

Interim Condensed Consolidated Financial Statements of

ESPIAL GROUP INC.

Quarters ended March 31, 2016 and 2015

(Unaudited)

ESPIAL GROUP INC.
Interim Condensed Consolidated Financial Statements
For the Quarters ended March 31, 2016 and 2015

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ESPIAL GROUP INC.

Interim Condensed Consolidated Balance Sheets

(In Canadian Dollars)

(Unaudited)

	March 31, 2016	December 31, 2015
CURRENT ASSETS		
Cash and cash equivalents	\$ 48,514,160	\$ 49,947,096
Accounts receivable	6,925,935	8,397,948
Investment tax credits receivable	487,593	413,920
Prepaid expenses and other assets	663,965	734,906
	56,591,653	59,493,870
Equipment (Note 6)	1,091,752	1,062,544
Intangible assets (Note 6)	1,609,056	1,658,610
Goodwill (Note 6)	3,632,604	3,632,604
	\$ 62,925,065	\$ 65,847,628
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 2,707,060	\$ 3,165,144
Deferred revenue	2,794,805	3,690,638
Total Liabilities	5,501,865	6,855,782
COMMITMENTS (Note 8)		
SHAREHOLDERS' EQUITY		
Share capital (Note 4)	126,600,874	126,583,844
Share based payments reserve	14,441,662	14,059,806
Deficit	(83,619,336)	(81,651,804)
	57,423,200	58,991,846
	\$ 62,925,065	\$ 65,847,628

APPROVED BY THE BOARD



Jaison Dolvane



Peter Seeligsohn

See accompanying notes

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Income and Loss and Comprehensive Income and Loss

(In Canadian Dollars)

(Unaudited)

	Three Months Ended	
	March 31, 2016	March 31, 2015
Software	\$ 2,440,739	\$ 2,413,027
Professional services	1,672,025	1,872,706
Support and maintenance	1,211,218	1,130,144
Revenue	5,323,982	5,415,877
Cost of revenue	1,928,983	1,169,387
Gross margin	3,394,999	4,246,490
Expenses		
Sales and marketing	1,264,443	1,146,086
General and administrative	864,748	790,041
Research and development	2,890,216	1,893,272
Amortization of intangible assets	174,683	161,219
	5,194,090	3,990,618
(Loss) income before other (expense) income	(1,799,091)	255,872
Interest income	86,732	36,390
Foreign exchange (loss) gain	(223,550)	103,756
(Loss) income before taxes	(1,935,909)	396,018
Income taxes	(31,623)	(36,793)
Net and comprehensive (loss) income	\$ (1,967,532)	\$ 359,225
(Loss) income per common share - basic	\$ (0.05)	\$ 0.01
Weighted average number of common shares outstanding - basic (Note 5)	37,355,246	27,050,961
(Loss) income per common share – diluted	\$ (0.05)	\$ 0.01
Weighted average number of common shares outstanding - diluted (Note 5)	37,355,246	28,801,098

See accompanying notes

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Cash Flows

(In Canadian Dollars)
(Unaudited)

	Three Months Ended	
	March 31, 2016	March 31, 2015
CASH (USED IN) PROVIDED BY OPERATING		
Net (loss) income	\$ (1,967,532)	\$ 359,225
Items not affecting cash		
Depreciation of property and equipment	68,451	48,043
Amortization of intangible assets	174,683	161,219
Share-based compensation expense	389,456	320,863
Provisions	-	(73,210)
	(1,334,942)	816,140
Changes in non-cash operating working capital items (Note 7)	115,364	(1,505,861)
	(1,219,578)	(689,721)
INVESTING		
Purchase of equipment	(97,659)	(34,409)
Purchase of intangibles	(125,129)	-
	(222,788)	(34,409)
FINANCING		
Proceeds from options exercised	9,430	270,554
Proceeds from warrants exercised (Note 4)	-	72,000
	9,430	342,554
Cash and cash equivalents outflow	(1,432,936)	(381,576)
Cash and cash equivalents, beginning of period	49,947,096	18,111,324
Cash and cash equivalents, end of period	\$ 48,514,160	\$ 17,729,748
Supplementary information:		
Interest received	\$ 86,732	\$ 36,390
Taxes paid	\$ 31,623	\$ 36,793

See accompanying notes

ESPIAL GROUP INC.

