



Liberty Defense

Liberty Defense Holdings, Ltd.

Interim Condensed Consolidated Financial Statements

Three and Nine Months Ended September 30, 2021 and 2020

UNAUDITED

Prepared by Management

(Expressed in U.S. dollars)

Liberty Defense Holdings, Ltd.

Interim Condensed Consolidated Statements of Financial Position

(Expressed in U.S. dollars)

Unaudited - Prepared by Management

	September 30, 2021	December 31, 2020
Assets		
Current assets:		
Cash	\$ 3,528,029	\$ 57,047
Amounts receivable, prepaids and deposits (note 4)	378,453	50,907
Loan receivable from Liberty (note 3 and 9)	–	1,963,179
	3,906,482	2,071,133
Non-current assets:		
Property & equipment (note 5)	842,813	–
Intangible assets and goodwill (note 3 and 6)	8,902,306	–
	9,745,119	–
Total assets	\$ 13,651,601	\$ 2,071,133
Liabilities		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 316,134	\$ 449,230
Working capital loans (note 7)	–	550,525
Paycheck protection program loan (note 8)	–	67,588
Convertible debentures (note 10)	–	1,531,309
Lease liabilities (note 11)	145,523	–
	461,657	2,598,652
Non-current liabilities:		
Non-current lease liabilities (note 11)	678,853	–
CEBA loan (note 12)	27,152	–
Deferred income tax liability (note 3)	2,365,612	–
Total liabilities	\$ 3,533,274	\$ 2,598,652
Shareholders' equity (deficiency)		
Share capital (note 13)	\$ 19,291,258	\$ 2,866,502
Equity reserves (note 14)	854,290	108,276
Accumulated other comprehensive (loss) income ("AOCI")	(156,864)	59,746
Deficit	(9,870,357)	(3,562,043)
Total shareholders' equity (deficiency)	10,118,327	(527,519)
Total liabilities and shareholders' equity (deficiency)	\$ 13,651,601	\$ 2,071,133

Nature of operations and going concern (note 1)

Subsequent events (note 19)

Approved by the Board of Directors on November XX, 2021, and signed on the Company's behalf by:

"William Frain"
Director

"Daryl Rebeck"
Director

The accompanying notes form an integral part of these interim condensed consolidated financial statements.

Liberty Defense Holdings, Ltd.

Interim Condensed Consolidated Statements of Loss and Comprehensive Loss

(Expressed in U.S. dollars)

Unaudited - Prepared by Management

	Three months ended September 30,		Nine months ended September 30,	
	2021	2020	2021	2020
Research and development:				
Consideration recovery for the DKL licensing agreement (note 6 (b))	\$	–	\$	–
Product development		(17,755)		613,050
Technology costs		278,325		312,265
Legal fees		67,083		139,522
Salaries & Consulting Fees (note 8 and 16)		943,358		1,489,373
Stock-based Compensation (note 14 and 16)		91,912		155,607
Office, rent and administration		29,428		40,672
Travel and miscellaneous		31,456		31,456
Depreciation (note 5)		31,184		75,757
Amortization (note 6 (a))		2,684		6,808
General Expenses:				
Consulting fees, salaries and benefits (note 8 and 16)		913,445		79,163
Depreciation (note 5)		15,492		–
Legal and professional fees		85,824		63,517
Stock based compensation (note 14)		146,678		7,364
Office, rent and administration		47,419		1,405
Regulatory and shareholder information		12,938		346
Travel, promotion and investor relations		183,368		12,620
RTO transaction costs (note 3)		(1,528)		–
		2,861,311		164,415
				6,332,795
				556,408
Other expense (income):				
Interest income		189		(44,333)
Interest expense		344		35,498
Accretion expense		571		34,934
Foreign exchange (gain) loss		(107,428)		66,474
		(106,324)		92,573
				(55,021)
				42,378
				41,181
				(53,019)
				25,738
				(97,075)
				63,521
				63,071
				(3,779)
				25,738
Total loss for the period	\$	(2,754,987)	\$	(256,988)
				\$ (6,308,314)
				\$ (582,146)
Other comprehensive income (loss)				
Items that may be reclassified subsequently to profit or (loss)				
Foreign currency translation adjustment	\$	(257,104)	\$	49,812
				(216,610)
Total items that may be reclassified subsequently to profit or loss		(257,104)		49,812
				(216,610)
				(57,833)
Total loss and comprehensive loss for the period	\$	(3,012,091)	\$	(207,176)
				\$ (6,524,924)
				\$ (639,979)
Weighted average number of common shares outstanding				
Basic and diluted		62,783,872		27,361,671
				44,034,831
				32,041,067
Loss per share				
Basic and diluted loss per share (note 15)	\$	(0.04)	\$	(0.01)
				(0.14)
				(0.02)

The accompanying notes form an integral part of these interim condensed consolidated financial statements.

Liberty Defense Holdings, Ltd.

Consolidated Statements of Changes in Shareholder' Equity (Deficiency)

(Expressed in U.S. dollars)

