivables	Loans and receivables	Amortized cost
Bank loan	Other financial liabilities	Amortized cost
Trade, other payables and accrued liabilities	Other financial liabilities	Amortized cost
Long-term debt	Other financial liabilities	Amortized cost
Government royalty program obligation	Other financial liabilities	Amortized cost
Obligation arising from shares issued by a subsidiary	Other financial liabilities	Amortized cost

The changes in accounting policy did not result in a change in carrying value for any financial instruments on transition date. Upon initial date of application of IFRS 9, there was no impact to the Company's consolidated financial statements as of the date of initial application.

Revenue Recognition

On January 1st, 2018, the Company adopted IFRS 15 Revenues from Contracts with Customers ("IFRS 15"), which replaces IAS 11 Construction Contracts, and IAS 18, Revenue and related interpretations. The Company elected to use the modified retrospective method of adoption and not to restate the comparative information for prior periods. As a result, the cumulative effect of initially applying IFRS 15 was recognized as an adjustment to the opening balance of the deficit at January 1, 2018. The impact in the deficit for this adjustment is an increase in deficit of $288,851. Comparative information has not been restated and continues to be reported under IAS 11 and IAS 18. The Company also elected to reflect the aggregate effect of all contract modifications occurring before January 1, 2018 when: identifying the satisfied and unsatisfied performance obligations in a contract, determining the transaction price, and allocating the transaction price to the satisfied and unsatisfied performance obligations.

The adoption of IFRS 15 has mainly affected the following areas:

- Revenues from multiple services, which must be accounted for separately.
- Percentage of completion and revenues from long-term production-type contracts.

Revenue recognition for obligations in China, previously accounted for using the percentage-of-completion method no longer meet the requirements for revenue recognition over time. Revenue for these contracts are recognized upon completion.

There is no material impact of this standard in the North-American and European divisions.

While these changes impact the timing of revenue and margin recognition, and result in a reduction of equity at transition, there is no change to cash flows nor change in profitability over the life of the contracts.

The impacts on the consolidated financial statements, are as follows:

Consolidated Statement of Financial Position

		2018	
	As reported $	Amounts without adoption of IFRS 15 $	IFRS 15 adjustments $
Assets			
Current assets			
Cash	2,382,146	2,382,146	-
Restricted cash (Note 29)	1,540,000	-	-
Trade and other receivables (Note 5)	6,865,331	6,598,739	266,592
Inventories (Note 6)	3,339,542	781,372	2,558,170
Investment tax credits receivable	15,943	15,943	-
Other current assets	260,743	260,743	-
Total current assets	14,403,705	11,578,943	2,824,762
Non-current assets			
Property, plant and equipment (Note 7)	281,818	281,818	-
Intangible assets (Note 8)	405,477	405,477	-
Total non-current assets	687,295	687,295	-
Total assets	15,091,000	12,266,238	2,824,762
Liabilities			
Current liabilities			
Credit facility (Note 10)	-	-	-
Trade, other payables and accrued liabilities (Note 11)	2,682,924	2,682,924	-
Contract liabilities (Note 12)	4,370,643	(1,037,048)	5,407,691
Current portion of long-term debt (Note 13a)	1,777,915	1,777,915	-
Current portion of government royalty program obligation (Note 13b)	100,515	100,515	-
Current portion of provisions (Note 14)	15,275	15,275	-
Current portion of obligation arising from shares issued by a subsidiary (Note 15)	198,300	198,300	-
Total current liabilities	9,145,572	3,737,881	5,407,691
Non-current liabilities			
Long-term debt (Note 13a)	1,902,647	1,902,647	-
Government royalty program obligation (Note 13b)	436,258	436,258	-
Obligation arising from shares issued by a subsidiary (Note 15)	3,971,053	3,971,053	-
Deferred rent	133,531	133,531	-
Provisions (Note 14)	40,324	40,324	-
Deferred tax liabilities	81,989	81,989	-
Total non-current liabilities	6,565,802	6,565,802	-
Total liabilities	15,711,374	10,303,683	5,407,691
Equity			
Share capital (Note 16)	26,508,168	26,508,168	-
Contributed surplus	3,691,192	3,691,192	-
Equity component of convertible debentures	189,645	189,645	-
Accumulated other comprehensive loss	(1,140,342)	(1,140,342)	-
Deficit	(29,869,037)	(27,286,108)	(2,582,929)
Total equity	(620,374)	1,962,555	(2,582,929)
Total liabilities and equity	15,091,000	12,266,238	2,824,762

Consolidated Statement of Income (Loss)

	2018		
	As reported $	Amounts without adoption of IFRS 15 $	IFRS 15 adjustments $
Revenue	20,208,496	25,652,986	(5,444,490)
Cost of goods sold	14,520,154	17,670,566	(3,150,412)
Gross margin	5,688,342	7,982,420	(2,294,078)
Research and development expenses (Note 19)	92,069	92,069	-
Selling and administrative expenses	7,215,500	7,215,500	-
Foreign exchange loss (gain)	(152,482)	(152,482)	-
Loss (gain) on conversion of shares issued by a subsidiary (Note 15)	116,090	116,090	-
	7,271,177	7,271,177	-
Operating Income (loss)	(1,582,835)	711,243	(2,294,078)
Other charge (income)	1,321,551	1,321,551	-
Net income (loss) for the year	(2,904,386)	(610,308)	(2,294,078)

Consolidated Comprehensive Income

	As reported **$**	**Amounts without adoption of IFRS 15** **$**	**IFRS 15 adjustment** **$**
Net income (loss) for the year	(2,904,386)	(610,308)	(2,294,078)
Other comprehensive loss			
Cumulative translation adjustment	(90,887)	(90,887)	-
Comprehensive loss for the year	(2,995,273)	(701,195)	(2,294,078)

Consolidated Statements of Cash Flows

	2018		
	As reported $	**Amounts without adoption of IFRS 15 $**	**IFRS 15 adjustment $**
Cash flows from			
Operating activities			
Net income (loss) for the year	(2,904,386)	(610,308)	(2,294,078)
Items not affecting cash			
Depreciation of property, plant and equipment (Note 7)	78,689	78,689	-
Amortization of intangible assets (Note 8)	139,079	139,079	-
Reversal of inventory write-down	(144,442)	(144,442)	-
Government grant	-	-	-
Accretion finance expenses and gain on revaluation of government royalty program obligation (Note 13b)	27,401	27,401	-
Accretion of the obligation arising from shares issued by a subsidiary (Note 15)	339,249	339,249	-
Exchange gain/loss on the obligation arising from shares issued by a subsidiary	116,090	116,090	-
Accretion of convertible debentures (Note 13a)	220,763	220,763	-
Stock-based compensation expense (Note 17)	352,897	352,897	-
Reversal of trade payables	-	-	-
Reversal of allowance for doubtful accounts (Note 18)	-	-	-
Deferred rent	716	716	-
	(1,773,944)	520,134	(2,294,078)
Change in non-cash working capital balances related to operations (Note 23)	(1,184,241)	(3,478,319)	(2,294,078)
	(2,958,185)	(2,958,185)	-
Investing activities			
Acquisition of property, plant and equipment	(146,953)	(146,953)	-
Acquisition of intangible assets	(139,290)	(139,290)	-
Receipt of R&D tax credit	13,634	13,634	-
	(272,609)	(272,609)	-
Financing activities			
Increase (decrease) of bank loan	-	-	-
Increase (decrease) of credit facility (Note 10)	(1,437,912)	(1,437,912)	-
Obligation arising from preferred shares issued by a subsidiary	(198,300)	(198,300)	-
Proceeds from debenture units	-	-	-
Increase from obligation under a capital lease	-	-	-
Debenture issue costs	-	-	-
Proceeds from issuance of share capital (Notes 16 et 17)	6,037,887	6,037,887	-
Long-term debt	1,899,578	1,899,578	-
Repayment of long-term debt	(22,236)	(22,236)	-
Repayment of government royalty program obligation (Note 13b)	(82,000)	(82,000)	-
	6,197,017	6,197,017	-
Net increase in cash and cash equivalent during the year	2,966,223	2,850,133	-
Cash – Beginning of the year	1,341,121	1,341,121	-
Effect of exchange rate changes on cash	(385,198)	(269,108)	-
Cash and cash restricted – End of the year	3,922,146	3,922,146	-

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries. Subsidiaries are entities controlled by the Company. Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Company has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Company considers all relevant facts and circumstances in assessing whether or not the Company's voting rights in an investee are sufficient to give it power, including:

- the size of the Company's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;

- potential voting rights held by the Company, other vote holders or other parties;

- rights arising from other contractual arrangements; and

- any additional facts and circumstances that indicate that the Company has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

Intercompany transactions, balances and unrealized gains and losses on transactions between different entities within the Company are eliminated. Subsidiaries comprise Xebec Adsorption (Shanghai) Co. Ltd., which is 70% owned, Xebec Adsorption USA Inc. (Houston) and Xebec Adsorption Europe SRL which are wholly owned. Subsidiaries are fully consolidated from the date on which control is obtained by the Company and are deconsolidated from the date that control ceases. The Company has the obligation to repurchase the Minority Shareholders' interest owned in Xebec Adsorption (Shanghai) Co. Ltd. under certain circumstances (see Note 15). Therefore, the accounts of Xebec Adsorption (Shanghai) Co. Ltd. are consolidated at 100% and the Minority Shareholders' interest is presented as a financial liability in these consolidated financial statements.

