# HERITAGE CANNABIS HOLDINGS CORP.

## INTERIM MANAGEMENT DISCUSSION AND ANALYSIS

## QUARTERLY HIGHLIGHTS

## For the Three- and Nine-Month Periods Ended July 31, 2022

*This Management Discussion and Analysis for Heritage Cannabis Holdings Corp. provides analysis of the Company's unaudited interim condensed consolidated financial results for the three-and nine-month periods ended July 31, 2022. The following information should be read in conjunction with the accompanying unaudited interim condensed consolidated financial statements and related notes for the three- and nine-month periods ended July 31, 2022 and the audited annual consolidated financial statements and related notes for the years ended October 31, 2021 and October 31, 2020.*

## Introduction

This Management Discussion and Analysis ("MD&A") focuses on significant factors that have affected the performance of Heritage Cannabis Holdings Corp. (the "Company" or "Heritage") and such factors that may affect its future performance. This MD&A should be read in conjunction with the Company's unaudited condensed consolidated financial statements and related notes for the three- and nine-month periods ended July 31, 2022 and the audited annual consolidated financial statements and related notes for the years ended October 31, 2021 and October 31, 2020, which were prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). Unless otherwise noted, all currency amounts are in Canadian dollars. This MD&A is dated September 27, 2022.

## Forward-Looking Statements

This MD&A contains forward-looking statements that relate to the Company's current expectations and views of future events. In some cases, these forward-looking statements can be identified by words or phrases such as "may", "might", "will", "expect", "anticipate", "estimate", "intend", "plan", "indicate", "seek", "believe", "predict" or "likely", or the negative of these terms, or other similar expressions intended to identify forward-looking statements. The Company has based these forward-looking statements on its current expectations and projections about future events and financial trends that it believes might affect its financial condition, results of operations, business strategy and financial needs. These forward-looking statements include, among other things, statements relating to:

- the Company's expectations regarding its revenue, expenses and research and development operations;
- the Company's anticipated cash needs and its needs for additional financing;
- the Company's intention to grow the business and its operations;
- expectations with respect to future production costs, capacity and yield;
- expectations regarding growth rates, growth plans and strategies;
- expectations with respect to the approval and/or amendment of the Company's licenses;
- expectations with respect to the future growth of its medical and recreational cannabis products;
- the medical benefits, safety, efficacy, dosing, and social acceptance of cannabis;
- the Company's competitive position and the regulatory and legal environment in which the Company operates;
- the Company's expected business objectives for the next twelve months;
- the Company's plans with respect to the payment of dividends;
- the Company's ability to obtain additional funds through the sale of equity or debt commitments;
- the future growth of the cannabis industry;
- the general level of consumer demand for the Company's products;
- the ability for the Company to access consumer markets for its products;
- the Company's ability to expand into international markets and further across domestic markets;
- the Company's relationship with its distribution partners;
- cannabis and cannabidiol oil processing efficiency and sales;
- impact of scientific findings regarding long-term impacts of Cannabis use or ability to cure medical issues;
- the ability of the Company to access sufficient power for generation of greenhouses;
- the efficiency of mechanical processing for hemp;

- the Company's ability to sustainably and effectively source the necessary materials to produce its products;
- the variability of hemp farming; and
- estimations and anticipated effects of the novel strain of coronavirus ("COVID-19") pandemic.

Forward-looking statements are based on certain assumptions and analyses made by the Company in light of the experience and perception of historical trends, current conditions and expected future developments and other factors it believes are appropriate and are subject to risks and uncertainties. In making the forward-looking statements included in this MD&A, the Company has made various material assumptions, including but not limited to (i) that regulatory requirements will be maintained; (ii) general business and economic conditions; (iii) the Company's ability to successfully execute its plans and intentions; (iv) the availability of financing on reasonable terms; (v) the Company's ability to attract and retain skilled staff; (vi) market competition; (vii) the products and technology offered by the Company's competitors; and (vii) that the Company's current good relationships with its suppliers, service providers and other third parties will be maintained. Although the Company believes that the assumptions underlying these statements are reasonable, they may prove to be incorrect, and the Company cannot assure that actual results will be consistent with these forward-looking statements. Given these risks, uncertainties and assumptions, investors should not place undue reliance on these forward-looking statements. Whether actual results, performance or achievements will conform to the Company's expectations and predictions is subject to a number of known and unknown risks, uncertainties, assumptions and other factors, including those listed under the heading "Risks and Uncertainties", included in this MD&A.

If any of these risks or uncertainties stated herein materialize, or if assumptions underlying the forward-looking statements prove incorrect, actual results might vary materially from those anticipated in those forward-looking statements. The assumptions referred to above and described in greater detail under "Risks and Uncertainties" should be considered carefully by readers.

The Company's forward-looking statements are based on the reasonable beliefs, expectations, and opinions of the senior management of the Company ("Management") on the date of this MD&A (or as of the date they are otherwise stated to be made). Although the Company has attempted to identify important factors that could cause actual results to differ materially from those contained in forward-looking statements, there may be other factors that cause results not to be as anticipated, estimated or intended. There is no assurance that such statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. The Company does not undertake to update or revise any forward-looking statements, except as, and to the extent required by applicable securities laws in Canada.

## United States Cannabis and Hemp Oil Industry Activities

In the future, the Company may be involved, directly or indirectly, in the cannabis and hemp oil industry in the United States where local state laws permit such activities.

The U.S. federal government regulates drugs through the Controlled Substances Act (21 U.S.C § 811), as amended (the "CSA") including cannabis. Cannabis is classified as a Schedule I drug. Under U.S. federal law, a Schedule I drug or substance has a high potential for abuse, no accepted medical use in the United States, and a lack of accepted safety for the use under medical supervision. The U.S. Food and Drug Administration has not approved marijuana as a safe and effective drug for any indication.

In the U.S., cannabis is largely regulated at the state level. State laws regulating cannabis are in direct conflict with the federal CSA. Although certain states authorize, medical or recreational cannabis production and distribution by licensed or registered entities, under U.S. federal law, the possession, use, cultivation and transfer of cannabis and any related drug paraphernalia is illegal. The Supremacy Clause of the United States Constitution establishes that the United States Constitution and federal laws made pursuant to it are paramount and in case of conflict between federal and state law, the federal law shall apply.

On January 4, 2018, U.S. Attorney General Jeff Sessions issued a memorandum to U.S. district attorneys which rescinded previous guidance from the U.S. Department of Justice specific to cannabis enforcement in the U.S., including the August 2013 memorandum by then Deputy Attorney General, James Cole (the "Cole Memorandum"). With the Cole Memorandum rescinded, U.S. federal prosecutors have been given discretion in determining whether to prosecute cannabis related violations of U.S. federal law.

There is no guarantee that state laws legalizing and regulating the sale and use of cannabis will not be repealed or overturned, or that local governmental authorities will not limit the applicability of state laws within their respective jurisdiction. Unless and until the U.S. Congress amends the CSA with respect to medical and/or adult-use cannabis, there is a risk that federal authorities may enforce current federal law. If the Company or any of its subsidiaries becomes involved in the cannabis industry in the United States in a manner which, although legal in a particular state, is illegal under the federal laws of the United States and the federal government elects to enforce such laws, or if existing applicable laws in such state are repealed or curtailed in such a manner as would result in the activities of the Company or any of its subsidiaries becoming illegal, the Company and its subsidiaries may be materially adversely affected by such enforcement measures. See "Risks and Uncertainties" of this MD&A for additional information.

In light of the political and regulatory uncertainty surrounding the treatment of U.S. cannabis-related activities, including the rescission of the Cole Memorandum discussed above, on February 8, 2018 the Canadian Securities Administrators published Canadian Securities Administrators Staff Notice 51-352 (Revised) – Issuers with U.S. Marijuana-Related Activities ("Staff Notice 51-352") setting out the Canadian Securities Administrator's disclosure expectations for specific risks facing issuers with cannabis-related activities in the U.S., Staff Notice 51-352 confirms that a disclosure-based approach remains appropriate for issuers with U.S. cannabis-related activities. Staff Notice 51-352 includes additional disclosure expectations that apply to all issuers with U.S. cannabis-related activities, including those with direct and indirect involvement in the cultivation and distribution of cannabis, as well as issuers that provide goods and services to third parties involved in the U.S. cannabis industry.

## Management's Responsibility for Financial Statements

The information provided in this MD&A, including the audited consolidated financial statements and related notes for the years ended October 31, 2021 and October 31, 2020, are the responsibility of Management. In the preparation of the accompanying unaudited interim condensed consolidated financial statements and related notes for the three- and nine-month periods ended July 31, 2022, estimates are sometimes necessary to make a determination of the future values for certain assets or liabilities. Management believes such estimates have been based on careful judgments and have been reflected in the accompanying interim condensed consolidated financial statements and related notes.

Management maintains a system of internal controls to provide reasonable assurance that the Company's assets are safeguarded and to facilitate the preparation of relevant and timely information.

## Company Overview

The Company was incorporated on October 25, 2007 under the Business Corporations Act of British Columbia as Trijet Mining Corp. The Company was called for trading on the TSX Venture Exchange on January 6, 2010. Effective March 8, 2013, Trijet Mining Corp. consolidated its share capital on a two-old-for-one-new basis and changed its name to Umbral Energy Corp. On October 20, 2014, the common shares of the Company (the "Common Shares") commenced trading on the Canadian Securities Exchange ("CSE") under the symbol "UMB.C" and delisted its Common Shares from the TSX Venture Exchange. On January 9, 2018, the Company completed a Fundamental Change of Business pursuant to CSE Policy 8 (as such term is defined in the CSE Policy 8), changed its name to Heritage Cannabis Holdings Corp., and began trading under the symbol "CANN.C". No consolidation of capital was completed. The Company currently operates as a cannabis issuer.

The Company's head office is located at 77 Bloor Street West, Suite 600,Toronto, Ontario, M5S 1M2. At its August 9, 2019 annual general and special meeting of the shareholders of the Company, the shareholders approved a continuance into Ontario, which was effective on November 4, 2019.

Heritage is a leading cannabis products company operating two licensed manufacturing facilities in Canada, and offers innovative products to both the medical and recreational legal cannabis markets in Canada, the U.S., and internationally. Heritage focuses on extraction and the creation of extract and extract-derivative products and brands for adult use and cannabis-based medical solutions. The Company has an extensive portfolio of high-quality cannabis products under the brands Purefarma, Pura Vida, Really Awesome Dope ("RAD"), Premium 5, feelgood., ArthroCBD, and CB4. In pursuit of its vision, Heritage has built an infrastructure and platform to advance its products to compete in domestic and international markets.

In Canada, Heritage operates through its wholly owned subsidiaries Voyage Cannabis Corp. ("Voyage") and CannaCure Corporation ("CannaCure"), both regulated under the Cannabis Act Regulations. Voyage holds a Health Canada issued cultivation, processing, and medical and adult use sales license, as well as an industrial hemp license, a cannabis oil sales license, and a cannabis research license. Voyage operates out of a 15,500 square foot processing facility in Falkland, British Columbia, which has been outfitted with extraction, downstream processing, formulation and packaging areas and an approved security-level vault. CannaCure holds a Health Canada cultivation, processing, and medical sales license, as well as industrial hemp, cannabis oil sales, and dried cannabis sales licenses under the Cannabis Act Regulations. CannaCure operates out of a 122,000 square foot facility in Fort Erie, Ontario, which formerly operated as a manufacturing plant for a pharmaceutical white labeler. Presently, approximately 24,260 square feet has been retrofitted for cannabis activities, and Management believes that the size and layout of the facility offer significant advantages in terms of expansion and diversification of product offerings and services. Management has earmarked the remainder of the facility for extraction and strategic partnerships, including related storage requirements.

On July 26, 2019, through a series of transactions, Heritage, through its subsidiary Heritage (US) Cali Corp. ("Cali Corp") acquired a 30% interest in EndoCanna Health, Inc. ("EndoCanna"), the Company's first investment in the United States.

In the U.S., Heritage operates primarily through its wholly owned subsidiary, Opticann Inc. ("Opticann"), a Colorado-based oral and topical cannabinoid company with the rights to exclusively sell non-psychoactive cannabinoids Cannabidiol ("CBD") and Cannabigerol ("CBG"), products made with the patented VESIsorb® drug delivery system for optimized absorption and stability. The Company indirectly owns 100% of the issued and outstanding shares of Opticann, which was incorporated on May 5, 2019.

The Company incorporated four new wholly-owned subsidiaries: 5450 Realty Inc. (November 1, 2019), Heritage (US) Oregon Corp. (March 23, 2020), Heritage (US) Colorado Corp. (September 24, 2020) and Heritage Cannabis Exchange Corp. (October 6, 2020), in each of which the Company owns or controls 100% of the issued and outstanding shares. The Company also acquired a 100% interest in Premium 5 Ltd. ("Premium 5") on January 25, 2021.

## Heritage Brands

### Purefarma

Purefarma is a brand that offers medicinal-grade cannabis formulations for the pharmaceutical, recreational, and cosmeceutical markets. Purefarma develops its products using its own proprietary modifications to industry-standard machinery and has industrialized a variety of proprietary production processes with in-house design-built equipment.

### Pura Vida

Heritage developed the Pura Vida product line, which is altruistically medicinal but recreationally focused, by leveraging the know-how of the Purefarma offerings. Pura Vida gained national recognition after entering several competitions and winning multiple awards for concentrates in the CBD, Indica, Sativa, and Hybrid categories at the Emerald Cup, High Times and Cannabis Cup prior to its acquisition by Heritage.

