



KELSO TECHNOLOGIES INC.

Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

Index	Page
Report of Independent Registered Public Accounting Firm	2 - 3
Consolidated Financial Statements	
Consolidated Statements of Financial Position	4
Consolidated Statements of Changes in Equity	5
Consolidated Statements of Operations and Comprehensive Loss	6
Consolidated Statements of Cash Flows	7
Notes to Consolidated Financial Statements	8 – 30

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE SHAREHOLDERS AND DIRECTORS OF KELSO TECHNOLOGIES INC.

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Kelso Technologies Inc. (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2017 and 2016, the consolidated statements of operations and comprehensive loss, changes in equity, and cash flows, for the years ended December 31, 2017, 2016 and 2015, and the related notes, comprising a summary of significant accounting policies and other explanatory information (collectively referred to as the "consolidated financial statements").

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2017 and 2016, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2017, 2016 and 2015, in accordance with International Financial Reporting Standards, as issued by the International Accounting Standards Board.

Material Uncertainty Related to Going Concern

Without modifying our opinion, we draw attention to Note 1 to the consolidated financial statements, which indicates that the Company has an accumulated deficit of \$19,288,072 as at December 31, 2017 and for the past few years has negative cash flows from operations. As stated in Note 1 to the consolidated financial statements, these events or conditions, along with other matters as set forth in Note 1, indicate that a material uncertainty exists that casts substantial doubt on the Company's ability to continue as a going concern.

Basis for Opinion

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement, whether due to error or fraud. Those standards also require that we comply with ethical requirements, including independence. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the United States federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

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An audit includes performing procedures to assess the risks of material misstatements of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, audit evidence regarding the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes evaluating the appropriateness of accounting policies and principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a reasonable basis for our audit opinion.

Smythe LLP

Chartered Professional Accountants

We have served as the Company's auditor since 2006.

Vancouver, Canada
March 27, 2018

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Kelso Technologies Inc.
Consolidated Statements of Financial Position
December 31,
(Expressed in US Dollars)

	2017	2016
Assets		
Current		
Cash and cash equivalents (Note 12)	\$ 411,223	\$ 2,312,279
Accounts receivable	653,445	637,845
Income tax receivable	-	753,223
Prepaid expenses	183,966	708,100
Inventory (Note 6)	3,980,243	5,206,129
	5,228,877	9,617,576
Deposit	-	3,763
Property, plant and equipment (Note 7)	2,991,546	3,194,492
Intangible assets (Note 8)	944,776	234,313
	\$ 9,165,199	\$ 13,050,144
Liabilities		
Current		
Accounts payable and accrued liabilities (Note 10)	\$ 878,699	\$ 271,600
Income tax payable (Note 11)	721,267	834,167
	1,599,966	1,105,767
Deferred income tax liability (Note 11)	-	172,433
	1,599,966	1,278,200
Shareholders' Equity		
Capital Stock (Note 9)	23,231,252	22,829,820
Obligation to Issue Shares (Notes 8 and 9)	131,527	192,946
Reserves (Note 9 (b))	3,490,526	3,021,339
Deficit	(19,288,072)	(14,272,161)
	7,565,233	11,771,944
	\$ 9,165,199	\$ 13,050,144

Approved on behalf of the Board:

"Peter Hughes" (signed)

Peter Hughes, Director

"Phil Dyer" (signed)

Phil Dyer, Director

See notes to consolidated financial statements

Kelso Technologies Inc.

Consolidated Statements of Changes in Equity

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

	Capital Stock		Obligation to issue shares	Reserves	Deficit	Total
	Number of common shares	Amount				
Balance, December 31, 2014	45,246,752	\$ 22,141,417	\$ -	\$ 2,375,598	\$ (7,918,089)	\$ 16,598,926
Exercise of options	825,000	373,723	-	(149,983)	-	223,740
Share-based expense	-	-	-	672,533	-	672,533
Dividends paid	-	-	-	-	(1,377,654)	(1,377,654)
Loss for the year	-	-	-	-	(2,510,826)	(2,510,826)
Balance, December 31, 2015	46,071,752	\$ 22,515,140	\$ -	\$ 2,898,148	\$ (11,806,569)	\$ 13,606,719
Exercise of options	340,000	314,680	-	(162,554)	-	152,126
Shares to be issued	-	-	192,946	-	-	192,946
Share-based expense	-	-	-	285,745	-	285,745
Net loss for the year	-	-	-	-	(2,465,592)	(2,465,592)
Balance, December 31, 2016	46,411,752	\$ 22,829,820	\$ 192,946	\$ 3,021,339	\$ (14,272,161)	\$ 11,771,944
Shares issued	500,000	401,432	(192,946)	-	-	208,486
Share-based expense	-	-	-	469,187	-	469,187
Shares to be issued	-	-	131,527	-	-	131,527
Net loss for the year	-	-	-	-	(5,015,911)	(5,015,911)
Balance, December 31, 2017	46,911,752	\$ 23,231,252	\$ 131,527	\$ 3,490,526	\$ (19,288,072)	\$ 7,565,233

See notes to consolidated financial statements

Kelso Technologies Inc.

Consolidated Statements of Operations and Comprehensive Loss

For the years ended December 31

(Expressed in US Dollars)

	2017	2016	2015
Revenues (Note 14)	\$ 6,062,778	\$ 8,077,143	\$ 18,910,122
Cost of Goods Sold (Notes 6 and 7)	5,044,093	6,098,902	13,809,993
Gross Profit	1,018,685	1,978,241	5,100,129
Expenses			
Office and administration	1,701,723	2,076,460	1,547,182
Management compensation (Note 10)	544,014	717,369	727,217
Research	1,572,714	704,868	783,680
Marketing	554,458	587,553	730,389
Travel	430,304	526,451	445,555
Accounting and legal	370,495	357,876	239,581
Share-based expense (Notes 9 (b)) and 10)	469,187	285,745	672,533
Consulting	251,055	246,501	421,869
Investor relations	84,000	84,000	84,000
Foreign exchange (gain) loss	(115,643)	(128,073)	584,162
Amortization (Notes 7 and 8)	17,088	3,024	3,024
Bad debts	82,042	-	-
	5,961,437	5,461,774	6,239,192
Loss Before the Following:	(4,942,752)	(3,483,533)	(1,139,063)
Interest income	3,875	28,755	30,809
Write-off of intangible assets (Note 8)	-	-	(298,484)
Write-off of inventory (Note 6)	(197,729)	-	-
Write-off of property, plant and equipment (Note 7)	(29,601)	-	-
Loss Before Taxes:	(5,166,207)	(3,454,778)	(1,406,738)
Income Tax Expense (Recovery) (Note 11)			
Current	22,137	(1,248,551)	1,191,020
Deferred	(172,433)	259,365	(86,932)
	(150,296)	(989,186)	1,104,088
Net Loss and Comprehensive Loss for the year	\$ (5,015,911)	\$ (2,465,592)	\$ (2,510,826)
Basic Loss Per Share (Note 13)	\$ (0.11)	\$ (0.05)	\$ (0.05)
Diluted Loss Per Share (Note 13)	\$ (0.11)	\$ (0.05)	\$ (0.05)
Weighted Average Number of Common Shares Outstanding			
Basic (Note 13)	46,848,053	46,215,861	45,779,903
Diluted (Note 13)	46,848,053	46,215,861	45,779,903