Unaudited - Prepared by Management

	Number of common shares*	Share capital	Obligation to issue shares	Equity reserves	AOI	Deficit	Total
Balance as at December 31, 2019	20,843,336	\$ 3,105,995	\$ 188,126	\$ -	\$ 47,654	\$ (2,752,232)	\$ 589,543
DKL shares returned to treasury (note 13)	(1,500,000)	(230,982)	-	-	-	230,982	-
Common shares returned to treasury (note 13)	(5,662,500)	(8,511)	-	-	-	8,511	-
Obligation to issue shares	-	-	(188,126)	-	-	-	(188,126)
Fair value of finder's warrants	-	-	-	31,884	-	-	31,884
Stock based compensation (note 14)	-	-	-	70,831	-	-	70,831
Foreign currency translation adjustment	-	-	-	-	(57,833)	-	(57,833)
Loss for the period	-	-	-	-	-	(582,146)	(582,146)
Balance as at September 30, 2020	13,680,836	\$ 2,866,502	\$ -	\$ 102,715	\$ (10,179)	\$ (3,094,885)	\$ (135,847)
Balance as at December 31, 2020	13,680,836	\$ 2,866,502	\$ -	\$ 108,276	\$ 59,746	\$ (3,562,043)	\$ (527,519)
Common shares retained by Liberty shareholders on RTO (note 3)	10,733,792	3,444,458	-	-	-	-	3,444,458
Convertible debentures converted into common shares (note 10)	5,825,467	1,495,507	-	-	-	-	1,495,507
Issue of subscription receipts and private placement (note 13)	31,510,000	10,408,864	-	-	-	-	10,408,864
Fair value of finder's warrants (note 13)	-	-	-	379,270	-	-	379,270
Stock based compensation (note 14)	-	-	-	377,467	-	-	377,467
Warrants exercised	50,000	30,610	-	(10,723)	-	-	19,887
Performance shares released from escrow (note 13 (a))	2,193,250	1,045,317	-	-	-	-	1,045,317
Foreign currency translation adjustment	-	-	-	-	(216,610)	-	(216,610)
Loss for the period	-	-	-	-	-	(6,308,314)	(6,308,314)
Balance as at September 30, 2021	63,993,345	\$ 19,291,258	\$ -	\$ 854,290	\$ (156,864)	\$ (9,870,357)	\$ 10,118,327

Number of common share information has been updated retroactively to reflect the share consolidation, please refer to note 3 and 13.

The accompanying notes form an integral part of these interim condensed consolidated financial statements.

Liberty Defense Holdings, Ltd.

Consolidated Statements of Cash Flows

(Expressed in U.S. dollars)

Unaudited - Prepared by Management

	Nine months ended September 30,	
	2021	2020
Cash (used in) provided by:		
Operating activities:		
Loss and comprehensive loss for the period	\$ (6,308,314)	\$ (582,146)
Items not involving cash:		
(Recovery of) consideration for DKL licensing agreement	–	(188,126)
Convertible debenture accretion expense (note 10)	39,054	63,071
Accrued interest on convertible debentures (note 10)	36,973	63,317
Unrealized foreign exchange	(53,019)	22,176
Accrued interest income on loan receivable from Liberty (note 3 and 9)	(55,021)	(92,753)
Accretion expense (note 11)	2,127	–
Depreciation	95,351	–
Amortization (note 6 (a))	6,808	–
Government loans forgiven (note 8)	(424,102)	–
Performance shares issued (note 13 (a))	1,045,317	–
Stock based compensation (note 14)	377,467	70,831
Changes in non-cash working capital:		
Amounts receivable and prepaids	(296,984)	25,730
Accounts payable and accrued liabilities	(411,476)	167,199
Cash used in operating activities	(5,945,819)	(450,701)
Investing activities:		
Addition to intangible (MIT)	(23,915)	–
Cash used in investing activities	(23,915)	–
Financing activities:		
Proceeds from issuance of common shares, net of share issue costs (note 13)	10,788,134	–
Proceeds in connection to warrants exercised	19,887	–
Overdraft acquired in RTO paid (note 3)	(107,556)	–
Cash advanced to Liberty as part of the loan (note 9)	(360,910)	(1,526,118)
Convertible debentures issued, net of transaction costs (note 10)	–	1,273,837
Working capital loans repayment (note 7)	(550,525)	–
Repayment of leases	(79,105)	–
Interest paid on convertible debentures	(137,175)	–
Cash provided by (used in) financing activities	9,572,750	(252,281)
Effect of foreign exchange rate changes on cash	(132,034)	(43,169)
Increase (decrease) in cash	3,470,982	(746,151)
Cash, beginning of the period	57,047	967,947
Cash, end of the period	\$ 3,528,029	\$ 221,796

During the period ended September 30, 2021 and 2020, the Company paid \$nil in income taxes and \$137,175 in interest expenses

Supplemental cash flow information

Fair value of brokers and finder's warrants (note 13 (a))	\$ 379,270	\$ 31,884
Performance shares issued (note 13 (a))	1,045,317	–
Fair value of shares ratiated by Liberty shareholders (note 3)	3,444,458	–
Convertible debentures converted into common shares (note 13 (a))	1,495,507	–
Additions to right of use assets (note 5)	701,274	–
DKL shares returned to treasury (note 6 (b))	–	230,932
Common shares returned to treasury (note 6 (b))	–	8,511

The accompanying notes form an integral part of these interim condensed consolidated financial statements.

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

1. Nature of operations and going concern

Liberty Defense Holdings, Ltd. (“Liberty” or the “Company”), is a public company (TSXV: SCAN, Frankfurt: L2D, OTCQB: LDDFF), that was incorporated under the Business Corporation Act of Ontario on June 8, 2012. The Company’s registered and records office is located registered address is 1055 West Georgia Street, 1500 Royal Centre, P.O. Box 11117. Vancouver, British Columbia, V6E 4N7, Canada.

The Company undertook a reverse takeover (“RTO”) transaction with DrawDown Detection, Inc. (“DrawDown” or “DD”) on March 17, 2021 (note 3) in which Liberty acquired all of the issued and outstanding common shares of DrawDown on a post-DrawDown consolidation basis in exchange for common shares of Liberty on a one to one basis post-Liberty consolidation. As described to undertake this transaction, Liberty completed a share consolidation on a 6.2 old shares to 1 new share basis and DrawDown also completed a share consolidation on a 2 old shares to 1 new share basis. Drawdown has been identified as the accounting acquirer and, accordingly, the Company is considered to be a continuation of Drawdown, and the net assets of the Company at the date of the reverse acquisition are deemed to have been acquired by Drawdown (Note 3). These interim condensed consolidated financial statements include the results of operations of the Company from March 17, 2021.

The Company, through its wholly owned subsidiary Liberty Defense Technologies Inc. (“LDT”), is principally engaged in the development and future commercialization of an active 3D imaging technology system, HEXWAVE, to detect concealed threats.