Changes in the Company's ownership interests in subsidiary that do not result in the Company losing control over the subsidiaries are accounted for as equity transactions or liability transactions depending on the conditions that these changes occurred. The carrying amounts of the Company's interests are adjusted to reflect the changes in their relative interests in the subsidiaries.

Inventories

Inventories are stated at the lower of cost and net realizable value for raw materials, work in progress and finished goods. Costs of raw materials are determined on an average cost basis. Work in progress and finished goods include materials, direct labour and production overhead. Net realizable value is the

estimated selling price for inventories less all estimated costs of completion and cost necessary to make the sale. Inventories are recorded net of any obsolescence provision.

A new assessment is made in each subsequent year when inventories are adjusted to net realizable value. When the circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in net realizable value because of changed economic circumstances, the amount of the write-down is reversed (i.e. the reversal is limited to the amount of the original write-down) so that the new carrying amount is the lower of cost and the revised net realizable value.

Property, plant and equipment

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

The major categories of property, plant and equipment are depreciated on a straight-line basis as follows:

Machinery and equipment	3 to 10 years
Office furniture and equipment	2 to 5 years
Computers	3 years
Moulds	5 years
Vehicles	5 years
Leasehold improvement	Lease term

The Company allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant components and depreciates each such component separately. Residual values, method of depreciation and useful lives of the assets are reviewed annually and adjusted if appropriate.

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of other gains and losses in the consolidated statement of income (loss).

Identifiable intangible assets

The Company's intangible assets consist of software, capitalized development costs of a new line and engineering standardisation costs when the criteria mentioned in the research and development expenses accounting policy are met. These assets are capitalized and amortized on a straight-line basis in the consolidated statement of income (loss) over the period of their expected useful lives.

Development costs are amortized over a period of five years. Engineering standardisation costs and software are amortized over a period of 3 years.

Impairment of non-financial assets

Property, plant and equipment and intangible assets are tested for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Long-lived assets that are not depreciated or amortized are subject to an annual impairment test. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units or CGUs). The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

The Company evaluates impairment losses for potential reversals when events or circumstances warrant such consideration.

Provisions

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

During the normal course of its operations, the Company assumes certain maintenance and repair costs under warranties offered on natural gas equipment, biogas, associated gas and hydrogen purification equipment. The warranties cover a period ranging from 12 to 18 months. A liability for the expected cost of the warranty-related claims is established when the product is delivered and completed. In estimating the warranty liability, historical material replacement costs and the associated labour costs are considered. Revisions are made when actual experience differs materially from historical experience.

Financial Instruments

Except for those trade receivables that do not contain a significant financing component and are measured at the transaction price in accordance with IFRS 15, all financial assets are initially measured at fair value adjusted for transaction costs where applicable.

Financial assets, other than those designated and effective as hedging instruments, are classified into the following categories:

- Amortized cost
- Fair value through profit or loss (FVTPL)
- Fair value through other comprehensive income (FVOCI)

In the years presented, the Company does not have any financial assets categorized as FVTPL or FVOCI.

The classification is determined by both, the Company's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset.

All income and expenses relating to financial assets that are recognized in income or loss are presented within finance expenses or finance income, except for impairment of trade receivables which is presented within selling and administrative expenses.

Financial assets are measured at amortized cost if the asset meet the following conditions and are not designated as FVTPL:

- They are held within a business model whose objective is to hold the financial assets and collect its contractual cash flows
- The contractual terms of the financial assets give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding.

After initial recognition, they are measured at amortized costs using the effective interest method. Discounting is omitted where the effect of discounting is immaterial. The Company cash, restricted cash, trade and other receivables fall into this category of financial instruments.

The adoption of IFRS 9 had little impact on the Company's accounting for impairment losses for financial assets by replacing IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. Following the adoption of IFRS 9, the recognition of credit losses is no longer dependent on the identification of an event generator of credit losses by the Company.

The Company considers a broader range of information when assessing credit risk and measuring expected credit losses, including past events, current conditions, reasonable and supportable forecasts that affect the expected collectability of the future cash flows on the instrument.

In applying this forward-looking approach, a distinction is made between:

- financial instruments that have not deteriorated significantly in credit quality since initial recognition or that have low credit risk ("Stage 1") and
- financial instruments that have deteriorated significantly in credit quality since initial recognition and whose credit risk in not low ("Stage 2").

"Stage 3" would cover financial assets that have objective evidence of impairment at the reporting date.

"12-month expected credit losses" are recognized for the first category while 'lifetime expected credit losses' are recognized for the second category.

Measurement of the expected credit losses is determined by a probability-weighted estimate of credit losses over the expected life of the financial instrument.

The Company's financial liabilities include bank loans, trade, other payables and accrued liabilities, long-term debt, government royalty program obligation and obligation arising from shares issued by a subsidiary.

Financial liabilities are initially measured at fair value and where applicable, adjusted for transaction costs unless the Company designated a financial liability at fair-value through profit of loss.

Subsequently, financial liabilities are measured at amortized cost using the effective interest method. All interest-related charges and, if applicable, changes in an instrument's faire value that are reported in income or loss are included within finance expense or finance income.

Government royalty program obligations

The Company receives from time to time, from different government agencies, funding designed to promote economic growth, create jobs and wealth and support sustainable development. In some of these arrangements, the Company has a contractual obligation to repay the contributions to the government agency, with repayments determined as a percentage of specified revenues over a contractually defined royalty year. Such arrangements are recognized as government royalty program obligations at initial recognition when the contribution is received. These obligations are estimated based on future projections, discounted using a rate that reflects the liability-specific risks. Over time, interest expense is recognized as a result of accretion of the long-term obligations, while royalty payments are recorded against the obligations. Subsequently, the government royalty program obligations are re-measured using the original discount rate when the future projections initially used to measure the obligations are revised. Resulting changes in the carrying amount of these obligations are recognized in the consolidated statement of income (loss) as finance income or finance expenses.

Share Capital

Share capital represents the amount received on the issue of shares, less issuance costs, net of any underlying income tax benefit from these issuance costs. If shares are issued when options and warrants are exercised, the share capital account also comprises the compensation costs previously recorded as contributed surplus. If shares are issued within the conversion option on convertible debentures exercise, the share capital account also comprise the equity component of convertible debentures

Proceeds from unit placements are allocated between shares and warrants according to the residual value method, where the difference between the fair value and issue price of the share when the warrants are issued is allocated to the warrants.

Basic and Diluted Income (Loss) per Share

Basic income (loss) per share is calculated by dividing net income (loss) for the year attributable to equity owners of the Company by the weighted average number of common shares outstanding during the year (Note 16).

Diluted income (loss) per share is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options and similar instruments is computed which assumes that if all dilutive securities had been exercised at the later of the beginning of the year and the date of issuance, as the case may be, the proceeds would be used to purchase common shares of the Company at the average market value during the year.

Revenues from Contracts with Customers

The Company earns revenues mainly from the sale of natural gas dryers, air dryers and hydrogen purification solutions (commercial equipment). The Company recognizes revenue on commercial equipment sales when it is probable that the economic benefits will flow to the Company and delivery has occurred. These criteria are generally met at the time the product is shipped and delivered to the customer and, depending on the delivery conditions, title and risk have passed to the customer. Provisions are established for estimated product returns and warranty costs at the time revenue is recognized. Cash received in advance of all of these revenue recognition criteria being met is recorded as contract liabilities.

Revenues from long-term production-type contracts such as biogas purification equipment and engineering service contracts are determined under the percentage-of-completion method whereby revenues are recognized based on the costs incurred to date in relation to the total expected costs of a contract (costs being composed mainly of materials and labour). Costs and estimated profit on contracts in progress in excess of amounts billed are reflected as work in progress. Cash received in advance of revenues being recognized on contracts is recorded as contract liabilities.

The Company monitors its contracts with customers on a regular basis to determine if a loss is likely to occur. If a loss is anticipated on a contract, the entire estimated loss is recorded as a cost of goods sold in the year in which the loss becomes evident and reasonably estimable.

Revenue is measured based on the price specified in the sales contract, net of discounts and estimated returns at the time of sale. Historical experience is used to estimate and provide for discounts and returns.

Revenues for contracts in China are recognized upon completion and the Company can determine that control has been transferred to the customer in accordance with the agreed-upon specifications in the contract.

Revenues from services are recorded when services have been rendered. For contract services that last over a year, revenue is recognized over the duration of the contract.

Segment reporting

The Company operates three business segments (the fourth, Oil and Gas, is been phased out):

1) Systems (Technology and Equipment) - Provide Renewable Natural Gas, Hydrogen and Renewable Hydrogen for a variety of applications, from fuel cells to fossil fuel replacement applications for low carbon transportation fuels.

2) Infrastructure (Renewable Gas Generation) – Project development of renewable natural gas production facilities, in the build, own and operate (BOO) model that will generate low-carbon renewable transport fuels and carbon credits.

3) Support (Industrial Air and Gas Products, Parts, Service and Operational Support) – foundational recurring revenue model.

4) Oil and Gas - Commercialization of innovative membrane technology.

For management purposes, the Company uses the same measurement policies as those in its financial statements.

In addition, corporate assets are used by each segment and are therefore not attributable to any segment in particular.