See notes to consolidated financial statements

Kelso Technologies Inc.
Consolidated Statements of Cash Flows
For the years ended December 31
(Expressed in US Dollars)

	2017	2016	2015
Operating Activities			
Net loss	\$ (5,015,911)	\$ (2,465,592)	\$ (2,510,826)
Items not involving cash			
Deferred income tax (recovery)	(172,433)	259,365	(86,932)
Amortization (Notes 7 and 8)	203,980	241,363	237,201
Write-off of intangible assets (Note 8)	-	-	298,484
Write-off of inventory (Note 6)	668,383	-	-
Write-off of property, plant and equipment	29,601	-	-
Share-based expense	469,187	285,745	672,533
Bad debts	82,042	-	-
Unrealized foreign exchange loss (gain)	(115,643)	(188,789)	715,292
	(3,850,794)	(1,867,908)	(674,248)
Changes in non-cash working capital			
Accounts receivable	(97,642)	1,068,643	1,143,692
Income tax receivable	753,223	-	-
Prepaid expenses and deposit	527,897	395,748	(1,036,399)
Inventory	567,764	775,790	(1,812,475)
Accounts payable and accrued liabilities	582,099	(275,098)	(2,575,558)
Income tax payable (recovery)	(112,900)	(1,240,165)	346,109
	2,220,441	724,918	(3,934,631)
Cash Used in Operating Activities	(1,630,353)	(1,142,990)	(4,608,879)
Investing Activities			
Intangible assets	(353,010)	(25,000)	-
Property, plant and equipment	(33,336)	(35,938)	(242,086)
Cash Used in Investing Activities	(386,346)	(60,938)	(242,086)
Financing Activities			
Issue of and subscription for common shares, net of share issue costs	-	152,126	223,740
Dividend paid	-	-	(1,377,654)
Cash Provided by (Used in) Financing Activities	-	152,126	(1,153,914)
Foreign Exchange Effect on Cash	115,643	188,789	(715,292)
Outflow of Cash and Cash Equivalents	(1,901,056)	(863,013)	(6,720,171)
Cash and Cash Equivalents, Beginning of Year	2,312,279	3,175,292	9,895,463
Cash and Cash Equivalents, End of Year	\$ 411,223	\$ 2,312,279	\$ 3,175,292

Supplemental Cash Flow Information (Note 12)
See notes to consolidated financial statements

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

1. NATURE OF OPERATIONS

Kelso Technologies Inc. (the "Company") was incorporated under the laws of British Columbia on March 16, 1987. The Company designs, engineers, markets, produces and distributes various proprietary pressure relief valves and manway securement systems designed to reduce the risk of environmental harm due to non-accidental events in the transportation of hazardous commodities via railroad tank cars. In addition, the Company is an engineering development company specializing in proprietary service equipment used in transportation applications. The Company trades on the Toronto Stock Exchange ("TSX") under the symbol "KLS", and the NYSE ("NYSE") under the trading symbol "KIQ". The Company listed on the TSX on May 22, 2014 and on the NYSE on October 14, 2014. The Company's head office is located at 13966 18B Avenue, South Surrey, British Columbia, V4A 8J1.

The Company's consolidated financial statements have been prepared on a going concern basis, which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

Several conditions may cast substantial doubt on the validity of this assumption. The Company has incurred operating losses of \$5,015,911 for the year ended December 31, 2017 (2016 - \$2,465,592; 2015 - \$2,510,826), has accumulated deficit of \$19,288,072 at December 31, 2017 (2016 - \$14,272,161), has limited resources and has operating cash outflows for the past several years. The Company has significant cash requirements to meet its production costs and administrative overhead. Its continuing operations are therefore dependent upon its ability to either secure additional equity capital, as required, or generate positive cash inflows from operations in the future. Management is planning to raise additional capital to finance operations and continue operations. There is no assurance that these plans will be successful.

These consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded assets or the recognition of liabilities that might be necessary should the Company be unable to secure additional equity capital or generate cash flow from operations in the future. Such adjustments could be material.

2. BASIS OF PREPARATION

(a) Statement of compliance

These consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

These consolidated financial statements have been prepared under the historical cost basis, except for financial instruments classified as available-for-sale ("AFS") and fair value through profit or loss ("FVTPL"). These consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

2. BASIS OF PREPARATION (Continued)

(b) Basis of presentation and consolidation

The consolidated financial statements include the accounts of the Company and its integrated wholly owned subsidiaries, Kelso Technologies (USA) Inc., Kel-Flo Industries Inc. (formerly Kelso Innovative Solutions Inc.) and KIQ Industries Inc., which are all Nevada, USA, corporations. KIQ X Industries Inc. is a British Columbia company incorporated on December 12, 2017. Intercompany transactions and balances have been eliminated on consolidation. A subsidiary is consolidated from the date upon which control is acquired by the Company and all material intercompany transactions and balances have been eliminated on consolidation.

Control is achieved when the Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

(c) Functional and presentation currency

The functional and presentation currency of the Company and its subsidiaries is the US dollar ("USD").

(d) Significant management judgments and estimation uncertainty

The preparation of consolidated financial statements in conformity with IFRS requires the Company's management to undertake a number of judgments, estimates and assumptions that affect amounts reported in the consolidated financial statements and notes thereto. Actual amounts may ultimately differ from these estimates and assumptions. The Company reviews its estimates and underlying assumptions on an ongoing basis. Revisions are recognized in the period in which the estimates are revised and may impact future periods.