Going concern

These interim condensed consolidated financial statements have been prepared on a going concern basis, which assumes the Company will continue its operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business. The Company incurred in a total loss during the nine months ended September 30, 2021, of \$6,308,314. Furthermore, the Company has limited financial resources, no source of operating cash flows, and there is no assurance that enough funding (including adequate financing) will be available to conduct further research and development. These factors indicate the existence of a material uncertainty that casts significant doubt upon the Company’s ability to continue as a going concern. As a result, the Company may be unable to realize its assets and discharge its liabilities in the normal course of business.

In March 2020, the World Health Organization declared coronavirus COVID-19 a global pandemic. This contagious disease outbreak, which has continued to spread, and any related adverse public health developments, has adversely affected workforces, economies, and financial markets globally, potentially leading to an economic downturn. It is not possible for the Company to predict the duration or magnitude of the adverse results of the outbreak and its effects on the Company’s business or ability to raise funds.

The application of the going concern concept is dependent upon the Company’s ability to generate future profitable operations and receive continued financial support from its creditors and shareholders. These interim condensed consolidated financial statements do not give effect to any adjustments that might be required should the Company be unable to continue as a going concern.

Management plans to continue to pursue equity and/or debt financing to support operations. There can be no assurance that these financing efforts will be successful. Failure to maintain the support of creditors and obtain additional external financing will cause the Company to curtail operations and the Company’s ability to continue as a going concern will be impaired. The outcome of these matters cannot be predicted at this time.

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

2. Basis of presentation

(a) Statement of compliance

These interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, “Interim Financial Reporting” using accounting policies consistent with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and interpretations issued by the International Financial Reporting Interpretations Committee (“IFRIC”).

These interim condensed consolidated financial statements were approved and authorized for issuance by the Board of Directors of the Company in November 29, 2021.

(b) Basis of presentation

These interim condensed consolidated financial statements include the accounts of the Company and its subsidiaries. This interim financial report does not include all of the information required of a full annual financial report and is intended to provide users with an update in relation to events and transactions that are significant to an understanding of the changes in financial position and performance of the Company since the end of the last annual reporting period. It is therefore recommended that this financial report be read in conjunction with the annual audited consolidated financial statements of the Company and DrawDown for the year ended December 31, 2020.

These interim condensed consolidated financial statements do not include all note disclosures required by IFRS for annual financial statements and, therefore, should be read in conjunction with the annual financial statements for the year ended December 31, 2020. In the opinion of management, all adjustments considered necessary for fair presentation of the Company’s financial position, results of operations and cash flows have been included. Operating results for the three and nine months ended September 30, 2021, are not necessarily indicative of the results that may be expected for the year ending December 31, 2021.

Certain amounts in prior years have been reclassified to conform to the current period presentation.

(c) Basis of measurement

These interim condensed consolidated financial statements have been prepared on a historical cost basis except for certain financial instruments which are measured at fair value. In addition, these interim condensed consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

(d) Functional and presentation currency

The functional currency of the Company is the Canadian dollar and the presentation currency of these interim condensed consolidated financial statements is the U.S. dollar (“USD”); therefore, references to \$ means USD and CAD\$ are to Canadian dollars.

(e) Basis of consolidation

These interim condensed consolidated financial statements include the financial statements of Liberty Defense Holdings, Ltd., and the entity controlled by the Company (its subsidiary), as follows:

Subsidiary	Place of Incorporation	Functional Currency	Beneficial Interest
Liberty Defense Technologies Inc	United States	USD	100%
DrawDown Detection Inc	Canada	CAD	100%
DrawDown Technologies Inc	United States	CAD	100%

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

2. Basis of presentation (continued)

(e) Basis of consolidation (continued)

Control exists when the Company has power over an investee, exposure or rights, to variable returns from its involvement with the investee and the ability to use its power over the investee to affect the amount of the Company's returns. All intercompany balances and transactions have been eliminated upon consolidation.

(f) Critical accounting estimates and judgments

The preparation of financial statements in conformity with IFRS, requires management to select accounting policies and make estimates and judgments that may have a significant impact on the condensed interim consolidated financial statements. Estimates are continuously evaluated and are based on management's experience and expectations of future events that are believed to be reasonable under the circumstances. Actual outcomes may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

The accounting judgements and estimates which have the most significant effect on these condensed interim consolidated financial statements were the same as those applied to the audited consolidated financial statements as at the period ended December 31, 2020.

3. Reverse Takeover of DrawDown

On March 17, 2021, Liberty and DrawDown completed a reverse acquisition transaction ("RTO") in which Liberty acquired all of the issued and outstanding common shares of DrawDown on a post-DrawDown consolidation basis in exchange for common shares of Liberty on a one to one basis post-Liberty consolidation. In addition, each outstanding option and/or purchase warrant to acquire DrawDown's common shares will become exercisable for common shares of Liberty in the same post-consolidation basis.

As a result of this share exchange described above, the former shareholders of DrawDown acquired control of Liberty. Accordingly, the acquisition constitutes a reverse acquisition and was accounted with the net assets acquired of Liberty recorded at fair value at the date of acquisition. Furthermore, for accounting purposes, DrawDown was treated as the accounting parent company (legal subsidiary) and Liberty will be treated as the accounting subsidiary (legal parent). As DrawDown was deemed to be the acquirer for accounting purposes, its assets, liabilities and operations since incorporation are included in these interim condensed consolidated financial statements at their historical carrying value.

The RTO was accounted for as a business combination and the acquisition method of accounting was used, whereby the purchase price is allocated to the identifiable assets and liabilities on the basis of fair value at the acquisition date. Provisional fair values have been allocated as at the reporting date and will be finalized as soon as the relevant information is available, within a period not to exceed twelve months from the acquisition date with retroactive restatement of the impact of adjustment to those provisional fair values effective as at the acquisition date. The purchase price allocations for the acquisition of Liberty reflects various fair value estimates and analyses, which are subject to change within the respective measurement periods. The primary areas of the purchase price allocations that are subject to change relate to the fair values of the valuation of intangible assets acquired and residual goodwill. The Company expects to continue to obtain information to assist in determining the fair value of the net assets acquired at each acquisition date during the measurement periods. Measurement period adjustments that the Company determines to be material will be applied retrospectively to the period of acquisition in the Company's consolidated financial statements, and, depending on the nature of the adjustments, other periods subsequent to the period of acquisition could also be affected.