Contract balances

Contract assets are recognized when goods or services are transferred to customers before consideration is received or before the Company has an unconditional right to payment for performance completed to date. Contract assets are subsequently transferred to receivables when the right of payment becomes unconditional. Contract assets include cost incurred and recorded margins in excess of advances and progress billings on long-term contracts.

Contract liabilities are recognized when amounts are received from customers in advance of transfer of goods or services. Contract liabilities are subsequently recognized in revenue as or when the Company performs under contracts. Contract liabilities include advances and progress billing in excess on long-term contracts cost incurred and recorded margins.

A net position of contract asset or contract liability is determined for each contract. The cash flows in respect of advances and progress billings, are classified as cash flows from operating activities.

Costs to obtain or fulfill a contract

The Company can recognize as an asset the incremental costs of obtaining a contract with a customer when those costs are expected to be recovered, costs that the Company would not have incurred if the contract had not been obtained.

Costs that would have been incurred regardless of whether the contract was obtained are recognized as an expense when incurred, unless those costs are explicitly chargeable to the customer regardless of whether the contract is obtained.

The Company recognizes the incremental costs of obtaining contracts as an expense when incurred because those costs are not expected to be recovered and are not charged to the customer.

Remaining performance obligations

The Company’s contracts are for delivery of goods within the next following 12 months of contract’s signature; therefore, the Company uses the practical expedient allowed in Paragraph 121(a) of IFRS 15.

Following Paragraph 121(a), the Company does not disclose the aggregate amount of the transaction price allocated to the performance obligations that are unsatisfied as of the end of the reporting period.

Government grants

Non-refundable grants relating to property, plant and equipment are accounted for as deferred government grants and amortized on the same basis as the related assets.

Research and experimental development tax credits are recognized using the cost reduction method when there is reasonable assurance of their recovery. Investment tax credits are subject to the customary approvals by the pertinent tax authorities. Adjustments, if required, are reflected in the year when such assessments are received.

Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the consolidated statement of income (loss) on a straight-line basis over the lease term.

Leases where the Company has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges. The interest element of the finance cost is charged to the consolidated statement of loss over the lease year so as to produce a constant yearly rate of interest on the remaining balance of the liability for each year. Assets acquired under finance leases are depreciated over the shorter of the useful life of the asset and the lease term.

Stock-based compensation plans

The Company accounts for stock options using the fair value method. Each tranche in an award is considered a separate award with its own vesting year and grant date fair value. Fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. The Black-Scholes model was developed to estimate the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, this model usually requires the input of assumptions, including expected stock price volatility. For options granted to directors, officers and employees of the Company, compensation expense is recognized over the tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually. For options granted to non-employees, the transaction is measured with reference to the fair value of the goods or services when received. Related expense is recognized over the period during which the goods or services from the non-employees are received.

A corresponding increase is recorded in contributed surplus when stock options are expensed. When stock options are exercised, share capital is credited by the sum of the consideration paid and the related amount previously recorded in contributed surplus.

Research and development expenses

Research expenses are charged to expenses as incurred. Development expenses are charged to expenses as incurred unless they meet criteria for deferral and amortization. During the year ended December 31, 2018 and 2017, development expenses related to development costs of a new line and engineering standardisation costs were deferred and accounted for an identified intangible asset.

Income taxes

Income tax comprises current and deferred tax. Income tax is recognized in the consolidated statement of income (loss) except to the extent that it relates to items recognized directly in other comprehensive income or equity, in which case the income tax is also recognized directly as such.

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

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

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

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

Foreign currency translation

Functional and presentation currency:

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

The financial statements of entities that have a functional currency different from that of the Company (foreign operations) are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the statement of financial position, and income and expenses – at the average rate of the year (to the extent this is considered a reasonable approximation to actual rates). All resulting changes are recognized in other comprehensive income (loss) as cumulative translation adjustment.

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control or significant influence over a foreign operation, the foreign currency gains or losses accumulated in other comprehensive income (loss) related to the foreign operation are recognized in profit or loss. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in other comprehensive income (loss) related to the subsidiary is reallocated between controlling and non-controlling interests.

Transactions and balances:

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the consolidated statement of income (loss).

Accounting standards issued but not yet applied that have relevance to the Company

In January 2016, IASB issued IFRS 16, "Leases", which specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. The standard will be mandatory for annual periods beginning on or after January 1, 2019.

Some of the impacts of this standard on the consolidated financial statements are as follow:

- New assets such as Buildings will be recognized. Total assets amount will increase affecting ratios such as asset turnover.
- New liabilities such as Building liabilities will be recognized. Total liabilities amount will increase affecting its financial leverage.
- Depreciation expense on the right to use asset and interest expense on the lease liability will replace the operating lease expense.
- The depreciation expense is included in operating costs and interest expenses are included in financing costs, instead of being included as operating expenses in the period incurred. Operating profit will increase as well as EBITDA amount, EBITDA is a non-IFRS financial measure.

The Company will elect to use the exemptions proposed by the standard on lease contract for which the lease terms end within 12 months as of the date of initial application, and lease contracts for which the underlying asset is of low value.

The Company has yet to assess the impact of this new standard on its consolidated financial statements.

4 Significant accounting judgments and estimation uncertainties

Critical accounting estimates and judgements

The Company makes estimates and assumptions concerning the future that will, by definition, seldom equal actual results. The following are the estimates and judgments applied by management that affect the Company's consolidated financial statements.

i. Inventories must be valued at the lower of cost and net realizable value.

   A write-down of inventory will occur when its estimated market value less applicable variable selling expenses is below its carrying amount. Materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they

will be incorporated are expected to be sold at or above cost. This estimation process involves significant management judgment and is based on the Company's assessment of market conditions for its products determined by historical usage, estimated future demand and, in some cases, the specific risk of loss on specifically identified inventory. Any change in the assumptions used in assessing this valuation will impact the carrying amount of the inventory and have a corresponding impact on cost of goods sold.

ii. Impairment of internally generated intangible assets

The Company performs a test for internally generated intangible assets impairment when there is any indication that internally generated intangible assets have suffered any impairment in accordance with the accounting policy stated in the summary of significant accounting policies of these consolidated financial statements. The recoverable amounts of internally generated intangible assets have been determined based on value-in-use calculations. The value in use calculation is based on a discounted cash flow model. These calculations require the use of estimates and forecasts of future cash flows. Qualitative factors, including, degree of variability in cash flows as well as other factors are considered when making assumptions with regard to future cash flows and the appropriate discount rate. A change in any of the significant assumptions or estimates used to evaluate internally generated intangible assets could result in a material change to the results of operations.

iii. Percentage of completion and revenues from long-term production-type contracts

Revenues recognized on long-term production-type contracts reflect management's best assessment by taking into consideration all information available at the reporting date and the result on each ongoing contract and its estimated costs. The management assesses the profitability of the contract by applying important judgments regarding milestones marked, actual work performed and estimated costs to complete. Actual results could differ because of these unforeseen changes in the ongoing contracts' models.

iv. Allowance for expected credit loss

Since January 1, 2018 the Company is following IFRS 9. The Company recognizes the impairment of financial assets in the amount of expected credit losses by means of the simplified approach, measuring impairment losses as lifetime expected credit losses the trade receivables have been assessed on a collective basis as they possess shared credit risk characteristics and have been grouped based on the days past due.

Prior periods have not been restated, under IAS 39, amounts were periodically reviewed for indications of impairment and the amount impaired had been provided for as allowance for doubtful accounts.

v. Liquidity risk

The assessment of the Company's ability to continue as a going concern and to raise sufficient funds to pay for its ongoing operations expenditures, meets its liabilities for the ensuing year, involve significant judgment based on historical experience and other factors including expectation of future events that are believed to be reasonable under the circumstances.

5 Trade and other receivables

	2018 $	2017 $
Trade receivables	4,282,399	2,760,659
Contract assets	1,917,919	-
Other receivables	1,096,687	1,462,159
Less: Allowance for expected credit loss (for doubtful accounts in 2017)	(431,674)	(89,559)
Trade and other receivables - net	6,865,331	4,133,259

Trade and other receivables are pledged as security for the credit facilities (see Notes 9 and 10)
Other receivables include $ 17,869 owed by an officer.

Note 28 includes disclosures relating to the credit risk exposure and analysis relating to the allowance for expected credit losses. Comparative refers to the IAS 39 measurement basis when applied an incurred loss model, whereas the current year applies IFRS 9 which uses an expected loss model.

6 Inventories

	2018 $	2017 $
Raw materials	2,298,807	1,381,780
Work in progress	1,040,735	581,612
Inventories	3,339,542	1,963,392

Cost of goods sold includes cost of inventories amounting to $7,209,080 in 2018 ($5,153,437 in 2017). During the current year, a reversal of a previous inventory write-down amounting to $144,442 ($189,065 in 2017) was recognized in inventory as the Company deems these parts recoverable for future orders. Inventories are pledged as security for the credit facilities (see Notes 9 and 10).