Significant management judgments

The following are significant management judgments in applying the accounting policies of the Company that have the most significant effect on recognition and measurement of assets, liabilities, income and expenses:

(i) Income taxes

The extent to which deferred tax assets can be recognized is based on an assessment of the probability of the Company generating future taxable income against which the deferred tax assets can be utilized. In addition, significant judgment is required in classifying transactions and assessing probable outcomes of tax positions taken, and in assessing the impact of any legal or economic limits or uncertainties in various tax jurisdictions.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

2. BASIS OF PREPARATION (Continued)

(d) Significant management judgments and estimation uncertainty (Continued)

Significant management judgments (Continued)

(ii) Functional currency

The functional currency for the Company and its subsidiaries is the currency of the primary economic environment in which the entity operates. The Company has determined its functional currency and that of its subsidiaries is the USD. Determination of functional currency may involve certain judgments to determine the primary economic environment and the Company reconsiders the functional currency of its entities if there is a change in events and conditions that determined the primary economic environment.

(iii) Assessment of a transaction as an asset acquisition or business combination

Management applied judgments relating to the acquisition of intellectual property to assess if the acquisition was a business combination or an asset acquisition. Management applied a three-element process to determine whether a business or an asset was purchased, considering inputs, processes and outputs of each acquisition in order to reach a conclusion (Note 8).

(iv) Research and development expenditures

The application of the Company's accounting policy for research and development expenditures requires judgment in determining whether an activity is determined to be research or development, and if deemed to be development, whether it is probable that future economic benefits will flow to the Company, which may be based on assumptions about future events or circumstances. Estimates and assumptions may change if new information becomes available. If new information becomes available indicating that it is unlikely that future economic benefits will flow to the Company, the amount capitalized is written off to profit or loss in the period the new information becomes available.

(v) Going concern assumption

The assessment of whether the going concern assumption is appropriate requires management to take into account all available information about the future, which is at least, but not limited to, twelve months from the end of the reporting period.

2. BASIS OF PREPARATION (Continued)

(d) Significant management judgments and estimation uncertainty (Continued)

Estimation uncertainty

Information about estimates and assumptions that have the most significant effect on the recognition and measurement of assets, liabilities, income and expenses is provided below. Actual results may be substantially different.

(i) Impairment of long-lived assets

Long-lived assets consist of intangible assets and property, plant and equipment.

At the end of each reporting period, the Company reviews the carrying amounts of its long-lived assets to determine whether there is any indication that the carrying amount is not recoverable. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). When an individual asset does not generate independent cash flows, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Assets are grouped together into 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. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs of disposal and value in use. Fair value is determined as the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

(ii) Useful lives of depreciable assets

The Company reviews its estimate of the useful lives of depreciable assets at each reporting date, based on the expected utilization of the assets. Uncertainties in these estimates relate to technical obsolescence that may change the utilization of certain intangible assets and equipment.

(iii) Inventories

The Company estimates the net realizable value of inventories, taking into account the most reliable evidence available at each reporting date. The future realization of these inventories may be affected by future technology or other market-driven changes that may reduce future selling prices. A change to these assumptions could impact the Company's inventory valuation and impact gross margins.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

2. BASIS OF PREPARATION (Continued)

(d) Significant management judgment and estimation uncertainty (Continued)

Estimation uncertainty (Continued)

(iv) Share-based expense

The Company grants share-based awards to certain officers, employees, directors and other eligible persons. For equity settled awards, the fair value is charged to the consolidated statement of operations and comprehensive income (loss) and credited to the reserves, over the vesting period using the graded vesting method, after adjusting for the estimated number of awards that are expected to vest.

The fair value of the equity-settled awards is determined at the date of the grant using the Black-Scholes option pricing model. Option pricing models require the input of highly subjective assumptions, including the expected volatility and expected life of the options. Changes in these assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's stock options.

(v) Allowance for credit losses

The Company provides for doubtful debts by analyzing the historical default experience and current information available about a customer's credit worthiness on an account by account basis. Uncertainty relates to the actual collectability of customer balances that can vary from the Company's estimation. At December 31, 2017, the Company has setup an allowance for doubtful accounts of \$82,042 (2016 - \$nil).

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.

(e) Approval of the consolidated financial statements

The consolidated financial statements of Kelso Technologies Inc. for year ended December 31, 2017 were approved and authorized for issue by the Board of Directors on March 27, 2018.

(f) New accounting standards issued but not yet effective

The standards listed below include only those which the Company reasonably expects may be applicable to the Company at a future date. The Company is currently assessing the impact of these future standards on the consolidated financial statements.

IFRS 9 Financial Instruments

IFRS 9 will replace IAS 39 *Financial Instruments: Recognition and Measurement* and IFRIC 9 *Reassessment of Embedded Derivatives*. The final version of this new standard supersedes the requirements of earlier versions of IFRS 9.

The main features introduced by this new standard compared with predecessor IFRS are as follows:

2. BASIS OF PREPARATION (Continued)

(f) New accounting standards issued but not yet effective (Continued)

- Classification and measurement of financial assets:

Debt instruments are classified and measured on the basis of the entity's business model for managing the asset and its contractual cash flow characteristics as either: "Amortized cost", "Fair value through other comprehensive income" or "Fair value through profit or loss" (default). Equity instruments are classified and measured as "Fair value through profit or loss" unless upon initial recognition elected to be classified as "Fair value through other comprehensive income".

- Classification and measurement of financial liabilities:

When an entity elects to measure a financial liability at fair value, gains or losses due to changes in the entity's own credit risk is recognized in other comprehensive income (as opposed to previously profit or loss).

- Impairment of financial assets:

An expected credit loss impairment model replaced the incurred loss model and is applied to financial assets at "Amortized cost" or "Fair value through other comprehensive income", lease receivables, contract assets or loan commitments and financial guarantee contracts. An entity recognizes 12-month expected credit losses if the credit risk of a financial instrument has not increased significantly since initial recognition, and lifetime expected credit losses otherwise.

- Hedge accounting:

Hedge accounting remains a choice, however is now available for a broader range of hedging strategies. Voluntary termination of a hedging relationship is no longer permitted. Effectiveness testing now needs to be performed prospectively only. Entities may elect to continue applying IAS 39 hedge accounting on adoption of IFRS 9 (until the IASB has completed its separate project on the accounting for open portfolios and macro hedging).