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

3. Reverse Takeover of DrawDown (continued)

Upon the completion of the RTO, there was identified goodwill and other intangible assets of \$8,885,199. This goodwill and other intangible assets were calculated as the difference between fair value of the consideration issued and the fair value of all other assets and liabilities acquired. None of the goodwill is deductible for tax purposes.

If Liberty had been consolidated into the Company's operations from January 1, 2021, our consolidated net loss for the nine months ended September 30, 2021 would have been approximately \$6,875,592.

The consideration transferred in this reverse acquisition where DrawDown issued no consideration to Liberty but instead Liberty issued 19,506,303 common shares to the shareholders of DrawDown is determined by the fair value of the number of shares that DrawDown would have had to issue to give the shareholders of Liberty the same percentage of equity interest in the combined entity that results from the reverse acquisition. The consideration of the acquisition is therefore \$3,444,458 for the shares and \$2,379,110 for the settlement of a pre-existing liability between the two entities.

The total consideration of the acquisition has been allocated based on provisional management's estimates of the relative fair value of assets acquired and liabilities assumed as follows:

	Amount
Assets acquired and liabilities assumed:	
Receivables & prepaids	\$ 35,000
Property and equipment	238,652
Intangible asset and goodwill	8,885,199
Bank overdraft	(107,556)
Accounts payable and accrued liabilities	(660,511)
Lease obligation	(201,604)
Deferred tax liability	(2,365,612)
Net assets acquired	\$ 5,823,568
Consideration:	
Fair value of shares retained by Liberty shareholders	3,444,458
Pre-existing liability settlement	2,379,110
Total consideration	\$ 5,823,568

4. Amounts Receivables, Prepaids and Deposits

As of September 30, 2021, the Company had \$271,858 (December 31, 2020 – \$31,839) in amounts receivables and \$106,595 (December 31, 2020 – \$19,068) in prepaids and deposits.

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

5. Property & Equipment

		Leasehold Improvements		Equipment	Right of Use Asset		Total
Cost							
At December 31, 2020	\$	-	\$	-	\$	-	\$ -
Additions RTO transaction (note 3)		6,735		32,410		199,507	238,652
Additions (1)		-		-		701,274	701,274
At September 30, 2021	\$	6,735	\$	32,410	\$	900,781	\$ 939,926
Accumulated Depreciation							
At December 31, 2020	\$	-	\$	-	\$	-	\$ -
Depreciation for the period		4,456		15,137		75,758	95,351
At September 30, 2021	\$	4,456	\$	15,137	\$	75,758	\$ 95,351
Foreign exchange movement							
At December 31, 2020	\$	-	\$	-	\$	-	\$ -
At September 30, 2021	\$	-	\$	-	\$	(1,762)	\$ (1,762)
Net Book Value							
At December 31, 2020	\$	-	\$	-	\$	-	\$ -
At September 30, 2021	\$	2,279	\$	17,273	\$	823,261	\$ 842,813

- (1) On July 2, 2021, the Company entered into a new office lease agreement for a period of seventy-six months whereby an initial right-of-use asset was recognized totaling \$701,274, using a 7.63% implicit interest rate.

6. Intangible Assets

(a) MIT License Agreements

The Company, through its wholly owned subsidiary Liberty Defense Technologies Inc. ("LDT"), has entered into agreements with the Massachusetts Institute of Technology ("MIT") and MIT's Lincoln Laboratory ("MIT LL"), including an exclusive patent licence agreement between MIT and LDT dated September 10, 2018, as amended from time to time (the "Licence Agreement"), a technology transfer agreement between LDT and MIT LL, effective August 24, 2018 (the "Technology Transfer Agreement"), and a cooperative research and development agreement between LDT and MIT dated as of December 21, 2018 ("CRADA"), such agreements providing LDT with an exclusive licence for patents, design assets and MIT LL technical expertise related to active three-dimensional imaging technology that are the core technology behind the HEXWAVE product.

The obligations under the Technology Transfer Agreement and the CRADA have now been completed. Liberty may consider extending the CRADA (and therefore changing its scope) if it determines that additional MIT LL technical expertise related to active three-dimensional imaging technology is required. Pursuant to the License Agreement, LDT has been granted the exclusive rights to MIT's patent in "multistatic sparse array topology for FFT-based field imaging" (MIT Case No. 1 8409L) (the "Patent"), which is being utilized in the development and application of the HEXWAVE product. The License Agreement is to be in effect until the expiration of the Patent, which is 14 years (December 2035). In granting LDT such patent rights, the Company shall pay MIT in addition to patent filing costs an annual maintenance fees as follows: 1) \$20,000 for 2019 (paid); \$50,000 for 2020 (paid); \$60,000 for 2021 (pending); \$100,000 for 2022; \$200,000 for 2023 and \$350,000 for 2024 and thereafter; and 2) a royalty of 5.7% of all future net sales of the Company. The Company shall also be required to achieve certain milestones.

The continuity of the outstanding balance for the intangible assets is as follows:

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

6. Intangible Assets

(a) MIT License Agreements (continued)

	MIT licenses	Intellectual property & goodwill	Total
Balance, December 31, 2019 and 2020	\$ -	\$ -	\$ -
Additions RTO transaction (note 3)	123,682	8,761,517	8,885,199
Additions	23,915	-	23,915
Amortization	(6,808)	-	(6,808)
Balance September 30, 2021	\$ 140,789	\$ 8,761,517	\$ 8,902,306

Intangible assets included as MIT licenses include payments in connection to reimbursement of global patent filing costs and annual maintenance fees. Additionally, intellectual property and goodwill was generated through the RTO transaction (Note 3) and it relates directly to costs incurred to develop and advance the HEXWAVE technology to the stage it was at when the RTO transaction closed.

(b) DKL License Agreement

On October 11, 2018, the Company through its wholly owned subsidiary DrawDown Technologies, Inc (“DDT”) entered into a license agreement (“the Licensing Agreement”) with DKL International, Inc (“DKL”), as amended on February 6, 2020, for the commercial development of DKL’s passive detection techniques and products that detect smokeless gunpowder from a standoff distance (the “Detection Technology”).

