

DIAMOND ESTATES WINES & SPIRITS INC.

CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2020 AND 2019



Independent auditor's report

To the Shareholders of Diamond Estates Wines & Spirits Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Diamond Estates Wines & Spirits Inc. and its subsidiaries (together, the Company) as at March 31, 2020 and 2019, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

What we have audited

The Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at March 31, 2020 and 2019;
- the consolidated statements of net loss and comprehensive loss for the years then ended;
- the consolidated statements of changes in shareholders' equity for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

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

Independence

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis.

PricewaterhouseCoopers LLP
PwC Centre, 354 Davis Road, Suite 600, Oakville, Ontario, Canada L6J 0C5
T: +1 905 815 6300; F: +1 905 815 6499

"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.



- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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

(Signed) "PricewaterhouseCoopers LLP"

Chartered Professional Accountants, Licensed Public Accountants

Oakville, Ontario
July 27, 2020

DIAMOND ESTATES WINES & SPIRITS INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
AS AT MARCH 31, 2020 AND 2019

	<u>2020</u>	<u>2019</u>
ASSETS		
Current:		
Accounts receivable (Note 6)	\$ 3,406,053	\$ 2,906,154
Inventories (Note 7)	22,099,156	19,462,687
Prepaid expenses	266,146	232,592
	<u>25,771,355</u>	<u>22,601,433</u>
Long term:		
Property, plant and equipment (Note 9)	18,208,422	18,773,456
Right-of-use assets (Note 10)	3,166,836	1,205,150
Intangible assets (Note 12)	2,804,615	3,155,141
	<u>\$ 49,951,228</u>	<u>\$ 45,735,180</u>
LIABILITIES		
Current:		
Accounts payable and accrued liabilities (Note 13)	\$ 7,159,859	\$ 6,342,500
Note payable (Note 14)	-	550,000
Unearned revenue and deposits received	60,810	60,810
Current portion of term loans payable (Note 15)	19,161,412	452,187
Current portion of leases liabilities (Note 16)	382,730	308,406
	<u>26,764,811</u>	<u>7,713,903</u>
Long term:		
Term loans payable (Note 15)	-	21,536,947
Lease liabilities (Note 16)	2,740,675	844,076
	<u>29,505,486</u>	<u>30,094,926</u>
SHAREHOLDERS' EQUITY		
Common shares (Note 17)	27,690,705	19,157,313
Contributed surplus	1,205,216	747,081
Accumulated deficit	(8,450,179)	(4,264,140)
	<u>20,445,742</u>	<u>15,640,254</u>
	<u>\$ 49,951,228</u>	<u>\$ 45,735,180</u>
Subsequent events (Note 26)		

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

Approved on behalf of the Board:

"David Beutel" Director

"Keith Harris" Director

DIAMOND ESTATES WINES & SPIRITS INC.
CONSOLIDATED STATEMENTS OF NET LOSS AND
COMPREHENSIVE LOSS
YEARS ENDED MARCH 31, 2020 AND 2019

	<u>2020</u>	<u>2019</u>
Revenue	\$ 26,794,230	\$ 28,123,103
Cost of sales		
Change in inventories of finished goods and raw materials consumed	13,700,815	14,978,177
Freight in & royalties in and other	980,850	914,339
Depreciation of property, plant and equipment and right-of-use assets used in production (Notes 9 & 10)	760,827	716,633
	<u>15,442,492</u>	<u>16,609,149</u>
Gross profit	<u>11,351,738</u>	<u>11,513,954</u>
Expenses		
Employee compensation and benefits	6,709,616	6,887,937
General and administrative	3,574,763	3,398,190
Advertising and promotion	1,745,664	1,624,755
Interest on long-term debt	1,113,986	1,164,394
Delivery and warehousing	821,852	739,350
Financing costs	135,050	93,706
Depreciation of property, plant and equipment and right-of-use assets used in selling and administration (Notes 9 & 10)	585,231	352,393
Amortization of intangible assets (Note 12)	344,277	340,530
Share based compensation (Note 18(d))	528,338	549,399
	<u>15,558,777</u>	<u>15,150,654</u>
Loss before undernoted item and income taxes	(4,207,039)	(3,636,700)
Other income (Note 5)	<u>-</u>	<u>300,109</u>
Loss before income taxes	(4,207,039)	(3,336,591)
Income taxes (recovery) (Note 20)	<u>(21,000)</u>	<u>(65,346)</u>
Net loss and comprehensive loss	<u>\$ (4,186,039)</u>	<u>\$ (3,271,245)</u>
Basic loss income per share (Note 17(a))	<u>\$ (0.02)</u>	<u>\$ (0.02)</u>

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

DIAMOND ESTATES WINES & SPIRITS INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
PERIOD FROM APRIL 1, 2018 TO MARCH 31, 2020

	Note	Common shares Shares	Amount	Contributed surplus	Accumulated deficit	Total
As at April 1, 2018		140,373,841	\$ 16,657,513	\$ 589,982	\$ (992,895)	\$ 16,254,600
Net loss and comprehensive loss		-	-	-	(3,271,245)	(3,271,245)
Share based compensation	18(d)	-	-	549,399	-	549,399
Common shares issued on acquisition of Backyards Vineyards Corp.	5 and 17(b)	4,687,500	1,500,000	-	-	1,500,000
Exercise of options	18(a)	3,250,000	965,670	(358,170)	-	607,500
Settlement of DSUs	19	200,405	34,130	(34,130)	-	-
As at March 31, 2019		148,511,746	19,157,313	747,081	(4,264,140)	15,640,254
Net loss and comprehensive loss		-	-	-	(4,186,039)	(4,186,039)
Share based compensation	18(d)	-	-	528,338	-	528,338
Proceeds on issuance of common shares	17(b)	49,133,805	9,335,423	-	-	9,335,423
Share issuance costs	17(b)	-	(1,112,234)	-	-	(1,112,234)
Exercise of options	18(a)	2,000,000	240,000	-	-	240,000
Settlement of DSUs	19	360,015	70,203	(70,203)	-	-
As at March 31, 2020		200,005,566	\$ 27,690,705	\$ 1,205,216	\$ (8,450,179)	\$ 20,445,742

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

DIAMOND ESTATES WINES & SPIRITS INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED MARCH 31, 2020 AND 2019

	<u>2020</u>	<u>2019</u>
Operating activities		
Net loss	\$ (4,186,039)	\$ (3,271,245)
Add (deduct) items not affecting cash		
Depreciation of property, plant and equipment and right-of-use assets	1,346,058	1,069,026
Amortization of intangible assets	344,277	340,530
Amortization of deferred finance fees	43,329	93,706
(Gain) loss on disposal of right-of-use assets	(10,897)	-
Gain on acquisition (Note 5)	-	(300,109)
Share based compensation	528,338	549,399
Recovery of deferred income taxes	(21,000)	(65,346)
Interest expense	1,113,986	1,164,394
Interest paid	<u>(1,113,986)</u>	<u>(1,085,223)</u>
	(1,955,934)	(1,504,868)
Change in non-cash working capital items		
Accounts receivable	(478,899)	(75,309)
Inventories	(2,690,865)	(1,040,798)
Prepaid expenses	(33,554)	343,992
Accounts payable and accrued liabilities	817,359	61,033
Unearned revenue and deposits received	-	60,810
	<u>(4,341,893)</u>	<u>(2,155,140)</u>
Investing activities		
Acquisition of Backyard Vineyards Corp., net of cash acquired (Note 5)	-	(609,386)
Purchase of property, plant and equipment	(280,131)	(951,790)
Purchase of intangible assets	(8,270)	(14,519)
Proceeds from sale lease back of property, plant and equipment (Note 11)	-	838,342
Repayment of note payable	<u>(550,000)</u>	<u>-</u>
	(838,401)	(737,353)
Financing activities		
Net repayments on revolving term loans and operating lines payable	(2,371,051)	3,045,953
Repayment on non-revolving term loans payable	(500,000)	(500,000)
Repayment of lease liabilities	(411,844)	(260,960)
Proceeds from issuance of common shares, net of share issuance costs	9,335,423	-
Share issue costs	(1,112,234)	-
Proceeds on exercise of options	240,000	607,500
	<u>5,180,294</u>	<u>2,892,493</u>
Change in cash	-	-
Cash, beginning of year	-	-
Cash, end of year	<u>\$ -</u>	<u>\$ -</u>

Non-cash transactions (Note 24)

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

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

1. **NATURE OF OPERATIONS**

- (a) Diamond Estates Wines & Spirits Inc. ("Diamond" or the "Company") is a public company listed on the TSX-V whose shares trade under the symbol "DWS.V". Its principal business activities include the production, marketing and sale of wine, and through its agency division, operating as Trajectory Beverage Partners ("TBP"), distribution and marketing activities for various beverage alcohol brands that it represents in Canada. The address of the Company's registered office and principal place of business is 1067 Niagara Stone Road, Niagara-On-The-Lake, Ontario, L0S 1J0. The operations and principal place of business of TBP are located at 100-435 North Service Road West, Oakville, Ontario, L6M 4X8.

(b) **COVID-19 pandemic:**

In March 2020, the World Health Organization characterized the outbreak of the novel strain of coronavirus, specifically identified as COVID-19, as a global pandemic. This has resulted in the governments enacting emergency measures to combat the spread of the virus. These measures, which include the implementation of travel bans, self-imposed quarantine periods and social distancing, have caused material disruption to business, resulting in a global economic slowdown. Equity markets have experienced significant volatility and weakness and the governments and central banks have reacted with significant monetary and fiscal interventions designed to stabilize economic conditions.