Applicable to the Company's annual period beginning January 1, 2018.

IFRS 2 Share-based Payment

The amendments provide guidance on the accounting for:

- the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based expenses;
- share-based expense transactions with a net settlement feature for withholding tax obligations; and
- a modification to the terms and conditions of a share-based expense that changes the classification of the transaction from cash-settled to equity-settled.

Applicable to the Company's annual period beginning January 1, 2018.

2. BASIS OF PREPARATION (Continued)

(f) New accounting standards issued but not yet effective (Continued)

IFRS 15 Revenue from Contracts with Customers

IFRS 15 provides a single, principles based five-step model to be applied to all contracts with customers.

The five steps in the model are as follows:

- Identify the contract with the customer
- Identify the performance obligations in the contract
- Determine the transaction price
- Allocate the transaction price to the performance obligations in the contracts
- Recognize revenue when (or as) the entity satisfies a performance obligation.

Guidance is provided on topics such as the point in which revenue is recognized, accounting for variable consideration, costs of fulfilling and obtaining a contract and various related matters. New disclosures about revenue are also introduced.

Applicable to the Company's annual period beginning on January 1, 2018.

IFRS 16 Leases

This new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both the lessee and the lessor. The new standard introduces a single lessee accounting model that requires the recognition of all assets and liabilities arising from a lease.

The main features of the new standard are as follows:

- An entity identifies as a lease a contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.
- A lessee recognizes an asset representing the right to use the leased asset, and a liability for its obligation to make lease payments. Exceptions are permitted for short-term leases and leases of low-value assets.
- A lease asset is initially measured at cost, and is then depreciated similarly to property, plant and equipment. A lease liability is initially measured at the present value of the unpaid lease payments.
- A lessee presents interest expense on a lease liability separately from depreciation of a lease asset in the statement of profit or loss and other comprehensive income.
- A lessor continues to classify its leases as operating leases or finance leases, and to account for them accordingly.
- A lessor provides enhanced disclosures about its risk exposure, particularly exposure to residual-value risk.

Applicable to the Company's annual period beginning January 1, 2019.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies.

(a) Cash equivalents

Cash equivalents include short-term liquid investments with maturities of three months or less, are readily convertible into known amounts of cash and which are subject to insignificant changes in value.

(b) Inventory

Inventory components include raw materials and supplies used to assemble valves and manway covers, as well as finished valves and manway covers. All inventories are recorded at the lower of cost on a weighted average basis and net realizable value. The stated value of all inventories includes purchase and assembly costs of all raw materials and supplies, and attributable overhead and amortization. A regular review is undertaken to determine the extent of any provision for obsolescence.

(c) Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses, if any. The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. A change in the expected useful life of the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

The Company amortizes intangible assets with finite lives on a straight-line basis over their estimated useful lives as follows:

Patents - 5 years
Rights - 2 years

Amortization begins when the intangible asset is ready for use. Product and technology development costs, which meet the criteria for deferral and are expected to provide future economic benefits with reasonable certainty are deferred and amortized over the estimated life of the products or technology once commercialization commences.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(d) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated amortization. Leasehold improvements are amortized on a straight-line basis over the lease term. Amortization is calculated over the estimated useful life of the property, plant and equipment at the following annual rates:

Building	– 4% declining-balance
Production equipment	– 20% declining-balance
Vehicles	– 30% declining-balance
Leasehold improvements	– 5 year straight-line

(e) Revenue recognition

Revenues are recognized when the risks and rewards of ownership have passed to the customer based on the terms of the sale, collection of the relevant receivable is probable, evidence of an arrangement exists and the sales price is fixed or determinable. Risks and rewards of ownership pass to the customer upon shipment of the pressure relief valves and/or manway securement systems. Provisions for sales discounts and returns from customers are made at the time of sale.

(f) Impairment of long-lived assets

The Company's tangible and intangible assets are reviewed for any indication of impairment at each statement of financial position date. If indication of impairment exists, the asset's recoverable amount is estimated. An impairment loss is recognized when the carrying amount of an asset, or its cash-generating unit, exceeds its recoverable amount. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of cash inflow from other assets or groups of assets.

The recoverable amount is the greater of the asset's fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the assets. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(g) Income taxes

(i) Current and deferred income taxes

Income tax expense, consisting of current and deferred tax expense, is recognized in the consolidated statements of operations. Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at period-end, adjusted for amendments to tax payable with regard to previous years.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(g) Income taxes (continued)

(i) Current and deferred income taxes (continued)

Deferred tax assets and liabilities and the related deferred income tax expense or recovery are recognized for deferred tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income (loss) in the period that substantive enactment occurs.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. To the extent that the Company does not consider it probable that a deferred tax asset will be recovered, the deferred tax asset is reduced. Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

(ii) Texas margin tax

Effective January 1, 2007, the state of Texas enacted an annual franchise tax known as the Texas margin tax, which is equal to 1% of the lesser of: (a) 70% of a taxable entity's revenue; and (b) 100% of total revenue less, at the election of the taxpayer: (i) cost of goods sold; or (ii) compensation. A provision for the margin tax owing has been recorded in the consolidated statements of operations and comprehensive loss.

(h) Foreign currency translation

The accounts of foreign balances and transactions are translated into USD as follows:

- (i) Monetary assets and liabilities, at the rate of exchange in effect at the consolidated statement of financial position date;
- (ii) Non-monetary assets and liabilities, at the exchange rates prevailing at the time of the acquisition of the assets or assumption of the liabilities; and
- (iii) Revenue and expense items (excluding amortization, which is translated at the same rate as the related asset), at the rate of exchange prevailing at the transaction date.

Gains and losses arising from translation of foreign currency are included in the determination of net income (loss).

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(i) Earnings per share

The Company presents basic earnings per share data for its common shares, calculated by dividing the earnings attributable to common shareholders of the Company by the weighted average number of shares outstanding during the period. The Company uses the treasury stock method for calculating diluted earnings per share. Under this method the dilutive effect on earnings per share is calculated on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds of such exercise would be used to purchase common shares at the average market price during the period. However, the calculation of diluted loss per share excludes the effects of various conversions and exercise of options and warrants that would be anti-dilutive.

