

Unaudited Condensed Interim Consolidated Financial Statements of

KNEAT.COM, INC.

(formerly Fortune Bay Corp.)

June 30, 2016

(Expressed in Canadian Dollars)

In accordance with National Instrument 51-102 Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of these condensed interim consolidated financial statements, they must be accompanied by a notice indicating that these condensed interim consolidated financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed interim consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management. The Company's independent auditor has not performed a review of these condensed interim consolidated financial statements in accordance with standards established by the Chartered Professional Accountants of Canada for a review of interim financial statements by an entity's auditor.

kneat.com, inc.

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Unaudited Interim Consolidated Statements of Financial Position

<i>Expressed in Canadian dollars</i>	June 30 2016	December 31 2015
Assets		
Current assets		
Cash	\$ 7,300,545	\$ 1,063,524
Accounts receivable and other (Note 5)	417,362	633,400
Total current assets	7,717,907	1,696,924
Accounts receivable (Note 5)	586,105	389,614
Property and equipment (Note 6)	413,292	423,133
Intangible assets (Note 7)	1,959,014	1,741,012
Total assets	\$ 10,676,318	\$ 4,250,683
Liabilities		
Current liabilities		
Accounts payable, accrued liabilities and deferred income (Note 8)	\$ 1,257,269	\$ 589,133
Directors' current account (Note 14)	160,111	259,146
Total current liabilities	1,417,380	848,279
Loan payable and accrued interest (Note 9)	937,542	973,250
Accounts payable, accrued liabilities and deferred income (Note 8)	195,251	186,086
Total liabilities	2,550,173	2,007,615
Equity		
Shareholders' equity	8,126,145	2,243,068
Total liabilities and equity	\$ 10,676,318	\$ 4,250,683

Commitments and contingencies (Note 16)

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

Approved on behalf of the Board of Directors on August 25, 2016

"Edmund Ryan"

Director

"Ian Ainsworth"

Director

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Unaudited Interim Consolidated Statements of Loss and Comprehensive Loss*Expressed in Canadian dollars*

	Three-month period ended June 30, 2016	Three-month period ended June 30, 2015	Six-month period ended June 30, 2016	Six-month period ended June 30, 2015
Revenue	\$ 19,263	\$ 201,202	\$ 37,206	\$ 348,743
Expenses				
Amortization of intangible assets	161,545	109,376	306,392	201,665
Administrative expenses (Note 11)	797,630	300,886	1,357,634	654,078
Interest and similar charges	34,215	6,351	42,163	12,759
Listing expense (Note 4)	3,799,810	-	3,799,810	-
Disbursement connected to the Transaction (Note 4)	436,616	-	436,616	-
Loss before income taxes	(5,210,553)	(215,411)	(5,905,409)	(519,759)
Income taxes (Note 12)	-	-	-	-
Net loss for the period	\$(5,210,553)	\$(215,411)	\$(5,905,409)	\$(519,759)
Other comprehensive loss				
Foreign currency translation adjustment to presentation currency	(26,054)	(52,600)	(69,510)	(54,134)
	\$(5,236,607)	\$(268,011)	\$(5,974,919)	\$(573,893)
Loss per share – basic and diluted	\$ (0.19)	\$ (0.01)	\$ (0.22)	\$ (0.02)
Weighted-average number of common shares outstanding				
Basic and diluted (Note 4, Note 10 (a))	27,591,107	24,891,867	27,383,543	24,243,597

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

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Unaudited Interim Consolidated Statements of Changes in Equity

Expressed in Canadian dollars

	Number of Common Shares (Note 4)	Common Shares	Warrants	Contributed Surplus	Translation Reserve	Retained Earnings (Deficit)	Total
		\$	\$	\$	\$	\$	\$
Balance, January 1, 2015	23,314,877	\$8,815,352	-	\$330,886	\$42,833	\$(8,664,213)	\$524,858
Net loss for the period	-	-	-	-	-	(519,759)	(519,759)
Other comprehensive loss for the period	-	-	-	-	(54,134)	-	(54,134)
	-	-	-	-	(54,134)	(519,759)	(573,893)
Shares issued during the period	3,636,753	2,308,656	-	-	-	-	2,308,656
Share-based compensation expense	-	-	-	21,406	-	-	21,406
Balance, June 30, 2015	26,951,630	\$11,124,008	-	\$352,292	\$(11,301)	\$(9,183,972)	\$2,281,027
Balance, December 31, 2015	27,178,260	\$11,275,304	-	\$385,106	\$255,947	\$(9,673,289)	\$2,243,068
Net loss for the period	-	-	-	-	-	(5,905,409)	(5,905,409)
Other comprehensive loss for the period	-	-	-	-	(69,510)	-	(69,510)
	-	-	-	-	(69,510)	(5,905,409)	(5,974,919)
Shares and warrants issued pursuant to the Transaction (Note 4)	12,385,424	11,518,443	67,424	250,477	-	-	11,836,344
Share-based compensation expense	-	-	-	21,652	-	-	21,652
Balance, June 30, 2016	39,563,684	\$22,793,747	\$67,424	\$657,235	\$186,437	\$(15,578,698)	\$8,126,145