Interim Condensed Consolidated Statements of Shareholders' Equity

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

	<u>Common Shares</u>		Warrants	Share-based payment reserve	(Deficit)	Shareholders' Equity
	Number	Amount				
Balance at December 31, 2014	26,886,267	\$91,072,570	\$928,063	\$12,986,590	(\$82,923,812)	\$22,063,411
Share-based compensation	-	-	-	320,863	-	320,863
Warrants exercised	100,000	101,864	(29,864)	-	-	72,000
Options exercised	378,180	489,863	-	(219,309)	-	270,554
Net and comprehensive income	-	-	-	-	359,225	359,225
Balance at March 31, 2015	27,364,447	\$91,664,297	\$898,199	\$13,088,144	(\$82,564,587)	\$23,086,053
Balance at December 31, 2015	37,348,057	\$126,583,844	\$ -	\$14,059,806	(\$81,651,804)	\$58,991,846
Share-based compensation	-	-	-	389,456	-	389,456
Options exercised (Note 4)	10,458	17,030	-	(7,600)	-	9,430
Net and comprehensive loss	-	-	-	-	(1,967,532)	(1,967,532)
Balance at March 31, 2016	37,358,515	\$126,600,874	\$ -	\$14,441,662	(\$83,619,336)	\$57,423,200

See accompanying notes

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements

for the Quarters ended March 31, 2016 and 2015 (unaudited)

(In Canadian Dollars, except share amounts)

1. DESCRIPTION OF BUSINESS

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

The Company’s address and principal place of business is 200 Elgin Street, Suite 1000, Ottawa, Ontario, K2P 1L5, Canada.

2. BASIS OF PRESENTATION

(a) Statement of Compliance

The unaudited interim condensed consolidated financial statements have been prepared in accordance with International Accounting Standards (“IAS”) 34 *Interim Financial Reporting as issued by the International Accounting Standards Board (“IASB”)* and do not include all information required for full annual financial statements for International Financial Reporting Standards (“IFRS”). These unaudited interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Annual Report for the year ended December 31, 2015 and were prepared using the same accounting policies, except as described below.

These unaudited interim condensed consolidated financial statements were approved and authorised for issue by the Board of Directors on, May 4, 2016.

(b) Basis of Measurement

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

(c) Basis of Consolidation

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

(d) Significant Accounting Policies

Except as disclosed below, the accounting policies applied in these unaudited interim condensed consolidated financial statements are the same as those applied in the Company’s consolidated financial statements as at and for the year ended December 31, 2015.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

3. NEW AND REVISED IFRS ACCOUNTING PRONOUNCEMENTS

Financial instruments

IFRS 9, Financial Instruments: Classification and Measurement (“IFRS 9”), was Issued in November 2009 and revised in October 2010, IFRS 9, as issued, is the first phase in the IASB’s project to replace IAS 39 Financial Instruments: recognition and measurement (“IAS 39”). This standard simplifies the classification of a financial asset as either at amortized cost or at fair value as opposed to the multiple classifications which were permitted under IAS 39. This standard also requires the use of a single impairment method as opposed to the multiple methods in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The standard also adds guidance on the classification and measurement of financial liabilities. The standard is effective for annual periods beginning January 1, 2018. The Company does not intend to adopt IFRS 9 at this time but continues to monitor the individual phases of the IASB project. The extent of the impact of adoption of IFRS 9 has not yet been determined.