(j) Share-based expense

The Company grants share options to acquire common shares of the Company to directors, officers, employees and consultants. The fair value of share-based expense to employees is measured at grant date, using the Black-Scholes option pricing model, and is recognized over the vesting period for employees using the graded vesting method. Fair value of share-based expenses for non-employees is recognized and measured at the date the goods or services are received based on the fair value of the goods or services received. If it is determined that the fair value of goods and services received cannot be reliably measured, the share-based expense is measured at the fair value of the equity instruments issued using the Black-Scholes option pricing model.

For both employees and non-employees, the fair value of share-based expense is recognized on the consolidated statement of operations and comprehensive loss, with a corresponding increase in reserves. The amount recognized as expense is adjusted to reflect the number of share options expected to vest. Consideration received on the exercise of stock options is recorded in capital stock and the related share-based expense in reserves is transferred to capital stock.

(k) Capital stock

Proceeds from the exercise of stock options and warrants are recorded as capital stock in the amount for which the option or warrant enabled the holder to purchase a share in the Company. Any previously recorded share-based expense included in the share-based expenses reserve is transferred to capital stock on exercise of options. Capital stock issued for non-monetary consideration is valued at the closing market price at the date of issuance. The proceeds from the issuance of units are allocated between common shares and warrants based on the residual value method. Under this method, the proceeds are allocated first to capital stock based on the fair value of the common shares at the time the units are priced and any residual value is allocated to the warrants reserve. Consideration received for the exercise of warrants is recorded in capital stock, and any related amount recorded in warrants reserve is transferred to capital stock.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

(l) Financial instruments

(i) Financial assets

The Company classifies its financial assets into one of the following categories, depending on the purpose for which the asset was acquired. The Company's accounting policy for each category is as follows:

Fair value through profit or loss

This category comprises derivatives, or assets acquired or incurred principally for the purpose of selling or repurchasing it in the near term. They are carried at fair value with changes in fair value recognized through profit or loss. Cash and cash equivalents are included in this category of financial assets.

Loans and receivables

These assets are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are carried at cost less any provision for impairment. Individually significant receivables are considered for impairment when they are past due or when other objective evidence is received that a specific counterparty will default. Accounts receivable are included in this category of financial assets.

(ii) Financial liabilities

The Company classifies its financial liabilities in the following category:

Other financial liabilities

Other financial liabilities are non-derivatives and are recognized initially at fair value, net of transaction costs incurred, and are subsequently stated at amortized cost using the effective interest rate method. Any difference between the amounts originally received, net of transaction costs, and the redemption value is recognized in profit or loss over the period to maturity using the effective interest method. Other financial liabilities are classified as current or non-current based on their maturity date. Accounts payable and accrued liabilities is included in this category of financial liability.

(m) Fair value hierarchy

The Company categorizes financial instruments measured at fair value at one of three levels according to the reliability of the inputs used to estimate fair values. The fair value of financial assets and financial liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Financial assets and liabilities in Level 2 are valued using inputs other than quoted prices for which all significant inputs are based on observable market data. Level 3 valuations are based on inputs that are not based on observable market data.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

4. CAPITAL MANAGEMENT

The Company considers its capital to be comprised of shareholders' equity.

The Company's objectives in managing its capital are to maintain its ability to continue as a going concern and to further develop its business. To effectively manage the Company's capital requirements, the Company has a planning and budgeting process in place to meet its strategic goals.

In order to facilitate the management of its capital requirements, the Company prepares expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. Management reviews the capital structure on a regular basis to ensure the above objectives are met. There have been no changes to the Company's approach to capital management during the year ended December 31, 2017. There are no externally imposed restrictions on the Company's capital.

5. FINANCIAL INSTRUMENTS

Financial instruments are agreements between two parties that result in promises to pay or receive cash or equity instruments. The carrying values of accounts receivable and accounts payable and accrued liabilities approximate their fair values due to their short term to maturity. The Company has exposure to the following risks from its use of financial instruments:

- Credit risk;
- Liquidity risk; and
- Market risk.

(a) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Cash and cash equivalents are placed with major Canadian and US financial institutions and the Company's concentration of credit risk for cash and cash equivalents and maximum exposure thereto is \$411,223 (2016 - \$2,312,279).

With respect to its accounts receivable, the Company assesses the credit rating of all customers and maintains provisions for potential credit losses, and any such losses to date have been within management's expectations. The Company's credit risk with respect to accounts receivable and maximum exposure thereto is \$735,487 (2016 - \$637,845). The Company's concentration of credit risk for accounts receivable with respect to its significant customers is as follows: Customer A is \$94,114 (2016 - \$73,500), Customer B is \$78,306 (2016 - \$nil) while Customer C is \$150,000 related to expense recovery (2016 - \$Nil) (Note 14). The Company has provided for an allowance for doubtful accounts amounting to \$82,042 at December 31, 2017 (2016 - \$nil).

To reduce the credit risk of accounts receivable, the Company regularly reviews the collectability of the accounts receivable to ensure there is no indication that these amounts will not be fully recoverable.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

5. FINANCIAL INSTRUMENTS (Continued)

(b) Liquidity risk

Liquidity risk is the risk that the Company will be unable to meet its financial obligations as they fall due. The Company's approach to managing liquidity risk is to ensure, as far as possible, that it will have sufficient liquid funds to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

At December 31, 2017, the Company has \$411,223 (2016 - \$2,312,279) of cash and cash equivalents to settle current liabilities of \$844,516 (2016 - \$271,600) consisting of the following: trade accounts payable of \$799,254 (2016 - \$235,600) and due to related party balance of \$45,262 (2016 - \$36,000). All payables are due within a year.

(c) Market risk

The significant market risks to which the Company is exposed are interest rate risk and currency risk.

(i) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in market interest rates. The Company's cash and cash equivalents consist of cash held in bank accounts and short-term liquid investments that earn interest at variable rates. Due to the short-term nature of these financial instruments, fluctuations in market rates of interest do not have a significant impact on the estimated fair value or future cash flows.

(ii) Currency risk

The Company is exposed to currency risk to the extent expenditures incurred or funds received and balances maintained by the Company are denominated in Canadian dollars ("CAD"). The Company does not manage currency risk through hedging or other currency management tools.