### Premium 5

Premium 5 is dedicated to creating high-quality, full-spectrum concentrates, selling a premium high-THC experience, and providing a healthier and more discrete way to medicate and consume.

Products offered under the Premium 5 brand are crafted from indoor-grown, fresh-frozen whole bud that have been carefully selected for optimal cannabinoid and terpene profiles to offer customers only the most exceptional quality. Premium 5 is a consumer-driven brand focused on providing high-demand products to their partners, consumers, and communities.

### RAD

RAD offers high-quality products at affordable prices, delivering quality concentrates and competitive price points to meet the needs and preferences of all types of cannabis consumers while effectively harnessing the captivating power of nostalgia in our brand messaging.

Products being offered under RAD are made from high quality flower inputs selected specifically for their Indica, Sativa, and Hybrid profiles, and excellent terpene profiles, offering consumers a high-quality choice while delivering on an affordable price point.

### feelgood.

feelgood. is a health and wellness brand dedicated to providing consumers with affordable, high-potency products while still maintaining the highest quality standards possible. With feelgood's safe and effective skin care and wellness products, Heritage acts through the brand to offer a variety of natural alternative options to help consumers find confidence in the products they use.

### ArthroCBD

ArthroCBD is an innovative hemp formulation that has 4x higher absorption of other products, as proven by a published human clinical trial. ArthroCBD delivers ingredients in effective levels for maximum, fast and lasting effect. ArthroCBD is also backed by extensive safety testing and human clinical data. ArthroCBD provides relief with no THC and without unwanted side-effects.

### CB4

CB4 medical cannabis products are based on trusted pharmaceutical technology platforms that are optimized for the effective delivery of cannabinoids – for maximum effect and to minimize unwanted effects. The CB4 suite of products are familiar to most medical patients and their caregivers: oral capsules, sublingual filmstrips, and topically administered products in the form of gels and creams. CB4 products are based on innovative pharmaceutical technology that deliver the best results consistently, safely, and in convenient dosage forms. These dosage forms are tested and optimized to deliver active ingredients for effective results. CB4 products also contain the highest quality ingredients and are thoroughly quality tested for consistency.

## Third Quarter Corporate Developments

The Company reports financial results on a consolidated basis and presents the following information to provide a more detailed description of the developments in the business.

### Corporate

On June 2, 2022, the Company announced that the cease trade order issued by the Ontario Securities Commission had been revoked, allowing the Company's shares to resume trading. The cease trade order was originally issued on March 2, 2022 and at the time, the Company's 2021 audit remained ongoing due to the Company's growth and acquisition activity in 2021. The cause of the delay was not material to the Company or its operations. The audit took longer to complete than originally anticipated by virtue of the fact that the Company's acquisition of Premium 5 in 2021 transitioned the Company from one with minimal provincial sales to one with numerous SKUs across 5 product verticals in less than 12 months. Notwithstanding the delay, the Company continued to operate normally without disruption and completed the Annual Filings on May 11, 2022, and subsequently completed the filings for the first quarter of 2022 on May 30, 2022.

### Recreational and Med-Rec Products

On June 6, 2022, Heritage announced that it had signed a definitive agreement for the supply of its products for sale on the medical platform of a major LP with one of the leading market shares in Canada. The major LP completed its initial purchase of Heritage brands, including RAD, Premium 5, and CB4, and are now offering Heritage products on the platform with the first shipment of 12 stock keeping units ("SKUs") completed in May. The relationship will also encompass white labelling of some products based on Heritage's product quality, variety, consistency, industry proven technology and innovation.

The third quarter of 2022 continued to see growing sales across Heritage's portfolio of innovative products and expanded distribution channels, including the launch of Heritage products on two of the largest market share online medical platforms in Canada. As sales momentum builds, the Company remains focused on increasing margins and cost containment. Spending and capital expenditures by Heritage are measured by their expected return on investment and ability to generate near-term revenues.

Heritage continues to add new stock keeping units ("SKUs") across all Canada and is participating in regular product calls by the provinces. Heritage proactively manages its offerings to stay price competitive in all segments, while also delivering innovative products and new flavour profiles to keep up with consumer demands, and successfully win provincial product calls.

### Equity Issuance

On June 17, 2022, the Company announced that 7,109,090 Common shares in the capital of the Company (the "Bonus Shares") were issued at a deemed price of $0.055 as compensation bonus to certain executive employees and consultants (the "Parties") based on corporate measures and individual performance of those individuals in 2021. The fair value of shares issued were measured at $355,455, determined based on the quoted share price at the issuance date, and recorded as share-based payment in the unaudited interim condensed consolidated financial statements for the three- and nine-month periods ended July 31, 2022.

The Bonus Shares were issued in reliance on certain prospectus exemptions available under National Instrument 45-106 – Prospectus Exemptions, and are subject to a four month and one day statutory hold period. As 3,745,454 of the Bonus Shares were issued to the Parties of the Company, the issuance of Bonus Shares (the "Compensation Bonus") constituted a "related party transaction" pursuant to Multilateral Instrument 61-101 – Protection of Minority Security Holders in Special Transactions ("MI 61-101"). The Company relied on exemptions from the formal valuation and minority approval requirements of MI 61-101 (pursuant to subsections 5.5(a) and 5.7(a)) as the fair market value of the securities distributed to, and the consideration received from, the related party did not exceed 25% of the Company's market capitalization. The Compensation Bonus was approved by the Company's board of directors. No special committee was established in connection with the Compensation Bonus or the participation of the applicable officers and directors in the Compensation Bonus, and no materially contrary view or abstention was expressed or made by any director of the Company in relation thereto.

## Corporate Developments Subsequent to the end of the Third Quarter

On August 8, 2022, Heritage announced a relationship with Harvest Care Medical, LLC, ("Harvest Care"), a leading grower, processor, and provider of top-quality medical cannabis products in the state of West Virginia, with ten dispensary licenses of which two are currently in operation. Harvest Care was granted one of ten cultivation licenses last year and will contribute the use of the license to the relationship, allowing Heritage to produce branded products to be offered to medical cannabis consumers in West Virginia.

Similar to Heritage's relationship in Missouri, under the agreement Heritage will supply production equipment to Harvest Care as well as provide training and supervision of staff on the proprietary methods of extraction and manufacturing of Heritage developed and branded products. The relationship will provide favourable shelf allocation for Heritage's branded products in Harvest Care's West Virginia dispensaries.

On September 15, 2022, Heritage acquired the remaining 25% interest in Voyage Cannabis Corp. and now owns 100% of the issued and outstanding shares in the capital of Voyage Cannabis Corp., a holder of various Health Canada cannabis licenses, through a share cancellation acquisition with Estek Ventures Corp. As consideration for the cancellation of 500 Class A Voting Common Shares and 400,000 Class G Non-Voting Preferred Shares in the capital of Voyage Cannabis Corp., the Company has issued Estek Ventures Corp. 2,000,000 Common Shares at a price of CAD$0.06 per share plus an additional CAD$50,000 in cash.

On September 16, 2022, Heritage entered into settlement agreement with the original shareholders of Purefarma Solutions Inc. (the "Original Purefarma Shareholders") to settle all outstanding obligations of Heritage to the Original Purefarma Shareholders pursuant to the terms of a share exchange agreement and share purchase agreement each dated December 7, 2018. In satisfaction of all claims related to earn-out share obligations and contingent cash payment obligations, the Original Purefarma Shareholders directed Heritage to issue 14,728,762 Common Shares to its corporate shareholder, 1187940 B.C. Ltd., at a price of CAD$0.05 per Common Share.

## Results of Operations

Selected financial highlights for the three- and nine-month periods ended July 31, 2022 and July 31, 2021 include the following:

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| *(in $CDN)* | July 31, 2022<br>$ | July 31, 2021<br>$ | July 31, 2022<br>$ | July 31, 2021<br>$ |
| Gross revenue | 10,799,784 | 5,111,945 | 30,848,238 | 11,544,016 |
| Net revenue (net of excise tax) | 7,495,885 | 4,314,314 | 21,528,280 | 9,410,105 |
| Cost of sales | 5,025,046 | 3,069,069 | 13,987,874 | 6,163,343 |
| Gross margin | 2,470,839 | 1,245,245 | 7,540,406 | 3,246,762 |
| General and administrative expenses | 5,390,047 | 8,335,897 | 14,635,045 | 18,894,828 |
| Other Income (Expenses) | 54,380 | (527,022) | 8,421,679 | (1,129,923) |
| Comprehensive Income (Loss) | (2,793,327) | (6,637,449) | 2,957,272 | (14,999,542) |

The Company reported gross revenue of $10,799,784 for the three months ended July 31, 2022, an increase of $5,687,839 compared to gross revenue of $5,111,945 for the three months ended July 31, 2021, representing an increase of 111%. The growth was driven by a continued increase in the Company's vape and concentrate offerings as well as the launch of the flower vertical. The increase from the prior year is a direct result of increasing our provincial listings and the continued advancement of our inclusion on third party medical platforms although the positive impact was partially offset in the quarter due to The British Columbia General Employees' Union (BCGEU) labour strike given sales to the province were 39% lower than the average of the previous two quarters.

For the nine-month period ended July 31, 2022, the Company recorded gross revenue of $30,848,238 an increase of $19,304,222 compared to gross revenue of $11,544,016 for the nine months ended July 31, 2021, representing an increase of over 167%. The increase in gross revenue was the result of the Company continued strong listing demand through the provincial boards in spite of the BCGEU labour strike and continued focus on cash management practices which are focused on managing inventory growth and availability.

See table below for additional detail.

| | Three months ended | | | Nine months ended | | |
|---|---|---|---|---|---|---|
| *(in $CDN)* | July 31, 2022<br>$ | July 31, 2021<br>$ | Change<br>% | July 31, 2022<br>$ | July 31, 2021<br>$ | Change<br>% |
| Revenue Category | | | | | | |
| Vape and Concentrates | 7,177,907 | 4,557,809 | 57% | 22,511,981 | 9,817,380 | 129% |
| Tincture Sales | 493,050 | 923,186 | (47%) | 2,056,774 | 1,989,944 | 3% |
| Flower | 2,092,715 | 11,572 | 17,984% | 4,877,569 | 11,572 | 42,050% |
| Edibles | 1,038,566 | 13,324 | 7,695% | 1,317,685 | 16,755 | 7,764% |
| Other | (2,454) | (393,946) | 99% | 84,229 | -291,635 | 129% |
| Total Gross Revenue | 10,799,784 | 5,111,945 | 111% | 30,848,238 | 11,544,016 | 167% |

Cost of sales for the three months ended July 31, 2022 was $5,025,046, an increase of $1,955,977 compared to $3,069,069 for the three months ended July 31, 2021. Cost of sales decreased on a percentage of sales basis as a result of improved operational efficiencies, which although were negatively impacted by system inventory corrections relating to the inventory system management launch and refinement. It is anticipated that these one-time negative impacts will be reduced or eliminated over the next quarter.

Cost of sales for the nine months ended July 31, 2022 was $13,987,874, an increase of $7,824,531, compared to $6,163,343 for the nine months ended July 31, 2021. Cost of sales increased as a function of the increased sales results and improved on a percentage of sales basis as a result of a continued focus on improving facility efficiencies.

Gross margin for the three months ended July 31, 2022 was $2,470,839 compared to gross margin of $1,245,245 for the three months ended July 31, 2021. The increase of $1,225,594 was primarily a result of increased sales activity and greater facility productivity which was partially offset by a higher excise percentage which increased to 31% from 16% in the prior period as a result of distribution expansion and product mix. Regulatory taxes continue to be one of the largest expenses of the business.

Gross margin for the nine months ended July 31, 2022 was $7,540,406 compared to gross margin of $3,246,762 for the nine months ended July 31, 2021. The increase of $4,293,644 was a result of increased sales activity as highlighted in the table above combined with improved operational efficiencies which were partially offset by a higher excise percentage which increased to 30% from 18% in the prior period driven by the production of higher THC products as well as increased sales in provinces with higher tax rates.

For the three months ended July 31, 2022, the Company recorded a net loss of $2,793,828 or $0.00 loss per share compared to a comprehensive loss of $6,705,674 or $0.01 loss per share for the three months ended July 31, 2021. The improvement over the prior period was due to the gross margin gains noted above and the cost management in general and administrative expenses combined with a $416,000 unrealized decrease in loss on contingent payables.

For the nine months ended July 31, 2022, the Company recorded a net income of $2,848,040 or $0.00 income per share compared to a comprehensive loss of $14,773,989 or $0.02 loss per share for the nine months ended July 31, 2021. The decrease in loss was primarily attributable to a non-cash accounting policy-related gain of $8,571,429 due to the change in fair market value between the share price used for the Premium 5 first milestone payment and the quoted share price at the time of award combined with the improvements in the operating business noted above.