Pursuant to the last amendment to the Licensing Agreement on February 6, 2020, DKL agreed to surrender back to DrawDown, 3,000,000 common shares in the capital of the Company with a fair value of \$230,982 that were issued to DKL on April 2, 2019 as part of the consideration for the Licensing Agreement. In addition to returning those shares, it was also agreed to cancel the cash portion of the consideration for an amount of \$80,000 and the obligation to issue 1,000,000 common shares with an estimated value of \$188,126 for a total of \$268,126 recorded as a recovery in the statement of loss.

On April 19, 2021, the Company gave notice of termination of the License Agreement. Such notice of termination served as formal notice that the Licensing Agreement was terminated in full effective six months following the date of this notice. Upon the effective date of the termination, the parties to the Licensing Agreement will have no further rights and/or obligations pursuant thereto. In order to settle any and all outstanding amounts owed to DKL under the Licensing Agreement the Company paid \$125,000 (Note 16).

7. Working Capital Loans

The Company received working capital loans in the amount of \$550,525 during the year ended December 31, 2020. These loans were paid in full during the three and nine months ended September 30, 2021. These loans were unsecured and non-interest bearing.

8. Paycheck Protection Program Loan

The Company, through its wholly owned subsidiary DrawDown Technology Inc, filed for a Paycheck Protection Program Loan (“PPP Loan”) under the Coronavirus Aid, Relief, and Economic Security Act and received \$67,588 on May 10, 2020. The PPP Loan had a 1% fixed interest rate per annum and a deferment period of 6 months. During 2021, the Company submitted to the Small Business Administration the application to request for forgiveness on the Company’s PPP Loan, which was fully approved. Additionally, on January 28, 2021, the Company obtained confirmation from the PPP Loan subscriber, Bank of America, that its PPP Loan is now

Liberty Defense Holdings, Ltd.

Notes to the Interim Condensed Consolidated Financial Statements

Unaudited – (Expressed in U.S. dollars, unless otherwise stated and per share amounts)

For the three and nine months ended September 30, 2021

8. Paycheck Protection Program Loan (continued)

considered paid in full, including any applicable interest. As a result, the balance owing in the amount of \$67,588 was recorded as a recovery against salaries and benefits under general expenses.

Subsequent to the RTO transaction (Note 3), the Company through its wholly owned subsidiary Liberty Defense Technology, Inc., submitted a similar application to request for forgiveness on the Liberty's PPP Loan, which was fully approved. On March 17, 2021, the Company obtained confirmation from the PPP Loan subscriber, Bank of America, that its PPP Loan is now considered paid in full, including applicable interest, therefore the liability balance recognized in the financial statements in the amount of \$356,514 was recorded as a recovery against R&D salaries and benefits.

9. Loan Receivable from Liberty

Before the completion of the RTO (Note 3), the Company had a loan agreement with DrawDown which provided for a maximum financing of \$2.0 million with a minimum of 12 months funding bearing 12% interest per annum. As March 17, 2021 when the RTO transaction was completed, the outstanding balance under the loan agreement was \$2,379,110 (December 31, 2020 – \$1,963,179) which formed part of the consideration on the RTO, including interest receivable of \$255,719.

10. Convertible Debentures

In connection with the RTO, the Company on March 5 and May 29, 2020, issued convertible debentures with a total face value of \$1,371,098 (CAD\$1,864,810). The instrument was unsecured, had a maturity of one year from its date of issuance and has an interest rate of 10% per annum payable at the end of the term or up on conversion. On March 17, 2021 the RTO was completed, and the debenture converted into DrawDown Units at CAD\$0.24 per DrawDown Unit. Each DrawDown Unit was comprised of one common share and one-half of one DrawDown warrant. The shares issued upon conversion of the DrawDown Units were exchanged for Liberty shares on a one for one basis along with the warrants and finder's warrants with the same economic terms and conditions.

The continuity of the outstanding balance for the convertible debentures is as follows:

	Amount
Balance, December 31, 2019	\$ -
Cash received	1,371,098
Finder's fee paid in cash	(92,108)
Legal fees	(5,153)
Fair value of finder's warrants	(31,884)
Accrued interest	100,203
Accretion expense	96,006
Foreign exchange movement	93,147
Balance December 31, 2020	\$ 1,531,309
Accrued interest	36,973
Accretion expense	39,054
Interest paid	(137,175)
Foreign exchange movement	25,346
Converted to common shares	(1,495,507)
Balance September 30, 2021	\$ -

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11. Leases

The lease liabilities for the period ended September 31, 2021 and year ended December 31, 2020 are as follows:

	September 30, 2021	December 31, 2020
Maturity analysis - contractual undiscounted cash flows		
Less than one year	\$ 145,523	\$ -
One to seven years	678,853	-
Total undiscounted lease liabilities	824,376	-
Lease liabilities included in the statement of financial position	824,376	-
Current	145,523	-
Non-current	678,853	-
Amounts recognized in profit or loss		
Interest on lease liabilities	\$ 6,376	\$ -

12. Canada Emergency Business Account (“CEBA”) Loan

As a result of closing the RTO transaction (Note 3), the Company acquired a CAD\$40,000 Canada Emergency Business Account loan (“CEBA Loan”) which was received by Liberty on May 5, 2020 and carries a 0% interest rate per annum, however, increases to 5% per annum if the loan is not repaid in full on or before December 31, 2022 (“Term Period”). In this case the loan is extended from January 1, 2023 to December 31, 2025 (“Extension Period”). The Company used the loan to help fund payroll, rent, and utilities under the appropriate guidelines in the loan agreements. On December 31, 2020, the CEBA loan converted to a term facility and if the Company pays 75% of the aggregate amount advanced to the credit facility on or before the Term Period, the remaining 25% of the amount advanced will be forgiven.

The net present value of the CEBA Loan as of September 30, 2021 is \$27,152 (December 31, 2020 – \$nil) and is recorded as a non-current liability.