The current challenging economic climate may negatively impact our customers and their demand for our products, our supply chains, lease agreements, banking agreements and related covenants (*see note 15*), which in turn may lead to adverse changes in cash flows, working capital levels and/or debt balances, which may also have a direct impact on the Company's operating results and financial position in the future. The situation is dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Company is not known at this time. The extent of such impact will depend on future developments, which are highly uncertain, including new information which may emerge concerning the spread and severity of COVID-19 and actions taken to address its impact, among others. The repercussions of this health crisis could have a material adverse effect on the Company's business, financial condition, liquidity and operating results.

The Company has been deemed an "essential service" by the Ontario government and therefore, is permitted to continue full operations. In response to COVID-19, the Company has implemented working practices to address potential impacts to its operations, employees and customers, including the closure of its retail locations, and will take further measures in the future if and as required. At present, the Company has not identified any material continuity-risks specifically associated with COVID-19.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation and statement of compliance

These consolidated financial statements have been prepared in compliance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). They were authorized for issuance by the Board of Directors on July 27, 2020.

The currency of presentation for these consolidated financial statements is the Canadian dollar, which is also the functional currency of the Company.

(b) Basis of consolidation

These consolidated financial statements include the accounts of the Company and its subsidiaries:

◆	Diamond Estates Wines & Spirits Ltd.	100%
◆	De Sousa Wines Toronto Inc.	100%
◆	Backyard Vineyards Corp. (<i>see note 5</i>)	100%

A subsidiary is an entity controlled by the Company. Control exists when the Company has power over an investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to use its power over the investee to affect its returns. The financial statements of a subsidiary are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries are changed when necessary to align them with the policies applied by the Company in these consolidated financial statements. All intercompany balances, income and expenses, and unrealized gains and losses resulting from intercompany transactions are eliminated in full.

Effective January 1, 2019, the operations of the agency business segment, previously operating in the Kirkwood Diamond Canada partnership, were transferred to TBP, a division of Diamond Estates Wines & Spirits Ltd.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. **SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

(c) **Financial instruments**

The Company's financial assets consist entirely of accounts receivable. The Company's financial liabilities consist of accounts payable and accrued liabilities, unearned revenue and deposits received, note payable, term loans payable and lease liabilities.

(i) **Measurement of financial instruments**

Effective April 1, 2018, the Company adopted IFRS 9: "Financial Instruments – Classification and Measurement of Financial Assets and Financial Liabilities" using the modified retrospective method. Under IFRS 9, financial assets and liabilities are initially recorded at fair value, including any directly attributable transaction costs, where permitted by the standard. For financial assets that are not subsequently held at fair value, the Company assesses whether there is evidence of impairment at each balance sheet date.

Financial instruments are classified into one of the following categories:

- ◆ Assets and liabilities at amortized cost
- ◆ Fair value through profit or loss ("FVTPL")
- ◆ Fair value through other comprehensive income ("FVOCI")

Subsequent measurement of financial instruments is based on their initial classification. Financial instruments classified as assets and liabilities at amortized cost

Transaction costs related to financial assets and liabilities at FVTPL are recognized in profit and loss. When incurred, transaction costs are deducted against the fair value of the all other financial instruments on initial recognition.

The fair values of accounts receivable, accounts payable and accrued liabilities, unearned revenue and deposits received and note payable approximate their fair values due to the short-term or demand nature of these instruments. The fair values of the term loans and lease liabilities approximate their carrying values as the contracted lending rates approximate the rates currently available for similar borrowing arrangements.

(ii) **Impairment of financial assets**

Financial assets are assessed for indicators of impairment at the end of each reporting period.

An expected credit loss model for financial assets is used under IFRS 9 in order to record allowances for loss. Under the model, expected credit losses are provided for on a forward-looking basis and are based on past history, current market conditions and estimates requiring management judgment. Applying the expected credit loss model on adoption of IFRS 9 did not have a significant impact on the Company's consolidated financial statements.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

(c) Financial instruments, continued

(iii) Hedge accounting

The Company has chosen not to apply hedge accounting to any of its derivative financial instruments. As a result of this policy choice, these derivative instruments are recorded initially and subsequently at fair value and the change in fair value is recorded directly in the consolidated statements of net loss and comprehensive loss. There were no such derivative instruments outstanding at March 31, 2020 and 2019.

(d) Inventory

Inventory that is purchased by the Company, including raw materials and wine, is valued at the lower of cost and net realizable value, with cost being determined on an average basis. Grapes produced from vineyards controlled by the Company that are part of inventory are measured at their fair value less costs to sell at the point of harvest. Inventory that is purchased by TBP is valued at the lower of cost and net realizable value, with cost being determined on a first-in, first-out basis.

Inventory of wine that is produced by the Company is valued at the lower of cost and net realizable value, with cost being determined on an average cost basis.

Inventories include all costs to purchase, convert and bring the inventories to their present location and condition. Such costs include purchase price net of discounts and rebates, applicable duties and taxes, transport and handling costs.

The Company tracks other inventory costs, such as direct labour, fixed and variable production overhead, including depreciation of production equipment, maintenance of production buildings and equipment and production management. These costs are allocated to inventory on a per litre basis.

(e) Property, plant and equipment

Depreciation is computed using the following annual rates and methods, which reflect the estimated useful life of the assets as follows:

◆	Buildings	40 years straight-line
◆	Vines	20 years straight-line
◆	Machinery and equipment	5 to 40 years straight-line
◆	Leasehold improvements	Straight-line over term of lease
◆	Vehicles	3 to 5 years straight-line
◆	Computer equipment	5 years straight-line

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. **SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

(f) **Biological assets**

The Company measures biological assets, consisting of grapes grown on vineyards controlled by the Company, at cost, which approximates fair value as there has been minimal biological transformation since the initial cost incurrence. The initial costs incurred are comprised of direct expenditures required to enable the biological transformation of agricultural produce.

At the point of harvest, the fair value of biological assets is determined by reference to local market prices for grapes of a similar quality and the same varietal. At this point, agricultural produce is measured at fair value less cost to sell, which becomes the basis for the cost of inventories after harvest.

Gains or losses arising from a change in fair value less costs to sell are included in the consolidated statements of income and comprehensive income in the period in which they arise.

(g) **Intangible assets**

Intangible assets acquired separately are initially recorded at fair market value and subsequently at cost less accumulated amortization and impairment losses. Subsequent expenditures on development and maintenance of computer software are expensed as incurred.

Intangible assets with finite lives are amortized straight line over their useful economic lives as follows:

◆	Distribution rights	-	11	years
◆	Customer lists	-	6	years
◆	Trademarks	-	5	years
◆	Computer software	-	1 - 5	years
◆	Website	-	5	years

Gains and losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in profit and loss when the asset is derecognized.

Indefinite lived intangible assets are not subject to amortization and are assessed annually for impairment using the method described in note 2. The pre-1993 winery licenses and BYV brand name have an indefinite life because the expected usage, period of control and other factors do not limit their life.

For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are largely independent cash flows (cash-generating units, or "CGUs").

All individual assets or CGUs are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable, with the exception of indefinite lived intangibles which are tested for impairment annually in accordance with IAS 36.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

An impairment loss is recognized for the amount by which the asset's or CGU's carrying amount exceeds its recoverable amount, which is the higher of fair value less costs to sell and value-in-use. To determine the value-in-use, management estimates expected future cash flows from each CGU and determines a suitable discount rate in order to calculate the present value of those cash flows. The data used for impairment testing procedures are directly linked to the Company's latest approved budget, adjusted as necessary to exclude the effects of future reorganizations and asset enhancements. Discount factors are determined individually for each cash-generating unit and reflect their respective risk profiles as assessed by management.

Impairment losses for CGUs reduce the carrying amount of the assets in that CGU. All assets are subsequently reassessed for indications that an impairment loss previously recognized may no longer exist. An impairment charge is reversed if the CGU's recoverable amount exceeds its carrying amount. Any reversal cannot result in the carrying amount exceeding the original value less the depreciation or amortization that would have been recognized.

Management has determined, using the above-noted valuation methods, that there is no impairment of intangible assets at March 31, 2020 and 2019.

(h) Unearned revenue and deposits received

Payments received from customers in advance of shipments are initially recorded in unearned revenue and deposits received. Revenue is recognized on actual shipment to the customer.

(i) Income taxes

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Tax on income is accrued using the tax rate that would be applicable to expected total annual earnings.

Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that the taxable profits will be available against which those deductible temporary differences can be utilized.

Such deferred tax assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither taxable profit nor accounting profit.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

(i) Income taxes, continued

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries and associates and interests in joint ventures, except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that the sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset tax assets against tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its tax assets and liabilities on a net basis.

(j) Provisions and contingencies

Provisions are recognized when a legal or constructive obligation exists as a result of past events and it is probable that an outflow of resources that can be reliably estimated will be required to settle the obligation. Where the effect is material, the provision is discounted using an appropriate current market-based pre-tax discount rate. The increase in the provision due to passage of time is recognized as interest expense.

When a contingency substantiated by confirming events can be reliably measured and is likely to result in an economic outflow, a liability is recognized at the best estimate required to settle the obligation. A contingent liability is disclosed where the existence of an obligation will only be confirmed by future events, or where the amount of a present obligation cannot be measured reliably or it is not probable to result in an economic outflow. Contingent assets are only disclosed when the inflow of economic benefits is probable. When the economic benefit becomes virtually certain, the asset is no longer contingent and is recognized in the consolidated financial statements.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

(k) Loss per share

Basic loss per share amounts are calculated by dividing consolidated net loss for the reporting period attributable to common shareholders by the weighted average number of common shares outstanding during the period.

Diluted loss per share amounts are calculated by dividing the consolidated net loss attributable to common shareholders by the weighted average number of shares outstanding during the year plus the weighted average number of shares that would be issued on the conversion of all the dilutive potential ordinary shares into common shares. Diluted income per share amounts are not presented if their inclusion would be anti-dilutive.