As at December 31, 2017 and 2016, the Company's had the following assets denominated in CAD (amounts presented in USD):

	December 31, 2017	December 31, 2016
Cash and cash equivalents	\$ 15,882	\$ 1,983,028
Accounts receivable	32,976	25,302
Accounts payable	(80,000)	(75,480)
	\$ (31,142)	\$ 1,932,850

Based on the above, assuming all other variables remain constant, a 14% (2016 – 14%) weakening or strengthening of the USD against the CAD would result in approximately \$4,400 (2016 - \$271,000) foreign exchange loss or gain in the consolidated statements of operations and comprehensive income (loss).

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

6. INVENTORY

	December 31, 2017	December 31, 2016
Finished goods	\$ 256,185	\$ 218,128
Raw materials and supplies	3,724,058	4,988,001
	\$ 3,980,243	\$ 5,206,129

Included in cost of goods sold is \$3,376,123 (2016 - \$4,642,761; 2015 - \$10,595,521) of direct material costs recognized as expense.

Inventory write-off during the year was \$668,383 (2016 - \$nil; 2015 - \$nil) of which \$470,654 (2016- \$nil; 2015- \$nil) is included in cost of goods sold and \$197,729 (2016 - \$nil; 2015 - \$nil) is included in general and administrative expenses.

7. PROPERTY, PLANT AND EQUIPMENT

Cost	Land	Building	Leasehold Improvements	Production Equipment	Vehicles	Total
Balance, December 31, 2015	\$ 12,558	\$ 2,955,901	\$ 43,715	\$ 803,645	\$ 28,181	\$ 3,844,000
Additions	-	-	-	6,337	29,601	35,938
Balance, December 31, 2016	\$ 12,558	\$ 2,955,901	\$ 43,715	\$ 809,982	\$ 57,782	\$ 3,879,938
Additions	-	-	-	-	33,336	33,336
Disposition	-	-	-	-	(29,601)	(29,601)
Balance, December 31, 2017	\$ 12,558	\$ 2,955,901	\$ 43,715	\$ 809,982	\$ 61,517	\$ 3,883,673
Accumulated Amortization						
Balance, December 31, 2015	\$ -	\$ 193,461	\$ 24,635	\$ 208,339	\$ 20,672	\$ 447,107
Amortization	-	110,498	5,593	119,995	2,253	238,339
Balance, December 31, 2016	\$ -	\$ 303,959	\$ 30,228	\$ 328,334	\$ 22,925	\$ 685,446
Amortization	-	106,078	2,696	96,330	1,577	206,681
Balance, December 31, 2017	\$ -	\$ 410,037	\$ 32,924	\$ 424,664	\$ 24,502	\$ 892,127
Carrying Value						
December 31, 2017	\$ 12,558	\$ 2,545,864	\$ 10,791	\$ 385,318	\$ 37,015	\$ 2,991,546
December 31, 2016	\$ 12,558	\$ 2,651,942	\$ 13,487	\$ 481,648	\$ 34,857	\$ 3,194,492

Included in cost of goods sold is \$186,892 (2016 - \$230,002; 2015 - \$237,177) of amortization related to property, plant and equipment.

Included in general and administrative expenses is \$9,528 (2016 - \$nil, 2015 - \$nil) of amortization related to property, plant and equipment.

Included in inventory is \$10,261 (2016 - \$8,337; 2015 - \$4,939) of amortization related to property, plant and equipment.

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

8. INTANGIBLE ASSETS

Cost	Patent	Rights	Product Development Costs	Total
Balance, December 31, 2015	\$ 40,840	\$ 65,000	\$ -	\$ 105,840
Additions	-	217,946	-	217,946
Balance, December 31, 2016	40,840	282,946	-	323,786
Additions	-	-	718,023	718,023
Balance, December 31, 2017	\$ 40,840	\$ 282,946	\$ 718,023	\$ 1,041,809
Accumulated Amortization				
Balance, December 31, 2015	\$ 21,449	\$ 65,000	\$ -	\$ 86,449
Amortization	3,024	-	-	3,024
Balance, December 31, 2016	24,473	65,000	-	89,473
Amortization	7,560	-	-	7,560
Balance, December 31, 2017	\$ 32,033	\$ 65,000	\$ -	\$ 97,033
Carrying Value				
December 31, 2017	\$ 8,807	\$ 217,946	\$ 718,023	\$ 944,776
December 31, 2016	\$ 16,367	\$ 217,946	\$ -	\$ 234,313

On November 10, 2016, the Company signed a technology development agreement to acquire all intellectual property rights (the "Products") of G & J Technologies (the "Vendor"). As consideration, acquisition costs of \$217,946 were incurred, consisting of \$25,000 in cash and 250,000 common shares with a fair value of \$192,946. The shares were issued during the year ended December 31, 2017.

On November 10, 2016, the Vendor also entered into a consulting agreement with the Company for a fee of \$10,000 per month. In addition, the Company will pay \$75,000 in cash and issue 750,000 common shares of the Company as follows:

- \$25,000 cash and 250,000 shares issuable on the filing of the first new patent application related to the Products (the Company paid the cash and issued the shares during the year ended December 31, 2017 with a fair value of \$208,486);
- \$25,000 cash and 250,000 shares issuable on the successful completion of a commercially viable production prototype for the first Product (the Company accrued for the cash payment and shares to be issued at December 31, 2017 with a fair value of \$131,527); and
- \$25,000 cash and 250,000 shares issuable on the completion of the sale of the first ten commercial vehicles incorporating the Products.

The Company is also required to pay a royalty to the Vendor of 2.5% of the net sales earned by the Company, to be paid within 30 days of the end of each calendar quarter. As at December 31, 2017 the Company has not earned any revenue from the sale of the Products. The Company has incurred \$718,023 (2016 - \$nil) of internal product development cost that has been recorded as deferred development costs at December 31, 2017.

During the year ended December 31, 2015, the Company determined that certain products could not generate independent cash flows, and accordingly impaired \$298,484 of product development costs.

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

9. CAPITAL STOCK

Authorized:

Unlimited Class A non-cumulative, preferred shares without par value, of which 5,000,000 are designated Class A, convertible, voting, preferred shares.

Unlimited common shares without par value.

Issued:

(a) Common shares

During the year ended December 31, 2017, the Company issued 250,000 shares with a fair value of \$192,946 pursuant to the acquisition of intellectual property rights of G&J Technologies and 250,000 shares with a fair value of \$208,486 pursuant to achieving the second milestone of the G&J Technologies technology development agreement. At the year end, the Company has an obligation to issue 250,000 shares with a fair value of \$131,527 pursuant to the agreement for achieving the third milestone of the G&J Technologies technology development agreement (Note 17).