General and administrative expenses for the three months ended July 31, 2022 were $5,390,047, a decrease of $2,945,850 from $8,335,897 for the comparable period in 2021. General and administrative expenses for the nine months ended July 31, 2022 were $14,635,045, a decrease of $4,259,783 from $18,894,828 for the comparable period in 2021. The net changes in general and administrative expenses were attributable to the following:

a) Advertising, travel and promotion for the three months ended July 31, 2022 was $203,282, a decrease of $407,027 from $610,309 for the comparable period in 2021. The decrease in the current period was essentially as the Company has continued to focus on cost control and minimize non-essential travel. Advertising, travel and promotion for the nine months ended July 31, 2022 was $579,277, a decrease of $570,820 from $1,150,097 for the comparable period in 2021. The decrease in the period was due to continued cost control over the current year.

b) Amortization expense for the three months ended July 31, 2022 was $1,243,398, a decrease of $2,335,117 from $3,578,515 for the comparable period in 2021. The decrease was largely due to a reduction in the intangible asset base resulting from the impairment charges in the fourth quarter of 2021. Amortization expense for the nine months ended July 31, 2022 was $3,788,053, a decrease of $4,159,353 from $7,947,406 for the comparable period in 2021. The decrease as mentioned above was a result of a lower intangible asset base resulting from the impairment charges in the fourth quarter of 2021.

c) Management and consulting fees for the three months ended July 31, 2022 were $304,590, a decrease of $247,056 from $551,646 for the comparable period in 2021 as a result of a continued focus to remain lean to manage its cash position and a focus on near-term core initiatives. Management and consulting fees for the nine months ended July 31, 2022 were $924,031, a decrease of $674,917 from $1,598,948 for the comparable period in 2021 as a result of a continued focus to remain lean to manage its cash position.

d) Occupancy, general and administrative expense for the three months ended July 31, 2022 was $1,042,301, a decrease of $738,740 from $1,748,041 for the comparable period in 2021. The decrease was primarily due to an increase in absorbed overhead costs as a result of increased production in the quarter. Occupancy, general and administrative expense for the nine months ended July 31, 2022 was $3,008,299, an decrease of $550,504 from $3,558,803 for the comparable period in 2021. The increase was primarily a function of increased production and efficiency over the year which increased the absorbed overhead costs this offset the increases in shipping and merchant fees

e) Professional fees for the three months ended July 31, 2022 were $202,152, a decrease of $162,187 from $364,339 for the comparable period in 2021. The decline in the current period was a result of reduced external accounting activity for quarterly reporting requirements. Professional fees for the nine months ended July 31, 2022 were $609,593, a decrease of $341,875 from $951,468 for the comparable period in 2021. Spending declined as the reduced external accounting fees in the current period more than offset the increased fees incurred in the first three months of the year.

f) Share-based payments for the three months ended July 31, 2022 were $463,290, an increase of $462,311 from $979 for the comparable period in 2021. The increase was primarily a result of performance-based share issuance to senior management as noted under “Equity Issuance” section of this MD&A. Share-based payments for the nine months ended July 31, 2022 were $676,434, an increase of $321,408 from $355,026 for the comparable period in 2021. The increase was primarily related to the share issuance in the current quarter as noted under “Equity Issuance” section of this MD&A.

g) Salaries, wages and benefits for the three months ended July 31, 2022, were $1,931,034 an increase of $481,966 from $1,449,068 for the comparable period in 2021. The increase is a result of a continued increase in the personnel in-line with the continued increases in sales activity as the Company grows and to ensure the Company has the appropriate personnel to facilitate future growth. Salaries, wages and benefits for the nine months ended July 31, 2022, were $5,049,358, an increase of $1,716,278 from $3,333,080 for the comparable period in 2021. The increase is a result of a continued increase in the Company’s internal resources from depressed COVID-19 levels to ensure future sales are maintained.

## Other Income and Expenses

Interest and other income for the three months ended July 31, 2022 was $44,269, an increase of $21,219 compared to $23,050 for the same period in 2021. This was essentially flat year over year. Interest and other income for the nine months ended July 31, 2022 was $182,547, an increase of $99,249 compared to $83,298 for the same period in 2021. This increase was a primarily the result of an insurance claim for equipment that was damaged in transit, the reversal of a payment relating from a product launch and interest earned on the note receivable which was new in the current year.

Interest and finance expenses for the three months ended July 31, 2022 were $306,583, an increase of $43,178 compared to $263,405 for the same period in 2021. The increase was due to the Company carrying a higher debt balance in 2022 compared to 2021 as well as rising interest rates. Interest and finance expenses for the nine months ended July 31, 2022 were $811,699, an increase of $150,388 compared to $661,311 for the same period in 2021. The increase was due to the Company carrying a higher debt balance in 2022 compared to 2021 and rising interest rates.

The share of loss from investment in associate for the three months ended July 31, 2022 was $43,277, a decrease of $9,704 compared to a loss of $33,573 for the same period in 2021. The results were primarily flat as Endocanna remains in re-build from changing its business model. The share of loss from investment in associate for the nine months ended July 31, 2022 was $95,330, a decrease of $49,620 compared to $144,950 for the same period in 2021. The decrease was a result of improved performance earlier in the year driven by cost reductions.

The unrealized gain on other investments for the nine months ended July 31, 2022 was $608,649 compared to $nil for the same period in 2021, and was $nil for the three months ended July 31, 2022 and 2021. The increase of $608,649 related to a revaluation to fair value of the investment in Stanley Park Digital immediately preceding the sale of the investment in the second quarter of 2022.

During the three months ended July 31, 2022, the Company had an unrealized loss on contingent consideration payable of $84,000, an increase of $416,000 compared to unrealized loss of $500,000 for the comparable period in 2021 primarily due to the revaluation on lower contingent consideration payable base as a result of Premium 55 first milestone payment made in the first quarter of 2022, and as a result of adjustments to the time periods of the contingent consideration settlement dates as time elapses. During the nine months ended July 31, 2022, the Company had an unrealized gain on contingent consideration payable of $8,331,429, an increase of $9,342,645 compared to unrealized loss of $1,011,216 for the comparable period in 2021. The decrease in the unrealized loss was mainly due to a non-cash gain relating to valuing the Premium 5 milestone payment at the share price at time of issuance compared to the share price used for the milestone award.

The unrealized gain on derivative liabilities for the three months ended July 31, 2022 was $443,971, an increase of $197,065 compared to a gain of $246,906 for the same period in 2021. The increase in the unrealized gain mainly relates to the revaluation of warrants issued to the former shareholders of Opticann and notes and warrants issued to Merida Fund III & IV ("Notes and Warrants"), whose value decreased as a result of decreased share price during current period.

The unrealized gain on derivative liabilities for the nine months ended July 31, 2022 was $206,083, a decrease of $398,173 compared to a gain of $604,256 for the same period in 2021. The decrease in the unrealized gain was a result of unrealized gain arising from the decreased fair value of warrants issued to the former shareholders of Opticann and Notes and Warrants due to the decreased share price during the year and shorter contractual term as time elapses, which was partially offset by an unrealized loss of $311,810 as a result of the revaluation of the Notes and Warrants from their relative fair value as part of the proceeds received at initial recognition in the first quarter of 2022 to their standalone fair value measured using a level 3 valuation technique in the subsequent revaluation periods as described in the Note 16 and 25 in the unaudited interim condensed consolidated financial statements.

## Adjusted EBITDA/Loss

The Company attributes the Adjusted EBITDA in the current period to a number of occurrences listed in the table below, which had a current period impact that is either non-cash based or due to factors that are period specific or one-time events. While the Company does not anticipate significant one-time expenses moving forward, it does expect to see some continued impact resulting in regulatory product change and system adjustments over the next period. The Company is driving significant cost reductions to maintain its path towards consistent positive EBITDA.

| | Three months ended July 31, 2022 $ | Three months ended July 31, 2021 $ | Nine months ended July 31, 2022 $ | Nine months ended July 31, 2022 $ |
|---|---|---|---|---|
| (Loss) Before Taxes | (2,864,828) | (7,617,674) | 1,327,040 | (16,777,989) |
| Amort. and Depreciation | 1,243,398 | 3,578,515 | 3,788,053 | 7,947,406 |
| Share-based payments | 463,290 | 979 | 676,434 | 355,026 |
| Regulatory product change | 668,317 | - | - | - |
| One-time system adjustments | 575,509 | - | - | - |
| Other (Income) | (54,380) | 527,022 | (8,421,679) | 1,129,923 |
| Professional fees | 129,670 | - | - | - |
| Adjusted EBITDA | 160,976 | (3,511,158) | (2,630,152) | (7,345,634) |

Non-GAAP Financial Measures

“Adjusted EBITDA” is supplemental, non-GAAP financial measures. The Company defines EBITDA as earnings before depreciation and amortization, depreciation and interest in cost of sales, income taxes, and interest. Additionally, the Company’s Adjusted EBITDA presented above excludes accretion, loss from discontinued operations, one-time costs and all other non-cash items. The Company has presented “Adjusted EBITDA” because its management believes it is a useful measure for investors when assessing and considering the Company’s continuing operations and prospects for the future. Furthermore, “Adjusted EBITDA” is a commonly used measurement in the financial community when evaluating the market value of similar companies. “Adjusted EBITDA” is not a measure of performance calculated in accordance with GAAP, and these metrics should not be considered in isolation of, or as a substitute for, the measurement of the Company’s performance prepared in accordance with GAAP. “Adjusted EBITDA,” as calculated and reconciled in the table above, may not be comparable to similarly titled measurements used by other issuers and is not necessarily a measure of the Company’s ability to fund its cash needs.

## Summary of Quarterly Results

The following tables set out selected consolidated financial information for the last eight quarters, which were prepared in accordance with IFRS accounting standards. More details and explanations on each of the quarterly financial data below can be found in the corresponding Management Discussion and Analysis.

| | July 31, 2022 $ | April 30, 2022 $ | January 31, 2022 $ | October 31, 2021 $ |
|---|---|---|---|---|
| Net revenues (1) | 7,495,885 | 7,491,184 | 6,541,211 | 4,649,025 |
| Comprehensive (loss) income | (2,799,327) | (500,614) | 6,257,213 | (42,685,990) |
| Basic and fully diluted (loss) income per share (2) | (0.00) | (0.00) | 0.01 | (0.06) |

| | July 31, 2021 $ | April 30, 2021 $ | January 31, 2021 $ | October 31, 2020 $ |
|---|---|---|---|---|
| Net revenues (1) | 4,314,314 | 3,575,175 | 1,520,616 | 1,429,973 |
| Comprehensive (loss) income | (6,637,449) | (5,151,011) | (3,211,082) | (4,745,405) |
| Basic and fully diluted (loss) income per share (2) | (0.01) | (0.01) | (0.01) | (0.01) |

(1) Revenues are net of excise tax.
(2) Basic loss per share equals fully diluted loss per share as any potential dilutive instruments are anti-dilutive.

During the fourth quarter of 2020 the Company posted lower sales as a result of transitioning from operating primarily as a third-party service provider to producing and selling its branded products to the provincial boards. The Company also wrote down goodwill as a result of its annual impairment analysis, which was offset by a recovery of an accounts payable from a vendor.

During the first quarter of 2021, the Company began to realize the impact of the transitioning from operating primarily a contract manufacturer to focusing on branded sales, which began in the fourth quarter of 2020, and resulted in an increase in sales revenue for the Company.

During the second quarter of 2021, the Company incurred higher losses as a result of higher amortization of intangible assets, as the Company continued to fund and build its platform to support future sales activity.

During the third quarter of 2021, the Company incurred higher losses as a result its increased spending to support future sales and potential market share gains. The Company continues to fund and build its platform to support future sales activity.

During the fourth quarter of 2021, the Company continued to experience record sales growth with the net revenues being partially offset by an accrual catch up for excise taxes. Increased losses were primarily due to impairment charges for intangible assets and goodwill.

During the first quarter of 2022, the Company recorded its 5th consecutive sequentially quarterly growth period. The continued growth has been a combination of commercial focus to lead with product innovation and products as consumers want as well operational improvements to maintain quality.

During the second quarter of 2022, the Company recorded a 15% increase in net revenues as the Company continued to see increasing demands for its product lines as well the loss was reduced significantly compared to prior periods as cost control and improved efficiencies positively impacted the results.

During the third quarter of 2022, the Company continued to record sequential increased revenue albeit the increase was offset by higher excise tax in the current quarter, while the bottom line improved year over year as a result of improved efficiency and cost control.

## Outlook

Despite turbulent markets, the Company has continued to grow its revenue base on a sequential basis by continuing build, expand or rationalize its successful SKU portfolio. While the current quarter was impacted by a number of one-time or legacy items, the Company continues to be focused on consistent positive cash flow while continuing to grow revenue.

The Company, continued to cross the positive EBITDA threshold, after adjusting for non-cash and non-recurring operational expenses, for the second consecutive quarter. The volatility in the market place has continued as many in the sector face significant headwinds as a result of a poor financial structure, tax burden and/or limiting brand or sales traction. The Company is focused on taking measures to insulate itself in the near-term from many of the pressures in the marketplace by continuing to focus internally.

The Company's entry into the flower market has been successful and it has continued to expand its SKU and penetration across the country.

Given the volatility discussed above, the success that the Company has had on third party medical platforms is growing and remains a marketplace for its growing product catalogue.

Heritage continues to expect it's U.S. strategy to have an effect later in 2022 as the built facilities move through the regulatory process.

As the Company continues to execute its Canadian and U.S. strategies, the potential impact of COVID-19 and the continued sector volatility could have a negative impact on production efficiency and product launches.