(l) Share based compensation

The Company offers a share option plan for its directors, officers and employees. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. The fair value of each tranche is measured using the Black-Scholes option pricing model. Share based payments expense is recognized upon vesting over the tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. Any consideration paid on exercise of share options is credited to share capital.

For equity settled transactions, the Company measures goods or services received at their fair value, unless that fair value cannot be estimated reliably, in which case the Company measures their value by reference to the fair value of the equity instruments granted.

(m) Deferred share units (DSUs)

The Company grants DSUs to directors as part of their compensation. The DSUs vest immediately upon grant and are only settled in shares. The fair value of each DSU is measured at the date of the grant using the Black-Scholes option pricing model. The resulting compensation expense is charged to income as share based compensation with a corresponding increase to contributed surplus.

(n) Foreign currency translation

In preparing the consolidated financial statements of the Company, transactions in currencies other than the Company's functional currency are recorded at the rates of exchange prevailing at the dates of the transactions. These consolidated financial statements are presented in Canadian dollars, which is also the functional currency of the Company. At the end of each reporting period, monetary assets and liabilities are translated using the foreign exchange rate at that date. Non-monetary assets and liabilities are translated using the historical rate on the date of the transaction. All gains and losses on translation of these foreign currency transactions are included in profit or loss.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. SIGNIFICANT ACCOUNTING POLICIES, CONTINUED

(o) Revenue recognition

The Company recognizes revenue from the sale of goods at a point in time when the performance obligation is fulfilled.

For transactions with provincial liquor boards and licensee retail stores, the Company's terms are "FOB shipping point". Accordingly, sales are recorded when the product is shipped from the Company's distribution facility. Sales to consumers through retail stores and estate wineries are recorded at the time the product is purchased.

Revenue from brand management is presented net of the related costs as the Company is acting as an agent in these transactions. Revenue is recognized when the related performance obligation is complete, there is certainty about receipt of the consideration and all related costs have been incurred. Commission income is recognized when products are sold and related performance obligations are fulfilled.

The following are deducted from gross revenue to arrive at reported revenue: (i) excise taxes collected on behalf of the federal government, (ii) licensing fees and levies paid on wine sold through the Company's independent Ontario retail stores, (iii) incentive and discount programs and shelving payments provided to customers, (iv) product returns and (v) breakage.

Revenue for custom processing, bulk wine storage and bottling is recognized over a period of time reflecting the Company's efforts to fulfil the related performance obligations.

(p) Uses of estimates and judgements

The preparation of these consolidated financial statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, include, but are not limited to, the following:

(i) COVID-19 estimation uncertainty

The COVID-19 pandemic has had a material impact on the global economy, the scale and duration of which remains uncertain. To date, there has been significant volatility in foreign exchange rates, restrictions on the conduct of businesses, including travel restrictions and supply chain disruptions. Depending on the duration and extent of the impact of COVID-19, this could materially impact the Company's results of operations, cash flows, and financial position and could result in changes to estimates used. Changes related to these could be material.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. **SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

(p) **Uses of estimates and judgements, continued**

(ii) **Fair value of grapes at the point of harvest**

Where possible, the fair value of grapes at the point of harvest is determined by reference to local market prices for grapes of a similar quality and the same varietal. For grapes for which local market prices are not readily available, the average price of similar grapes is used. The fair value of grapes is included in the cost of bulk wine inventory.

(iii) **Property, plant and equipment and right-of-use assets**

Property, plant and equipment and right-of-use assets represent a significant proportion of the asset base of the Company as they amount to 42.8% (2019 - 43.7%) of total assets. Therefore, estimates and assumptions made to determine their carrying value and related depreciation are critical to the Company's financial position and performance.

IFRS requires management to test for impairment of property, plant and equipment and right-of-use assets if events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment testing is an area involving management judgement, requiring assessment as to whether the carrying value of assets can be supported by the net present value of future cash flows derived from such assets using cash flow projections which have been discounted at an appropriate rate.

The charge in respect of periodic depreciation is derived after determining an estimate of an asset's expected useful life and the expected residual value at the end of its life. The useful lives and residual values of the Company's assets are determined by management at the time the asset is acquired and reviewed annually for appropriateness. The lives are based on historical experience with similar assets as well as anticipation of future events which may impact their life.

(iv) **Gross versus net presentation**

When deciding the most appropriate basis for presenting revenue or costs of revenue, both the legal form and substance of the agreement between the Company and its business partners are reviewed to determine each party's respective role in the transaction. Where the Company's role in a transaction is that of principal, revenue is recognized on a gross basis. This requires revenue to comprise the gross value of the transaction billed to the customer, after trade discounts, with any related expenditure charged as an operating cost. Where the Company's role in a transaction is that of an agent, revenue is recognized on a net basis with revenue representing the margin earned.

(v) **Useful life of intangible assets**

Significant judgement is involved in the determination of useful life for the computation of amortization of intangible assets. No assurance can be given that actual useful lives will not differ significantly from current assumptions.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. **SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

(p) **Uses of estimates and judgements, continued**

(vi) **Impairment of intangible assets**

Testing intangible assets for impairment involves estimating the recoverable amount of the CGUs to which intangible assets are allocated. This requires making assumptions about future cash flows, growth rates, market conditions and discount rates, which are inherently uncertain. Actual amounts may vary from these assumptions and cause significant adjustments.

(q) **Business combinations**

Business combinations are accounted for using the acquisition method, whereby acquired assets and liabilities are recorded at fair value as of the date of acquisition with the excess of the purchase consideration over such fair value being recorded as goodwill.

If the fair value of the net assets acquired exceeds the purchase consideration, the difference is recognized immediately as a gain on acquisition in the consolidated statement of net income and comprehensive income.

Acquisition costs are expensed during the period in which they are incurred and are included in general and administrative expenses.

The Company measures the identifiable assets acquired and liabilities assumed at their fair values on the date of acquisition. This requires estimates and judgments to be made, which are inherently subjective. As such, the amounts assigned to individual identifiable assets and liabilities, including the fair value of inventories, long-lived assets, the recognition and measurement of any unrecorded intangible assets and the determination of goodwill or the gain on acquisition are impacted. Due to the nature of these estimates, the purchase price allocation impacts the Company's reported assets and liabilities and future net earnings due to the impact on future cost of goods sold, amortization and impairment tests. In some circumstances, at the acquisition date, provisional values are used in accounting for a business combination, they may be adjusted retrospectively in subsequent periods pending confirmation or completion of the valuation of the acquired business. However, the measurement period will not exceed one year from the acquisition date.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

2. **SIGNIFICANT ACCOUNTING POLICIES, CONTINUED**

(r) **Leases**

The Company recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Company by the end of the lease term or the cost of the right-of-use asset reflects that the Company will exercise a purchase option. In that case, the right-of-use asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property, plant and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate. Generally, the Company uses its incremental borrowing rate as the discount rate.

The Company determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease and type of the asset leased.

Lease payments included in the measurement of the lease liability are comprised of (i) fixed payments, and (ii) the exercise price under a purchase option that the Company is reasonably certain to exercise, lease payment in an optional renewal period if the Company is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in rate, if there is a change in the Company's estimate of the amount expected to be payable under a residual value guarantee, or if the Company changes its assessment of whether it will exercise a purchase, extension or termination option.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

Leases with a term less than twelve months or of a low value are expensed as incurred.

DIAMOND ESTATES WINES & SPIRITS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2020 AND 2019

3. RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

(c) IFRS 16 "Leases"

In January 2016, the IASB issued IFRS 16 Leases ("IFRS 16"), which supersedes IAS 17 Leases, as well as several interpretations of leases. IFRS 16 eliminates the classification of leases by a lessee between operating and finance leases and introduces a single, on-balance sheet accounting model for lessees. As a result, the Company has recognized right-of-use ("ROU") assets representing its rights to use the underlying assets and lease liabilities representing its obligation to make lease payments. The details of the accounting policy adopted are disclosed in note 2(r).

Transition

The Company adopted IFRS 16 in its financial statements for the period beginning April 1, 2019, using the modified retrospective approach under which the cumulative effect of initial application is recognized in retained earnings at April 1, 2019. Accordingly, the prior period financial information has not been restated – i.e. it is presented, as previously reported, under IAS 17 and related interpretations. The disclosure requirements in IFRS 16 have not been applied to comparative information.

The Company used the following practical expedients as permitted under the new IFRS 16 standard:

- i) Leases with a remaining lease term of fewer than twelve months on April 1, 2019 are classified as short-term leases.
- ii) Leases of low dollar value continue to be expensed as incurred.
- iii) Initial direct costs from the measurement of the right-of-use asset at the date of initial application have been excluded.
- iv) Hindsight has been used when determining the lease term.

As a result of initially applying IFRS 16, in relation to the leases that were previously classified as operating leases, the Company recognized lease liabilities of \$2,385,244 as at April 1, 2019, which were measured at the present value of the remaining lease payments, discounted using the Company's incremental borrowing rate of 5.2%. The associated ROU assets (*see note 10*) were measured at the lease liability amount on April 1, 2019 resulting in no adjustment to the opening balance of retained earnings. The ROU assets and lease liabilities recognized as of April 1, 2019, which were previously classified as operating leases, relate to the Company's lease of its production and retail facility in Langley, BC and corporate offices in Oakville, Ontario.