13. Share Capital

(a) Common share transactions for the year ended September 30, 2021

- i) On July 15, 2021, the Company issued 50,000 common shares for gross proceeds of \$19,887 in connection with warrants exercised. The fair value of these warrants exercised was \$10,723 and was transferred from the equity reserves and recorded against share capital. Additionally, On July 21, 2021, the Company issued 2,193,250 capital markets performance shares to certain employees and a consultant of the Company with an estimated fair value of \$1,045,317.
- ii) On June 17, 2021, the Company closed a brokered private placement of 14,260,000 units (“Units”) at a price of CAD\$0.50 per Unit for gross proceeds of \$5,777,490 (CAD\$7,130,000). Each Unit consists of one common share of the Company and one-half of one common share purchase warrant (each whole warrant, a “Warrant”). Each Warrant entitles the holder thereof to acquire one additional Common Share of the Company at a price of CAD\$0.75 per Common Share within 24 months. The Company paid to the agent a cash commission of \$448,464 (CAD\$553,450) and issued to the agent 1,106,900 non-transferable compensation warrants (the “Compensation Warrants”). Each Compensation Warrant entitles the Agent to acquire one Common Share of the Company at a price of CAD\$0.50 per Common Share within 24 months with a fair value of \$237,384. The Company also incurred \$76,391 in legal and filing fees.

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13. Share Capital (continued)

(a) Common share transactions for the year ended September 30, 2021 (continued)

- iii) On March 17, 2021, DrawDown completed a share consolidation of two old common shares for one new basis in connection to the completion of the RTO transaction. All shares and per share data presented in the Company's interim condensed consolidated financial statements have been retroactively adjusted to reflect the share consolidation unless otherwise noted.
- iv) A total of 10,733,792 common shares were issued upon completion of the RTO transaction on March 17, 2021 with a fair value of \$3,444,458. Also, the convertible debentures issued in connection to the RTO transaction (note 3) were converted into DrawDown Units and immediately exchanged for Liberty shares on a one for one basis along with the warrants and finder's warrants under the same economic terms and conditions. A total of 5,825,468 common shares were issued with a fair value of \$1,495,507.
- v) As part of the RTO transaction on March 12, 2021, the Company closed a financing with a total of 17,250,000 subscription receipts for one Unit (the "Unit") at a price of \$0.30 (CAD\$0.40) per Unit for total proceeds of \$5,535,499 (CAD\$6,900,000). Each Unit is comprised of one common share and one-half of one purchase warrant. Each whole purchase warrant entitles the holder thereof to purchase one share at \$0.45 (CAD\$0.60) per share for a period of two years. The Company issued 1,098,125 compensation warrants to the agents. Each compensation warrant entitles the agents to acquire one common share of the company at a price of CAD\$0.40 per common share within 24 months with a fair value of \$141,886.

(b) Common share transactions for the year ended December 31, 2020

- i) Pursuant to the February 6, 2020, amendment to the Licensing Agreement, DKL agreed to surrender back to the Company, 1,500,000 common shares that were issued to DKL on April 2, 2019 as part of the consideration for the Licensing Agreement with a state value of \$230,982 (CAD\$300,000).
- ii) On April 12, 2020, a total of 5,662,500 common shares were cancelled and return to treasury. These shares were issued in connection to a private placement closed on March 5, 2019, where the Company issued 5,662,500 at CAD\$0.0005 for gross proceeds of \$8,511 (CAD\$11,325).

14. Equity Reserves

(a) Share-based compensation

The Company maintains an Omnibus Equity Incentive Plan (the "Incentive Plan") which is comprised of stock options, restricted share units ("RSUs") and deferred share units ("DSUs"). The maximum number of Common Shares reserved for issuance, in the aggregate, under the Incentive Plan is 10% of the aggregate number of common shares issued and outstanding to be granted to directors, officers, employees, and consultants under certain restrictions. The purpose of the Incentive Plan is to promote greater alignment of interests between employees and shareholders, and to support the achievement of the Company's longer-term performance objectives, while providing a long-term retention element.

Unless the Board decides, or the grant agreement specifies otherwise, the Incentive Plan provides that Options will vest as to approximately 16.67% (1/6) every six-month interval following the date of such grant for those participants who have provided their services to the Company for at least one year. For those participants who have provided their services to the Company for less than one year, Options will vest as to 33.34% (1/3) one year from the date of grant, and 16.67% (1/6) vesting every six months thereafter. The Board shall fix the exercise price of any Option when such Option is granted, which shall not be less than the closing price of the Common Shares on the Exchange on the day prior to the date of grant (the "Market Value"). An Option shall be exercisable during a period established by the

Liberty Defense Holdings, Ltd.

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14. Equity Reserves (continued)

(a) Share-based compensation (continued)

Board, which shall commence on the date of the grant and shall terminate no later than ten (10) years after the date of grant of the Award or such shorter period as the Board may determine.

With respect to RSUs, the plan provides RSUs to be issued to directors, officers, employees and consultants of the Company so that they may participate in the growth and development of Liberty. Subject to the specific provisions of the RSU plan, eligibility, vesting period, terms of the RSUs and the number of RSUs granted are to be determined by the Board of Directors at the time of the grant.

The fair value of the stock options granted were estimated using the Black-Scholes option valuation model with the following weighted average assumptions:

	September 30, 2021	December 31, 2020
Risk-free interest rate	0.92%	1.34%
Expected dividend yield	Nil	Nil
Stock price volatility	79.11%	62.05%
Expected life (in years)	5 years	5 years
Weighted average fair value per option	CAD\$0.38	CAD\$0.20

The continuity of the number of stock options issued and outstanding, adjusted for the share consolidation is as follows:

	Number of stock options	Weighted average exercise price
Outstanding, December 31, 2019	-	CAD\$ -
Granted	437,500	0.50
Outstanding, December 31, 2020	437,500	CAD\$ 0.50
RTO transaction	230,645	4.96
Granted	2,535,000	0.50
Outstanding, September 30, 2021	3,203,145	CAD\$ 0.82

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14. Equity Reserves (continued)

(a) Share-based compensation (continued)

As at September 30, 2021, the number of stock options outstanding and exercisable, adjusted for the share consolidation was:

Expiry date	Outstanding		Exercisable	
	Number of stock options	Exercise price	Remaining contractual life (years)	Number of stock options
01-May-24	50,000	CAD\$ 0.50	2.59	50,000
15-Jun-24	37,500	CAD\$ 0.50	2.71	37,500
01-Jul-24	75,000	CAD\$ 0.50	2.75	75,000
08-Jul-24	75,000	CAD\$ 0.50	2.77	75,000
31-Jul-24	50,000	CAD\$ 0.50	2.84	50,000
23-Aug-24	37,500	CAD\$ 0.50	2.90	37,500
25-Sep-24	37,500	CAD\$ 0.50	2.99	37,500
29-Sep-24	75,000	CAD\$ 0.50	3.00	75,000
Apr 9 and Jul 2, 2024	230,645	CAD\$ 4.96	2.76	230,645
07-Apr-26	2,195,000	CAD\$ 0.50	4.52	-
10-Jun-26	100,000	CAD\$ 0.50	4.70	-
28-Jul-26	240,000	CAD\$ 0.50	4.83	-
	3,203,145			668,145

Total stock-based compensation expense as a result of options granted and vested during the three and nine months ended September 30, 2021, was \$189,859 and \$328,736 respectively (three and nine months ended September 30, 2020 – \$7,364 and \$70,831 respectively).

(b) Restricted share units

During the period September 30, 2021, the Company granted 1,000,000 RSUs to directors, officers and an employee; these instruments shall be settled with common shares of the Company, are restricted until April 7, 2026 and vest at 100% on April 7, 2024. The following table summarizes the movements in Liberty's outstanding RSUs:

	Number of equity settled restricted share units
Outstanding, December 31, 2019 and 2020	-
Granted	1,000,000
Outstanding, September 30, 2021	1,000,000

The estimated fair value of the equity settled RSUs granted during the period ended September 31, 2021 was CAD\$382,393 (September 31, 2021: \$nil) and will be recognized as an expense over the vesting period of the RSUs. The fair value of the equity settled RSUs as at the grant date is calculated in accordance with a Black Scholes option pricing model using the following inputs:

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14. Equity Reserves (continued)

(b) Restricted share units (continue)

	April 7, 2021
Risk-free interest rate	0.94%
Expected dividend yield	Nil
Stock price volatility	79.05%
Expected life (in years)	5 years
Fair value	CAD\$0.38

Total stock-based compensation expense as a result of RSUs grants during the three and nine months ended September 30, 2021, was \$48,731 and \$48,731 respectively (three and nine months ended September 30, 2020 – \$nil and \$nil respectively).

(c) Share purchase warrants

As at September 30, 2021, the continuity of the number of share purchase warrants outstanding is as follows:

	Warrants outstanding	Exercise Price
Outstanding, December 31, 2019	1,740,000	CAD\$ 0.20
Issued	208,286	0.40
Cancelled	(1,740,000)	0.20
Outstanding, December 31, 2020	208,286	CAD\$ 0.40
RTO transaction	1,738,166	6.48
Issued	20,872,759	0.62
Cancelled	(1,423,650)	6.82
Exercised	(50,000)	0.50
Outstanding, September 30, 2021	21,345,561	CAD\$ 0.68

As part of the RTO transaction (Note 3), the Company had 1,738,166 (share purchase warrants with a weighted average exercise price of CAD\$6.48. Subsequently, from this balance, on April 3, 2021 a total of 1,423,650 with an exercise price of CAD\$6.82 were cancelled without being exercised.

During the period ended September 30, 2021, the Company issued share purchase warrants in connection to the following transactions:

- i) As part of the June 17, 2021 financing, the Company issued a total of 7,130,000 share purchase warrant. Each warrant entitles the holder thereof to acquire one additional common share of the Company at a price of CAD\$0.75 within 24 months. The Company also issued the agent 1,106,900 non-transferable compensation warrants (the “Compensation Warrants”). Each Compensation Warrant entitles the agent to acquire one common share of the Company at a price of CAD\$0.50 within 24 months with a fair value of \$237,384.
- ii) A part of the completion of the RTO transaction (Note 3), and the concurrent financing, the Company on March 17, 2021, issued 2,912,734 share purchase warrants as a result of converting all outstanding convertible debentures. These instruments have an exercise price of CAD\$0.40 and can be exercised within a period of 24 months. The Company also issued 8,625,000 share purchase warrants in connection to units sold in this private placement with an exercise price of CAD\$0.60 and an exercise period of 24 months. Additionally, the Company issued a total of 1,098,125 as finder’s warrants under the same economic terms and conditions of units with an estimated fair value of \$141,886.

Liberty Defense Holdings, Ltd.

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14. Equity Reserves (continued)

(c) Share purchase warrants (continued)

As at September 30, 2021, the continuity of the number of share purchase warrants units outstanding is as follows:

	Warrants units outstanding	Exercise Price
Outstanding, December 31, 2019 and 2020	-	-
RTO transaction	81,280	CAD\$ 4.96
Cancelled	(81,280)	CAD\$ 4.96
Outstanding, September 30, 2021	-	

The fair value of the share purchase warrants was estimated using the Black-Scholes option valuation model with the following weighted average assumptions:

	September 30, 2021	December 31, 2020
Risk-free interest rate	0.32%	0.59%
Expected dividend yield	Nil	Nil
Stock price volatility	98.38%	86.93%
Expected life (in years)	2 years	2 years
Fair value	CAD\$0.21	CAD\$0.10

The outstanding number of share purchase warrants is as follows:

Expiry date	Outstanding		
	Number of warrants	Exercise price	Remaining contractual life (years)
5-Mar-22	123,300	CAD\$0.40	0.43
29-May-22	84,986	CAD\$0.40	0.66
9-Jan-22	314,516	CAD\$4.96	0.28
11-Mar-23	1,098,125	CAD\$0.40	1.44
11-Mar-23	8,625,000	CAD\$0.60	1.44
17-Mar-24	2,912,734	CAD\$0.50	2.46
17-Jun-23	7,130,000	CAD\$0.75	1.71
17-Jun-23	1,056,900	CAD\$0.50	1.71
	21,345,561		

15. Loss Per Share

Basic loss per share amounts is calculated by dividing the net loss for the period by the weighted average number of common shares adjusted for the share consolidation outstanding during the period.

