

Interim Condensed Consolidated Financial Statements of

ESPIAL GROUP INC.

Quarters ended March 31, 2017 and 2016

(Unaudited)

ESPIAL GROUP INC.

Interim Condensed Consolidated Financial Statements

For the Quarters ended March 31, 2017 and 2016

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ESPIAL GROUP INC.

Interim Condensed Consolidated Balance Sheets

(In Canadian Dollars)

(Unaudited)

	March 31, 2017	December 31, 2016
CURRENT ASSETS		
Cash and cash equivalents	\$ 41,707,814	\$ 43,047,878
Accounts receivable	8,176,253	10,475,563
Investment tax credits receivable	371,740	321,018
Prepaid expenses and other assets	817,532	653,055
	51,073,339	54,497,514
Property and equipment (Note 6)	1,466,869	1,420,957
Intangible assets (Note 6)	1,635,188	1,818,067
Goodwill (Note 6)	3,632,604	3,632,604
	\$ 57,808,000	\$ 61,369,142
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 3,384,732	\$ 4,542,527
Provisions (Note 10)	272,026	334,591
Deferred revenue	1,548,052	2,054,323
	5,204,810	6,931,441
Total Liabilities	5,204,810	6,931,441
COMMITMENTS (Note 8)		
SHAREHOLDERS' EQUITY		
Share capital (Note 4)	124,900,373	125,362,413
Share based payments reserve	16,029,337	15,601,861
Deficit	(88,326,520)	(86,526,573)
	52,603,190	54,437,701
	\$ 57,808,000	\$ 61,369,142

APPROVED BY THE BOARD



Jaison Dolvane



Peter Seeligsohn

See accompanying notes

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Loss and Comprehensive Loss

(In Canadian Dollars)

(Unaudited)

	Three Months Ended	
	March 31, 2017	March 31, 2016
Revenue		
Software	\$ 5,025,351	\$ 2,440,739
Professional services	1,585,934	1,672,025
Support and maintenance	2,052,725	1,211,218
Total revenue	8,664,010	5,323,982
Cost of revenue	2,236,021	1,928,983
Gross margin	6,427,989	3,394,999
Expenses		
Sales and marketing	1,655,158	1,264,443
General and administrative	1,006,700	864,748
Research and development	5,285,630	2,890,216
Amortization of intangible assets	182,879	174,683
	8,130,367	5,194,090
Loss before other expense	(1,702,378)	(1,799,091)
Other expense	(82,996)	(223,550)
Interest income	62,544	86,732
Loss before taxes	(1,722,830)	(1,935,909)
Income taxes	(77,117)	(31,623)
Net loss and comprehensive loss	\$ (1,799,947)	\$ (1,967,532)
Loss per common share - basic	\$ (0.05)	\$ (0.05)
Weighted average number of common shares outstanding - basic (Note 5)	36,540,333	37,355,246
Loss per common share – diluted	\$ (0.05)	\$ (0.05)
Weighted average number of common shares outstanding - diluted (Note 5)	36,540,333	37,355,246

See accompanying notes to interim condensed consolidated financial statements

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Shareholders' Equity

(In Canadian Dollars, except share amounts)
(Unaudited)

	Three Months Ended	
	March 31, 2017	March 31, 2016
CASH USED IN		
OPERATING		
Net loss	\$ (1,799,947)	\$ (1,967,532)
Items not affecting cash		
Depreciation of property and equipment	99,831	68,451
Amortization of intangible assets	182,879	174,683
Share-based compensation expense (Note 9)	432,486	389,456
Provisions	(62,565)	-
	(1,147,316)	(1,334,942)
Changes in non-cash operating working capital items (Note 7)	420,045	115,364
	(727,271)	(1,219,578)
INVESTING		
Purchase of equipment	(145,743)	(97,659)
Purchase of intangibles	-	(125,129)
	(145,743)	(222,788)
FINANCING		
Options exercised	6,183	9,430
Share repurchase program	(473,233)	-
	(467,050)	9,430
Net cash and cash equivalents outflow	(1,340,064)	(1,432,936)
Cash and cash equivalents, beginning of period	43,047,878	49,947,096
Cash and cash equivalents, end of period	\$ 41,707,814	\$ 48,514,160
Supplementary Information		
Interest Received	\$ 62,544	\$ 86,832
Taxes paid	\$ 77,117	\$ 31,623