During the year ended December 31, 2016, the Company issued 340,000 shares pursuant to the exercise of share purchase options for gross proceeds of \$152,126. Fair value previously recognized on options exercised of \$162,554 was reclassified from reserves to capital stock. As at December 31, 2016, the Company has an obligation to issue 250,000 shares with a fair value of \$192,946 in relation to the intellectual property rights acquired during the year.

During the year ended December 31, 2015, the Company issued 825,000 shares pursuant to the exercise of share purchase options for gross proceeds of \$223,740. Fair value previously recognized on options exercised of \$149,983 was reclassified from reserves to capital stock.

(b) Stock options

The Company has a stock option plan (the "Plan") available to employees, directors, officers and consultants with grants under the Plan approved from time to time by the Board of Directors. Under the Plan, the Company is authorized to issue options to purchase an aggregate of up to 10% of the Company's issued and outstanding common shares. Each option can be exercised to acquire one common share of the Company. The exercise price for an option granted under the Plan may not be less than the market price at the date of grant less a specified discount dependent on the market price.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

9. CAPITAL STOCK (Continued)

(b) Stock options (Continued)

Options to purchase common shares have been granted to directors, employees and consultants as follows:

Exercise Price	Expiry Date	December 31, 2016	Granted	Exercised	Expired	December 31, 2017
\$1.45	March 31, 2017	670,000	-	-	(670,000)	-
\$2.12	August 25, 2017	400,000	-	-	(400,000)	-
\$0.70(CAD)	October 7, 2019	28,571	-	-	-	28,571
\$6.85(CAD)	November 14, 2019	100,000	-	-	-	100,000
\$1.30	August 18, 2021	1,325,000	-	-	-	1,325,000
\$0.90	July 6, 2022	-	50,000	-	-	50,000
\$0.30	November 28, 2022	-	825,000	-	-	825,000
Total outstanding		2,523,571	875,000	-	(1,070,000)	2,328,571
Total exercisable		1,198,571	275,000	-	-	845,238

Exercise Price	Expiry Date	December 31, 2015	Granted	Exercised	Expired	December 31, 2016
\$5.90	January 2, 2016	500,000	-	-	(500,000)	-
\$2.12(CAD)	August 25, 2017	500,000	-	-	(100,000)	400,000
\$0.58(CAD)	July 22, 2016	340,000	-	(340,000)	-	-
\$1.45	March 31, 2017	770,000	-	-	(100,000)	670,000
\$0.65	October 30, 2017	80,000	-	-	(80,000)	-
\$6.25	July 7, 2019	100,000	-	-	(100,000)	-
\$0.70(CAD)	October 7, 2019	28,571	-	-	-	28,571
\$6.85(CAD)	November 14, 2019	100,000	-	-	-	100,000
\$1.30	August 18, 2021	-	1,325,000	-	-	1,325,000
Total outstanding		2,418,571	1,325,000	(340,000)	(880,000)	2,523,571
Total exercisable		2,085,238	-	-	-	1,198,571

A summary of the Company's stock options as at December 31, 2017 and 2016, and changes for the years then ended are as follows:

	Number	Weighted Average Exercise Price
Outstanding, December 31, 2015	2,418,571	\$2.68
Granted	1,325,000	\$1.30
Exercised	(340,000)	\$0.43
Expired	(880,000)	\$4.52
Outstanding, December 31, 2016	2,523,571	\$1.61
Granted	875,000	\$0.33
Exercised	-	-
Expired	(1,070,000)	\$1.70
Outstanding, December 31, 2017	2,328,571	\$1.11

The weighted average contractual life for the remaining options at December 31, 2017 is 4.01 years (2016 – 2.75).

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

9. CAPITAL STOCK (Continued)

(b) Stock options (Continued)

Share-based expense

Share-based expense of \$469,187 (2016 - \$285,745; 2015 - \$672,533) was recognized in the year ended December 31, 2017 for stock options. The share-based expense relates to options granted during December 31, 2017, 2016 and 2015, which vest over time.

The fair value of stock options is determined using the Black-Scholes option pricing model with assumptions as follows:

	Year ended December 31, 2017	Year ended December 31, 2016	Year ended December 31, 2015
Risk-free interest rate (average)	1.56%	0.58%	0.77%
Estimated volatility (average)	61.95%	64.76%	52.38%
Expected life in years	5.00	4.18	1.50
Expected dividend yield	0.00%	0.00%	0.00%
Estimated forfeitures	0.00%	0.00%	0.00%
Grant date fair value per option	\$0.1652	\$0.63	\$0.77

Option pricing models require the use of highly subjective estimates and assumptions, including the expected stock price volatility. Expected volatility was determined using the Company's historical stock prices.

10. RELATED PARTY TRANSACTIONS

Related party transactions not otherwise described in these consolidated financial statements are shown below. The remuneration of the Company's directors and other members of key management, being the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer and the Executive Vice-President of Business Development who have the authority and responsibility for planning, directing and controlling the activities of the Company, consist of the following amounts:

	December 31, 2017	December 31, 2016	December 31, 2015
Management compensation	\$ 544,014	\$ 717,368	\$ 727,217
Management bonus*	\$ -	\$ -	\$ -
Share-based expense**	\$ 264,172	\$ 160,854	\$ 553,011
Directors' fees	\$ 67,000	\$ 66,000	\$ 34,500

* The Company has management bonus agreements whereby 10% of the annual income before taxes and share-based expense is equally distributed to management.

** Share-based expense consists of the key management portion of the fair value of options granted calculated using the Black-Scholes option pricing model and does not include any cash compensation.

As at December 31, 2017, amounts due to related parties included accounts payable, which are unsecured and have no interest or specific terms of payments, of \$45,262 (2016 - \$36,000) consisting of \$16,500 (2016 - \$36,000) for directors' fees and \$28,762 (2016 - \$nil) for management fees.

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

11. INCOME TAXES

During the 2015 fiscal year, a tax liability in the amount of \$2,004,272 was recorded with respect to estimated US outstanding taxes payable. During the year ended December 31, 2016, new information was obtained indicating that there was a reduction of \$1,170,105, therefore no income tax should be payable. The reversal of the tax provision has been accounted for as a change in tax estimate and has been adjusted prospectively as an income tax recovery during the year ended December 31, 2016. The amounts included in income tax payable represent penalties and interest.