The difference between the undiscounted operating lease commitments of the Company as of March 31, 2019 and the discounted lease obligation of the Company as of April 1, 2019 is as follows:

Operating lease commitments disclosed as at March 31, 2019	\$ 3,504,308
Less: Short-term leases	<u>(29,748)</u>
Undiscounted lease liabilities	3,474,560
Discount using the Company's incremental borrowing rate	<u>(1,089,316)</u>
Lease liabilities recognized as at April 1, 2019	<u>\$ 2,385,244</u>

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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3. **RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS, CONTINUED**

In relation to those leases under IFRS 16, the Company has recognized \$3,166,836 of ROU assets, net of accumulated depreciation, and \$3,123,405 of lease liabilities as at March 31, 2020. During the year ended March 31, 2020, the Company has recognized \$446,497 of depreciation expense and \$160,395 of interest expense from these leases, instead of operating lease expense.

(d) **IFRIC 23 "Uncertainty over Income Tax Treatments"**

On June 7, 2017, the IASB issued IFRIC Interpretation 23 Uncertainty over Income Tax Treatments (the "Interpretation"). The Interpretation provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments.

The Interpretation requires:

- an entity to contemplate whether uncertain tax treatments should be considered separately, or together as a group, based on which approach provides better predictions of the resolution;
- an entity to determine if it is probable that the tax authorities will accept the uncertain tax treatment; and
- if it is not probable that the uncertain tax treatment will be accepted, measure the tax uncertainty based on the most likely amount or expected value, depending on whichever method better predicts the resolution of the uncertainty.

The Company adopted the Interpretation in its financial statements for the period beginning on April 1, 2019. The adoption of the Interpretation did not have a material impact on the Company's financial statements.

- (e) **IFRS 9 "Financial Instruments"** has been amended to enable companies to measure at amortized cost some prepayable financial assets with negative compensation. The amendment to IFRS 9 also clarifies how to account for the modification of a financial liability. Most modifications of financial liabilities will result in immediate recognition of a gain or loss. The amendment is effective for annual periods beginning on or after January 1, 2019. The adoption of these amendments did not have a material impact on the consolidated financial statements.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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4. FUTURE ACCOUNTING PRONOUNCEMENTS

As at the date of authorization of these consolidated financial statements, the IASB has issued the following new or revised standards as detailed below. The Company has yet assessed the impact of these standards on the consolidated financial statements. Early adoption is permitted for each standard.

(a) IAS 1 "Presentation of Financial Statements, and IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors"

These standards have been amended to use a consistent definition of materiality throughout all accounting standards, clarify the explanation of the definition of material and incorporate some of the guidance in IAS 1 about immaterial information. The amendments are effective for annual periods beginning on or after January 1, 2020.

(b) IFRS 3 "Business Combinations"

This standard has been amended to improve the definition of a business. The amendments will help companies determine whether an acquisition made is of a business or a group of assets. To be considered a business, an acquisition would have to include an input and a substantive process that together significantly contribute to the ability to create outputs. The amendments are effective for annual periods beginning on or after January 1, 2020.

(c) IAS 1 "Presentation of Financial Statements", and IAS 8, "Accounting Policies, Changes in Accounting Estimates and Errors"

This standard has been amended to clarify the classification of liabilities as current or non-current. The amendments are effective for annual periods beginning on or after January 1, 2022.

5. ACQUISITION OF BACKYARD VINEYARDS CORP.

On June 28, 2018, the Company acquired 100% of the common shares of Backyard Vineyards Corp. ("BYV") for total consideration of \$2,800,000, of which \$750,000 was funded in cash, \$1,500,000 was funded by the issuance of 4,687,500 common shares and \$550,000 was funded by the assumption of a note payable (*see note 14*). The results of operations from June 29, 2018 onward have been included in the consolidated financial statements and this acquisition has been accounted for as a business combination.

The following table summarizes the amounts paid or payable at the purchase date and the allocation of the purchase price to the identifiable assets acquired and liabilities assumed based on management's estimate of the fair values at the date of acquisition.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED MARCH 31, 2020 AND 2019

5. **ACQUISITION OF BACKYARD VINEYARDS CORP., CONTINUED**

	<u>Backyard Vineyards Corp.</u>
Assets acquired:	
Cash	\$ 140,614
Accounts receivable	35,269
Inventories	1,325,959
Prepays and deposits	<u>36,750</u>
	1,538,592
Property, plant and equipment	1,470,000
Intangible assets - customer list	70,000
Intangible assets - brand name	<u>219,000</u>
	<u>3,297,592</u>
Liabilities assumed:	
Accounts payable and accrued liabilities	132,137
Deferred income taxes	<u>65,346</u>
	<u>197,483</u>
Net assets acquired	3,100,109
Total purchase consideration	<u>2,800,000</u>
Gain on acquisition	<u>\$ 300,109</u>

The gain on acquisition of BYV resulted from the recognition of tax losses which arose as a result of the write down of the tax basis in goodwill to its fair market value on the acquisition of control that can be used to offset future taxable income of BYV. This gain has been recorded as other income in the consolidated statement of net loss and comprehensive loss.

6. **ACCOUNTS RECEIVABLE**

	<u>2020</u>	<u>2019</u>
Trade receivables	\$ 2,761,979	\$ 2,488,688
Accrued receivables	623,074	417,466
Income taxes recoverable	<u>21,000</u>	-
	<u>\$ 3,406,053</u>	<u>\$ 2,906,154</u>

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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7. **INVENTORIES**

	<u>2020</u>	<u>2019</u>
Bulk wine	\$ 14,980,806	\$ 12,753,901
Bottled wine and spirits	6,548,457	6,208,841
Bottling supplies and packaging	569,893	499,945
	<u>\$ 22,099,156</u>	<u>\$ 19,462,687</u>

The Company had a \$80,697 provision for inventory obsolescence included in the consolidated statements of net loss and comprehensive loss for the year ended March 31, 2020 (2019 - \$227,138).

8. **BIOLOGICAL ASSETS**

Biological assets consist of grapes prior to harvest that are controlled by the Company. The Company owns land in Ontario to grow grapes in order to secure a supply of quality grapes for the making of wine. As at March 31, 2020, the Company held grape vines planted on 18.2 acres (2019 - 38 acres), 5.5 of which were on held through the operating lease of the BYV winery property. During the year ended March 31, 2020, the Company harvested 22.4 tons of grapes (2019 - 152 tons) valued at \$59,776 (2019 - \$172,900).

The changes in the carrying amount of biological assets are as follows:

	<u>2020</u>	<u>2019</u>
Carrying value, beginning of year	\$ -	\$ -
Net increase in fair value less costs to sell due to biological transformation	59,776	172,900
Transferred to inventory on harvest	<u>(59,776)</u>	<u>(172,900)</u>
Carrying value, end of year	<u>\$ -</u>	<u>\$ -</u>

The Company is exposed to financial risk because of the long period of time between the cash outflow required to plant grape vines, cultivate vineyards, and harvest grapes and the cash inflow from selling wine and related products from the harvested grapes. Substantially all of the grapes from owned and leased vineyards are used in the Company's winemaking processes. Owned and leased vineyards, in combination with supply contracts with grape growers, are used to secure a supply of domestic grapes. These strategies reduce the financial risks associated with changes in the grape prices.

DIAMOND ESTATES WINES & SPIRITS INC.
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9. **PROPERTY, PLANT AND EQUIPMENT**

	<u>Land</u>	<u>Buildings</u>	<u>Machinery, equipment and vines</u>	<u>Leasehold improvements</u>	<u>Equipment</u>	<u>Vehicles</u>	<u>Computer equipment</u>	<u>Total</u>
<u>Cost</u>								
As at April 1, 2018	\$ 1,135,432	\$ 16,233,630	\$ 10,492,835	\$ 62,700	\$ 102,512	\$ 29,790	\$ 418,819	\$ 28,475,718
Additions	3,795	23,307	817,008	-	-	-	107,720	951,830
Disposals	-	-	(838,342)	-	-	-	-	(838,342)
Acquired on purchase of BYV	-	-	1,461,946	-	-	-	8,054	1,470,000
As at March 31, 2019	1,139,227	16,256,937	11,933,447	62,700	102,512	29,790	534,593	30,059,206
Additions	3,650	65,207	198,538	-	-	-	12,736	280,131
As at March 31, 2020	<u>\$ 1,142,877</u>	<u>\$ 16,322,144</u>	<u>\$ 12,131,985</u>	<u>\$ 62,700</u>	<u>\$ 102,512</u>	<u>\$ 29,790</u>	<u>\$ 547,329</u>	<u>\$ 30,339,337</u>
<u>Accumulated depreciation</u>								
As at April 1, 2018	\$ -	\$ 3,882,848	\$ 5,972,564	\$ 43,391	\$ 100,092	\$ 29,790	\$ 348,773	\$ 10,377,458
Depreciation	-	381,265	493,223	1,740	870	-	31,194	908,292
As at March 31, 2019	-	4,264,113	6,465,787	45,131	100,962	29,790	379,967	11,285,750
Depreciation	-	377,776	416,658	7,569	1,550	-	41,612	845,165
As at March 31, 2020	<u>\$ -</u>	<u>\$ 4,641,889</u>	<u>\$ 6,882,445</u>	<u>\$ 52,700</u>	<u>\$ 102,512</u>	<u>\$ 29,790</u>	<u>\$ 421,579</u>	<u>\$ 12,130,915</u>
<u>Net book value</u>								
As at March 31, 2019	<u>\$ 1,139,227</u>	<u>\$ 11,992,824</u>	<u>\$ 5,467,660</u>	<u>\$ 17,569</u>	<u>\$ 1,550</u>	<u>\$ -</u>	<u>\$ 154,626</u>	<u>\$ 18,773,456</u>
As at March 31, 2020	<u>\$ 1,142,877</u>	<u>\$ 11,680,255</u>	<u>\$ 5,249,540</u>	<u>\$ 10,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 125,750</u>	<u>\$ 18,208,422</u>