7 Property, plant and equipment

	Machinery and Equipment [1] $	Office furniture and equipment $	Computers [1] $	Moulds $	Vehicles $	Leasehold Improvement $	Total $
Cost							
Balance at December 31, 2016	577,892	147,712	270,845	166,577	35,984	-	1,199,010
Additions	5,431	6,951	13,728	-	-	-	26,110
Effect of movements in exchange rates	(3,192)	(1,761)	550	(103)	-	-	(4,506)
Balance at December 31, 2017	580,131	152,902	285,123	166,474	35,984	-	1,220,614
Additions	7,708	-	118,795	-	-	20,450	146,953
Disposals	-	-	(58,195)	-	-	-	(58,195)
Effect of movements in exchange rates	8,422	3,003	4,530	2,837	-	-	18,792
Balance at December 31, 2018	596,261	155,905	350,253	169,311	35,984	20,450	1,328,164
Accumulated depreciation							
Balance at December 31, 2016	381,738	128,906	249,450	128,394	35,984	-	924,472
Depreciation	46,208	9,154	15,224	16,998	-	-	87,584
Effect of movements in exchange rates	(72)	(387)	510	(125)	-	-	(74)
Balance at December 31, 2017	427,874	137,673	265,184	145,267	35,984	-	1,011,982
Depreciation	38,974	9,065	14,927	13,386	-	2,337	78,689
Accumulated depreciation of assets disposed	-	-	(58,195)	-	-	-	(58,195)
Effect of movements in exchange rates	4,160	2,871	4,002	2,837	-	-	13,870
Balance at December 31, 2018	471,008	149,609	225,918	161,490	35,984	2,337	1,046,346
Carrying Amount							
At December 31, 2017	152,257	15,229	19,939	21,207	-	-	208,632
At December 31, 2018	125,253	6,296	124,335	7,821	-	18,113	281,818

Depreciation of $78,689 (2017 – $87,584) is included in the consolidated statement of income (loss) for the year ended December 31, 2018: $55,161 (2017 – $67,966) in cost of goods sold; and $23,528 (2017 – $19,618) in selling and administrative expenses.

Property, plant and equipment are pledged as security for the credit facilities (see Notes 9 and 10)

1 including equipment under finance lease. The cost of equipment under finance lease amount to $58,051 ($54,294 in 2017) and the accumulated depreciation amount to $14,454 ($4,883 in 2017).

8 Intangible assets

	Other	Internally generated		
	Software $	Development costs $	Engineering standardisation $	Total intangible assets $
Cost				
Balance at December 31, 2016	327,192	298,975	-	626,167
Additions	-	2,084	306,618	308,702
Effect of movements in exchange rates	10,203	-	-	10,203
Balance at December 31, 2017	337,395	301,059	306,618	945,072
Additions	-	-	139,290	139,290
Receipt of R&D tax credit	-	-	(13,634)	(13,634)
Effect of movements in exchange rates	5,039	-	-	5,039
Balance at December 31, 2018	342,434	301,059	432,274	1,075,767
Accumulated amortization				
Balance at December 31, 2016	286,990	148,434	-	435,424
Amortization for the year	20,629	59,696	-	80,325
Effect of movements in exchange rates	10,927	33	-	10,960
Balance at December 31, 2017	318,546	208,163	-	526,709
Amortization for the year	15,313	60,212	63,554	139,079
Effect of movements in exchange rates	4,502	-	-	4,502
Balance at December 31, 2018	338,361	268,375	63,554	670,290
Carrying amount				
At December 31, 2017	18,849	92,896	306,618	418,363
At December 31, 2018	4,073	32,684	368,720	405,477

Amortization of $139,079 (2017 – $80,325) is included in the consolidated statement of income (loss) for the year ended December 31, 2018: $72,609 (2017 – $20,213) in cost of goods sold; and $66,470 (2017 – $60,112) in selling and administrative expenses.

9 Bank loan

The Company has access to credit facilities in the amount of $2,000,000 with National Bank of Canada which are guaranteed by Export Development Canada at 75%, and bear interest at the Canadian Prime Rate plus 2.75%, per annum and are limited by certain margin requirements concerning trade and other receivables and inventories. No credit facilities were used as at December 31, 2018 (2017 – $ NIL).

The credit facilities are secured by a first ranking hypothec of $2,100,000 on all movable property of the Company.

As of December 31, 2018, the company has a guarantee facility of $12,000,000 with National Bank of Canada sponsored at 100% by Export Development Canada. Stand by fees at an annual rate of 0.75% is calculated on the unused portion of this operating credit. As at December 31, 2018, three guarantee facilities are used for a total of $ 1,784,216 one of which is an ongoing facility of $ 337,994 with Toronto-Dominion Bank of Canada.

10 Credit Facility

On December 12, 2016, the Company contracted a facility loan with Export Development Canada ("EDC") for an amount of $2,000,000. This amount is available in four advances. The facility bears an interest of prime rate plus 6.3% (9.75%) (9.5% in 2017). This interest is payable every month. This amount shall be repaid based on the completion of certain project milestones.

The facility loan is secured by a second ranking hypothec in all present and future movable property of the Company.

The following table summarizes the activity related to the facility with EDC during the period ended:

	2018 $	2017 $
Balance – Beginning of year,	1,437,912	-
Addition	-	2,000,000
Repayment	(1,437,912)	(562,088)
Balance – End of year,	-	1,437,912

11 Trade, other payables and accrued liabilities

	2018 $	2017 $
Trade payables	1,726,384	2,741,565
Accrued liabilities	868,297	723,441
Payables to related parties (Note 25)	-	29,310
Other payables	88,243	91,439
Trade, other payables and accrued liabilities	2,682,924	3,585,755

12 Contract balances

Contract assets

	2018 $	2017 $
Cost incurred and recorded margins	8,416,984	-
Less: advances and progress billing	(6,499,065)	-
	1,917,919	-

Contract assets are included in trade and other receivables in the financial statements and Note 5 (information not available for 2017)

Contract liabilities

	2018 $	2017 $
Advances and progress billings	8,613,690	4,440,708
Less: cost incurred and recorded margin	(4,243,047)	(3,719,712)
	4,370,643	720,996

13 Long-term debt and government royalty program obligation

a) Long-term debt

	2018 $	2017 $
Obligation under a capital lease, repayable in monthly instalments of $1,607 including interest calculated at 13% maturing in October 2018, secured by equipment under finance lease.	-	18,669
Obligation under a capital lease, repayable in monthly instalments of $352 including interest calculated at 12% maturing in September 2020, secured by equipment under finance lease.	6,908	10,475
Unsecured Convertible debentures	1,774,076	2,216,570
Obligation under a working capital line, bearing an interest rate of 11% per annum, maturing in July 2021 [2]	1,899,578	-
Long-term debt	3,680,562	2,245,714
Current portion	(1,777,915)	(22,236)
	1,902,647	2,223,478

[2] The Obligation under a working capital line, has been recorded at its fair value less transactions costs directly attributable to its acquisition. Transaction costs are being amortized over the duration of the obligation with a face value of $2,000,000 at maturity.

On November 16, 2017, the Company has completed an Unsecured Convertible Debentures ("Debentures") financing for aggregate gross proceeds of $2,024,149. The Debentures will reach maturity on November 15, 2019 and bearing an annual interest rate of 8%, convertible into common shares of the Company at a price of $0.65 per share. The unpaid interests are convertible at the highest price of $0.65 per common share or the fair value of the common share at the request of the debenture holder.

The Company used the residual value method to allocate the principal amount of the Debenture between the liability and the equity component. Under this method, the value of the equity component of $186,177 (net of deferred tax liability of $81,989) was determined by deducting the fair value of the liability component from the principal amount of the financing. The fair value of the liability component was $1,626,594 computes as the present value of future principal and interest payments discounted at a rate of 17.50%. The effective interest method is used to measure the Debenture after the initial recognition.

On November 30, 2016, the Company has completed an Unsecured Convertible Debentures ("Debentures") financing for aggregate gross proceeds of $1,000,000. The Debentures will reach maturity on November 30, 2019 and bearing an annual interest rate of 9%, convertible into common shares of the Company at a price of $0.15 per share. The unpaid interests are convertible at the highest price of $0.15 per common share or the fair value of the common share at the request of the debenture holder.

The Company used the residual value method to allocate the principal amount of the Debenture between the liability and the equity component. Under this method, the value of the equity component of $150,304 (net of deferred tax liability of $59,316) was determined by deducting the fair value of the liability component from the principal amount of the financing. The fair value of the liability component was $790,380 computes as the present value of future principal and interest payments discounted at a rate of 19.50%. The effective interest method is used to measure the Debenture after the initial recognition.

During the year, 4,766,665 common shares were issued as a result of the exercise of the conversion option by some of the debenture holders. From this amount, 4,666,665 common shares belong to the Debentures completed on November 30, 2016 and at December 31, 2018 all its conversion options have been exercised. The balance of 100,000 common shares comes from the Debentures completed on November 16, 2017. The common shares issued included the carrying value of the liability component to the date of conversion. The conversion is a non-cash transaction and thus is excluded from the consolidated statement of cash flows.

On July 23, 2018, the Company obtained $23 million of additional financial support from Export Development Canada (EDC), Canada's export credit agency. The financial support consists of a $12 million letter of guarantee facility with EDC, which will be used to support the issuance of multiple bank guarantees. The letter of guarantee facility bears an interest at the rate of at the Canadian Prime Rate of the Bank plus 2.50% per annum, payable every month. Stand-by fees at an annual rate of 0.75% calculated on the unused portion of the letter of guarantee facility shall be payable monthly. Two credit facilities of $11 million, with a three-year term, consisting of a $2

million working capital line and a $9 million Purchase Order (PO) facility. The credit facilities and the three-year term bear an interest at the rate of 11% per annum, payable every month.