See accompanying notes to interim condensed consolidated financial statements

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Shareholders' Equity

(In Canadian Dollars, except share amounts)
(Unaudited)

	Common Shares		Share Based Payments Reserve	(Deficit)	Shareholders' Equity (Deficit)
	Number	Amount			
Balance at December 31, 2015	37,348,057	\$126,583,844	\$14,059,806	\$(81,651,804)	\$58,991,846
Share-based compensation	-	-	389,4566	-	389,456
Options exercised (Note 4)	10,458	17,030	(7,600)	-	9,430
Net and comprehensive loss	-	-	-	(1,967,532)	(1,967,532)
Balance at March 31, 2016	37,358,515	\$126,600,874	\$14,441,662	\$(83,619,336)	\$57,423,200
Balance at December 31, 2016	36,721,394	\$125,362,413	\$15,601,861	\$(86,526,573)	\$54,437,701
Share-based compensation	-	-	432,486	-	432,486
Shares repurchased and cancelled (Note 4)	(218,400)	(473,233)	-	-	(473,233)
Options exercised	6,400	11,193	(5,010)	-	6,183
Net and comprehensive loss	-	-	-	(1,799,947)	(1,799,947)
Balance at March 31, 2017	36,509,394	\$124,900,373	\$16,029,337	\$(88,326,520)	\$52,603,190

See accompanying notes to interim condensed consolidated financial statements

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

1. DESCRIPTION OF BUSINESS

Espial Group Inc. (“Espial” or the “Company”) develops multiscreen client software solutions for set top box (“STB”) and other devices as well as back-office software TV delivery systems for TV service providers using HTML5 as a key ingredient in high performance, cloud based TV user experiences. Leveraging open standards, including HTML5 and the RDK stack, Espial client solutions deliver user experiences with fast performance, elegant design and ease-of-use on STBs and Smart TV’s. This allows customers to provide its consumers with interfaces that enable rich user experiences, innovative new Web services, TV programming, On-Demand content, and service provider apps.

The Company is incorporated in Canada. The Company’s address and principal place of business is 200 Elgin Street, Suite1000, Ottawa, Ontario K2P 1L5 Canada.

2. BASIS OF PRESENTATION

(a) Statement of Compliance

The unaudited interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standards (“IAS”) 34 *Interim Financial Reporting as issued by the International Accounting Standards Board (“IASB”)* and do not include all information required for full annual financial statements for International Financial Reporting Standards (“IFRS”). These unaudited interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Annual Report for the year ended December 31, 2016 and were prepared using the same accounting policies, except as described below.

These unaudited interim condensed consolidated financial statements were approved and authorised for issue by the Board of Directors on, May 2, 2017.

(b) Basis of Measurement

These unaudited interim condensed consolidated statements have been prepared on a historical cost basis. The policies were consistently applied to all the periods presented unless otherwise noted. All figures presented in the interim condensed consolidated financial statements and tabular disclosures to the interim condensed consolidated financial statements are reflected in Canadian dollars, which is the functional currency of the Company and each of its subsidiaries.

(c) Basis of Consolidation

These unaudited interim condensed consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its wholly owned subsidiaries), Espial Inc., Espial DE, Inc., Espial (UK) Limited, Espial Unipessoal LDA, Espial SAS (formerly Bluestreak Technologie SAS), Espial Group Limited and Espial Limited. All intercompany balances and revenue and expense transactions have been eliminated on consolidation.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

(d) Significant Accounting Policies

Except as disclosed below, the accounting policies applied in these unaudited interim condensed consolidated financial statements are the same as those applied in the Company's consolidated financial statements as at and for the year ended December 31, 2016.

3. NEW AND REVISED IFRS ACCOUNTING PRONOUNCEMENTS

The following amendments were adopted by the Company in the fiscal year.

IAS 7: Disclosure Initiative

On January 7, 2016 the IASB issued Disclosure Initiative (Amendments to IAS 7).

The amendments apply prospectively for annual periods beginning on or after January 1, 2017. Earlier application is permitted. The amendments require disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes. The Company has adopted this amendment with no impact on the unaudited condensed consolidated interim financial statements.