IFRS 15, Revenue from Contracts with Customers

In May, the IASB issued IFRS 15, Revenue from Contracts with Customers (“IFRS 15”), a new standard on revenue recognition. The new standard provides a framework that replaces existing revenue recognition guidance in IFRS. The standard contains the following:

- a single model that applies to contracts with customers; and
- two approaches to recognizing revenue – at a point in time or over time.

The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. The new standard also provides application guidance on numerous topics, including warranties; licences; and when to capitalize costs of obtaining or fulfilling contracts that are not addressed in other accounting standards (e.g., inventory). IFRS 15 applies for annual periods beginning on or after January 1, 2018. Early application is permitted. The extent of the impact of adoption of IFRS 15 has not yet been determined.

IFRS 16: Leases

In January 2016, the International Accounting Standards Board issued IFRS 16, Leases, which specifies how to recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Consistent with its predecessor, IAS 17, the new lease standard continues to require lessors to classify leases as operating or finance. IFRS 16 is to be applied retrospectively for annual periods beginning on or after January 1, 2019. Earlier application is permitted if IFRS 15 Revenue from contract with customers has also been applied. The Company does not intend to early adopt this standard and is currently evaluating the impact of adopting this standard..

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Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

4. SHARE CAPITAL

Share capital consists of an unlimited number of common shares of which 37,358,515 common shares were issued and outstanding at March 31, 2016 (December 31, 2015 – 37,348,057).

On May 6, 2015 the Company completed a public offering of 8,750,000 common shares at a price of \$4.00 per Common Share on a bought-deal basis. The aggregate gross proceeds to the Company for the Offering were \$35,000,000. The net proceeds, after deducting share issue costs of \$2,383,312, which have been netted against the value of the common shares, were \$32,616,688.

Stock option plans

As at March 31, 2016, there were 2,792,959 options for common shares remaining available for issuance under the 2007 option plan. Options are granted periodically and vest over four years. One quarter of the options vest after 12 months and the remainder vest in thirty-six equal tranches over the three years thereafter. The maximum term of these options is ten years. The Company uses the Black-Scholes option pricing model to value the options at the time of grant. Management periodically reviews the estimates used for calculating the fair value of options, volatility is calculated at the time of option grant using historical share price trading activity, ranging from 80% to 92%; risk-free interest rate is based on the government of Canada bond rate, estimated at 0.61% at the time of issue; dividend yield is NIL%; expected life of each option is 1.5 years after vesting. The forfeiture rate was estimated at 10%.

During the three months ended March 31, 2016, there were 695,000 options granted. The per share fair value of stock options granted during the three months ended March 31, 2015 was \$1.20.

The following table summarizes information about option activity for the quarter ended March 31, 2016:

	Number of Options	Weighted-average Exercise Price
Outstanding, at December 31, 2015	4,012,119	\$2.25
Granted	695,000	\$1.99
Exercised	(10,458)	\$0.90
Forfeited	(17,917)	\$2.62
Outstanding, at March 31, 2016	4,678,744	\$2.22

	Number of Options	Weighted-average Exercise Price
Outstanding, at December 31, 2014	3,508,000	\$1.78
Granted	1,047,500	\$2.96
Exercised	(491,425)	\$0.77
Forfeited	(51,956)	\$2.05
Outstanding, at December 31, 2015	4,012,119	\$2.25

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Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

The following table summarizes information about stock options outstanding at March 31, 2016:

Range of Exercise Prices	Options Outstanding		Options Exercisable	
	Number Outstanding	Weighted Average Remaining Life	Number Outstanding	Weighted Average Exercise Price
\$0.26 - \$1.00	1,381,362	4.5	1,275,324	\$0.85
\$1.01 - \$2.00	894,500	8.9	141,370	\$1.63
\$2.01 - \$4.00	2,294,983	8.4	787,897	\$2.89
\$4.01 - \$7.00	107,899	1.7	107,899	\$6.75
	4,678,744	7.2	2,312,490	\$1.87