The financial support is secured by a first ranking hypothec in all present and after acquired inventory and accounts receivables related to contracts.

b) Government royalty program obligation

In 2012, the Company signed a settlement agreement with Technology Partnership Canada (TPC) with regard to the Company's Fast Cycle Pressure Swing Adsorption and Gas Management systems and Pulsar Pressure Swing Adsorption project. The Company had to pay $250,000 at the execution of the agreement and $1,000,000 spread over four equal annual non-interest-bearing payments, starting on January 31, 2013. Furthermore, the Company was liable to pay up to $750,000 in contingent payments based on proceeds from the sale by the Company of its intellectual property. Upon closing of the transaction, the Company paid $540,000 out of the $750,000 total contingent-based payments. On October 23, 2012, the Company accrued another $150,000 out of the $750,000 total contingent based payments, following additional proceeds received, leaving a potential maximum amount to be paid of $60,000 as at December 31, 2012.

In 2013, the Company realized the last milestone pursuant to the transaction and paid the remaining $60,000. The Company renegotiated its payments terms with TPC, changing from an annual payment of $250,000 to monthly payments of $24,500 but adding an extra year to term.

In February 2017, a new amendment to this agreement was reached changing the preceding payments terms from monthly payments of $24,500 to monthly payments of:

- $29,505 upon execution including interest
- $5,000 starting from March 1, 2017 to January 1, 2018
- $7,000 starting from February 1, 2018 to January 1, 2019
- $8,000 starting from February 1, 2019 to January 1, 2020
- $10,000 starting from February 1, 2020 to January 1, 2021
- $15,000 starting from February 1, 2021 to October 1, 2022
- $20,000 on November 1, 2022 and December 1, 2022
- And the balance of $22,540 on January 1, 2023.

The following table summarizes the activity related to the government royalty program obligation during the period ended:

	2018 $	2017 $
Balance – Beginning of year,	591,372	757,540
Gain on revaluation of government royalty program	-	(117,095)
Accretion finance expenses	27,401	25,927
Repayment	(82,000)	(75,000)
Balance – End of year,	536,773	591,372
Current portion	(100,515)	(86,826)
	436,258	504,546

The carrying amount of the government royalty program obligation has been calculated by discounting the future cash flows at a 5% interest rate.

14 Provisions

	2018 $	2017 $
Balance – Beginning of the year	22,290	218,059
Provision for the year	33,309	-
Used during the year	-	(195,769)
Balance – End of year,	55,599	22,290
Current portion of provision	15,275	16,689
Non- Current provision	40,324	5,601

Warranty cost

The company offers warranties 18 months after shipping or 12 months after start-up to the purchasers of its gas purification and natural gas dryers.

15 Obligation arising from shares issued by subsidiary

In September 2015, as a result of a Sino-foreign equity joint venture agreement, Xebec Adsorption (Shanghai) Co. Ltd., a subsidiary of Xebec Adsorption Inc. (“Xebec”), issued 1,714,285 common shares, representing a 30% participation, to Shanghai Chengyi New Energy Venture Capital Co. Ltd. (28.26%), an investment subsidiary of Shanghai based Shenergy Group, Shanghai Zhiyi Enterprise Management Consulting Co. Ltd. (0.1%) and Shanghai Liuhuan Investment Co. Ltd. (1.64%), a company held by a group of employees of Xebec Adsorption (Shanghai) Co. Ltd., (collectively the “Minority Shareholders”) for a net cash consideration of $3,423,075 (RMB 16,370,515).

Pursuant to this agreement, Xebec has the obligation to repurchase the Minority Shareholders' interest in Xebec Adsorption (Shanghai) Co. Ltd., for a consideration of no less than the initial investment and annualized return of 10% if a) the achievement of specific financial targets were not achieved in any given year prior to December 31, 2020, or b) should the Minority Shareholders not divest by December 31, 2020 and should the Minority Shareholders exercise their put option with respect to a) or b) as mentioned above.

On July 24, 2018, the Minority Shareholders of Xebec Adsorption (Shanghai) Co. Ltd. and Xebec Adsorption Inc. agreed that Xebec Adsorption Inc. will pay the Minority Shareholders $198,300 (RMB 1 million) per year including 2018 until the EDC loan expiry or latest up to December 31, 2020 (whichever is earlier). Xebec Adsorption Inc. will also fulfill its repurchase obligation according to the original agreement, by paying the full repurchase price in one lump sum either at EDC loan expiry or latest by December 31, 2020. The 2018 annual fee was paid in the fourth quarter of 2018. The annual fees will be considered a deduction to the repurchase price at the time of repurchase.

On July 25, 2018, the Minority Shareholders of Xebec Adsorption (Shanghai) Co. Ltd, agreed that, for a period beginning on the date hereof up to the date that Export Development Canada has been repaid in full (including capital, interests and fees) under the EDC Financing Arrangement, it shall not exercise any of its divestment, refund, compensation and other equity repurchase rights.

Xebec recorded the proceeds from this transaction, as a financial liability in these consolidated financial statements. The obligation to repurchase and the related annualized return is presented under "Obligation arising from shares issued by a subsidiary". The conversion of the financial liability denominated in the functional currency of our subsidiary Xebec Adsorption (Shanghai) Co. Ltd. (RMB) will be converted at the exchange rate at the end of each reporting period with gain and losses presented in the statement of income (loss) under "Gain/Loss on conversion of shares issued by a subsidiary".

	2018 $	2017 $
Balance – Beginning of year	3,912,314	3,582,135
Accretion interest	339,249	332,537
Effect of exchange rate change on obligation	116,090	(2,358)
Annual reimbursement	(198,300)	-
Balance – End of year	4,169,353	3,912,314
Current Portion	(198,300)	-
	3,971,053	3,912,314

16 Share Capital

a) The Company is incorporated under the Canada Business Corporations Act, and its authorized share capital consists of an unlimited number of common shares, without par value.

b) On November 7, 2018 the Company closed a short form prospectus offering through a syndicate of agents. In connection with the closing of the Offering, the Company issued a total of 8,208,666 Units, at a price of $0.75 per Unit, for aggregate gross proceeds of $6,156,500.

On November 30, 2018 the Company closed the Over-Allotment of an additional 1,231,300 units for additional gross proceeds of $923,475.

Each Unit is comprised of one common share of the Company and one half of one common share purchase warrant. Each Warrant entitles the holder thereof to purchase one Common Share, at a price of $1.05 per Common Share, for a period of 18 months from the closing date of the Offering.

In connection with the Offering, the Company paid to the Agents a cash commission equal to 6% of the gross proceeds of the Offering, including the proceeds raised pursuant to the exercise of the Over-Allotment Option. The Company also granted the Agents non-transferable options entitling the Agents to purchase 566,398 Common Shares. (Equal to 6% of the aggregate number of Units issued by the Company under the Offering). Each such Compensation Option entitling the holder thereof to acquire one Common Share at an exercise price of $0.75 for a period of 18 months from the closing date of the Offering. The fair value of the 566,398 warrants was $166,472.

A total of 9,439,966 units were issued under the offering at a price of $0.75 per unit for aggregate gross proceeds of $7,079,975. The issuance costs, excluding the non transferable options to the agents were $1,095,287. For a total of 9,439,966 shares and 4,719,983 warrants. The amount attributed to the warrants was $24,626. For 4,104,333 warrants, no value was attributed because the share price was higher than $0.75. For 615,650 warrants, an amount of $0.02 per share was allocated to warrants.

c) Income (loss) per share

i) Basic

Basic income (loss) per share is calculated using net income (loss) as the numerator and the weighted average number of shares as denominator. No adjustments to net income were necessary in 2018 and 2017.

	2018 **$**	**2017** **$**
Net income (loss) attributable to shareholders of the Company	(2,904,386)	96,752
Weighted average number of shares used in basic income per share	42,737,000	40,562,060
Basic income (loss) per share	(0.07)	0.002

ii) Diluted

For the year ended December 31, 2018, convertible debentures and outstanding stocks options would have been anti-dilutive.

For the year ended December 31, 2017, convertible debentures and outstanding stock options with an average exercise price of over $0.40 would have been anti-dilutive.

The reconciliation of the weighted average number of shares for the purpose of diluted income per share to the weighted average number of shares used in the calculation of basic income per share is as follows:

	2017
Weighted average number of shares used in basic income per share	40,562,060
Shares deemed to be issued for no consideration in respect of share-based payments	4,674,896
Weighted average number of shares used in diluted income per share	45,236,956

17 Stock options

The stock option plan allowed for the issuance of stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards and other stock-based awards. Under the Plan, a fixed number of 8,500,873 common shares are available for grant. As at December 31, 2018, the maximum number of common shares available for issuance under all stock-based compensation arrangements is 2,199,115

Under the terms of the Xebec Adsorption Stock Option Plan, stock options are granted with an exercise price not less than the volume-weighted average trading price of the common shares for the five trading days prior to the date of grant. The terms and conditions for acquiring and exercising options are set by the Board of Directors. Stock options for employees vest no less than at grant date and no more than quarterly.