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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10. **RIGHT OF USE ASSETS**

	<u>Building</u>	<u>Vehicles</u>	<u>Machinery and equipment</u>	<u>Total</u>
<u>Cost</u>				
As at April 1, 2018	\$ -	\$ 792,133	\$ -	\$ 792,133
Additions	-	54,369	838,342	892,711
As at March 31, 2019	-	846,502	838,342	1,684,844
Right-of-use assets on transition to IFRS 16 (see note 3(a))	2,385,244	-	-	2,385,244
Additions	-	54,486	-	54,486
Disposals	-	(56,963)	-	(56,963)
As at March 31, 2020	\$ 2,385,244	\$ 844,025	\$ 838,342	\$ 4,067,611
<u>Accumulated depreciation</u>				
As at April 1, 2018	\$ -	\$ 260,094	\$ -	\$ 260,094
Depreciation	-	210,867	8,733	219,600
As at March 31, 2019	-	470,961	8,733	479,694
Depreciation	213,082	212,457	20,958	446,497
Disposals	-	(25,416)	-	(25,416)
As at March 31, 2020	\$ 213,082	\$ 658,002	\$ 29,691	\$ 900,775
<u>Net book value</u>				
As at March 31, 2019	\$ -	\$ 375,541	\$ 829,609	\$ 1,205,150
As at March 31, 2020	\$ 2,172,162	\$ 186,023	\$ 808,651	\$ 3,166,836

11. **WINERY EQUIPMENT SALE AND LEASEBACK**

On November 26, 2018, the Company completed the sale and leaseback of certain winery equipment to the Bank of Montreal ("BMO"). The details of the sale and leaseback, both done at fair value were as follows:

- (a) The equipment was sold to BMO for cash proceeds of \$838,342 and resulted in the effective disposition of the winery equipment, previously classified as property, plant and equipment. The proceeds were equal to the net book value of the equipment sold and as such, no gain or loss on disposal was recognized.
- (b) The Company will lease the winery equipment from BMO for a period of seven years with the option to purchase the equipment at the end of the lease term for \$1. Blended principal and interest payments of \$11,777 are due monthly, with interest at 4.94%.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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12. **INTANGIBLE ASSETS**

	<u>Pre-1993 winery licenses</u>	<u>Distribution rights</u>	<u>Customer Lists</u>	<u>Brand Names</u>	<u>Trademarks</u>	<u>Computer software</u>	<u>Website</u>	<u>Total</u>
<u>Cost</u>								
As at April 1, 2018	\$ 750,000	\$ 8,819,763	\$ -	\$ -	\$ 52,358	\$ 197,198	\$ 15,335	\$ 9,834,654
Acquired on purchase of BYV	-	-	70,000	219,000	-	-	-	289,000
Additions	-	-	-	-	-	14,519	-	14,519
As at March 31, 2019	750,000	8,819,763	70,000	219,000	52,358	211,717	15,335	10,138,173
Additions	-	-	-	-	-	-	8,270	8,270
Disposal	-	-	-	-	-	(14,519)	-	(14,519)
As at March 31, 2020	<u>\$ 750,000</u>	<u>\$ 8,819,763</u>	<u>\$ 70,000</u>	<u>\$ 219,000</u>	<u>\$ 52,358</u>	<u>\$ 197,198</u>	<u>\$ 23,605</u>	<u>\$ 10,131,924</u>
<u>Accumulated amortization</u>								
As at April 1, 2018	\$ -	\$ 6,403,848	\$ -	\$ -	\$ 48,871	\$ 187,227	\$ 2,556	\$ 6,642,502
Amortization	-	316,120	10,500	-	872	9,971	3,067	340,530
As at March 31, 2019	-	6,719,968	10,500	-	49,743	197,198	5,623	6,983,032
Amortization	-	328,120	11,667	-	872	-	3,618	344,277
As at March 31, 2020	<u>\$ -</u>	<u>\$ 7,048,088</u>	<u>\$ 22,167</u>	<u>\$ -</u>	<u>\$ 50,615</u>	<u>\$ 197,198</u>	<u>\$ 9,241</u>	<u>\$ 7,327,309</u>
<u>Net book value</u>								
As at March 31, 2019	<u>\$ 750,000</u>	<u>\$ 2,099,795</u>	<u>\$ 59,500</u>	<u>\$ 219,000</u>	<u>\$ 2,615</u>	<u>\$ 14,519</u>	<u>\$ 9,712</u>	<u>\$ 3,155,141</u>
As at March 31, 2020	<u>\$ 750,000</u>	<u>\$ 1,771,675</u>	<u>\$ 47,833</u>	<u>\$ 219,000</u>	<u>\$ 1,743</u>	<u>\$ -</u>	<u>\$ 14,364</u>	<u>\$ 2,804,615</u>

DIAMOND ESTATES WINES & SPIRITS INC.
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12. INTANGIBLE ASSETS, CONTINUED

- (a) The pre-1993 winery licenses issued to Lakeview Cellars Estate Winery Limited and De Sousa Wines Toronto Inc. grant the licensees considerably more flexibility than post-1993 licenses with respect to blending practices, location of operations and other wine-making matters. These licenses are transferable at the discretion of the Alcohol and Gaming Commission of Ontario ("AGCO"). The Company determined the recoverable amount of the pre-1993 winery license by estimating their fair value less costs to sell.

The Company determined the recoverable amount of the pre-1993 winery licenses by estimating their fair value less costs of disposal in use.

- (b) Distribution rights represent exclusive rights to act as an agent and/or distributor in certain provinces for various beverage alcohol products. These agency relationships are for either a fixed, renewable or unlimited term, subject to termination clauses in the agreements. Under these clauses, and under common law, the Company would be entitled to compensation, typically equal to one month's commission earnings for each year of representation, in the event that a contract is terminated. The distribution rights acquired as part of the TBP (formerly Kirkwood Diamond Canada) acquisition were valued at fiscal 2014 gross margin, normalized for variable selling costs and client relationships retained. The Company estimated that these distribution rights had an original useful life of 17 years, and that the acquisition cost would be amortized on a straight-line basis over their estimated remaining life as of October 1, 2014, the commencement date of the partnership, of 11 years.

13. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	<u>2020</u>	<u>2019</u>
Trade accounts payable	\$ 6,332,819	\$ 4,903,840
Holdbacks payable	789,743	1,332,662
Government remittances payable	37,297	105,998
	<u>\$ 7,159,859</u>	<u>\$ 6,342,500</u>

14. NOTE PAYABLE

The note payable was due to Azura Management (Kelowna) Corp. ("AMKC"), bore interest at 5% and was due June 28, 2019. The Company agreed to an extension of the due date to July 31, 2019 at which date it was repaid in full.

DIAMOND ESTATES WINES & SPIRITS INC.
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15. **TERM LOANS PAYABLE**

As at March 31, 2020, the balances outstanding on the Company's term loans were as follows:

	<u>2020</u>	<u>2019</u>
BMO term loans:		
Revolving operating term loan	\$ 10,315,621	\$ 12,686,672
Non-revolving term loan	<u>8,875,000</u>	<u>9,375,000</u>
	19,190,621	22,061,672
Financing costs	<u>(29,209)</u>	<u>(72,538)</u>
	19,161,412	21,989,134
Current portion	<u>(19,161,412)</u>	<u>(452,187)</u>
	<u>\$ -</u>	<u>\$ 21,536,947</u>

The BMO credit agreement is dated September 29, 2017 and was amended pursuant to a first amending agreement dated July 29, 2019, a second amending agreement dated December 17, 2019 and a third amending agreement dated May 15, 2020, and a fourth amending agreement dated July 24, 2020. It is guaranteed by a general security agreement covering the assets of the Company and its subsidiaries and is subject to the following facilities detailed below.

The agreement in effect as of March 31, 2020 had a maturity date of September 26, 2020. As that maturity date falls within twelve months of the reporting date, all indebtedness has been classified as current. The classification is expected to go back to long-term based on the extension of the credit agreement to July 1, 2022 under the terms of the fourth amending agreement.

The revolving operating term loan is for working capital and general corporate requirements and is subject to the following terms:

- (a) Revolving credit facility of up to \$13,000,000, subject to specified borrowing base margin limitations
- (b) Monthly interest only payments at CAD prime rate +1.00%
- (c) Standby fee of 0.50% on available unused revolving term credit to be paid on the last day of each quarter

The non-revolving term loan is for the purpose of refinancing the previous term debt and funding scheduled fiscal 2020 capital expenditures. The loan is subject to the following terms:

- (a) Initial principal of \$10,000,000, amortized over a period of 20 years
- (b) Monthly interest only payments at CAD prime rate +1.25%
- (c) Quarterly principal payments of \$125,000

The BMO credit agreement includes the following sub-facilities:

- (a) Letter of credit sub-facility included under the umbrella of the \$13,000,000 revolving term loan, up to a maximum of \$1,000,000 at a rate of CAD prime +2.50% having a term of up to 1 year. As at March 31, 2020 there were letters of credit in the amount of \$74,641 outstanding with BMO (2019 - \$24,641).

DIAMOND ESTATES WINES & SPIRITS INC.
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15. **TERM LOANS PAYABLE, CONTINUED**

- (b) Bankers' acceptance ("BA") sub-facility included under the umbrella of the revolving and non-revolving term loans, with a minimum draw of \$1,000,000, terms of 28 to 182 days, fees charged at rates 2.50% to 2.75% per annum on the face amount of the BA plus interest at the BA rate. A swap is in place on the non-revolving term loan to fix the effective interest rate at 4.90% (BA rate of 1.96%) and effective until September 2020.
- (c) Treasury risk management facility of up to \$1,500,000 to facilitate hedging of interest rate risk and foreign exchange risk at market rates as determined by the lender. As at March 31, 2020 and March 31, 2019 there were no amounts outstanding on this facility.