	Three months ended September 30,		Nine months ended September 30,	
	2021	2020	2021	2020
Loss attributable to common shareholders	\$ (2,754,987)	\$ (256,988)	\$ (6,308,314)	\$ (582,146)
Weighted average number of shares	62,783,872	27,361,671	44,034,831	32,041,067
Basic and diluted loss per share	\$ (0.04)	\$ (0.01)	\$ (0.14)	\$ (0.02)

The Company incurred a net loss for the period ended September 30, 2021 and 2020, therefore all outstanding stock options and share purchase warrants, if any, have been excluded from the calculation of diluted loss per share since the effect would be anti-dilutive.

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16. Related Party Transactions

The Company's related parties consist of the Company's directors, officers and companies associated with them including 1214852 B.C. LTD., a company where Omar Garcia Abrego, the Chief Financial Officer is a shareholder.

(a) Compensation of key management personnel:

Key management personnel include members of the Board, the Chief Executive Officer, Chief Financial Officer, Chief Technology Officer, and Chief Operating Officer. The net aggregate compensation paid, or payable and related party transactions are shown as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2021	2020	2021	2020
Short-term benefits	\$ 526,151	\$ 53,732	\$ 953,015	\$ 310,603
Share-based compensation	152,809	-	247,439	-
Consulting services (1)	38,960	32,840	183,272	94,172
	\$ 717,920	\$ 86,572	\$ 1,383,725	\$ 404,775

(1) Includes fees paid or payable to 1214852 B.C. LTD.

(b) Related party balances:

As of September 30, 2021, the Company had a balance payable of \$145,789 (December 31, 2020 – \$449,230). This payable balance includes accounts payable and accrued liabilities relating to consulting services from directors, officers or their related companies, included in compensation of key management personnel. These related party balances are unsecured, non-interest bearing and have no specific terms of settlement.

Additionally, during the year ended December 31, 2020, the Company received working capital loans. The outstanding balance at December 31, 2020 was in the amount of \$550,525 from Directors and officers or their related parties. During the period ended September 30, 2021, all of these working capital loans were paid in full and the outstanding balance at September 30, 2021 is \$nil. These working capital loans were unsecured and non-interest bearing.

(c) DKL International Inc:

Howard Sidman a former member of the Board of Directors of DrawDown is also the founder and president of DKL. Included in accounts payable and accrued liabilities as of December 31, 2020 was \$56,500 payable to DKL.

DrawDown also paid or accrued \$49,829 for the period ended September 30, 2020 to DKL in relation to research and development costs (September 30, 2021 \$nil).

17. Financial Instruments

As of September 30, 2021, the Company's financial instruments comprise cash, amounts receivables, and accounts payable and accrued liabilities, none of which are valued at fair value. The fair values of amounts receivables and accounts payable and accrued liabilities approximate their carrying values due to their short-term maturity. The carrying amount of the CEBA loan approximates fair value as it is discounted using a market rate of interest.

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18. Segmented Information

The Company operates in one reportable operating segment, being the research and development of new technology for the security industry.

Geographic segmentation of assets and liabilities are as follows:

	Canada	United States	Total
Current assets	\$ 3,535,422	\$ 371,060	\$ 3,906,482
Non-current assets			
Property & equipment	78,791	764,022	842,813
Intangible assets	-	8,902,306	8,902,306
Total assets, September 30, 2021	\$ 3,614,213	\$ 10,037,388	\$ 13,651,601
Current liabilities	-	461,657	461,657
Non-current liabilities	63,091	3,008,526	3,071,617
Total liabilities, September 30, 2021	\$ 63,091	\$ 3,470,183	\$ 3,533,274

	Canada	United States	Total
Current assets	\$ 2,005,581	\$ 65,552	\$ 2,071,133
Total assets, December 31, 2020	\$ 2,005,581	\$ 65,552	\$ 2,071,133
Current liabilities	\$ 2,358,321	\$ 240,331	\$ 2,598,652
Total liabilities, December 31, 2020	\$ 2,358,321	\$ 240,331	\$ 2,598,652

As of December 31, 2020 the Company did not have any non-current assets or liabilities.

19. Subsequent Events

- On July 12, 2021, the Company signed the Cooperation and Project Funding Agreement with The Israel-US Binational Industrial Research and Development (BIRD) Foundation, BIRD HLS Program, for \$1 million. The BIRD HLS program is sponsored jointly by the Development Homeland Security (“DHS”) and the Israel Ministry of Public Security (MOPS). The BIRD Foundation is an organization that provides capital for joint industrial research and development between American and Israeli companies. Under the terms of the agreement, the Company agreed to partner with Levitection Ltd (“Levitection”), an Israeli company to integrate Levitection’s technology with the Company’s HEXWAVE technology. On October 28, 2021 the BIRD HLS Program notified both Liberty Defense Technologies and Levitection that a decision has been made to enter into an orderly business shutdown procedure due to Levitection Ltd. inability to achieve positive cash flow or attract an investment. The Bird Foundation approved the termination of the project, and the funding previously advanced to the Company on July 8, 2021 for \$113,634 was returned to the Bird HLS Foundation on November 9, 2021.
- On October 20, 2021 the Company received from Transportation Security Administration’s (TSA) a contract award for \$500,000 as part of the TSA On-Person Screening Capability Program for demonstration and evaluation of the HEXWAVE and its expanded capabilities for screening Aviation Workers at a TSA designated location to enhance detection and throughput performance. The Company is required to have the HEXWAVE technology working at certain locations to collect and share data with TSA on identified threats to further develop algorithms to improve the recognition of threats with desire probability of detection.
- On November 1, 2021 the Company granted 465,000 stock options to recently hired employees. The stock options have a five-year term from the date of the grant, are exercisable at a price of CAD\$0.46 per share, and vest at 25% after six months from the grant date, and 25% every six months thereafter for a total vesting period of twenty-four months.