Stock option activity for the year ended December 31, is presented below:

		2018		2017
	Number of options	**Weighted average exercise price $**	**Number of options**	**Weighted average exercise price $**
Outstanding – Beginning of year,	7,829,030	0.19	5,855,337	0.11
Granted	835,000	0.69	3,119,193	0.20
Exercised	(307,272)	0.17	(1,140,500)	0.05
Cancelled	(2,020,000)	0.12	(5,000)	0.22
Expired	(35,000)	0.22	-	-
Outstanding – End of year,	6,301,758	0.27	7,829,030	0.19
Exercisable – End of year,	4,511,231	0.16	5,804,837	0.13

The average share price for the exercised options was $0.17 ($0.05 in 2017)

(expressed in Canadian dollars)

As at December 31, 2018, options outstanding and exercisable are as follows:

Expiry date	Weighted-Average Exercise Price	Number of Options Outstanding	Weighted-Average Remaining life	Number of Options exercisable
December 22, 2018 [3]	$0.10	1,399,500	0.00	1,399,500
June 12, 2020	$0.16	258,065	1.45	258,065
April 25, 2021	$0.15	100,000	2.32	100,000
May 29, 2021	$0.14	200,000	2.41	200,000
December 19, 2022	$0.55	400,000	3.97	133,332
January 7, 2023	$0.05	400,000	4.02	400,000
March 5, 2024	$0.18	2,098,193	5.18	1,883,332
August 29, 2024	$0.49	500,000	5.66	100,000
December 19, 2024	$0.55	111,000	5.96	37,002
May 14, 2025	$0.60	100,000	6,37	-
November 19, 2025	$0.70	735,000	6.89	-
	$0.27	**6,301,758**	**3.86**	**4,511,231**

As at December 31, 2017 options outstanding and exercisable are as follows:

Expiry date	Weighted-Average Exercise Price	Number of Options Outstanding	Weighted-Average Remaining life	Number of Options exercisable
August 11, 2018	$0.22	232,272	0.6	232,272
December 22, 2018	$0.10	1,519,500	1.0	1,519,500
June 12, 2020	$0.16	258,065	2.4	258,065
April 25, 2021	$0.15	100,000	3.3	100,000
May 29, 2021	$0.14	200,000	3.4	200,000
September 22, 2021	$0.12	2,000,000	3.7	2,000,000
December 19, 2022	$0.55	400,000	5.0	-
January 8, 2023	$0.05	400,000	5.0	400,000
March 5, 2024	$0.18	2,108,193	6.2	1,095,000
August 29, 2024	$0.49	500,000	6.7	-
December 19, 2024	$0.55	111,000	7.0	-
	$0.19	**7,829,030**	**4.1**	**5,804,837**

[3] Expiry date of the options fell in a black out period. Options will be available for exercise once blackout period has been lifted.

On May 14, 2018, the Company granted 100,000 stock options to an employee. The options are exercisable at $0.60 per share and expire on May 14, 2025. The options are subject to vesting criteria such that 33% shall vest on the first anniversary date and 33% shall vest every twelve months thereafter. The corresponding stock-based compensation amounted to $55,701, which was estimated using the Black-Scholes Option Pricing Model with the following assumptions:

Risk-free interest rate	2.30%
Annualized volatility [4]	133%
Share price	$0.60
Dividend rate	0.00%
Expected life of options	7 years

On November 19, 2018, the Company granted 735,000 stock options to an officer. The options are exercisable at $0.70 per share and expire on November 19, 2025. The options are subject to vesting criteria such that 33% shall vest on the first anniversary date and 33% shall vest every twelve months thereafter. The corresponding stock-based compensation amounted to $480,521, which was estimated using the Black-Scholes Option Pricing Model with the following assumptions:

Risk-free interest rate	2.47%
Annualized volatility [4]	129%
Share price	$0.70
Dividend rate	0.00%
Expected life of options	7 years

During the year, the Company expensed $352,897 (2017 - $372,603) which totally relates to stock options granted in 2017 and 2018.

On March 5, 2017, the Company granted 2,108,193 stock options to directors, officers and employees. The options are exercisable at $0.18 per share and expire on March 5, 2024. The options are subject to vesting criteria such that 1,095,000 shall vest on the grant date, 795,000 shall vest on March 5, 2018 and 218,193 shall vest on March 5, 2019. The grant of these stock options was conditional to the approval of the increase of the pool of the stock options of the Company by the shareholders at the Annual General Meeting and the TSX Venture Exchange. These approvals were obtained respectively on June 15, 2017 and August 9, 2017. The corresponding stock-based compensation amounted to $354,118, which was estimated using the Black-Scholes Option Pricing Model with the following assumptions:

[4] The expected volatility used was based on the historic volatility of the Company share price.

Risk-free interest rate	1.55%
Annualized volatility [4]	137%
Share price	$0.18
Dividend rate	0.00%
Expected life of options	7 years

On August 29, 2017, the Company granted 500,000 stock options to an employee. The options are exercisable at $0.49 per share and expire on August 29, 2024. The options are subject to vesting criteria such that 20% shall vest on the first anniversary date and 20% shall vest every twelve months thereafter. The corresponding stock-based compensation amounted to $227,026, which was estimated using the Black-Scholes Option Pricing Model with the following assumptions:

Risk-free interest rate	1.80%
Annualized volatility [4]	138%
Share price	$0.49
Dividend rate	0.00%
Expected life of options	7 years

On December 19, 2017, the Company granted 511,000 stock options to directors. The options are exercisable at $0.55 per share. 400,000 expire on December 19, 2022 and 111,000 expire on December 19, 2024. The options are subject to vesting criteria such that 33% shall vest on the first anniversary date and 33% shall vest every twelve months thereafter. The corresponding stock-based compensation amounted to $252,250, which was estimated using the Black-Scholes Option Pricing Model with the following assumptions:

Risk-free interest rate	1.57%
Annualized volatility [4]	140%
Share price	$0.55
Dividend rate	0.00%
Expected life of options	5 years

and,

Risk-free interest rate	1.77%
Annualized volatility [4]	*138%*
Share price	$0.55
Dividend rate	0.00%
Expected life of options	7 years

In 2017, 2,808,193 options were granted to employees at weighted average fair value of $0.26 and 311,000 options were granted to non-employees at a weighted average fair value of $0.55

18 Expenses by nature

	2018 $	2017 $
Material	7,213,460	5,457,118
Employee salaries and benefits	7,023,186	5,521,600
Subcontract cost	2,930,882	867,993
Professional fees	1,390,407	818,272
Travel expenses	759,616	658,667
Rent and repairs and maintenance	692,548	700,393
Office expense	481,062	239,660
Stock-based compensation	352,897	372,603
Bad Debt	347,591	(8,873)
Amortization and depreciation	217,768	167,908
Advertising	217,259	114,144
Other	108,978	(96,193)
Reversal of trade payables	-	(303,363)
Reversal of allowance for doubtful accounts	-	(315,145)
	21,735,654	14,194,784

19 Research and development expenses

	2018 $	2017 $
Employee salaries and benefits	65,157	25,212
Professional fees	14,230	10,848
Subcontract cost	12,500	11,844
Travel expenses	182	502
Material	-	23,884
Government grants	-	(2,083)
Research and development tax credits	-	(29,663)
Reversal of trade payables	-	(71,658)
	92,069	(31,114)

20 Finance expenses

	2018 $	2017 $
Accretion of the obligation arising from shares issued by a subsidiary (Note 15)	339,249	332,537
Interest on convertible debentures	415,590	197,228
Interest and bank charges	312,495	191,093
Interest on short term debt	116,770	186,802
Accretion and revaluation of government royalty program obligation (Note 13b)	27,401	25,927
Interest on long term debt	111,657	203
Reversal of trade payables	-	(322,638)
	1,323,162	611,152

21 Compensation of key management

Compensation awarded to key management included:

	2018 $	2017 $
Salaries and short-term employee benefits	1,351,103	1,256,164
Stock-based compensation	235,374	318,922
Consulting	112,675	-
	1,699,152	1,575,086

Key management included the Company’s senior management and members of the Board of Directors.

22 Income taxes

Effective tax rate

The income tax expense attributable to earnings differs from the amounts computed by applying the combined federal and provincial tax rate of 26.7% (26.8% on December 31, 2017) to earning before income taxes as a result of the following:

	2018 $	2017 $
Income (loss) before income taxes	(2,904,386)	96,752
Expected income tax (recovery)	(775,471)	25,930
Tax expense at combines statutory rate	-	-
Increase (decrease) in income taxes resulting from:	-	-
Temporary difference unrecognized (recognized)	733,356	(412,952)
Difference in foreign tax rate	(787)	(19,557)
Stock base compensation	94,223	99,858
Change of deferred tax rates	(170,871)	108,285
Foreign exchange on consolidation	18,779	854
Expired losses	141,334	67,007
Other	(40,563)	130,575
	-	-

Composition of deferred income taxes in the Consolidated Statement of Income (Loss)

	2018 $	2017 $
Inception and reversal of temporary differences	(562,485)	304,667
Temporary difference not recorded	733,356	(412,952)
Change in deferred tax rate	(170,871)	108,285
	-	-

Movement of deferred income tax in 2018

	January 1, 2018 $	P&L $	Equity Component $	December 31, 2018 $
Contingency reserve	(81,989)	-	-	(81,989)
Intangible assets	(49,974)	(509)	-	(50,483)
Debentures	(98,821)	76,343	-	(22,478)
Government royalty program	(24,160)	7,262	-	(16,898)
Non-capital losses	172,955	(83,096)	-	89,859
	(81,989)	-	-	(81,989)

Movement of deferred income tax in 2017

	January 1, 2017 $	P&L $	Equity Component $	December 31, 2017 $
Contingency reserve	-	(81,989)	-	(81,989)
Intangible assets	-	(49,974)	-	(49,974)
Debentures	(53,975)	37,143	(81,989)	(98,821)
Government royalty program	-	(24,160)	-	(24,160)
Non-capital losses	53,975	118,980	-	172,955
	-	-	(81,989)	(81,989)

As at December 31, 2018, deductible timing differences for which the company has not recognized deferred tax asset are as follows:

	Federal $	Quebec $	China $	USA $	Italy $
Property and equipment	1,050,119	1,050,119	-	-	-
Scientific research and development expenses	24,706,785	24,711,456	-	-	-
Operating losses carried forward	56,508,935	58,360,534	1,630,298	274,812	540,767
Other	1,313,097	1,313,097	-	-	-
	83,578,936	85,435,206	1,630,298	274,812	540,767

The ability to realize the tax benefits is dependent upon a number of factors, including the future profitability of operations. Deferred tax assets are recognized only to the extent that it is probable that sufficient taxable profits will be available to allow the asset to be recovered. Accordingly, some deferred tax assets have not been recognized, these deferred tax assets not recognized equal an amount of $ 22,975,885 ($22,191,258 in 2017).