The Company also has an available delayed draw term loan of \$2,500,000 to finance future capital expenditures at a rate of CAD prime +1.25%, repayable in quarterly principal instalments commencing at the end of the fiscal quarter in which the initial draw takes place. A standby fee in the amount of 0.55% to be payable quarterly is due on the undrawn portion of this loan. There was no balance drawn on this facility as at March 31, 2020 and March 31, 2019.

A master lease finance line facility of \$2,500,000 is available to the Company to finance equipment under the BMO Equipment Leasing Group and shall reduce monthly in accordance with agreed upon terms based on market rates at the time of each advance. As at March 31, 2020 there was a balance of \$714,969 drawn on this facility (2019 - \$792,860).

The BMO credit agreement is subject to the following major financial covenants:

- (a) Minimum fixed charge coverage ratio of 1.25 | 1
- (b) Maximum ratio of total liabilities to tangible net worth of 2.00 | 1
- (c) Annual capital expenditures are not to exceed \$1,500,000 in fiscal years subsequent to March 31, 2019 without prior bank approval.

On July 29, 2019, the terms of certain financial covenants with BMO were amended. The fixed charge coverage ratio was amended to include the net proceeds of the Lassonde brokered private placement (*see note 17(b)*) as equivalent to earnings before interest, depreciation and amortization for the 12 month period ending October 2020.

On December 17, 2019, the credit agreement was further amended to essentially increase the borrowing base by extending the definition of Eligible Insured Receivables (through additional export insurance).

On May 15, 2020, terms of the financial credit agreement were amended upon execution of a third amending agreement as follows:

- the definitions of certain EBITDA adjustments were refined.
- the maturity date was extended to September 30, 2021.
- capital expenditure limit was revised to \$1,000,000 for the fiscal years ending March 31, 2021 and 2022.
- the delayed draw term loan of \$2,500,000 was removed.

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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15. **TERM LOANS PAYABLE, CONTINUED**

The terms of the credit facility were further changed upon execution of a fourth amending agreement dated July 24, 2020, as follows:

- the maturity date was extended to July 1, 2022, meaning all indebtedness is expected to be classified as long-term until June 30, 2021.
- the definitions of certain EBITDA adjustments were refined for the quarters ending September 30, 2020 and December 31, 2020.
- the minimum fixed charge coverage ratio was amended to 1.20|1.00 and 1.05|1.00 respectively for the quarters ending September 30, 2020 and December 31, 2020.
- quarterly principal payments of \$125,000 were deferred for the quarters ending September 30, 2020 and December 31, 2020.
- no distributions to shareholders are allowed without prior lender consent.

As consideration for the lender entering into the fourth amending agreement, the Company has agreed to issue 750,000 warrants to the lender, with each such warrant being exercisable for one common share in the Company at an exercise price of \$0.16 per common share, vesting immediately and expiring as of July 1, 2022.

16. **LEASE LIABILITIES**

As a result of initially applying IFRS 16, the Company recognized lease liabilities of \$2,385,244 as at April 1, 2019 (*see note 3(a)*). During the year ended March 31, 2020, the Company has not entered into any new lease agreements with Element Inc, which secures Company's obligations under the terms of the lease. Movement in the lease liabilities consist of the following;

	<u>2020</u>	<u>2019</u>
Lease liabilities, beginning of year	\$ 1,152,482	\$ 520,731
Lease liabilities on transition to IFRS 16	2,385,244	-
Lease liabilities for assets acquired under lease	54,486	892,711
Lease liabilities for assets disposed of under lease	(56,963)	-
Interest payable on lease liabilities	160,395	32,444
Repayments during the year	<u>(572,239)</u>	<u>(293,404)</u>
Lease liabilities, end of year	3,123,405	1,152,482
Current portion	<u>382,730</u>	<u>308,406</u>
Long term portion	<u>\$ 2,740,675</u>	<u>\$ 844,076</u>

The following amounts were recognized in profit and loss during the year

Interest expense on lease liabilities	\$ 160,395
Depreciation on right-of-use assets	446,497
Expense related to short-term leases	81,156
Expenses related to leases of low-value assets	\$ -

DIAMOND ESTATES WINES & SPIRITS INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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17. **SHARE CAPITAL AND OTHER EQUITY INSTRUMENTS**

Continuity schedules for each component of the Company's share capital and other equity instruments are disclosed in the consolidated statements of changes in shareholders' equity for the period from April 1, 2018 to March 31, 2020. Details of major changes in each component during the current reporting period are as follows:

(a) **Loss per share**

Basic loss per share is computed using the weighted average number of common shares outstanding. The weighted average number of common shares outstanding for the year ended March 31, 2020 was 179,384,775 (2019 - 145,802,051).

As at March 31, 2020, the following potentially dilutive equity instruments were outstanding: (1) 8,050,000 options (2019 - 11,850,000), and (2) 1,815,037 deferred share units (2019 - 1,622,000). The fully diluted number of common shares outstanding for the year ended March 31, 2020 was 209,870,603 (2019 - 161,983,746).

(b) **Issuance of common shares**

On June 28, 2018, the Company issued 4,687,500 common shares valued at \$0.32 per share in settlement of \$1,500,000 of the purchase consideration paid to acquire Backyard Vineyards Corp. (see note 5).

On July 29, 2019, the Company completed a brokered private placement with Lassonde Industries Inc. ("Lassonde") to issue 36,900,000 common shares at \$0.19 per share for gross proceeds of \$7,011,000, less issuance costs of \$895,491 for cash proceeds of \$6,115,509.

On October 30, 2019, the Company closed a private placement of 12,233,805 common shares at \$0.19 per share for gross proceeds of \$2,324,423, less issuance costs of \$216,743, for cash proceeds of \$2,107,680.

(c) **Settlement of deferred share units**

On April 3, 2018, on the retirement of a member of the Board of Directors, 200,405 DSUs were settled in common shares of the Company.

DIAMOND ESTATES WINES & SPIRITS INC.
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18. **STOCK OPTIONS**

The Company has adopted a stock option plan under which it may grant options to acquire shares of the Company to directors, officers and consultants of the Company. The maximum number of common shares issuable pursuant to the plan is equal to 10% of the issued and outstanding common shares at the close of business on the date of any grant, with an additional restriction of 5% to any one individual in a twelve month period.

Stock option activity for the years ended March 31, 2020 and 2019 was as follows:

	<u>2020</u>		<u>2019</u>	
	<u>Options</u>	<u>Weighted -average exercise price (\$)</u>	<u>Options</u>	<u>Weighted- average exercise price (\$)</u>
Outstanding, beginning of year	11,850,000	0.25	7,175,000	0.19
Options exercised (<i>see note 18(b)</i>)	(2,000,000)	0.12	(3,250,000)	0.19
Expiry of options (<i>see note 18(c)</i>)	(2,950,000)	-	(175,000)	-
Granted to BOD and key management (<i>see note 18(a)</i>)	1,150,000	0.20	7,100,000	0.28
Granted to CFO (<i>see note 18(a)</i>)	-	-	1,000,000	0.20
Outstanding, end of year	<u>8,050,000</u>	<u>0.26</u>	<u>11,850,000</u>	<u>0.25</u>

As at March 31, 2020, the issued and outstanding options to acquire common shares of the Company are as follows:

<u>Grant date</u>	<u>Number of options</u>		<u>Exercise price (\$)</u>	<u>Remaining life</u>	<u>Expiry date</u>
	<u>Granted</u>	<u>Exercisable</u>			
January 15, 2018	500,000	250,000	0.29	2.79	January 14, 2023
February 27, 2018	500,000	250,000	0.27	2.91	February 26, 2023
October 1, 2018	4,900,000	1,225,000	0.28	3.50	September 30, 2023
January 23, 2019	1,000,000	250,000	0.20	3.89	January 22, 2024
August 12, 2019	250,000	-	0.19	4.37	August 11, 2024
September 28, 2019	<u>900,000</u>	<u>-</u>	0.20	4.49	September 27, 2024
	<u>8,050,000</u>	<u>1,975,000</u>	0.26	3.66	

(a) Issuance of options

- (i) On October 1, 2018, the Company issued stock options to its directors and key members of the management team. A total of 7,100,000 stock options were issued with an exercise price of \$0.28 per share with a term of five years, vesting evenly on each anniversary date over 4 years. The fair value of these options was calculated with the Black-Scholes option pricing model, using the assumptions of: (1) risk free interest rate of 2.02%, (2) expected volatility of 90.51%, (3) expected life of 5 years, and (4) dividend yield of 0.0%, the fair value attributed to each option was \$0.20.

DIAMOND ESTATES WINES & SPIRITS INC.
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18. STOCK OPTIONS, CONTINUED

- (ii) On January 23, 2019, the Company issued a total of 1,000,000 stock options to a key member of management with an exercise price of \$0.20 per share. The fair value of these options was calculated with the Black-Scholes option pricing model, using the assumptions of: (1) risk free interest rate of 1.93%, (2) expected volatility of 88.05%, (3) expected life of 5 years, and (4) dividend yield of 0.0%, the fair value attributed to each option was \$0.20.
- (iii) On August 12, 2019, the Company issued stock options to a key member of the management team. 250,000 stock options were issued with an exercise price of \$0.19 per share with a term of five years, vesting evenly on each anniversary date over 4 years. The fair value of these options was calculated with the Black-Scholes option pricing model, using the assumptions of: (1) risk free interest rate of 1.23%, (2) expected volatility of 86.73%, (3) expected life of 5 years, and (4) dividend yield of 0.0%, the fair value attributed to each option was \$0.19.
- (iv) On September 28, 2019, the Company issued stock options to its directors and key members of the management team. A total of 900,000 stock options were issued, of which 400,000 were to Lassonde, with an exercise price of \$0.20 per share with a term of five years, vesting evenly on each anniversary date over 4 years. The fair value of these options was calculated with the Black-Scholes option pricing model, using the assumptions of: (1) risk free interest rate of 1.23%, (2) expected volatility of 86.73%, (3) expected life of 5 years, and (4) dividend yield of 0.0%, the fair value attributed to each option was \$0.12.