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

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Unaudited Interim Consolidated Statements of Changes in Cash Flows

<i>Expressed in Canadian dollars</i>	Six-month period ended June 30, 2016	Six-month period ended June 30, 2015
Operating activities		
Net loss for the period	\$ (5,905,409)	\$ (519,759)
Charges to loss not involving cash:		
Depreciation	35,801	12,806
Share-based compensation	17,669	13,191
Interest on cumulative redeemable convertible preference shares	11,819	11,760
Amortization of intangible assets	306,392	201,665
Listing expense	3,799,810	-
Non-cash professional fees	-	55,119
Unrealized foreign exchange loss	66,057	-
Increase in non-current accounts receivable	(221,933)	(187,254)
Decrease in non-current accounts payable, accrued liabilities and deferred income	18,739	10,313
Net change in non-cash working capital related to operations (Note 13)	517,374	(125,324)
Net cash used in operating activities	(1,353,681)	(527,483)
Financing activities		
Proceeds from issuance of shares	-	2,253,806
Proceeds from issuance of debenture to kneat.com (Note 2)	1,479,200	-
Receipt of cash from the Transaction	6,775,609	-
Net cash provided by financing activities	8,254,809	2,253,806
Investing activities		
Additions to intangible assets	(614,009)	(394,374)
Additions to property and equipment	(46,178)	(56,254)
Net cash provided by investing activities	(660,187)	(450,628)
Effects of exchange rates on cash	(3,920)	(7,958)
Increase in cash	6,237,021	1,267,737
Cash, beginning of period	1,063,524	18,330
Cash, end of period	\$ 7,300,545	\$ 1,286,067

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

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements

1. NATURE OF OPERATIONS

kneat.com, inc. (the "Company" or "kneat.com") (formerly Fortune Bay Corp.), was incorporated on December 12, 2013 under the laws of the Canada Business Corporations Act. On June 27, 2016, the Company completed a Transaction with Kneat Solutions Limited (refer to Note 2 and Note 4 for details). The Company commenced trading on the TSX Venture Exchange ("TSX-V") as kneat.com on July 5, 2016 under the symbol KSI (TSX-V). kneat.com's head office is located at Unit 7, Castletroy Park Business Centre, Castletroy, Limerick, Ireland. The registered office of kneat.com is at Suite 2001, 1969 Upper Water Street, Halifax, Nova Scotia, B3J 3R7.

Kneat Solutions Limited, a wholly owned subsidiary of the Company, is in the business of developing and marketing a software application for modelling regulated data intensive processes for pharmaceutical, biotechnology and medical device manufacturers.

The Company's operations have been financed through the sale of shares, issuance of debt, revenue generated from customers and research and development tax credits. The Company has incurred significant operating losses and negative cash flows from operations since inception and has an accumulated deficit of \$15.6 million as at June 30, 2016.

2. TRANSACTION WITH KNEAT SOLUTIONS LIMITED

On June 27, 2016, kneat.com (formerly Fortune Bay Corp.) completed a transaction with Kneat Solutions Limited and 9617337 Canada Limited (now renamed Fortune Bay Corp., herein after referred to as "Spinco"), pursuant to which it: (i) spun-out its resources properties to Spinco by way of a court-approved plan of arrangement in Ontario (the "Arrangement"); and (ii) acquired 100% of the issued and outstanding ordinary shares of Kneat Solutions Limited by way of a concurrent scheme of arrangement in Ireland (the "Merger"), collectively referred to as the "Transaction".

Pursuant to the Transaction, shareholders of kneat.com on the close of business on June 24, 2016 received one (1) new common share of kneat.com (each a "kneat.com share") and one and one half (1.5) of a common share of Spinco (a "Spinco Share") in exchange for each three (3) common shares of kneat.com held by them on June 24, 2016.

Upon completion of the Transaction on June 27, 2016, shareholders of kneat.com on June 24, 2016 held 31.3% of the issued and outstanding kneat.com shares, with the former shareholders of Kneat Solutions Limited holding the remaining 68.7% of the issued and outstanding kneat.com shares. In addition to acquiring all the issued and outstanding shares of Kneat Solutions Limited, kneat.com retained net \$8.0 million of cash.