5. EARNINGS (LOSS) PER SHARE

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

	2016	2015
Issued common shares at January 1	37,348,057	26,886,267
Effect of shares issued from warrants	-	37,778
Effect of shares issued from options	7,189	126,916
Weighted average number of basic common shares at March 31	37,355,246	27,050,961
Effect of warrants on issue	-	678,316
Effect of share options on issue	-	1,071,821
Weighted average number of diluted common shares at March 31	37,355,246	28,801,098

Options and warrants that are anti-dilutive are not included in the computation of diluted earnings per share. For the three months ended March 31, 2016, due to the net loss, all options were excluded from the calculation of diluted earnings per share because they are anti-dilutive. As at March 31, 2015, 1,942,899 stock options and 210,528 warrants were excluded from the calculation of diluted earnings per share because they are anti-dilutive.

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Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

6. SEGMENTED INFORMATION

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

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

	Three months	
	March 31, 2016	March 31, 2015
Europe	\$3,407,180	\$2,913,080
Asia Pacific	1,113,020	1,161,278
North America	803,782	1,341,519
	\$5,323,982	\$5,415,877

For the quarter ended March 31, 2016, the Company had one customer that accounted for 28% of revenue. For the quarter ended March 31, 2015, the Company had two customers that individually accounted for 21% and 11% of revenue. As at March 31, 2016 two customers accounted for 31% and 23% of accounts receivable.

As at December 31, 2015 three customers accounted for 24%, 13% and 11% respectively of accounts receivable.

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

	March 31, 2016	December 31, 2015
Canada	\$819,631	\$788,634
United States	89,395	94,183
United Kingdom	161,504	157,644
France	21,222	22,083
	\$1,091,752	\$1,062,544

The following table sets forth intangible assets attributable to Canada (the Company's country of domicile), the United States and the United Kingdom. The three regions hold all of the Company's intangible assets. The goodwill is owned by Canada, \$291,796, and the United States, \$3,340,808

	March 31, 2016	December 31, 2015
Canada	\$ 745,032	\$ 681,310
United States	1,807	1,953
United Kingdom	862,217	975,347
	\$ 1,609,056	\$ 1,658,610

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

7. CHANGES IN NON-CASH OPERATING WORKING CAPITAL ITEMS

	Three months	
	March 31, 2016	March 31, 2015
Accounts receivable	\$ 1,472,013	\$ (1,010,118)
Investment tax credits receivable	(73,673)	(75,521)
Prepaid expenses and other assets	70,941	(105,610)
Accounts payable and accrued liabilities	(458,084)	(416,362)
Deferred revenue	(895,833)	101,750
	<u>\$ 115,364</u>	<u>\$ (1,505,861)</u>

8. COMMITMENTS

The Company has entered into several operating leases for office space and various equipment leases.

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

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

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

2016	\$ 645,560
2017	819,870
2018	804,671
2019	806,377
2020 to 2024	<u>3,351,705</u>
	<u>\$ 6,428,183</u>

Lease payments recognized as an expense during the three month periods ended March 31, 2016 and 2015 were \$228,314 and \$194,235 respectively.

ESPIAL GROUP INC.

Notes to Interim Condensed Consolidated Financial Statements for the Quarters ended March 31, 2016 and 2015 (unaudited) (In Canadian Dollars, except share amounts)

9. EMPLOYEE BENEFITS EXPENSE

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

	March 31, 2016	March 31, 2015
Salaries	\$ 3,264,644	\$ 2,503,229
Benefits	677,479	439,253
Variable compensation and other labour costs	244,800	323,459
Share-based payments	389,456	320,863
	\$ 4,576,379	\$ 3,586,804

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

	March 31, 2016	March 31, 2015
Sales and marketing	\$ 84,578	\$ 27,197
General and administration	228,576	258,702
Research and development	76,302	34,964
	\$ 389,456	\$ 320,863