As at December 31, 2017, deductible timing differences for which the company has not recognized deferred tax asset are as follows:

	Federal $	Quebec $	China $	USA $	Italy $
Property and equipment	995,217	995,217	-	-	-
Scientific research and development expenses	24,583,744	24,587,643	-	-	-
Capital losses carried forward	219,247	219,247	-	-	-
Operating losses carried forward	54,175,945	56,733,006	1,434,206	708,665	49,800
Other	688,795	688,795	-	-	-
	80,662,948	83,223,908	1,434,206	708,665	49.800

As at December 31, 2018, the Company has non-capital tax losses, which are available to reduce taxes in futures years and expired as follows:

	Federal $	Quebec $	China $	USA $	Italy $
2038	1,317,958	1,296,110	-	-	-
2037	-	-	-	269,292	-
2036	1,486,941	1,480,325	-	-	-
2035	1,328,532	1,328,532	-	5,520	-
2034	-	2,635,090	-	-	-
2033	326,251	326,251	-	-	-
2032	546,237	494,621	-	-	-
2031	443,287	433,086	-	-	-
2030	12,361,610	12,361,610	-	-	-
2029	7,283,831	7,295,856	-	-	-
2028	10,824,277	10,824,277	-	-	-
2027	6,794,635	6,794,635	-	-	-
2026	7,229,354	7,229,354	-	-	-
2025	6,566,022	5,860,787	-	-	-
2024	-	-	-	-	-
2022	-	-	720,513	-	-
2021	-	-	909,785	-	-
Unlimited	-	-	-	-	540,767
	56,508,935	58,360,534	1,630,298	274,812	540,767

The Company has scientific research and experimental development expenses of $24,706,785 (2017 – $24,583,744) which are available to be carried forward indefinitely and deducted against future taxable income otherwise calculated. The potential benefit has not been recorded in the accounts.

As at December 31, 2018, the Company also has investment tax credits of $5,591,036 (2017 – $5,678,183) available to offset future Canadian federal income taxes payable. The potential benefit of the investment tax credits has not been recognized in the accounts.

23 Supplemental Cash flow information

For the year ended December 31, net change in non-cash working capital balances related to operations consists of the following:

	2018 **$**	**2017** **$**
Decrease (increase) in assets:		
Trade and other receivables	(2,732,073)	(1,368,673)
Inventories	(1,231,708)	(444,811)
Investment tax credits receivable	-	32,010
Other current assets	(587)	(71,861)
Increase (decrease) in liabilities:		
Trade payables, other payables and accrued liabilities	(902,831)	660,157
Contract liabilities	3,649,648	(221,579)
Provisions	33,310	(195,769)
	(1,184,241)	(1,610,526)

24 Commitments

- Research Agreement with McGill University

  In August 2018, Xebec Adsorption Inc. ("Xebec"), has signed a Research Agreement to co-develop a prototype reactor to produce Renewable Natural Gas (RNG) using a Power-to-Gas (P2G) process with McGill University. This process combines electricity generated from renewable sources with carbon dioxide (CO2) generated from waste. The project is being funded by Xebec as the Industrial sponsor and by the Natural Sciences and Engineering Research Council of Canada (NSERC) through a Collaborative Research and Development grant of $360,000 over a period of three years.

  In consideration of McGill carrying out the Project, Xebec is committed to fund the Project with $90,000 over the period of three years. The funds will be paid in accordance with the following schedule:

  i. $30,000 upon signing
  ii. $30,000 upon the first anniversary of the Effective Date
  iii. $30,000 upon receiving the final report.

- Following is a summary of Xebec's contractual obligations and commitments regarding operating leases:

As at December 31, 2018	**Payment Due by Period**			
	1 year	2 - 5 years	Beyond 5 years	Total
	$	$	$	$
Operating leases	554,981	1,565,606	1,080,139	3,200,726

Operating leases include one building in Blainville, Quebec, one building in Shanghai, China, and various equipment leases. The operating leases expenses for the year ended December 31, 2018 amounted to $442,784 ($440,519 in 2017)

25 Related party transactions

The following table presents a summary of the related party transactions during the period:

	2018	**2017**
	$	**$**
Marketing and professional services expenses paid to companies controlled by members of the immediate family of an officer	183,432	158,900

These transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

26 Capital management

The Company's objective when managing capital is to use short-term funding sources to manage its working capital requirements and fund capital expenditures required to execute its operating and strategic plans.

The Company's capital structure is composed of the following:

	2018 $	2017 $
Cash	(2,382,146)	(1,341,121)
Restricted cash	(1,540,000)	
Bank loan	-	-
Credit facility	-	1,437,912
Long-term debt	3,680,562	2,245,714
Government royalty program obligation (Note 13 b)	536,773	591,372
Obligation arising from shares issued by a subsidiary (Note 15)	4,169,353	3,912,314
	4,464,542	6,846,191
Equity	(620,374)	(4,390,290)
	3,844,168	2,455,901

The Company is not subject to any capital requirements imposed by regulators.

27 Segmented information

The Company has four business segments and specializes in the Industrial Air and Gas Products, the Clean Technology, the Renewable Gas Generation and the Oil and Gas.

For the year ended December 31, revenue summarized by country, as determined by location of the customers, is as follows:

	2018 $	2017 $
Revenue		
United States	6,816,590	3,174,092
Canada	4,800,012	4,028,670
France	2,655,914	4,022,726
Italy	2,469,183	-
China	1,889,742	2,405,773
Other	1,577,055	1,114,670
	20,208,496	14,745,931

Sales of $6,740,569 ($ 2,417,498 in 2017) arose from the two (one in 2017) Company's largest customers. No other single customer contributed more than 10 % to the company's revenue for both 2018 and 2017.

Incomes (losses) summarized by business segments are as follows:

For the year ended December 31, 2018

	Systems	Support	Infrastructure [5]	Oil and Gas [6]	Corporate	Total
	$	$	$	$	$	$
Revenues	14,022,914	6,085,430	-	100,152	-	20,208,496
COGS	10,462,581	4,057,573	-	-	-	14,520,154
Gross margin	3,560,333	2,027,857	-	100,152	-	5,688,342
Gross Margin %	25%	33%	-	100%	-	28%
		-				
Research and Development expenses	92,069	-	-	-	-	92,069
Selling and administrative expenses	1,397,270	944,663		-	4,873,567	7,215,500
Foreign exchange loss	-	-	-	-	(152,482)	(152,482)
Loss on conversion of shares issued by a subsidiary	-	-	-	-	116,090	116,090
Financial income	-	-	-	-	(1,611)	(1,611)
Financial expense	-	-	-	-	1,323,162	1,323,162
Total expenses	1,489,339	944,663	-	-	6,158,726	8,592,728
Segment income (loss)	2,070,994	1,083,194	-	100,152	(6,158,726)	(2,904,386)

[5] Infrastructure segment is a project in development that will start in 2019. No costs have been associated to the segment as of December 31st, 2018.

[6] The Oil and Gas segment is been phased out to allow the Company to develop new Infrastructure segment.