## Long Term Debt

On March 31, 2021, the Company entered into a refinance agreement with BJK Holdings Ltd. (the "BJK Loan Agreement") in the amount of $7,000,000, with an implicit interest rate of 10%. Pursuant to the BJK Loan Agreement, BJK Holdings Ltd. advanced the Company $7,000,000 on April 1, 2021. The loan was originally payable in full upon maturity of the loan, on October 1, 2022, with monthly interest only payments made based on the outstanding balance of the loan, calculated monthly, in arrears. Monthly interest is calculated at the Royal Bank of Canada prime lending rate plus 1.25% per annum. A one-time setup fee of $965,000 was paid to BJK Holdings Ltd. on April 1, 2021. The loan may be prepaid in full at any time without penalty. The loan is secured by the following:

(i) A promissory note in the amount of $7,000,000;

(ii) mortgages and assignments of rents over certain properties owned by the Company;

(iii) an environmental indemnity agreement;

(iv) an encumbrance and charge of all of the Borrowers' right, title and interest in the Borrowers' present and future personal property and assets by way of a general security agreement;

(v) an assignment of proceeds from the Borrowers' sales;

(vi) assignments and postponements of creditors' claims from creditors of the Borrowers;

(vii) joint and several unlimited guarantees inclusive of assignments and postponements of creditors' claims from each of the guarantors, including five of the Company's remaining subsidiaries (together the "Guarantors");

(viii) general security agreements from the Borrowers and Guarantors inclusive of serial specific registration on certain assets;

(ix) a pledge by the Company, each of its subsidiaries and all the investees in which the Company holds interests;

(x) an assignment of material contracts and insurance agreements granted by the Company and each guarantor; and(xi) solicitors' opinions for Borrowers.

Furthermore, on March 31, 2021, the Company repaid the outstanding balance of its term loan with Trichome Financial Corp. (the "Trichome Credit Facility") of $4,863,163 in full.

On October 6, 2021, the Company amended the loan agreement by establishing three credit facilities for a maximum amount of $14,775,000 (collectively the "Loan") as follows:

(i) Facility 1: the initial loan is increased from $7,000,000 to $7,175,000, with the increase of $175,000 to be used by the Company to pay to the lender an extension fee of $175,000 to extend the due date to February 1, 2023;

(ii) Facility 2: an additional loan $2,600,000 will be advanced at the Royal Bank of Canada prime rate plus 1.25% per annum;

(iii) Facility 3: a revolving line of credit up to maximum of $5,000,000 shall be established at an interest rate of 18% per annum.

The Loan is currently due on February 1, 2023 and therefore is presented as a current liability in the interim condensed consolidated financial statements for the nine months ended July 31, 2022. If the Loan is repaid in its entirety on or before October 1, 2022, the lender will repay the $175,000 extension fee for Facility 1 to the Company. As at July 31, 2022, the Company has received a total of $11,822,261 in principal, with the remaining line of credit of $2,952,739 available for advance. As part of the amendments, the Company also issued 10,000,000 warrants to the lender. Each warrant is exercisable into one Heritage Common Share at an exercise price of $0.25 per share and has a term of 24 months expiring on October 8, 2023.

## Liquidity

Managing the Company's liquidity and capital structure requires maintaining sufficient working capital to fund the Company's operating and strategic growth requirements.

The table below sets out the Company's current assets, short-term liabilities and working capital as at July 31, 2022 and October 31, 2021.

| | July 31, 2022 | October 31, 2021 |
|---|---|---|
| | $ | $ |
| Current Assets | 35,219,436 | 29,281,960 |
| Current Liabilities | 29,627,246 | 8,977,054 |
| Working Capital | 5,592,190 | 20,304,906 |

As at July 31, 2022, the Company had cash and short-term investments of $6,048,689 compared to $4,713,577 at October 31, 2021.

The table below summarizes the Company's use of cash for the three- and nine-month periods ended July 31, 2022 and July 31, 2021.

| | Three-month periods ended | | Nine month periods ended | |
|---|---|---|---|---|
| | July 31, 2022 | July 31, 2021 | July 31, 2022 | July 31, 2021 |
| | $ | $ | $ | $ |
| Cash Flows Provided by (Used in): | | | | |
| Operating Activities | 1,771,468 | (6,074,253) | 1,057,032 | (16,467,934) |
| Investing Activities | (737,687) | (302,627) | (1,717,817) | 3,247,560 |
| Financing Activities | (22,251) | (13,526) | 1,995,897 | 13,937,682 |

During the three-month period ended July 31, 2022, cash flows provided by operating activities was $1,771,468 compared to cash flows used of $6,074,253 for the three months ended July 31, 2021. The outflows decreased by $7,845,721 as the Company continued to manage its cash cycle while offsetting additional inventory buildup.

During the nine-month period ended July 31, 2022, cash provided from operating activities was $1,057,032 compared to cash flows used of $16,467,934 for the nine months ended July 31, 2021. The outflows decreased by $9,679,245 as the Company continued to focus on spending control efficiencies while converting inventory buildup into cash generating opportunities and further managing its cash cycle.

During the three-month period ended July 31, 2022, cash flows used in investing activities were $737,687 compared to cash flows used of $302,627 for the three months ended July 31, 2021. The decrease in cash was a function of capital spending on equipment to drive increased capacity and efficiency in the current year with a specific focus on increasing capacity in both solventless, hydrocarbon extraction and regulatory approved storage areas.

During the nine-month period ended July 31, 2022, cash flows used in investing activities were $1,717,817 compared to cash flows provided by investing activities of $3,247,560 for the nine months ended July 31, 2021. The decrease in cash of $4,965,377 was a function of no redemptions of short-term investments during the current period while an additional $2,450,477 was spent to increase facility capacity and loan out to US opportunities.

During the three months ended July 31, 2022, cash used in financing activities was $22,251 compared to cash used by financing activities of $13,526 in the comparable period. The period was essentially flat year over year.

During the nine months ended July 31, 2022, cash provided by financing activities was $1,995,897 compared to $13,937,682 in the comparable period. The decrease of $11,941,785 was primarily due to a long-term debt issuance and proceeds from issuance of units in the prior periods.

The progression of the COVID-19 pandemic may impact the Company's cash position and ability to raise funds to maintain the Company's planned growth and development activities.

## Capital Resources

Given the continued nature of the COVID-19 pandemic, there are certain uncertainties related to the short and long term impacts of the COVID-19 pandemic on the Company's liquidity and capital resources along with rising interest rates. However, Management continues to closely monitor the evolving situation and is looking into all possible actions that could minimize the impact of the COVID-19 pandemic.

The Company has $35,219,436 of current assets, which is primarily comprised of $6,048,689 in cash and short-term investments, $7,525,991 in accounts receivable and $18,693,808 in inventory with an additional $2,952,739 available under the Company's line of credit. If the Company assumes zero growth, the combination of the Company's usual net working capital and the funds received is sufficient to fund the Company's operations. The combination of continued growth and/or the impact of COVID-19 constraints could require additional capital resources.

At the reporting date, the Company had long-term financial debts amounting to $4,327,968, including $9,745 of long-term debt (as detailed under the "Long-Term Debt" heading of this MD&A and Note 14 of the interim condensed consolidated financial statements), note that $11,822,261 of the debt under this category was reclassified to current liability as a result of the maturity date being February 1, 2023), $663,074 of lease liabilities (as described more particularly under Note 13 of the interim condensed consolidated financial statements), $1,140,000 relating to contingent consideration payable to the former shareholders of Purefarma, Voyage and Premium 5 (as described more particularly under Note 15 of the interim condensed consolidated financial statements), and $2,515,149 relating to derivative liabilities issued as part of the consideration for the acquisition of Opticann and issued to Merida Fund III & IV (as described more particularly under Note 16 of the interim condensed consolidated financial statements).

## Outstanding Share Capital

The Company has the following shares outstanding as of September 27, 2022:

| | Number of shares outstanding |
|---|---|
| **Balance, October 31, 2019** | **473,718,024** |
| Shares issued for acquisition - Opticann | 21,918,698 |
| Shares issued for acquisition – Pura Vida brand | 500,000 |
| **Balance, October 31, 2020** | **496,136,722** |
| Shares issued for acquisition – Premium 5 Ltd. | 150,000,000 |
| Exercise of stock options | 2,549,644 |
| Shares issued for RSU's | 5,076,628 |
| **Balance, January 31, 2021** | **653,762,994** |
| Shares issued for public offering | 98,900,000 |
| Shares issued for acquisition (net working capital) – Premium 5 Ltd. | 30,156,643 |
| Shares issued for BJK facility – broker fee | 170,000 |
| **Balance, April 30, 2021** | **782,989,637** |
| Shares issued for advisory services – Merida Capital | 495,049 |
| **Balance, July 31, 2021** | **783,484,686** |
| Shares issued for marketing services – Zoomer Media Ltd. | 1,250,000 |
| Shares issued for Merida loan – commitment fee | 1,393,884 |
| **Balance, October 31, 2021** | **786,125,570** |
| Shares issued for warrant exercise | 29,809 |
| Shares issued for Premium 5 milestone | 107,142,857 |
| **Balance, January 31, 2022** | **893,301,236** |
| - | - |
| **Balance, April 30, 2022** | **893,301,236** |
| Indemnity Share Cancellation - Opticann | (933,333) |
| Shares issued for management performance | 7,109,090 |
| **Balance, July 31, 2022** | **899,476,993** |
| Shares issued for Voyage and Purefarma settlements | 16,728,762 |
| **Balance, September 27, 2022** | **916,205,755** |
| Warrants | 115,823,000 |
| Outstanding Options | 24,763,440 |
| **Balance including unexercised warrants and options, September 27, 2022** | **1,056,792,195** |

## Off-Balance Sheet Arrangements

As of the date of this MD&A, there are no off-balance sheet arrangements to which the Company is committed.

## Transactions with Related Parties

All related party transactions are in the normal course of operations and pertain to compensation of Management. The related party transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. Management compensation transactions for the three- and nine-month periods ended July 31, 2022 and July 31, 2021 are summarized as follows:

Transactions with directors, officers and companies controlled by directors, officers and/or their families. (1)

| | Three months ended | | Nine months ended | |
|---|---|---|---|---|
| | July 31, 2022<br>$ | July 31, 2021<br>$ | July 31, 2022<br>$ | July 31, 2021<br>$ |
| Management fees | 15,000 | 52,000 | 35,000 | 172,000 |
| Consulting fees | 67,250 | 67,250 | 201,750 | 324,061 |
| | 82,250 | 119,250 | 236,750 | 496,061 |
| Key Management Compensation | | | | |
| Salary and short-term benefits | 98,763 | 172,029 | 296,290 | 333,537 |
| Share-based payments | 224,578 | - | 297,972 | 353,075 |
| | 323,341 | 172,029 | 594,262 | 686,612 |

(1) Key management personnel are persons responsible for planning, directing, and controlling activities of an entity, and include executive and non-executive directors.

As at July 31, 2022 the Company was owed $48,831 (October 31, 2021 - $48,831) from related parties and owed $8,000 (October 31, 2021 - $27,229) to related parties.

## Critical Accounting Estimates

The preparation of these interim condensed consolidated financial statements in conformity with IFRS requires Management to make judgments and estimates that affect the reported amounts of assets and liabilities and disclosures of contingent assets and contingent liabilities at the date of the interim condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The interim condensed consolidated financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the interim condensed consolidated financial statements and may require accounting adjustments based on future occurrences.

Revisions to accounting estimates are recognized in the period in which the estimate is revised and may affect both the period of revision and future periods. While Management believes that the estimates are reasonable, actual results could differ materially from those estimates and may impact the future results of operations.

(i) COVID-19 Estimation Uncertainty

In March 2020, the World Health Organization declared the outbreak of COVID-19 a global pandemic. Government measures to limit the spread of COVID-19, including the closure of non-essential businesses, had an impact on the Company's operations from the second quarter of 2020. As at July 31, 2022, management did not identify any impairment indicators that suggest material impairment of the Company's assets or a significant change in the fair value of the assets due to COVID-19.

Due to the rapid developments and uncertainty surrounding COVID-19, it is not possible to predict the impact that COVID-19 will have on the Company's business, financial position and operating results in the future. In addition, it is possible that estimates in the Company's consolidated financial statements will change in the near term as a result of COVID-19 and the effect of any such changes could be material, which could result in, among other things, impairment of long-lived assets including intangibles and goodwill. The Company is closely monitoring the impact of the pandemic on all aspects of its business.

(ii) Share-based payment transactions

Certain equity-settled transactions are measured by reference to the fair value of the equity instruments granted. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This also requires determining the most appropriate inputs to the valuation model including the expected life of the share option or warrant, volatility, and dividend yield. These estimates are utilized noted in Note 18 and Note 21 of the interim condensed consolidated financial statements.

(iii) Business combinations

In a business combination, the Company may acquire assets and assume certain liabilities of an acquired entity. Judgement is used in determining whether an acquisition is a business combination or an asset acquisition. Estimates are made as to the fair value of the identifiable assets acquired and the liabilities assumed on the acquisition date, as well as the fair value of consideration paid and contingent consideration payable. In certain circumstances, such as the valuation of property, plant and equipment, intangible assets and goodwill acquired, the Company may rely on independent third-party valuators. The determination of these fair values involves a variety of assumptions, include revenue growth rates, expected operating income, discount rates, and earnings multiples.

(iv) Estimated useful lives and depreciation of property, plant and equipment, right-of-use asset and intangible assets with finite lives

Depreciation and amortization of property, plant and equipment, right-of-use asset and intangible assets with finite lives are dependent upon estimates of useful lives and when the asset is available for use, which are determined through the exercise of judgment and are dependent upon estimates that take into account factors such as economic and market conditions, frequency of use, anticipated changes in laws and technological improvements. These estimates are noted in Note 10 and Note 11 of the interim condensed consolidated financial statements.