IAS 12: Recognition of Deferred Tax Assets for Unrealized Losses

On January 19, 2016 the IASB issued Recognition of Deferred Tax Assets for Unrealized Losses (Amendments to IAS 12).

The amendments apply retrospectively for annual periods beginning on or after January 1, 2017. Earlier application is permitted. The amendments clarify that the existence of a deductible temporary difference depends solely on a comparison of the carrying amount of an asset and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount or expected manner of recovery of the asset. The amendments also clarify the methodology to determine the future taxable profits used for assessing the utilization of deductible temporary differences. The Company has adopted this amendment with no impact on the unaudited condensed consolidated interim financial statements.

The following is a list of standards and amendments that have been issued but not yet adopted by the Company.

IFRS 9 Financial Instruments

On July 24, 2014 the IASB issued the complete IFRS 9 (IFRS 9 (2014)). The mandatory effective date of IFRS 9 is for annual periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions. Early adoption is permitted.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements

for the three months ended March 31, 2017 and 2016 (unaudited)

(In Canadian Dollars, except share amounts)

The restatement of prior periods is not required and is only permitted if information is available without the use of hindsight. IFRS 9 (2014) introduces new requirements for the classification and measurement of financial assets. Under IFRS 9 (2014), financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. The standard introduces additional changes relating to financial liabilities. It also amends the impairment model by introducing a new 'expected credit loss' model for calculating impairment. IFRS 9 (2014) also includes a new general hedge accounting standard which aligns hedge accounting more closely with risk management. This new standard does not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness, however it will provide more hedging strategies that are used for risk management to qualify for hedge accounting and introduce more judgment to assess the effectiveness of a hedging relationship. Special transitional requirements have been set for the application of the new general hedging model.

The Company intends to adopt IFRS 9 (2014) in its financial statements for the annual period beginning on January 1, 2018. The extent of the impact of adoption of the standard has not yet been determined.

IFRS 15: Revenue from Contracts with Customers

On May 28, 2014 the IASB issued IFRS 15 *Revenue from Contracts with Customers*. The new standard is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted. IFRS 15 will replace IAS 11 *Construction Contracts*, IAS 18 *Revenue*, IFRIC 13 *Customer Loyalty Programmes*, IFRIC 15 *Agreements for the Construction of Real Estate*, IFRIC 18 *Transfer of Assets from Customers*, and SIC 31 *Revenue – Barter Transactions Involving Advertising Services*. On April 12, 2016, the IASB issued *Clarifications to IFRS 15, Revenue from Contracts with Customers*, which is effective at the same time as IFRS 15.

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. The new standard applies to contracts with customers. It does not apply to insurance contracts, financial instruments or lease contracts, which fall in the scope of other IFRSs. The clarifications to IFRS 15 provide additional guidance with respect to the five-step analysis, transition, and the application of the Standard to licenses of intellectual property.

The Company has commenced an implementation plan to develop the necessary accounting policies, estimates and judgments required to adopt IFRS 15. The implementation plan includes an assessment of the standard and the Company's policy as well as any changes required to business processes, systems and internal controls upon adoption of IFRS 15. The Company is not currently in the position to make a reliable estimate of the impact of IFRS 15 on the consolidated financial statements. The Company intends to adopt IFRS 15 and the clarifications in its financial statements for the annual period beginning on January 1, 2018.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements

for the three months ended March 31, 2017 and 2016 (unaudited)
(In Canadian Dollars, except share amounts)

IFRS 2: Share Based Payment

On June 20, 2016, the IASB issued amendments to IFRS 2 Share-based Payment, clarifying how to account for certain types of share-based payment transactions. The amendments apply for annual periods beginning on or after January 1, 2018. As a practical simplification, the amendments can be applied prospectively. Retrospective, or early, application is permitted if information is available without the use of hindsight.

The amendments provide requirements on the accounting for: 1) the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; 2) share-based payment transactions with a net settlement feature for withholding tax obligations; and 3) a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

The Company intends to adopt the amendments to IFRS 2 in its financial statements for the annual period beginning on January 1, 2018 and does not expect the amendments to have a material impact on the financial statements.

IFRS 16: Leases

On January 13, 2016 the IASB issued IFRS 16 *Leases*. The new standard is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted for entities that apply IFRS 15 *Revenue from Contracts with Customers* at or before the date of initial adoption of IFRS 16. IFRS 16 will replace IAS 17 *Leases*.