The Company has approximately \$5,748,000 in non-capital losses in the US that may be applied against future taxable income (expiring in 2032 or later).

The tax effect items that give rise to significant portions of the deferred income tax assets and deferred income tax liabilities at December 31, 2017 and 2016 are as follows:

	December 31, 2017	December 31, 2016
Non-capital loss carry-forwards	\$ 372,616	\$ -
Deferred income tax assets	\$ 372,616	\$ -
Deficiency (excess) of carrying value over tax value of property, plant and equipment	\$ (154,043)	\$ (169,251)
Excess of carrying value over tax value of intangible assets	(218,573)	(3,182)
Deferred income tax liability	\$ (372,616)	\$ (172,433)
Net deferred tax asset (liability)	\$ -	\$ (172,433)

Significant unrecognized tax benefits and unused tax losses for which no deferred tax assets is recognized as of December 31, 2017 and 2016 are as follows:

	December 31, 2017	December 31, 2016
Excess of tax value over carrying value of mineral properties	\$ 13,807	\$ 13,077
Non-capital losses carried forward	4,126,977	-
Unrealized foreign exchange gain	115,642	-
Unrecognized deductible temporary differences	\$ 4,256,426	\$ 13,077

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

11. INCOME TAXES (Continued)

Income tax expense differs from the amount that would be computed by applying the Canadian statutory income tax rate of 26.00% (2016 - 26.00%; 2015 - 26.00%) to income (loss) before income taxes as follows:

	December 31, 2017	December 31, 2016	December 31, 2015
Loss before income taxes	\$ (5,166,207)	\$ (3,454,778)	\$ (1,406,738)
Statutory income tax rate	26.00%	26.00%	26.00%
Income tax (benefit) liability computed at statutory tax rate	(1,343,214)	(898,242)	(365,752)
Items not deductible for income tax purposes	(100,626)	114,580	174,859
Under/(over) provision of taxes in prior years	-	(824,607)	1,201,114
Change in timing differences	187,473	372,451	(447,394)
Impact on foreign exchange on tax assets and liabilities	117,313	162,359	133,131
Difference between Canadian and foreign taxes	(464,959)	(119,976)	-
Unused tax losses and tax offsets not recognized	1,431,580	(414,825)	418,224
Income tax expense (recovery)	(172,433)	(1,608,260)	1,114,182
Penalties and interest included in income tax expense	-	614,283	-
Texas margin tax and branch tax (recovery)	22,137	4,791	(10,094)
Income tax expense (recovery)	\$ (150,296)	\$ (989,186)	\$ 1,104,088

12. SUPPLEMENTAL CASH FLOW INFORMATION

	December 31, 2017	December 31, 2016	December 31, 2015
Obligation to issue shares for intangible assets (Note 8)	\$ 131,527	\$ 192,946	\$ -
Shares issued for intangible assets	\$ 401,432	\$ -	\$ -
Intangible assets in accounts payable and accrued liabilities	\$ 25,000	\$ -	\$ -
Interest paid	\$ -	\$ 1,040	\$ -
Income taxes paid	\$ -	\$ 20,693	\$ 817,774

	December 31, 2017	December 31, 2016
Cash and Cash Equivalents is comprised of:		
Cash	\$ 411,223	\$ 375,799
Guaranteed investment certificates	-	1,936,480
	\$ 411,223	\$ 2,312,279

KELSO TECHNOLOGIES INC.
Notes to Consolidated Financial Statements
For the years ended December 31, 2017, 2016 and 2015
(Expressed in US Dollars)

13. EARNINGS PER SHARE

The calculation of basic and diluted earnings (loss) per share for the relevant years is based on the following:

	December 31, 2017	December 31, 2016	December 31, 2015
Net loss for the year	\$ (5,015,911)	\$ (2,465,592)	\$ (2,510,826)
Basic weighted average number of common shares outstanding	46,848,053	46,215,861	45,779,903
Effect on dilutive securities:			
Options	-	-	-
Warrants	-	-	-
Diluted weighted average number of common shares outstanding	46,848,053	46,215,861	45,779,903
Basic loss per share	\$ (0.11)	\$ (0.05)	\$ (0.05)
Diluted loss per share	\$ (0.11)	\$ (0.05)	\$ (0.05)

14. SIGNIFICANT CUSTOMERS

The following table represents sales to individual customers exceeding 10% of the Company's annual revenues:

	December 31, 2017	December 31, 2016	December 31, 2015
Customer A	\$ 2,934,404	\$ 2,511,850	\$ 8,555,088
Customer B	\$ 896,965	\$ 2,107,426	\$ 2,045,215
Customer C	\$ -	\$ -	\$ 3,196,253
Customer D	\$ -	\$ -	\$ 1,959,883

All Customers are major US and Canadian corporations who have displayed a pattern of consistent timely payment of accounts owing.

The Company is obligated to pay a 5% royalty from sales of their manway securement systems. During the year ended December 31, 2017, there were revenues from sales of the manway securement systems totalling \$183,337 (2016 - \$224,945).

15. EMPLOYEE BENEFITS

Total employee benefit expenses, including salary and wages, management compensation, share-based expense and benefits for the year ended December 31, 2017 amounted to \$3,448,877 (2016 - \$3,800,497; 2015 - \$4,525,853).

16. SEGMENTED INFORMATION

The Company operates in two business segments with operations and long-term assets in the United States. The two business segments include the design, production and distribution of various proprietary pressure relief valves, and active suspension control system for off road vehicles. At December 31, 2017, long-term assets of \$1,044,771 (2016 - \$247,547) relates to the active suspension control system segment and the remaining balance relates to pressure relief valves segment. During the years ended December 31, 2017, 2016 and 2015 there was no revenue related to the active suspension control system.

KELSO TECHNOLOGIES INC.

Notes to Consolidated Financial Statements

For the years ended December 31, 2017, 2016 and 2015

(Expressed in US Dollars)

17. SUBSEQUENT EVENTS

Subsequent to the year-end, the Company paid \$25,000 and issued 250,000 shares to G&J Technologies for the third milestone payment of the G&J technology development agreement that was accrued at December 31, 2017 (Note 8).