For the year ended December 31, 2017

	Systems	Support	Infrastructure	Oil and Gas	Corporate	Total
	$	$	$	$	$	$
Revenues	8,902,695	4,457,380	-	1,385,856	-	14,745,931
COGS	6,180,724	2,794,488	-	2,497	-	8,977,709
Gross margin	2,721,971	1,662,892	-	1,383,359	-	5,768,222
Gross Margin %	31%	37%	-	100%	0%	39%
		-				
Research and Development expenses	(31,114)	-	-	-	-	(31,114)
Selling and administrative expenses	933,784	805,745		285,775	3,191,771	5,217,075
Insurance compensation for damage to inventories					(132,366)	(132,366)
Foreign exchange loss	-	-	-	-	131,149	131,149
Gain on conversion of shares issued by a subsidiary	-	-	-	-	(2,358)	(2,358)
Financial income	-	-	-	-	(122,068)	(122,068)
Financial expense	-	-	-	-	611,152	611,152
Total expenses	902,670	805,745	-	285,775	3,677,280	5,671,470
Segment income (loss)	1,819,301	857,147		1,097,584	(3,677,280)	96,752

The location of the Company's non-current assets by geographic region as of December 31st is as follows:

	2018	2017
	$	$
Non-current assets		
Canada	595,284	520,491
Asia	44,918	66,570
United States	37,343	39,934
Italy	9,750	-
	687,295	626,995

28 Financial instruments

a. Measurement categories and fair values, including valuation methods and assumptions

The following tables show the carrying values and fair values of assets and liabilities by category as of:

December 31, 2018	**Amortized Cost**		**Amortized Cost**	
	Carrying amount $	**Fair value $**	**Carrying amount $**	**Fair value $**
Cash	2,382,146	2,382,146		
Restricted cash	1,540,000	1,540,000		
Trade and other receivables	4,532,122	4,532,122		
Other current assets	13,500	13,500		
Trade, other payables and accrued liabilities			2,054,443	2,054,443
Long-term debt			3,673,654	3,673,654
Government royalty program obligation			536,773	536,773
Obligation arising from shares issued by a subsidiary			4,169,353	4,169,353

December 31, 2017	Loans and receivables		Other financial liabilities	
	Carrying amount $	Fair value $	Carrying amount $	Fair value $
Cash	1,341,121	1,341,121	-	-
Trade and other receivables	3,094,761	3,094,761	-	-
Other current assets	13,500	13,500	-	-
Credit facility	-	-	1,437,912	1,437,912
Trade, other payables and accrued liabilities	-	-	3,032,213	3,032,213
Long-term debt	-	-	2,216,570	2,216,570
Government royalty program obligation	-	-	591,372	591,372
Obligation arising from shares issued by a subsidiary	-	-	3,912,314	3,912,314

The carrying values of cash, restricted cash, trade and other receivables, trade and other payables, accrued liabilities, bank loan and credit facility approximate their fair value due to their short-term maturities. The methods and assumptions used in estimating the fair values of other financial assets and financial liabilities are as follows:

- Long-term debt (classified in level 2 of the fair value hierarchy): The Company's long-term debt carry fixed interest rates. The fair value of the Company's debt obligations has been calculated by discounting the future cash flows of the long-term debt at the interest rate of similar debt instruments.

- Government royalty program obligation (classified in level 2 of the fair value hierarchy): Fair value of the government royalty program obligation has been calculated by discounting the future cash flows at the interest rate for a similar loan in the market.

- Obligation arising from shares issued by a subsidiary (classified in level 2 of the fair value hierarchy): Fair value of the obligation arising from shares issued by a subsidiary has been calculated by computing an annualized return of 10% on the initial consideration

- The Company's financial instruments that are measured subsequent to initial recognition at fair value and financial instruments measured at amortized cost for which the fair value is disclosed are grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

  Level 1 — Fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
  Level 2 — Fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 — Fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

b. Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party fails to meet its contractual obligations. The Company's primary credit risk is its cash, restricted cash and outstanding trade and other receivables. The carrying amount of its outstanding trade and other receivables represents the Company's estimate of its maximum credit exposure.

As of January 1, 2018, the Company determines whether the credit risk of a financial asset has increased significantly since initial recognition considering reasonable and supportable information that is relevant and available without undue cost or effort, this includes both quantitative and qualitative information and analysis, based on the Company's historical experience and informed credit assessment and including forward-looking information.

The Company assumes that the credit risk on a financial asset has increased significantly if it is more than 30 days past due. (120 days past due for the Chinese subsidiary)

The Company considers a financial asset to be in default when the customer is unlikely to pay its credit obligations to the Company in full, without recourse by the Company to actions such as realising security (if any is held) or the financial asset is more that 120 days past due.

Previously, the Company regularly monitored its credit risk exposure and took steps such as employing credit-approval procedures, establishing credit limits, using credit assessments and monitoring practices to mitigate the likelihood of these exposures from resulting in an actual loss.

Bad debt expense amounted to $347,591 in 2018 (recovery in 2017 – $324,018). As at December 31, 2018, the Company's three largest trade debtors accounted for 28% (10%, 9% and 9%) of the total trade receivables balance (2017 – 29% (13%, 9% and 7%)).

Details of trade and other receivables were as follows:

	2018 $	2017 $
Current trade receivables	1,622,324	838,415
Trade receivables past due by:		
1–30 days	1,010,599	470,099
31–60 days	428,050	277,461
61–90 days	175,950	327,850
Over 90 days	1,045,476 [7]	846,834
Total trade receivables	4,282,399	2,760,659
Allowance for expected credit loss (for doubtful accounts in 2017)	(431,674)	(89,559)
Contract Assets	1,917,919	-
Other receivables	1,096,687	1,462,159
Total trade and other receivable	6,865,331	4,133,259

The following table summarizes the changes in the allowance for doubtful accounts for trade and other receivables:

	2018 $	2017 $
Balance - Beginning of year	(89,559)	(448,291)
Change in the allowance for expected credit loss (for doubtful accounts in 2017) (provision for impairment)	(342,115)	324,018
Unused amounts reserved	-	34,714
Balance – end of year	(431,674)	(89,559)

The Company's cash is maintained at financial institutions with high credit ratings; therefore, the Company considers the risk of non-performance on this instrument to be remote. To date, the Company has not incurred any losses related to its cash.

c. Market risk

i. Currency risk

Certain financial assets and financial liabilities are exposed to foreign exchange fluctuations. Taking into account the amounts denominated in the currencies indicated below and assuming that all of the other variables remain unchanged, a fluctuation in exchanges rates would have an impact on the Company's net income (loss). Management believes that a 10% change in exchange rates would be reasonably possible and that the impact on net income (loss) of such a change would be approximately $238,723 for 2018 (2017 – $129,964). As at December 31, 2018, the following

[7] Most of the trade receivables over 90 days belong to the Chinese subsidiary, where it is part of the normal business process to have accounts over 90 days.

accounts are shown in their original currencies and converted into Canadian dollars. The Company does not use financial instruments to reduce this risk.

	2018	
	US dollar	**Euro**
Cash	685,763	341
Trade and other receivables	488,211	66,970
Trade and other payables	477,234	18,931
	1,651,207	86,242
Equivalent in Canadian dollars	2,252,577	134,649

	2017	
	US dollar	**Euro**
Cash	169,728	10,216
Trade and other receivables	612,994	-
Trade and other payables	345,659	(130,472)
	1,128,381	(120,256)
Equivalent in Canadian dollars	1,415,554	(181,010)

ii. Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of financial instruments will fluctuate as market interest rates change.

The Company is exposed to interest rate risk on its credit facility, for which the interest rates charged fluctuate based on the bank's prime rate. As at December 31, 2018, credit facility amounted to $ NIL (2017 – $1,437,912). If the interest rate on the credit facility had been 50 basis points higher (lower), related to the credit facility as at December 31, 2018, net income would have been $10,070 (2017 – $11,218) lower (higher).

d. Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due.

The following are the contractual maturities of financial liabilities and other liabilities as at December 31:

					2018
	Carrying amount $	Contractual cash flow $	0 to 12 months $	13 to 24 months $	Thereafter $
Financial liabilities					
Trade and other payables and accrued liabilities	2,054,443	2,054,443	2,054,443	-	-
Government royalty program obligation	536,773	600,540	95,000	118,000	387,540
Obligation under capital lease	6,908	7,859	4,600	3,259	-
Obligation under a working capital line	1,899,578	2,564,164	219,397	220,000	2,124,767
Convertible debentures	1,774,076	2,109,440	2,109,440	-	-
Obligation arising from shares issued by a subsidiary	4,169,353	4,169,353	198,300	3,971,053	-
	10,441,131	11,505,799	4,681,180	4,312,312	2,512,307

					2017
	Carrying amount $	Contractual cash flow $	0 to 12 months $	13 to 24 months $	Thereafter $
Financial liabilities					
Credit facility	1,437,912	1,535,939	1,535,939	-	-
Trade and other payables and accrued liabilities	3,032,213	3,032,213	3,032,213	-	-
Government royalty program obligation	591,372	682,540	82,000	95,000	505,540
Obligation under capital lease	29,144	31,261	23,878	4,219	3,164
Convertible debentures	2,216,570	3,173,569	231,143	2,942,426	
Obligation arising from shares issued by a subsidiary	3,912,314	3,912,314	-	-	3,912,314
	11,219,525	12,367,836	4,905,173	3,041,645	4,421,018

Contractual interest amounts on floating interest rates are established based on the spot rates as at the statement of financial position dates.

The Company's development is financed through a combination of borrowing under the existing credit facilities and the issuance of debt and equity (Note 1).

29 Subsequent event

As of January 1st, 2019, Xebec Adsorption Inc has acquired all the outstanding shares of Compressed Air International Inc. (CAI) for a purchase price of $2,200,000. $1,540,000 has been paid in cash while $660,000 will be earned out over the next three years.

CAI is a distributor and full-service supplier of industrial compressed air and gas products with locations in Woodbridge and Guelph, Ontario. In business for 20 years, CAI offers an extensive range of compressors, genuine and OEM-equivalent compressor parts, compressed adsorption and refrigerant air dryers, filtration products, emergency and preventative maintenance service as well as complete installation and service packages.

CAI's principals will remain with CAI after the acquisition to optimize CAI's integration in Xebec's industrial compressed air treatment business.

The purchase price allocation is not completed.