(v) Impairment of property, plant and equipment, right-of-use asset and intangible assets other than goodwill

The assessment of any impairment on property, plant and equipment, right-of-use asset and intangible assets other than goodwill is dependent upon estimates of recoverable amounts. As the recoverable amount is the higher of fair value less costs of disposal ("FVLCS") and value in use ("VIU"), management must consider factors such as economic and market conditions, estimated future cash flows, discount rates and asset-specific risks. No impairment was recognized on any intangible assets with finite useful lives as no impairment indicators became known during the nine months ended July 31, 2022 as stated in Note 10 and Note 11 of the interim condensed consolidated financial statements.

(vi) Impairment of goodwill

The impairment test for cash generating units ("CGUs") to which goodwill is allocated is based on the higher of VIU and FVLCD of the CGU, determined in accordance with the expected cash flow approach. The calculation is based on assumptions including, but not limited to, the cash flow growth rate and the discount rate. As at July 31, 2022, management did not identify any impairment indicators that suggest material impairment of the Company's goodwill.

(vii) Determination of CGUs

Management is required to use judgement in determining which assets or group of assets make up appropriate CGUs for the level at which goodwill and intangible assets with indefinite lives are tested for impairment. A CGU is defined as the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets.

(viii) Valuation of financial instruments

The Company makes estimates and assumptions relating to the fair value measurement and disclosure of its convertible promissory note receivable, private company investments, contingent consideration payable and warrant liabilities. The fair values are determined using a variety of valuation techniques, as described further herein this MD&A, under the heading "Fair Value of Financial Instruments". The inputs to these models are derived from observable market data where possible, but where observable market data are not available, Management's judgment is required to establish fair values.

(ix) Control, joint control or significant influence

In determining the appropriate basis of accounting for the Company's interests in investees, judgment is applied regarding the degree to which the Company has the ability to control or exert significant influence over, directly or indirectly, the investees' financial and operating activities.

(x) Income taxes and recoverability of potential deferred tax assets

Income taxes and tax exposures recognized in the consolidated financial statements reflect Management's best estimate based on facts known at the reporting date. When the Company anticipates a future income tax payment based on its estimates, it recognizes a liability. The difference between the expected amount and the final tax outcome has an impact on current and deferred taxes when the Company becomes aware of this difference.

In addition, when the Company incurs losses for income tax purposes, it assesses the probability of taxable income being available in the future based on its budgeted forecasts. These forecasts are adjusted to take into account certain non-taxable income and expenses and specific rules on the use of unused credits and tax losses. When the forecasts indicate that sufficient future taxable income will be available to deduct the temporary differences, a deferred tax asset is recognized for all deductible temporary differences. These estimates are stated in Note 19 of the interim condensed consolidated financial statements.

(xi) Inventory

Inventory is valued at the lower of cost and net realizable value. Determining net realizable value requires the Company to make assumptions about estimated selling prices in the ordinary course of business, the estimated costs of completion and the estimated variable costs to sell. These are stated in Note 4 of the interim condensed consolidated financial statements.

(xii) Expected credit losses on financial assets

Determining an allowance for expected credit losses ("ECLs") for all debt financial assets not held at fair value requires management to make assumptions about the historical patterns for the probability of default, the timing of collection and the amount of incurred credit losses. These assumptions are adjusted based on Management's judgment about whether economic conditions and credit terms are such that actual losses may be higher or lower than what the historical patterns suggest. These are stated in Note 24 of the interim condensed consolidated financial statements.

(xiii) Going concern

The assessment of the Company's ability to execute its strategy by funding future working capital requirements involves judgement. Management monitors future cash requirements to assess the Company's ability to meet these future funding requirements. This is addressed in Note 1 of the interim condensed consolidated financial statements.

(xiv) Provisions

Provisions are recognized when the Company has a present obligation, legal or constructive as a result of a previous event, if it is probable that the Company will be required to settle the obligation and a reliable estimate can be made of the obligation. The amount recognized is the best estimate of the expenditure required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligations. Provisions are reviewed at the end of each reporting period and adjusted to reflect the current best estimate of the expected future cash flows. All obligations are noted in the liability section of the interim condensed consolidated financial statements.

## Changes in Accounting Policies Including Initial Adoption

(a) Amendment to IAS 1, Presentation of Financial Statements, Issued but not Yet Effective

IAS 1 was amended in January 2020 to address inconsistences with how entities apply the standard over classification of current and non-current liabilities. The amendment serves to address whether, in the statement of financial position, debt and other liabilities with an uncertain settlement should be classified as current or non-current. The amendment is effective for annual reporting periods beginning on or after January 1, 2023. Earlier adoption is permitted. The Company will adopt this amendment as of the effective date, and is currently assessing the impacts of adoption.

(b) Amendment to IAS 37, Provisions, Contingent Liabilities and Contingent Assets, Issued but not Yet Effective

IAS 37 was amended in May 2020 to clarify the costs a company should include as the cost of fulfilling a contract when assessing whether a contract is onerous. The amendment is effective for annual reporting periods beginning on or after January 1, 2022. Earlier adoption is permitted. The Company will adopt the amendment as of the effective date, and is currently assessing the impacts of adoption.

(c) Amendment to IAS 16, Property, Plant and Equipment, Issued but not Yet Effective

IAS 16 was amended in May 2020 to prohibit deducting from the cost of an item of property, plant and equipment any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognizes the proceeds from selling such items, and the cost of producing those items, in profit or loss. The amendment is effective for annual reporting periods beginning on or after January 1, 2022. Earlier adoption is permitted. The Company will adopt the amendment as of the effective date, and is currently assessing the impacts of adoption.

(d) Amendment to IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors, Issued but not Yet Effective

In February 2021, the International Accounting Standards Board (“IASB”) issued ‘Definition of Accounting Estimates’ to help entities distinguish between accounting policies and accounting estimates. The amendment is effective for annual reporting periods beginning on or after January 1, 2023. Earlier adoption is permitted. The Company will adopt the amendment as of the effective date, and is currently assessing the impacts of adoption.

## Financial Instruments and Risk Management

The Company is exposed to risks that arise from its use of financial instruments. This section describes the Company’s objectives, policies and processes for managing those risks and the methods used to measure them. Further quantitative information pertaining to these risks is presented throughout the interim consolidated financial statements.

There have been no substantive changes in the Company’s exposure to financial instrument risks, its objectives, policies and processes for managing those risks, or the methods used to measure them since October 31, 2021, unless otherwise stated.

(a) Credit risk

Credit risk is the risk of a potential loss to the Company if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company has moderate exposure to credit risk from its cash, short-term investments, accounts receivable, and convertible promissory note receivable. The risk exposure is limited to their carrying amounts at the statement of financial position date. The risk for cash and short-term investments is mitigated by holding these balances with highly-rated Canadian financial institutions. The Company therefore does not expect any credit losses on its cash and short-term investments.

The Company's accounts receivable balance consists of the following as at:

| | July 31, 2022<br>$ | October 31, 2021<br>$ |
|---|---|---|
| Trade accounts receivable from customers | 7,549,106 | 4,621,574 |
| Expected credit losses | (248,699) | (91,194) |
| Net trade receivables | 7,300,407 | 4,530,380 |
| Interest and other receivables | 225,584 | 242,905 |
| | 7,525,991 | 4,773,285 |

The Company provides credit to certain customers in the normal course of business and has established credit evaluation and monitoring processes to mitigate credit risk. Credit risk for customers is assessed on a case-by-case basis and a provision is recorded where required. As at July 31, 2022, the Company identified certain accounts that may result in a credit losses on its accounts receivable, for which expected credit losses were recognized.

The Company has assessed that there is a concentration of credit risk, as 76% of the Company’s trade accounts receivable is due from three customers as at July 31, 2022 (as at October 31, 2021 - 77% of the balance due from three customers).

An analysis of the aging of trade accounts receivable (net of allowance) is as follows as at:

| | July 31, 2022<br>$ | October 31, 2021<br>$ |
|---|---|---|
| Current (30 days or less) | 3,902,667 | 2,397,231 |
| 31-60 days | 2,599,132 | 1,558,194 |
| 61-90 days | 132,391 | 93,189 |
| Greater than 90 days | 666,217 | 481,766 |
| | 7,300,407 | 4,530,380 |

(b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet the financial obligations associated with its financial liabilities as they come due. The Company manages liquidity risk through the management of its capital structure. As at July 31, 2022, the Company had working capital of $5,592,190 (as at October 31, 2021 – $20,304,906). The Company does not yet have consistent and on-going positive cash flows from operations and as such, the Company may be dependent upon the issuance of new equity and/or debt to advance its production efforts and meet its financial obligations. If equity or debt financing is required, failure to obtain such financing on a timely basis may cause the Company to postpone, reduce or terminate its production plans. The Company has the following undiscounted contractual obligations subject to liquidity risk:

| | <1 year<br>$ | 2-5years<br>$ | > 5 years<br>$ |
|---|---|---|---|
| Accounts payable and accrued liabilities | 15,123,328 | - | - |
| Long-term debt | 11,829,284 | 10,535 | - |
| Derivative liabilities with cash settlement option | - | 1,923,600 | - |
| Contingent consideration payable | 645,176 | - | - |
| Total | 27,597,788 | 1,934,135 | - |

(c) Market Risk

(i) Foreign currency risk

Foreign currency risk is the risk that a variation in exchange rates between the Canadian dollar and other foreign Currencies will affect the Company's operations and financial results. The Company is exposed to this risk on its investment in EndoCanna, an associate that bears the U.S. dollar as its functional currency. The Company is required to translate the financial position and operating results of EndoCanna into Canadian dollars and to recognize its share of the resulting translation gain or loss in other comprehensive loss. The Company is further exposed to the risk through Opticann, a wholly owned subsidiary operating in United States and through its derivative liabilities denominated in USD. As at July 31, 2022 and October 31, 2021, the Company has not entered into any hedging agreements to mitigate foreign currency risk. As such, the Company's financial position and financial results may be adversely affected by the unfavorable fluctuations in currency exchange rates.

The following table provides a summary of financial assets and liabilities denominated in USD as at:

| | July 31, 2022<br>$ | October 31, 2021<br>$ |
|---|---|---|
| Cash | 4,997 | 3,579 |
| Accounts receivable | 659 | 659 |
| Accounts payable and other liabilities | 13,652 | 39,484 |
| Investment in associate | 2,385,023 | 2,459,747 |
| Derivative liabilities | 1,664,478 | 663,526 |

A 10% strengthening of the Canadian dollar against the foreign currencies listed above would increase other comprehensive loss by $137,064 for the nine-month period ended July 31, 2022 (for the year ended October 31, 2021 - $382,481). A 10% weakening of the Canadian dollar against the foreign currencies listed above would result in an equal, but opposite effect.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's short-term investments and finance lease earn fixed rates of interest in the range from 0.7% to 1.05% per annum and 10.00% per annum respectively. The Company is exposed to this risk on its long-term debt, part of which bears interest at a Canadian prime rate plus 1.25% per annum. As at July 31, 2022 and October 31, 2021, the Company had no hedging agreements in place.

(ii) Price risk

Price risk is the risk of variability in fair value due to movements in equity or market prices. As at July 31, 2022 and October 31, 2021, the Company is exposed to this risk on its contingent consideration payable in Heritage

Common Shares pursuant to the acquisition of Opticann, Purefarma and Premium 5, and the derivative liabilities payable in Common Shares.

## Fair Value of Financial Instruments

Assets recorded at fair value in the statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets and liabilities;

Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly; and

Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Financial instruments are measured either at fair value or at amortized cost. The table below lists the valuation methods used to determine the fair value of each financial instrument.

| | |
|---|---|
| **Financial Instruments measured at fair value** | |
| Contingent consideration payable | Discounted cash flow (Level 3) or Black-Scholes model (Level 3) |
| Convertible promissory note receivable | Amount due on demand (Level 3) |
| Derivative liabilities | Market value (Level 3) or Black-Scholes model (Level 3) |
| Other investments | Market Value (Level 3) |
| Note Receivable | Market Value (Level 3) |
| **Financial instruments measured at amortized cost** | |
| Cash; Short-term investments; Accounts receivable; Other current assets; Accounts payable and accrued liabilities | Carrying amount (approximates fair value due to short-term nature) |
| Long-term debt | Carrying value at the effective interest rate which approximates fair value |

During the three and nine-month periods ended July 31, 2022 and 2021, there were no transfers of amounts between levels.

## Conflicts of Interest

Certain officers and directors of the Company are officers and/or directors of or are associated with other cannabis companies. Such associations may give rise to conflicts of interest. The directors are required by law, however, to act honestly and in good faith with a view to the best interests of the Company and its shareholders and to disclose any personal interest which they may have in any material transaction which is proposed to be entered into with the Company and to abstain from voting as a director for the approval of any such transaction. As of the date of this MD&A, no conflict of interest has been disclosed by the Company's directors and officers, or identified by the Company.

## United States Operations and Regulatory Framework

As of July 31, 2022, the Company did not have any direct, indirect or material ancillary involvement in the United States cannabis industry and accordingly is not currently subject to Staff Notice 51-352. The Company currently has immaterial exposure to US cannabis operations in connection with: (a) its non-controlling 30% ownership interest in EndoCanna; (b) its subsidiary, Opticann; and (d) the equipment purchase and service agreement with Harvest Care.