(b) Exercise of options

- (i) On April 10, 2018, 150,000 of the stock options originally granted on November 24, 2014, were exercised at the purchase price of \$0.11 for total proceeds of \$16,500.
- (ii) On September 21, 2018, 500,000 of the stock options originally granted on September 24, 2013 were exercised at the purchase price of \$0.25 and 2,000,000 of the stock options originally granted on September 24, 2013 were exercised at the purchase price of \$0.20 per share for total proceeds of \$525,000.
- (iii) On November 1, 2018, 350,000 of the stock options originally granted on November 24, 2014 were exercised at the purchase price of \$0.11 per share for total proceeds of \$38,500.
- (iv) On November 24, 2018, 250,000 of the stock options originally granted on November 24, 2014 were exercised at the purchase price of \$0.11 per share for total proceeds of \$27,500.
- (v) On October 30, 2019, 2,000,000 of the stock options originally granted on November 10, 2014 were exercised at the purchase price of \$0.12 per share for total proceeds of \$240,000.

(c) Expiry of options

- (i) During the year ended March 31, 2019, a total of 175,000 options, initially granted on November 24, 2014 expired unexercised on the departure of two executives of the Company.
- (ii) During the first quarter of fiscal 2020, a total of 2,250,000 options, including 500,000 options initially granted on June 5, 2014, 250,000 options initially granted on January 15, 2018 and 1,500,000 options initially granted on October 1, 2018, expired unexercised on the departure of five executives of the Company.
- (iii) During the second quarter of fiscal 2020, a total of 250,000 options, initially granted on January 15, 2018, expired unexercised on the departure of an executive of the Company.
- (iv) During the third quarter of fiscal 2020, a total of 450,000 options, initially granted on October 1, 2018, expired unexercised on the departure of two executives of the Company.

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18. **STOCK OPTIONS, CONTINUED**

(d) Share based compensation

Total share based compensation recognized for the year ended March 31, 2020 was \$528,338 (2019 - \$549,399) based on accrual of previously granted options expected to vest in the reporting period and the issuance of DSUs as described in note 19.

19. **DEFERRED SHARE UNITS ("DSUs")**

On September 26, 2019, the Board of Directors approved an increase in the maximum number of common shares reserved for issuance under the Company's DSU plan (the "DSU Plan") from 2,000,000 to 3,000,000, which is approximately 1.5% of the then issued and outstanding common shares. The DSU Plan provides that the maximum number of DSUs issuable to insiders (as that term is defined by the Exchange) pursuant to the DSU Plan, together with any common shares issuable pursuant to any other security-based compensation arrangement of the Company, will not exceed 10% of the total number of outstanding common shares. The DSUs issued under this plan to non-executive directors are to be settled in common shares of the Company when the director retires from all positions with the Company.

(a) Issuance of DSUs:

On August 31, 2018, the Company issued an aggregate of 259,167 DSUs to non-executive directors under the DSU Plan in settlement of \$77,750 of deferred directors' compensation.

On May 27, 2019, the Company issued an aggregate of 256,618 DSUs to non-executive directors under the DSU Plan in settlement of \$43,625 of deferred directors' compensation.

On October 19, 2019, the Company issued an aggregate of 185,255 DSU's to non-executive directors under the DSU plan in settlement of \$36,125 of deferred directors' compensation.

On January 22, 2020, the Company issued an aggregate of 111,080 DSU's to non-executive directors under the DSU plan in settlement of \$24,436 of deferred directors' compensation

(b) Settlement of DSUs

To date, a total of 2,375,378 DSUs have been issued, of which 1,815,037 remain outstanding, after the following settlements of DSUs into common shares of the Company: (i) 200,405 DSUs on April 3, 2018 upon the retirement of a member of the Board of Directors, (ii) 332,451 on September 27, 2019 on the retirement of a member of the Board of Directors, and (iii) 27,564 DSUs on October 19, 2019 for the same member of the Board.

DIAMOND ESTATES WINES & SPIRITS INC.
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20. **INCOME TAXES**

(a) **Income rate reconciliation**

The reconciliation of the combined Canadian federal and provincial statutory income tax rates on the net income for the years ended March 31, 2020 and 2019 is as follows:

	<u>2020</u>	<u>2019</u>
Net loss before recovery of income taxes	\$ (4,207,039)	\$ (3,336,591)
Expected income tax recovery	<u>26.50%</u>	<u>26.50%</u>
Expected income tax recovery	\$ (1,114,865)	\$ (884,197)
Decrease (increase) resulting from:		
Co-op refundable credit	(21,000)	-
Non-deductible expenses	153,311	175,251
Change in tax benefits not recognized	844,331	724,501
Tax rate differential	(6,149)	(1,372)
Other	<u>123,372</u>	<u>(79,529)</u>
Recovery of income taxes	\$ <u>(21,000)</u>	\$ <u>(65,346)</u>

The recovery of income taxes was \$21,000 for the year ended March 31, 2020 (2019 - \$65,346).

(b) **Deferred tax**

The following table summarizes the components of deferred tax:

	<u>2020</u>	<u>2019</u>
Deferred tax asset		
Non-capital losses carried forward	\$ 1,842,787	\$ 2,238,807
Reserves	-	16,149
Deferred tax liabilities		
Property, plant and equipment	(1,734,214)	(1,882,156)
Intangible assets	(74,129)	(273,035)
Inventory	-	(65,779)
Deferred financing costs	(2,495)	(33,986)
ROU assets and capital leases	<u>(31,949)</u>	<u>-</u>
Net deferred tax liabilities	\$ <u>-</u>	\$ <u>-</u>

DIAMOND ESTATES WINES & SPIRITS INC.
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20. **INCOME TAXES, CONTINUED**

(c) **Unrecognized deferred tax assets**

Deferred taxes are provided as a result of temporary differences that arise due to the differences between the income tax values and the carrying amount of assets and liabilities. Deferred tax assets have not been recognized in respect of the following deductible temporary differences:

	<u>2020</u>	<u>2019</u>
	\$	\$
Non-capital losses carried forward	19,045,330	16,475,281
Capital losses carried forward	397,338	397,388
Share issuance and deferred financing costs	284,946	500,039
Reserves	205,087	216,405
Intangible assets	549,936	1,809,197
Property, plant and equipment	4,340	-
ROU assets and liability	77,459	-

The non-capital loss carry forwards expire as noted in the table below. The net capital loss carry forwards may be carried forward indefinitely, but can only be used to reduce capital gains. Share issue and financing costs will be fully amortized in 2023. The remaining deductible temporary differences may be carried forward indefinitely. Deferred tax assets have not been recognized in respect of these items because it is not probable that future taxable profit will be available against which the group can utilize the benefits therefrom.

2028	\$ 915,543
2029	632,792
2030	8,635,937
2031	3,750,634
2032	2,007,278
2033	475,778
2034	1,665,014
2035	1,387,850
2036	331,652
2037	217,839
2038	1,621,516
2039	2,288,057
2040	<u>2,074,149</u>
	<u>\$ 26,004,039</u>

DIAMOND ESTATES WINES & SPIRITS INC.
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21. **KEY MANAGEMENT COMPENSATION, RELATED PARTY TRANSACTIONS AND BALANCES**

During the years ended March 31, 2020 and 2019, the Company had the following related party transactions, including (i) compensation of key management personnel and directors, and (ii) transactions with entities related to or controlled by directors, as follows:

	<u>2020</u>	<u>2019</u>
Salary	\$ 1,136,901	\$ 1,151,480
Director fees	72,250	80,250
Share based compensation under stock option plan (<i>see note 18(d)</i>) and DSU Plan (<i>see note 19</i>)	528,338	549,399
Commissions	64,091	-
Winery lease payments	80,000	100,000
Grape purchases	115,143	110,089

Accounts payable and accrued liabilities as at March 31, 2020 includes \$100,852 (2019 - \$481,184) with respect to balances owing to related parties for the transactions disclosed above.

22. **SEGMENTED INFORMATION**

Business segments

The Company operates in two business segments, namely (i) distribution and sales of products represented in Canada under agency agreements with third parties, and (ii) sales of manufactured wines. The following table presents selected financial information associated with each of these segments for the years ended March 31, 2020 and 2019:

	<u>March 31, 2020</u>		
	Agency	Manufactured wines	Consolidated
	\$	\$	\$
Gross revenue	13,844,882	13,567,029	27,411,911
Inter-segment revenue	(617,681)	-	(617,681)
Net revenue	<u>13,227,201</u>	<u>13,567,029</u>	<u>26,794,230</u>
Gross profit	5,610,776	5,740,962	11,351,738
Interest on long-term debt	331,923	782,063	1,113,986
Depreciation and amortization	947,878	742,457	1,690,335
Additions of property, plant and equipment and intangible assets	-	288,401	288,401
	<u>Statement of financial position balances as at</u>		
	<u>March 31, 2020</u>		
Intangible assets	1,771,675	1,032,940	2,804,615
Total assets	7,105,728	42,845,500	49,951,228
Total liabilities	5,068,246	24,437,240	29,505,486

DIAMOND ESTATES WINES & SPIRITS INC.
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22. **SEGMENTED INFORMATION, CONTINUED**

	<u>March 31, 2019</u>		
	Agency	Manufactured	Consolidated
	\$	wines	\$
Gross revenue	13,629,912	14,982,026	28,611,938
Inter-segment revenue	(488,835)	-	(488,835)
Net revenue	<u>13,141,077</u>	<u>14,982,026</u>	<u>28,123,103</u>
Gross profit	5,819,900	5,694,054	11,513,954
Interest on bank indebtedness	106,321	1,058,073	1,164,394
Depreciation and amortization	473,979	935,577	1,409,556
Additions of property, plant and equipment and intangible assets	282,867	1,576,153	1,859,020
Fair value of property, plant and equipment acquired on purchase of BYV	-	1,470,000	1,470,000
	<u>Statement of financial position balances as at</u>		
	<u>March 31, 2019</u>		
Intangible assets	1,055,060	2,100,081	3,155,141
Total assets	6,927,879	38,807,301	45,735,180
Total liabilities	3,541,346	26,553,580	30,094,926

Transactions between segments are measured at the exchange amount, which approximates fair value. All of the Company's assets are located in Canada.