This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. This standard substantially carries forward the lessor accounting requirements of IAS 17, while requiring enhanced disclosures to be provided by lessors. Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided.

The Company intends to adopt IFRS 16 in its financial statements for the annual period beginning on January 1, 2019. The extent of the impact of adoption of the standard has not yet been determined.

4. SHARE CAPITAL

Share capital consists of an unlimited number of common shares of which 36,509,394 common shares were issued and outstanding at March 31, 2017 (December 31, 2016 – 36,721,394).

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements

for the three months ended March 31, 2017 and 2016 (unaudited)
(In Canadian Dollars, except share amounts)

Share Repurchase Program

In September 2016, Espial announced its plan to repurchase up to 3,221,191 of its common shares, representing 10% of its public float of common shares, through a Normal Course Issuer Bid (NCIB). During the recent quarter Espial repurchased for cancellation a total of 218,400 common shares for a total cost of \$473,233. The issuer bid commenced on August 24, 2016 and expires on August 23, 2017.

Stock Option Plans

As at March 31, 2017, there were 1,194,542 options for common shares remaining available for issuance under the stock option plan. Options are granted periodically and vest over four years. One quarter of the options vest after 12 months and the remainder vest in thirty-six equal tranches over the three years thereafter. The maximum term of these options is ten years. The Company uses the Black-Scholes option pricing model to value the options at the time of grant. Management periodically reviews the estimates used for calculating the fair value of options, volatility is calculated at the time of option grant using historical share price trading activity, ranging from 62% to 83%; risk-free interest rate is based on the government of Canada bond rate, estimated at 0.75% at the time of issue; dividend yield is NIL%; expected life of each option is 1.5 years after vesting. The forfeiture rate was estimated at 10%.

During the three months ended March 31, 2017, there were 753,500 options granted. The per share fair value of stock options granted during the three months ended March 31, 2017 was \$1.43.

The following table summarizes information about option activity for the three months ended March 31, 2017 and for the year ended December 31, 2016.

	Number of Options	Weighted-average Exercise Price
Outstanding, at December 31, 2016	5,372,237	\$2.19
Granted	753,500	\$2.65
Exercised	(6,400)	\$0.97
Forfeited	(12,000)	\$2.01
Outstanding, at March 31, 2017	6,107,337	\$2.24

	Number of Options	Weighted-average Exercise Price
Outstanding, at December 31, 2015	4,012,119	\$2.25
Granted	1,442,000	\$2.00
Exercised	(21,437)	\$0.76
Forfeited	(60,445)	\$2.66
Outstanding, at December 31, 2016	5,372,237	\$2.19

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

The following table summarizes information about stock options outstanding at March 31, 2017:

Range of Exercise Prices	Options Outstanding		Options Exercisable	
	Number Outstanding	Weighted Average Remaining Life	Number Outstanding	Weighted Average Exercise Price
\$0.26 - \$1.00	1,356,951	3.5	1,346,329	\$0.84
\$1.01 - \$2.00	904,500	7.9	337,620	\$1.82
\$2.01 - \$4.00	3,738,039	8.3	1,379,323	\$2.94
\$4.01 - \$7.00	107,847	0.7	107,847	\$6.75
	6,107,337	7.0	3,171,119	\$2.06

5. LOSS PER SHARE

The following table summarized the calculation of the weighted average number of basic and diluted common shares for the three months ended March 31:

Three months ended March 31	2017	2016
Issued common shares at January 1	36,721,394	37,348,057
Effect of shares issued from options	1,600	7,189
Effect of shares repurchased under NCIB	(182,661)	-
Weighted average number of basic common shares at March 31	36,540,333	37,355,246
Effect of warrants on issue	-	-
Effect of share options on issue	-	-
Weighted average number of diluted common shares for the three months ended March 31	36,540,333	37,355,246

Options that are anti-dilutive are not included in the computation of diluted earnings per share. For the three month-periods ended March 31, 2017 and 2016, due to the net loss, all options were excluded from the calculation of diluted earnings per share because they are anti-dilutive.