EndoCanna concentrates in endocannabinoid DNA testing. EndoCanna has developed a home-based DNA test kit using a saliva collection. The test kit analyzes over 500 genes and more than 550,000 single nucleotide polymorphisms in the human body and provides a personalized "EndoDecoded" report, identifying how an individual's specific genetic makeup interacts with cannabinoids and terpenes. The custom report helps customers select cannabis with the right cannabinoid profile and assist with choosing the formulation, dosage, and best delivery method for their needs.

Opticann has an exclusive licensing agreement to use the patented VESIsorb® drug delivery system for absorption into the system. Although Opticann currently has no active operations in the United States, Opticann is preparing for the eCommerce launch of ArthroCBD, a CBD 25 mg softgel brand formulated using VESIsorb®. In addition, the Company is planning on selling the ArthroCBD through over-the-counter sales at leading U.S. retailers.

OptiCann developed arthrocbd.com as an e-commerce platform to sell CBD-based products in compliance with the Farm Bill (as hereinafter defined). The Company anticipates that the platform will utilize plug-ins from WooCommerce to power e-commerce functionality and Slate Payment software for payment processing, both of which were selected following a thorough diligence process undertaken by Opticann. The Company operationalized the site in May 2021.

The ArthroCBD branded products produced by Opticann are derived from industrial hemp, which may be sold legally under U.S. federal law, whether through retail sales or online, pursuant to the Agriculture Improvement Act of 2018, Pub. L. 115-334 (the "Farm Bill").

The passage of the Farm Bill materially altered federal law governing hemp by removing hemp from the CSA and establishing a federal regulatory framework for hemp production in the United States. Among other provisions, the Farm Bill: (a) explicitly amends the CSA to exclude all parts of the cannabis plant (including its cannabinoids, derivatives, and extracts) containing a delta-9 tetrahydrocannabinol concentration of not more than 0.3% on a dry weight basis from the CSA’s definition of "marihuana"; (b) permits the commercial production and sale of hemp; (c) precludes states, territories, and Indian tribes from prohibiting the interstate transport of lawfully-produced hemp through their borders; and (d) establishes the United States Department of Agriculture ("USDA") as the primary federal agency regulating the cultivation of hemp in the United States, while allowing states, territories, and Indian tribes to obtain (or retain) primary regulatory authority over hemp activities within their borders after receiving approval of their proposed hemp production plan from the USDA. Any such plan submitted by a state, territory, or Indian tribe to the USDA must meet or exceed minimum federal standards and receive USDA approval. Any state, territory, or Indian tribe that does not submit a plan to the USDA, or whose plan is not approved by the USDA, will be regulated by the USDA; provided that states retain the ability to prohibit hemp production within their borders. The Farm Bill will remain in effect until December 2023.

On October 31, 2019, the USDA issued an interim final rule (the "IFR") to implement the Farm Bill and on March 22, 2021, the final rule (the “Final Rule”) implementing the Farm Bill became effective. The Final Rule established regulations governing commercial hemp production in the United States and provides the framework for state departments of agriculture and Indian tribes to begin implementing commercial hemp production programs. In addition, following the issuance of the IFR, the USDA stated that it will begin, and has since begun, reviewing hemp production plans submitted by states, territories, and Indian tribes. Pursuant to the Farm Bill, the USDA has 60 days from the date a plan is submitted to approve or disapprove it. As of the date hereof, several states and Indian tribes have submitted plans to the USDA, some of which have been approved or disapproved.

The Farm Bill neither affects nor modifies the Federal Food, Drug and Cosmetic Act, thus expressly preserving the U.S. Food and Drug Administration’s (the "FDA") authority to regulate food, drugs, dietary supplements, and cosmetics containing cannabis and/or cannabis-derived compounds, such as CBD. On the same date that the Farm Bill was signed into law, the FDA issued a statement (i) reaffirming its jurisdiction over products containing cannabis and/or cannabis-derived compounds and (ii) restating its position that "it [is] unlawful to introduce food containing added CBD into interstate commerce, or to market CBD products as, or in, dietary supplements, regardless of whether the substances are hemp-derived," because CBD is an active ingredient in an FDA-approved drug and was the subject of substantial clinical investigations that were made public before it was marketed as a food or dietary supplement. Following the passage of the Farm Bill, the FDA has also acknowledged that "there is substantial public interest in marketing and accessing CBD in food, including dietary supplements . . . [and] [t]he statutory provisions that currently prohibit marketing CBD in these forms also allow the FDA to issue a regulation creating an exception, and some stakeholders have asked that the FDA consider issuing such a regulation to allow for the marketing of CBD in conventional foods or as a dietary supplement, or both." The FDA held a public hearing in May 2019 to obtain scientific data and information about the safety, manufacturing, product quality, marketing, labeling, and sale of products containing cannabis or cannabis-derived compounds, and also established a high-level internal working group to explore potential pathways for various types of CBD products to be lawfully marketed. Since the passage of the Farm Bill, the FDA has issued numerous warning letters to companies for illegally selling CBD products in interstate commerce.

Como Health LLC has built its operating facility and no sales have generated to date. Harvest Care has not begun its operations with the Company's equipment.

In accordance with Staff Notice 51-352, the Company will evaluate, monitor and reassess this disclosure, and any related risks, on an ongoing basis and the same will be supplemented, amended and communicated to investors in public filings, including in the event of government policy changes or the introduction of new or amended guidance, laws or regulations regarding cannabis regulation.

## Risks and Uncertainties

The following are certain factors relating to the Company's business which prospective investors should carefully consider before deciding whether to purchase Common Shares. The following information is a summary only of certain risk factors and is qualified in its entirety by reference to, and must be read in conjunction with, the detailed information appearing elsewhere in this MD&A. These risks and uncertainties are not the only ones the Company is facing or may ever face. Additional risk and uncertainties not presently known to the Company, or that are currently deemed immaterial, may also impair operations. If any such risks actually occur, the business, financial condition, liquidity and results of operations could be materially adversely affected.

*Additional Financing*

From time to time, the Company may require additional financing. The Company's ability to obtain additional financing, if and when required, will depend on investor demand, operating performance, the condition of the capital markets and other factors. If the Company raises additional funds through the issuance of equity, equity-linked or debt securities, those securities may have rights, preferences, or privileges senior to the rights of holders of Common Shares, and existing holders of such shares may experience dilution.

*Reliance on Licenses*

Failure to comply with the Health Canada licensing requirements, pursuant to the Cannabis Act and Cannabis Act Regulations, including any failure to apply for and secure the requisite licenses from Health Canada and maintain the Company's existing licenses would have a material, adverse impact on the business, financial condition and operating results of the Company as a whole, including all subsidiaries, whether or not the subsidiaries are license holders.

*Reliance on Facilities*

The Company's existing facilities in Falkland, British Columbia and Fort Erie, Ontario are integral to the Company's operations, as is the Company's ability to outfit its existing facilities to integrate the extraction capabilities of Purefarma. Any adverse changes or developments affecting either facility may impact the Company's ability to produce cannabis and cannabis products, its business, its financial condition, and the results of its operations.

*Volatile Market Price for Common Shares*

The market price for Common Shares may be volatile and subject to wide fluctuations in response to numerous factors, many of which are beyond the Company's control, including the following:

- actual or anticipated fluctuations in the Company's quarterly results of operations;
- recommendations by securities research analysts;
- changes in the economic performance or market valuations of companies in the industry in which the Company operates;
- addition or departure of the Company's executive officers and other key personnel;
- release or expiration of transfer restrictions on outstanding Common Shares;
- sales or perceived sales of additional Common Shares;
- operating and financial performance that vary from the expectations of management, securities analysts, and investors;
- regulatory changes affecting the Company's industry generally and its business and operations;
- announcements of developments and other material events by the Company or its competitors;
- fluctuations to the costs of vital production materials and services;
- changes in global financial markets and global economies and general market conditions, such as interest rates and price volatility of CBD and THC as active product ingredients;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving the Company or its competitors;
- operating and share price performance of other companies that investors deem comparable to the Company or from a lack of market comparable companies; and
- news reports relating to trends, concerns, technological or competitive developments, regulatory changes and other related issues in the Company's industry or target markets.

Financial markets have recently experienced significant price and volume fluctuations that have particularly affected the market prices of equity securities of companies and that have often been unrelated to the operating performance, underlying asset values or prospects of such companies. Such volatility has been particularly evident with regards to the share prices of cannabis companies that are reporting issuers in Canada. Accordingly, the market price of Common Shares may decline even if the Company's operating results, underlying asset values or prospects have not changed. Additionally, these factors, as well as other related factors, may cause decreases in asset values that are lasting and not temporary, which may result in impairment losses. There can be no assurance that continuing fluctuations in share price and volume will not occur. If such increased levels of volatility and market turmoil continue, the Company's operations could be adversely impacted, and the trading price of Common Shares may be materially adversely affected.

*Limited Market for Securities*

There can be no assurance that an active and liquid market for the Common Shares will be maintained and an investor may find it difficult to resell any securities of the Company.

*Licensing Requirements Under the Cannabis Regulations*

The market for cannabis (including medical cannabis) in Canada is regulated by the Controlled Drug and Substances Act, the Cannabis Act and Cannabis Act Regulations, the Narcotic Control Regulations, and other applicable laws. Any applicant seeking to become a licensed cultivator, producer and/or seller under the Cannabis Act Regulations is subject to stringent Health Canada licensing requirements. The government of Canada has only issued to date a limited number of licenses under the Cannabis Regulations to cultivate, process and/or sell cannabis. There are, however, several hundred applicants for licenses. The number of licenses granted could have an impact on the operations of the Company. Because of the early stage of the industry in which the Company operates, the Company expects to face additional competition from new entrants. If the number of users of cannabis in Canada increases, the demand for products will increase, and the Company expects that competition will become more intense, as current and future competitors begin to offer an increasing number of diversified products. To remain competitive, the Company will require a continued level of investment in research and development, marketing, sales, and client support. The Company may not have sufficient resources to maintain research and development, marketing, sales, and client support efforts on a competitive basis which could materially and adversely affect the business, financial condition and results of operations of the Company.

*Holding Company Status*

The Company is a holding company, and essentially, all of its operating assets are the capital stock of its subsidiaries. As a result, investors in the Company are subject to the risks attributable to its subsidiaries. As a holding company, the Company conducts substantially all of its business through its subsidiaries, which generate substantially all of its revenues. Consequently, the Company's cash flows and ability to complete current or desirable future enhancement opportunities are dependent on the earnings of its subsidiaries and the distribution of those earnings to the Company. The ability of these entities to pay dividends and other distributions will depend on their operating results and will be subject to applicable laws and regulations, which require that solvency and capital standards be maintained by such companies and contractual restrictions contained in the instruments governing their debt. In the event of a bankruptcy, liquidation or reorganization of any of the Company's subsidiaries, holders of indebtedness and trade creditors will generally be entitled to payment of their claims from the assets of those subsidiaries before any assets are made available for distribution to the Company.

*Force Majeure Events - COVID 19*

In December 2019, the novel coronavirus COVID-19 was reported to have surfaced in Wuhan, China. On March 11, 2020, the World Health Organization declared this outbreak a global pandemic. Major health issues and pandemics, such as COVID-19, may adversely affect trade, global and local economies, and the trading prices of the Common Shares. The outbreak may affect the supply chain of the Company and may restrict the level of economic activity in affected areas, which may adversely affect the price and demand for the Company's products as well as the Company's ability to collect outstanding receivables from its customers. It is possible that the Company may be required to declare an event of *force majeure* under certain existing contracts and temporarily close one or more of its facilities and suspend operations. Given the ongoing and dynamic nature of the circumstances, the extent to which COVID-19 will impact the Company's financial results and operations is uncertain. It is possible, however, that the Company's business operations and financial performance in 2021 and beyond may be materially adversely affected by this global pandemic.

*Management of Growth*

The Company may be subject to growth-related risks arising from expansion of its operations and further acquisitions. Such growth-related risks include capacity constraints and increased pressure on the Company's internal systems and controls. The ability of the Company to manage growth effectively will require continued implementation and improvement of its operational and financial systems and to expand, train and manage its employee base. The inability of the Company to deal with growth may have a material adverse effect on its business, financial condition, results of operations, and general prospects.

*Reliance on Management*

The success of the Company is dependent upon the ability, expertise, judgment, discretion, and good faith of its senior management. While employment agreements and incentive programs are customarily used as primary methods of retaining the services of key employees, these agreements and incentive programs cannot assure the continued services of such employees. Any loss of the services of such individuals could have a material adverse effect on the Company's business, operating results, or financial condition.

*Conflicts of Interest*

The Company may be subject to various potential conflicts of interest because of the fact that some of its officers and directors may be engaged in a range of business activities. In addition, the Company's executive officers and directors may devote time to their outside business interests, so long as such activities do not materially or adversely interfere with their duties to the Company, as applicable. External business interests may require significant time and attention of the Company's executive officers and directors. In some cases, executive officers and directors may have fiduciary obligations associated with external business interests that may interfere with their abilities to devote time to the Company's business and affairs, as applicable, and this could adversely affect the Company's operations.

In addition, the Company may also become involved in transactions that conflict with the interests of its respective directors and the officers, who may from time to time deal with persons, firms, institutions or corporations with which the Company may be dealing, or which may be seeking investments similar to those desired by it. The interests of these persons, firms, institutions or corporations could conflict with those of the Company. In addition, from time to time, these persons, firms, institutions or corporations may be competing with the Company for available investment opportunities. Conflicts of interest, if any, will be subject to the procedures and remedies provided under the applicable laws and in accordance with Company policies including its Fraud Prevention Policy and Related Party Transaction Policy. In the event that such a conflict of interest arises at a meeting of the Company's directors, a director who has such a conflict will abstain from voting for or against the approval of such participation or such terms. In accordance with the applicable laws, the directors of the Company are required to act honestly, in good faith and in the best interests of the Company.