Geographic information

	<u>2020</u>	<u>2019</u>
Revenue		
Canada	\$ 25,144,719	\$ 23,068,640
China and other	<u>1,649,511</u>	<u>5,054,463</u>
	<u>\$ 26,794,230</u>	<u>\$ 28,123,103</u>

23. **FINANCIAL INSTRUMENTS AND RISK FACTORS**

(a) Risk management

The Company is exposed to interest rate risk, credit risk, foreign currency risk, liquidity risk and concentration risk associated with its financial assets and liabilities. Management has the overall responsibility for the establishment and approval of the Company's risk management policies. The Company's objectives are to manage the risks and risk exposure through a combination of sound business practices and the involvement of management in the daily operations.

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23. **FINANCIAL INSTRUMENTS AND RISK FACTORS, CONTINUED**

(b) Classification of financial instruments

The classification and measurement of the financial assets and liabilities, as well as their carrying amounts and fair values, are as follows:

Assets/liabilities	Category	Measurement	2020		2019	
			Carrying amount	Fair value	Carrying amount	Fair value
			\$	\$	\$	\$
Accounts receivable	Financial assets	Amortized cost	3,406,053	3,406,053	2,906,154	2,906,154
Accounts payable and accrued liabilities	Financial liabilities	Amortized cost	7,159,859	7,159,859	6,342,500	6,342,500
Unearned revenue and deposits received	Financial liabilities	Amortized cost	60,810	60,810	60,810	60,810
Note payable	Financial liabilities	Amortized cost	-	-	550,000	550,000
Term notes payable	Financial liabilities	Amortized cost	19,161,412	19,161,412	21,989,134	21,989,134
Lease Liabilities	Financial liabilities	Amortized cost	3,123,405	3,123,405	1,152,482	1,152,482

(c) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument might be adversely affected by a change in interest rates. In seeking to minimize the risks from interest rate fluctuations, the Company manages exposure through its normal operating and financing activities. The Company is exposed to interest rate risk primarily through its floating interest rate bank indebtedness, credit facilities and lease liabilities. Assuming that other variables remain constant, a 1% change in the prime lending rate as at March 31, 2020 would impact interest expense and net income by \$223,000 (2019 - \$234,000).

(d) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the Company by failing to discharge its obligations. The Company is exposed to credit risk on its accounts receivable. Its exposure is generally limited to the carrying amount on the consolidated statements of financial position. The Company minimizes credit risk on cash by depositing with only reputable financial institutions.

Management reviews credit risk on the Company's trade receivables through established credit monitoring policies, including analysis of historical payment trends, customer history and events to assess if there should be any allowance for accounts receivable for balances that are impaired. Provisions are recognized based on the expected credit losses in order to reflect risks related to bad debts.

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23. **FINANCIAL INSTRUMENTS AND RISK FACTORS, CONTINUED**

(c) **Credit risk, continued**

Aged amounts receivable and related provision are as follows:

	<u>2020</u>	<u>2019</u>
Current	\$ 2,705,511	\$ 1,684,139
30 days past due	509,159	549,178
60 days past due	78,775	182,803
90 days past due	102,569	260,497
120 days past due	221,972	381,554
Amount provided for	<u>(211,933)</u>	<u>(152,017)</u>
	<u>\$ 3,406,053</u>	<u>\$ 2,906,154</u>

The Company reviews a new customer's credit history before extending credit and conducts regular reviews of its existing customers' credit performance. Customers with no credit evaluation are required to pay cash with no credit terms. The Company has a credit insurance policy with Coface on a significant export customer to a maximum of \$2,000,000 (2019 - \$675,000 with EDC) at any one time. Based on the historical information and the credit quality of accounts receivable, management has assessed credit risk as low. It is reasonably possible that the actual amount of loss, if any, incurred on trade receivables will differ from management's estimate.

(e) **Concentration risk**

Concentration risk is the risk arising from a dependence on one customer or supplier for a significant portion of sales or purchases. The risk of a significant customer having financial difficulties would have a negative impact on the Company. During the year ended March 31, 2020, sales to three customers, including the Liquor Control Board of Ontario ("LCBO") comprised 45.6% (2019 - 55.7%) of total revenue. As at March 31, 2020, these three customers represented 28.2% of accounts receivable (2019 - 25.6%).

The Company has many other sales to distributors and customers and, other than disclosed above, is not dependent on the sales to any one single customer.

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23. **FINANCIAL INSTRUMENTS AND RISK FACTORS, CONTINUED**

(f) **Foreign currency risk**

Foreign currency risk is the risk that changes in foreign currency rates will adversely affect the Company. The Company conducts transactions with parties worldwide, and as a result, certain of the Company's accounts receivable and accounts payable balances are denominated in United States dollars ("USD"), Australian dollars ("AUD"), Euros ("EUR") and British pounds ("GBP"). A significant change in currency exchange rate between the Canadian dollar relative to these currencies could have an effect on the operating results. The Company has not hedged its exposure to currency fluctuations. Based on this exposure and assuming that all other variables remain constant, a +/- 10% change in the value of the Canadian dollar relative to these currencies as at March 31, 2020 would affect net income and comprehensive income by approximately \$19,000 (2019 - \$27,000).

(g) **Liquidity risk**

Liquidity risk is the risk arising from the Company not being able to meet its obligations as they come due. The Company manages its liquidity needs by carefully monitoring scheduled debt servicing payments for its financial liabilities as well as forecasting cash inflows and outflows due in day-to-day business. The data used for analyzing these cash flows is consistent with that used in the contractual maturity presented in bank indebtedness and term loans payable (*see note 15*).

Total current liabilities as at March 31, 2020 of \$26,764,811 (2019 - \$7,713,903), which includes accounts payable and accrued liabilities, unearned revenue and deposits received, note payable, current portion of term loans payable and lease liabilities, are considered current and are due within 12 months of the end of the reporting period.

As at March 31, 2020, the Company had a working capital surplus (deficiency) of \$(993,456) (2019 - \$14,887,530). The working capital deficiency as at March 31, 2020 resulted from the classification of long-term debt as current (*see note 15*), and is expected to go back to long-term based on the extension of the credit agreement to July 1, 2022 under the terms of the fourth amending agreement.

The following table outlines the Company's contractual undiscounted obligations. The Company analyzes contractual obligations for financial liabilities in conjunction with other commitments in managing liquidity risk. Contractual obligations include term loans payable, lease liabilities, and contracts for the purchase of grapes, packaging and other raw materials.

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23. **FINANCIAL INSTRUMENTS AND RISK FACTORS, CONTINUED**

	<1 year	2-3 years	4-5 years \$ (000's)	>5 years	Total
Accounts payable and accrued liabilities	7,160	-	-	-	7,160
Term loans payable	19,161	-	-	-	19,161
Lease liabilities	403	835	855	1,620	2,858
Purchase contracts for grapes, packaging and other raw materials	4,021	3,970	220	-	7,991
Total contractual obligations	<u>30,745</u>	<u>4,805</u>	<u>1,075</u>	<u>1,620</u>	<u>37,170</u>

The Company has entered into grape purchase contracts with certain suppliers to purchase their crops at the time of harvest for prices set by the market. The amount of the commitment will change based on the total tonnes harvested or the prices set by the market for specific grapes, and the amount included in the table above represents management's best estimate of the Company's commitment over the periods noted.

24. **NON-CASH TRANSACTIONS**

	2020 \$	2019 \$
Property, plant and equipment and right-of-use assets acquired under lease liabilities	54,486	892,711
Right-of-use assets and lease liabilities on transition to IFRS	2,385,244	-
Lease liabilities for assets disposed of under lease	(56,963)	-
Issuance of note payable in exchange for shares	-	550,000
Issuance of common shares on settlement of DSUs	70,203	34,130
Issuance of common shares on acquisition of Backyard Vineyards Corp.	-	1,500,000

25. **CAPITAL DISCLOSURES**

The Company's objectives when managing capital are to provide a return for owners and ensure sufficient resources are available to meet day-to-day operations. Capital is considered to consist entirely of total equity and bank indebtedness. The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company or in the light of changes in economic conditions and the risk characteristics of the underlying assets. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable.

The Company is subject to externally imposed capital requirements related to its term loans (see note 15) and there has been no change in the overall capital risk management strategy during the year.

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26. **SUBSEQUENT EVENTS**

(a) **BMO credit facility - 3rd amendment**

On May 15, 2020, the Company executed a third amending agreement to its credit facility with BMO (*see note 15*).

(b) **BMO credit facility - 4th amendment**

On July 24, 2020, the Company executed a fourth amending agreement to its credit facility with BMO (*see note 15*).