6. SEGMENTED INFORMATION

The Company operates in one operating segment: computer software solutions. The Company engages in business activities from which it earns license, support and professional services revenues and incurs expenses.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

Revenues from external customers are attributed to geographic areas based on the location of the contracting customers. The following table sets forth external revenue by geographic areas:

	Three months ended	
	March 31, 2017	March 31, 2016
Europe	\$ 3,054,971	\$ 3,407,180
Asia Pacific	520,672	1,113,020
North America	5,088,367	803,782
	\$ 8,664,010	\$ 5,323,982

For the three months ended March 31, 2017, the Company had two customers that individually accounted for 49% and 19% of revenue. For the three months ended March 31, 2016, the Company had one customer that individually accounted for 28% of revenue.

As at March 31, 2017 three customers accounted for 41%, 22% and 18% of accounts receivable. As at December 31, 2016 two customers accounted for 32% and 27% respectively of accounts receivable.

The following table sets forth property and equipment attributable to Canada (the Company's country of domicile), the United States, and the United Kingdom. The three regions hold all of the Company's equipment.

	March 31, 2017	December 31, 2016
Canada	\$848,725	\$861,526
United States	344,092	357,369
United Kingdom	274,052	202,062
	\$1,466,869	\$1,420,957

The following table sets forth intangible assets attributable to Canada (the Company's country of domicile), the United States and United Kingdom. The three regions hold all of the Company's intangible assets.

	March 31, 2017	December 31, 2016
Canada	\$ 595,800	\$ 667,403
United States	627,734	627,837
United Kingdom	411,654	522,827
	\$ 1,635,188	\$ 1,818,067

Of the goodwill of \$3,632,604, \$291,796 is attributable to Canada, and \$3,340,808 is attributable to the United States.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

7. CHANGES IN NON-CASH OPERATING WORKING CAPITAL ITEMS

	Three Months	
	March 31, 2017	March 31, 2016
Accounts receivable	\$ 2,299,310	\$ 1,472,013
Investment tax credits receivable	(50,722)	(73,673)
Prepaid expenses and other assets	(164,477)	70,941
Accounts payable and accrued liabilities	(1,157,795)	(458,084)
Deferred revenue	(506,271)	(895,833)
	<u>\$420,045</u>	<u>\$ 115,364</u>

8. COMMITMENTS

The Company has entered into several operating leases for office space and various equipment leases. The Company rents premises in Canada, the United States and the United Kingdom under operating leases, which expire at varying dates up to September 2024. The lease agreements provide for base rent plus the Company's proportionate share of taxes and operating costs. The leases do not contain contingent rent clauses, purchase options, escalation clauses, or any restrictions regarding further leasing or additional debt.

The equipment leases are all for periods of three years or less, contain purchase options at fair value at termination of lease, do not contain any contingent rent clauses, escalation clauses, any restrictions regarding dividends, further leasing or additional debt.

The Company's minimum lease commitments over the remaining life of the leases are as follows:

2017	\$ 817,705
2018	941,580
2019	777,691
2020	763,532
2021 to 2024	<u>2,480,604</u>
	\$ 5,781,112

Lease payments recognized as an expense during the three month periods ended March 31, 2017 and 2016 were \$439,386 and \$228,314, respectively.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the three months ended March 31, 2017 and 2016 (unaudited) (In Canadian Dollars, except share amounts)

9. EMPLOYEE BENEFITS EXPENSE

The following table presents the employee benefits earned by the employees during the periods noted below:

	Three Months Ended	
	March 31, 2017	March 31, 2016
Salaries	\$ 5,437,462	\$ 3,264,644
Benefits	1,151,431	677,479
Variable compensation and other labour costs	512,563	244,800
Share based payments	432,486	389,456
	\$ 7,533,942	\$ 4,576,379

The following table presents the share-based compensation expense by function during the periods noted below:

	Three Months Ended	
	March 31, 2017	March 31, 2016
Sales and marketing	\$ 109,775	\$ 84,578
General and administration	196,318	228,576
Research and development	126,393	76,302
	\$ 432,486	\$ 389,456

10. PROVISIONS

The Company has provided an estimated cost for an onerous contract it assumed in the acquisition of the Whole Home Solution.

Provisions for the quarter ended March 31, 2017 were:

	Onerous Contract
Opening December 31, 2016	\$ 334,591
Impact of foreign exchange	(2,616)
Utilized	(59,949)
Closing March 31, 2017	\$272,026