*Litigation*

The Company may become party to litigation from time to time in the ordinary course of its business, which could adversely affect its operations. Should any litigation in which the Company becomes involved be determined against it, such a decision may adversely affect the Company's ability to continue operating, adversely affect the market price of Common Shares, and use significant resources. Even if the Company is involved in litigation and succeeds, litigation can redirect significant Company resources. Litigation may also create a negative perception of the Company's brand and the brands of its subsidiaries.

*Dividends*

The Company's policy is to retain earnings to finance the development and enhancement of its products and to otherwise reinvest in the Company's businesses. Therefore, the Company does not anticipate paying cash dividends on Common Shares in the foreseeable future. Any decision to declare and pay dividends in the future will be made at the discretion of the Board and will depend on, among other things, financial results, cash requirements, contractual restrictions and other factors that the Board may deem relevant. As a result, investors may not receive any return on investment in the Common Shares unless they sell them for a share price that is greater than that at which such investors purchased them.

*Liquidity Risk*

The Company's ability to remain liquid over the long term depends on its ability to obtain additional financing. The Company has in place planning and budgeting processes to help determine the funds required to support normal operating requirements on an ongoing basis as well as its planned development and capital expenditures. The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due.

*Cyber Security*

The Company relies on certain internal processes, infrastructure and information technology systems to efficiently operate its business in a secure manner. The Company's risk and exposure to these matters cannot be fully mitigated because of, among other things, the evolving nature of these threats. As a result, cyber security and the continued development and enhancement of controls, training, processes designed to protect systems, computers, software, date and networks from attack, damage or unauthorized access is a priority. The inability to continue to enhance or prevent a failure of these internal processes, infrastructure or information technology systems could negatively impact the Company's ability to operate its business.

*Intellectual Property Risk*

The success of the Company's business depends in part on its ability to protect its ideas, technology and proprietary know-how. Even as the Company moves to protect its intellectual property with trademarks and trade processes, patents, copyrights or by other means, it is not assured that competitors will not develop similar technologies, methods or that in the event of an infringement, the Company will be able to exercise its legal rights. Actions taken to protect or preserve intellectual property rights may require significant resources such that said actions meaningfully impact the ability to successful grow the business.

*Third Party Transportation*

The Company is required to rely on third party transportation services. The Company is exposed to the inherent risks associated with relying on third party transportation service providers, including logistical problems, delays, loss or theft of product, and increased shipping costs. Any delay in transporting the product, breach of security or loss of product, could have material adverse effect on the Company's business, financial performance and results of operations. Moreover, any breach of security and loss of product during transport could affect the Company's status as a Licensed Producer, as such term is defined in the Cannabis Act.

<u>Risks related to operating in the Cannabis Industry</u>

*The Cannabis Industry is Subject to Competition*

There is potential that the Company will face intense competition from other companies, some of which can be expected to have longer operating histories and more financial, production and marketing resources and experience than the Company. Additionally, there is potential that the industry will undergo consolidation, creating larger companies that may have increased geographic scope and other economies of scale. Increased competition by larger, better-financed competitors with geographic or other structural advantages could materially and adversely affect the business, financial condition and results of operations of the Company.

As noted previously under the sub-heading entitled "*Licensing Requirements Under the Cannabis Regulations*," because of the early stage of the industry in which the Company operates in the cannabis market, the Company expects to face additional competition from new entrants. If the number of users of cannabis in Canada increases, the demand for products will increase and the Company expects that competition will become more intense, as current and future competitors begin to offer an increasing number of diversified products and pricing strategies. To remain competitive, the Company will require a continued high level of investment in research and development, marketing, sales and client support. The Company may not have sufficient resources to maintain research and development, marketing, sales and client support efforts on a competitive basis which could materially and adversely affect the business, financial condition and results of operations of the Company.

*Consumer perception*

Consumer perception regarding the safety, efficacy and quality of cannabis can be significantly influenced by scientific research or findings, regulatory investigations, litigation, media attention and other publicity regarding consumption of medicinal marijuana products. There can be no assurance that consumer perception will remain positive or that adverse research reports, findings, proceedings, media attention or publicity, with or without merit, will not have a material and adverse impact on the cannabis industry as a whole, or the Company's ability to sell its products.

*Regulatory Risks*

The Company's subsidiaries operate in a new industry which is highly regulated, highly competitive and evolving rapidly. As such, new risks may emerge, and management may not be able to predict all such risks or be able to predict how such risks may result in actual results differing from the results contained in any forward-looking statements. The Company's ability to grow, store, process and sell cannabis in Canada is dependent on obtaining licenses from Health Canada and the need to maintain such licenses in good standing. As noted previously under the sub-heading entitled "*Reliance on Licenses*," failure to: (i) comply with the requirements of a license; and (ii) maintain a license would have a material adverse impact on the business, financial condition and operating results of the Company.

The Company will incur ongoing costs and obligations related to regulatory compliance. Failure to comply with regulations may result in additional costs for corrective measures, penalties or in restrictions of the Company's operations. In addition, changes in regulations, more vigorous enforcement thereof or other unanticipated events could require extensive changes to the Company's operations, increased compliance costs or give rise to material liabilities, which could have a material adverse effect on the business, results of operations and financial condition of the Company.

The industry is subject to extensive controls and regulations, which may significantly affect the financial condition of market participants. The marketability of any product may be affected by numerous factors that are beyond the Company's control and which cannot be predicted, such as changes to government regulations, including those relating to taxes and other government levies which may be imposed. Changes in government levies, including taxes, could reduce the Company's earnings and could make future capital investments or the Company's operations uneconomic. The industry is also subject to numerous legal challenges, which may significantly affect the financial condition of market participants and which cannot be reliably predicted.

*The Company is subject to changes in Canadian laws, regulations and guidelines which could adversely affect the Company's future business, financial condition and results of operations.*

The Company's operations are subject to various laws, regulations and guidelines relating to the manufacture, management, packaging/labelling, advertising, sale, transportation, storage and disposal of cannabis but also including laws and regulations relating to drugs, controlled substances, health and safety, the conduct of operations and the protection of the environment. Changes to such laws, regulations and guidelines due to matters beyond the control of the Company may cause adverse effects business, financial condition and results of operations of the Company. The Company endeavours to comply with all relevant laws, regulations and guidelines. To the best of the Company's knowledge, the Company is in compliance or in the process of being assessed for compliance with all such laws, regulations and guidelines.

On June 30, 2016, the Canadian Federal Government established the Task Force on Cannabis Legalization and Regulation to seek input on the design of a new system to legalize, strictly regulate and restrict access to marijuana. On November 30, 2016, the Task Force on Cannabis Legalization and Regulation completed its review and published a report outlining its recommendations. On April 13, 2017, the Canadian Federal Government released Bill C-45, which proposed the enactment of the Cannabis Act, to regulate the production, distribution and sale of cannabis for unqualified adult use. On October 17, 2018, the Cannabis Act, as well as laws to address drug-impaired driving, protect public health and safety and prevent youth access to cannabis, came into force.

The Cannabis Act prohibits testimonials and branding and packaging that is appealing to youth. The restrictions on advertising, marketing and the use of logos and brand names could have a material adverse impact on the Company's business, financial condition and results of operation. The legislative framework pertaining to the Canadian adult-use cannabis market is developing and subject to change. In addition, the governments of every Canadian province and territory have, to varying degrees, announced proposed, and in some cases enacted, regulatory regimes for the distribution and sale of cannabis for adult-use purposes within those jurisdictions.

*Environmental Regulations and Risks*

The Company's operations are subject to environmental regulation. These regulations mandate, among other things, the maintenance of air and water quality standards and land reclamation. They also set forth limitations on the generation, transportation, storage and disposal of solid and hazardous waste. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations.

Government approvals and permits are currently, and may in the future, be required in connection with the Company's operations. To the extent such approvals are required and not obtained, the Company may be curtailed or prohibited from the proposed production of cannabis or from proceeding with the development of their operations as currently proposed.

Failure to comply with applicable laws, regulations and permitting requirements may result in enforcement actions thereunder, including orders issued by regulatory or judicial authorities causing operations to cease or be curtailed, and may include corrective measures requiring capital expenditures, installation of additional equipment, or remedial actions. The Company may be required to compensate those suffering loss or damage by reason of its operations and may have civil or criminal fines or penalties imposed for violations of applicable laws or regulations.

*Vulnerability to Rising Energy Costs*

The Company's cannabis growing operations consume considerable energy and produce certain carbon emissions, particularly as the Company cultivates its products in indoor facilities, making the Company vulnerable to rising energy costs and any regulation regarding carbon pricing. Rising or volatile energy costs and regulation regarding carbon pricing may adversely impact the business of the Company and its ability to operate profitably.

*Restrictions on Sales Activities*

The industry is in its early development stage and restrictions on sales and marketing activities imposed by Health Canada, various medical associations, other governmental or quasi-governmental bodies or voluntary industry associations may adversely affect the Company's ability to conduct sales and marketing activities and could have a material adverse effect on the Company's respective businesses, operating results and financial conditions.

*Product Liability*

As a manufacturer and distributor of products designed to be ingested or inhaled by humans, the Company faces an inherent risk of exposure to product liability claims, regulatory action and litigation if its products are alleged to have caused significant loss or injury. In addition, the manufacture and sale of products involve the risk of injury or loss to consumers due to tampering by unauthorized third parties, product contamination, unauthorized use by consumers or other third parties. Previously unknown adverse reactions resulting from human consumption of the Company's products alone or in combination with other medications or substances could occur. The Company may be subject to various product liability claims, including, among others, that the Company's products caused injury, illness or loss, include inadequate instructions for use or include inadequate warnings concerning possible side effects or interactions with other substances. A product liability claim or regulatory action against the Company could result in increased costs, adversely affect the Company's reputation with its respective clients and consumers generally, and adversely affect the results of operations and financial conditions of the Company.

*Product Recalls*

Manufacturers and distributors of products may be subject to the recall or return of their products for a variety of reasons, including product defects, such as contamination, unintended harmful side effects or interactions with other substances, packaging safety and inadequate or inaccurate labeling disclosure. If any of the Company's products are recalled due to an alleged product defect or for any other reason, the Company could be required to incur the unexpected expense of the recall and any legal proceedings that might arise in connection with the recall. The Company may lose a significant amount of sales and may not be able to replace those sales at an acceptable margin, or at all. In addition, a product recall may require significant Management attention and may require a substantial change in the Company's manufacturing process.

*Operating Risk and Insurance Coverage*

The Company has insurance to protect its assets, operations and employees. While the Company believes its insurance coverage is customary in its current state of operations, such insurance is subject to coverage limits and exclusions and may not be available for the risks and hazards to which the Company is exposed. However, the Company may also be unable to maintain insurance to cover these risks at economically feasible premiums. Insurance coverage may not continue to be available or may not be adequate to cover any resulting liability. The Company might also become subject to liability for pollution or other hazards, which the Company may not be insured against or which the Company may elect not to insure against because of premium costs or other reasons. Losses from these events may cause the Company to incur significant costs that could have a material adverse effect upon the Company's financial performance and results of operations.

*Unfavourable Publicity or Consumer Perception*

Management of the Company believes the cannabis industry is highly dependent upon consumer perception regarding the safety, efficacy and quality of the cannabis produced. Consumer perception of the Company's proposed products can be significantly influenced by scientific research or findings, regulatory investigations, litigation, media attention and other publicity regarding the consumption of cannabis products. There can be no assurance that future scientific research, findings, regulatory proceedings, litigation, media attention or other research findings or publicity will be favourable to the cannabis market or any particular product, or consistent with earlier publicity.

Future research reports, findings, regulatory proceedings, litigation, media attention or other publicity that are perceived as less favourable than, or that question, earlier research reports, findings or publicity could have a material adverse effect on the demand for the Company's proposed products and the business, results of operations, financial condition and cash flows of the Company. The Company's dependence upon consumer perceptions means that adverse scientific research reports, findings, regulatory proceedings, litigation, media attention or other publicity, whether or not accurate or with merit, could have a material adverse effect on the Company, the demand for its proposed products, and the business, results of operations, financial condition and cash flows of the Company. Further, adverse publicity reports or other media attention regarding the safety, efficacy and quality of cannabis in general, or the Company's proposed products specifically, or associating the consumption of cannabis with illness or other negative effects or events, could have such a material adverse effect. Such adverse publicity reports or other media attention could arise even if the adverse effects associated with such products resulted from consumers' failure to consume such products appropriately or as directed.

<ins>Overview of United States Regulations of Cannabis</ins>

*Regulatory scrutiny of the Company's interests in the United States*

The Company's interests in the United States cannabis market, and future licensing arrangements, may become the subject of heightened scrutiny by regulators, stock exchanges, clearing agencies and other authorities in Canada. As a result, the Company may be subject to significant direct and indirect interaction with public officials. There can be no assurance that this heightened scrutiny will not in turn lead to the imposition of certain restrictions on the Company's ability to carry on its business in the United States.

Government policy changes or public opinion may also result in a significant influence over the regulation of the cannabis industry in Canada, the United States or elsewhere. A negative shift in the public's perception of cannabis in the United States or any other applicable jurisdiction could affect future legislation or regulation. It has been reported by certain publications in Canada that The Canadian Depository for Securities Limited is considering a policy shift that would see its subsidiary, CDS, refuse to settle trades for cannabis issuers that have investments in the United States. CDS is Canada's central securities depository, clearing and settlement hub settling trades in the Canadian equity, fixed income and money markets. Neither CDS nor its parent company have issued any public statement with regard to these reports. However, if CDS were to proceed in the manner suggested by these publications, and apply such a policy to the Company, it would have a material adverse effect on the ability of holders of securities of the Company to make trades. In particular, the securities of the Company would become highly illiquid, as investors would have no ability to effect a trade of the securities through the facilities of a stock exchange.

Government policy changes or public opinion may also result in a significant influence over the regulation of the cannabis industry in Canada, the United States or elsewhere. A negative shift in the public's perception of medical or recreational cannabis in the United States or any other applicable jurisdiction could affect future legislation or regulation. Among other things, such a shift could cause state jurisdictions to abandon initiatives or proposals to legalize medical and/or recreational cannabis, thereby limiting the number of new state jurisdictions into which the Company could expand. Any inability to fully implement the Company's expansion strategy may have a material adverse effect on the Company's business, financial condition and results of operations.

*Cannabis remains illegal under federal law in the United States, and therefore, strict enforcement of federal laws regarding cannabis would likely result in our inability to execute our business plan.*

Cannabis, other than hemp (defined by the U.S. government as Cannabis sativa L. with a tetrahydrocannabinol (THC) concentration of not more than 0.3% on a dry weight basis), is a Schedule I controlled substance under the CSA. In December 2018, the U.S. government changed hemp's legal status. The Farm Bill, removed hemp and extracts of hemp, including CBD, from the CSA schedules. Accordingly, the production, sale and possession of hemp or extracts of hemp, including certain CBD products, no longer violate the CSA. U.S. states have implemented a patchwork of different laws on hemp and its extracts, including CBD. Additionally, the U.S. Food and Drug Administration claims that the Food, Drugs & Cosmetics Act significantly limits the legality of hemp-derived CBD products.

Even in U.S. states or territories that have legalized cannabis to some extent, the cultivation, possession, and sale of cannabis all violate the CSA and are punishable by imprisonment, substantial fines and forfeiture. Moreover, individuals and entities may violate federal law if they aid and abet another in violating the CSA, or conspire with another to violate the law, and violating the CSA is a predicate for certain other crimes, including money laundering laws and the Racketeer Influenced and Corrupt Organizations Act. The U.S. Supreme Court has ruled that the federal government has the authority to regulate and criminalize the sale, possession and use of cannabis, even for individual medical purposes, regardless of whether it is legal under state law. For over five years, however, the U.S. government has not prioritized the enforcement of those laws against cannabis companies complying with state law and their vendors. No reversal of that policy of prosecutorial discretion is expected under a Biden administration given his campaign's position on cannabis, discussed further below, although prosecutions against state-legal entities cannot be ruled out.

On January 4, 2018, then U.S. Attorney General Jeff Sessions issued a memorandum for all U.S. Attorneys (the "Sessions Memo") rescinding certain past U.S. Department of Justice ("DOJ") memoranda on cannabis law enforcement, including the Memorandum by former Deputy Attorney General James Michael Cole (the "Cole Memo") issued on August 29, 2013, under the Obama administration. Describing the criminal enforcement of federal cannabis prohibitions against those complying with state cannabis regulatory systems as an inefficient use of federal investigative and prosecutorial resources, the Cole Memo gave federal prosecutors discretion not to prosecute state law compliant cannabis companies in states that were regulating cannabis, unless one or more of eight federal priorities were implicated, including use of cannabis by minors, violence, or the use of federal lands for cultivation. The Sessions Memo, which remains in effect, states that each U.S. Attorney's Office should follow established principles that govern all federal prosecutions when deciding which cannabis activities to prosecute. As a result, federal prosecutors could and still can use their prosecutorial discretion to decide to prosecute even state-legal cannabis activities. Since the Sessions Memo was issued over three years ago, U.S. Attorneys have generally not prioritized the targeting of state law compliant entities.

Then Attorney General William Barr testified in his confirmation hearing on January 15, 2019, that he would not upset "settled expectations," "investments," or other "reliance interest[s]" arising as a result of the Cole Memo, and that he did not intend to devote federal resources to enforce federal cannabis laws in states that have legalized cannabis "to the extent people are complying with the state laws." He stated: "My approach to this would be not to upset settled expectations and the reliance interests that have arisen as a result of the [Cole Memo] and investments have been made and so there has been reliance on it, so I don't think it's appropriate to upset those interests." He also implied that the CSA's prohibitions of cannabis may be implicitly nullified in states that have legalized cannabis: "[T]he current situation … is almost like a back-door nullification of federal law." Industry observers generally have not interpreted Attorney General Barr's comments to suggest that the DOJ would proceed with cases against participants who entered the state-legal industry after the Cole Memo's rescission. Nevertheless, while Attorney General Barr did not initiate any criminal prosecutions against state-legal cannabis companies, he did launch multiple antitrust investigations related to several cannabis mergers during 2020. Currently, the post of Attorney General is held by Merrick Garland who has repeatedly stated that he feels the Department of Justice should not be using its limited resources to go after state-legal cannabis businesses.

As such, there is no assurance that each U.S. Attorney's Office in each judicial district will not choose to strictly enforce federal laws governing cannabis sales in the event the Company commences any cannabis activities in the United States. The Company believes that the basis for the U.S. federal government's lack of recent enforcement with respect to the cannabis industry extends beyond the strong public sentiment and ongoing prosecutorial discretion. Since 2014, versions of the U.S. omnibus spending bill have included a provision prohibiting the DOJ, which includes the Drug Enforcement Administration, from using appropriated funds to prevent states from implementing their medical-use cannabis laws. In USA vs. McIntosh, the U.S. Court of Appeals for the Ninth Circuit held that the provision prohibits the DOJ from spending funds to prosecute individuals who engage in conduct permitted by state medical-use cannabis laws and who strictly comply with such laws. The court noted that, if the spending bill provision were not continued, prosecutors could enforce against conduct occurring during the statute of limitations even while the provision was previously in force. Other courts that have considered the issue have ruled similarly, although courts disagree about which party bears the burden of proof of showing compliance or noncompliance with state law. Consequently, it is feasible that in the future that Company may directly or indirectly sell adult-use cannabis, if permitted by such state and local laws now or in the future, and therefore may be outside any protections extended to medical-use cannabis under the spending bill provision. This could subject us to greater and/or different federal legal and other risks as compared to businesses where cannabis is sold exclusively for medical use, which could in turn materially adversely affect our business. Furthermore, any change in the federal government's enforcement posture with respect to state-licensed cannabis sales, including the enforcement postures of individual federal prosecutors in judicial districts where the Company may operate, would result in our inability to execute our then business plan, and we would likely suffer significant losses with respect to client base, which would adversely affect our operations, cash flow and financial condition.

While President Biden's position on cannabis falls short of full legalization, he campaigned on a platform of relaxing enforcement of cannabis proscriptions, including decriminalization generally, though the specific timeframe under which such decriminalization will occur is unknown. According to the Biden campaign website: "A Biden Administration will support the legalization of cannabis for medical purposes and reschedule cannabis as a CSA Schedule II drug so researchers can study its positive and negative impacts. This will include allowing the [Department of Veteran's Affairs] to research the use of medical cannabis to treat veteran-specific health needs." He has pledged to "decriminalize" cannabis, which could prompt his U.S. Attorney General to issue policy guidance to U.S. Attorneys that they should not enforce federal cannabis prohibition against state law compliant entities and others legally transacting business with them. Indeed, the Biden-Sanders Unity Platform, which was released at the time President Biden won the Democratic Party nomination for President, affirmed that his administration would seek to "[d]ecriminalize marijuana use and legalize marijuana for medical purposes at the federal level;" "allow states to make their own decisions about legalizing recreational use;" and "automatically expunge all past marijuana convictions for use and possession." Vice President Harris echoed these intentions during the vice presidential debate, saying that "[w]e will decriminalize marijuana and we will expunge the records of those who have been convicted of marijuana[-related offenses]." While President Biden's promise to decriminalize likely would mean that the federal government would not criminally enforce the Schedule II status against state legal entities, the implications are not entirely clear.

Although the U.S. Attorney General could issue policy guidance to federal prosecutors that they should not interfere with cannabis businesses operating in compliance with states' laws, any such guidance would not have the force of law, and could not be enforced by the courts. The President alone cannot legalize medical cannabis, and as states have demonstrated, legalizing medical cannabis can take many different forms. While rescheduling cannabis to the CSA's Schedule II would ease certain research restrictions, it would not make the state medical or adult-use programs federally legal. Recent steps taken by the Biden Administration and Congress have spurred some hope of drug policy change. Notably, President Biden appointed known medical cannabis advocate Dr. Rahul Gupta as the director of the Office of National Drug Control Policy. Further, on July 14, 2021, United States Senators Cory Booker, Ron Wyden and Chuck Schumer, released a draft of their long-awaited comprehensive cannabis reform legislation, the Cannabis Administration and Opportunity Act, which would effectively decriminalize cannabis in the United States by removing it from the CSA and which would empower states to implement their own cannabis laws (“Senate Cannabis Act”). However, while industry observers are hopeful that the Senate Cannabis Act will spur helpful discussions related to decriminalization, strong Republican opposition makes it difficult for any assurances to be made regarding its passage. Accordingly, we cannot predict the timing of any change in federal law or possible changes in federal enforcement. In the unlikely event that the federal government were to reverse its long-standing hands-off approach to the state legal cannabis markets and start more broadly enforcing federal law regarding cannabis, this may hinder potential expansion opportunities of the Company into the United States.

*Anti-money laundering laws and regulations*

The Company is subject to a variety of laws and regulations domestically and in the United States that involve money laundering, financial recordkeeping, and proceeds of crime, including the Bank Secrecy Act, as amended by Title III of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act), Sections 1956 and 1957 of U.S.C. Title 18 (the Money Laundering Control Act), the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (Canada), as amended, and the rules and regulations thereunder, the Criminal Code (Canada) and any related or similar rules, regulations or guidelines, issued, administered or enforced by governmental authorities in the United States and Canada. Banks often refuse to provide banking services to businesses involved in the U.S. cannabis industry due to the present state of the laws and regulations governing financial institutions in the United States. The lack of banking and financial services presents unique and significant challenges to businesses in the medical cannabis industry. The potential lack of a secure place in which to deposit and store cash, the inability to pay creditors through the issuance of checks and the inability to secure traditional forms of operational financing, such as lines of credit, are some of the many challenges presented by the unavailability of traditional banking and financial services.

In February 2014, the Department of the Treasury Financial Crimes Enforcement Network ("FinCEN"), a division of the U.S. Department of Treasury, issued the FinCEN Guidance, providing instructions to banks seeking to provide services to cannabis-related businesses. The FinCEN Guidance states that in some circumstances, it is permissible for banks to provide services to cannabis-related businesses without risking prosecution for violation of federal money laundering laws. It refers to supplementary guidance that former Deputy Attorney General James M. Cole issued to federal prosecutors relating to the prosecution of money laundering offenses predicated on cannabis-related violations of the CSA. While the FinCEN Guidance has not been rescinded by the DOJ at this time, it remains unclear whether the current administration will follow its guidelines. Overall, the DOJ continues to have the right and power to prosecute crimes committed by banks and financial institutions, such as money laundering and violations of the Bank Secrecy Act that occur in any U.S. state, including in states that have legalized the applicable conduct, and the DOJ's current enforcement priorities could change for any number of reasons, including a change in administration, the opinions of the President of the United States or the United States Attorney General. A change in the DOJ's enforcement priorities could result in the DOJ prosecuting banks and financial institutions for crimes that previously were not prosecuted. On September 25, 2019, the U.S. House of Representatives passed the Secure and Fair Enforcement Banking Act of 2019 (commonly known as the SAFE Banking Act) which aims to provide safe harbor and guidance to financial institutions that work with legal U.S. cannabis businesses. The SAFE Banking Act will next require passage by the U.S. Senate. On September 23, 2021, the U.S. House of Representatives approved a defense spending bill (the National Defense Authorization Act) including an amendment that contained cannabis banking reform. However, the Senate text of the bill does not contain the same language, which means the discrepancy would need to be settled in a bicameral conference committee after the Senate passes its version of the legislation.

In the event that any of the Company's operations, or any proceeds thereof, any dividends or distributions therefrom, or any profits or revenues accruing from such operations in the United States were found to be in violation of money laundering legislation or otherwise, such transactions may be viewed as proceeds of crime under one or more of the statutes noted above or any other applicable legislation. This could restrict or otherwise jeopardize the ability of the Company to declare or pay dividends, effect other distributions or subsequently repatriate such funds back to Canada. Furthermore, while there are no current intentions to declare or pay dividends in the foreseeable future, in the event that a determination was made that the Company's proceeds from operations (or any future operations or investments in the United States) could reasonably be shown to constitute proceeds of crime, the Company may decide or be required to suspend declaring or paying dividends without advance notice and for an indefinite period of time.

## Additional Information

Additional information relating to the Company, including the Company’s annual information form, may be found on the Company’s website at www.heritagecann.com, the SEDAR website located at www.sedar.com or the Canadian Stock Exchange website located at www.thecse.com/en.

BY ORDER OF THE BOARD

Heritage Cannabis Holdings Corp.

“David Schwede”

CEO and Director

September 27, 2022