The shareholders of Kneat Solutions Limited, through owning 68.7% of the outstanding kneat.com shares on completion of the Transaction, control kneat.com. As a consequence of the Transaction, the shareholders of Kneat Solutions Limited acquired control over the combined entity. kneat.com, after its reorganization, does not meet the definition of a business, therefore the Transaction is outside the scope of IFRS 3 *Business Combinations*. The transaction has therefore been accounted for under IFRS 2 *Share-based payment*. Under this basis of accounting, the consolidated entity is considered to be a continuation of Kneat Solutions Limited, with the net identifiable assets of kneat.com deemed to have been acquired by Kneat Solutions Limited. Refer to Note 4 for further details.

On March 24, 2016, the Board of Directors of kneat.com (formerly Fortune Bay Corp.) approved the payment of €1,000,000 to Kneat Solutions Limited as consideration for a Series A Secured Debenture ("the Debenture") with an interest rate of 7.25% per annum and a maturity date of July 1, 2016. As the Transaction was completed prior to July 1, 2016, the Debenture became an intercompany loan between kneat.com and Kneat Solutions Limited and the

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements

kneat.com net cash balance due on closing of the Transaction was reduced by the amount of the Debenture plus all accrued interest.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these unaudited condensed interim consolidated financial statements, except as discussed below.

a) Statement of Compliance and Basis of Consolidation

The unaudited condensed interim consolidated financial statements of the Company and all its subsidiaries have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”). The Board of Directors approved these unaudited condensed interim consolidated financial statements for issue on August 25, 2016.

These unaudited condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* (“IAS 34”), as issued by the IASB. Accordingly, certain information normally included in annual financial statements prepared in accordance with IFRS, as issued by the IASB, has been omitted or condensed. The unaudited condensed interim consolidated financial statements should be read in conjunction with the audited financial statements of the Company and of Kneat Solutions Limited for the year-ended December 31, 2015.

The policies applied in these unaudited condensed interim consolidated financial statements are based on IFRS as of August 25, 2016, the date the Board of Directors approved the financial statements. Any subsequent changes to IFRS that are given effect in the Company’s annual consolidated financial statements for the year-ended December 31, 2016 could result in the restatement of these unaudited condensed interim consolidated financial statements.

These unaudited condensed interim consolidated financial statements include certain assets, liabilities and results of operations of the Company, including the following subsidiaries:

<u>Subsidiary</u>	<u>Principal Activity</u>	<u>Country of Incorporation</u>
Kneat Solutions Limited	Operations	Ireland
Kneat Solutions Inc.	Operations	United States

The Company consolidates the wholly-owned subsidiaries on the basis that it controls these subsidiaries through its ability to govern their financial and operating policies. There are no non-controlling interests and therefore all comprehensive income (loss) is attributable to the shareholders of the Company.

These financial statements have been prepared using the same policies and methods of computation as the annual consolidated financial statements of the Company and of Kneat Solutions Limited for the year-ended December 31, 2015. Refer to Note 3, *Summary of Significant Accounting Policies*, of the Fortune Bay Corp. annual consolidated financial statements for the year-ended December 31, 2015 and Note 3, *Accounting Policies*, of the Kneat Solutions Limited annual consolidated financial statements for the year-ended December 31, 2015 for information on the accounting policies as well as new accounting standards not yet effective.

b) Foreign currency translation

Items included in the financial statements of each entity included in these consolidated financial statements are measured using the currency of the primary economic environment in which the entity operates (the “functional currency”). The consolidated financial statements are presented in Canadian dollars. Assets and

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liabilities of each foreign entity are translated into Canadian dollars at the exchange rate in effect on the statement of financial position date. Revenue and expenses are translated at the average rate in effect during the period. Unrealized translation gains and losses are recorded as a cumulative translation adjustment, which is included in other comprehensive income or loss, which is a component shareholders' equity. The functional currency of Kneat Solutions Limited is the EURO ("€") and the functional currency of Kneat Solutions Inc. is the United States Dollar ("USD"). The legal parent entity, kneat.com, has a Canadian dollar functional currency.

Foreign currency transactions are translated as follows: (i) monetary assets and liabilities denominated in currencies other than the functional currency are translated into the functional currency at the exchange rate prevailing at the statement of financial position date; and (ii) non-monetary assets and liabilities denominated in foreign currencies and measured in terms of historic costs are translated using rates of exchange at the transaction dates.

c) Critical accounting judgments and estimates

The preparation of the financial statements in conformity with IFRS requires management to make judgments and estimates that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results could differ from these estimates.

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

Information about critical accounting judgments and estimates in applying accounting policies that have the most significant impact on the amounts recognized in the consolidated financial statements are outlined below.

Accounting for the Transaction

In order to account for the Transaction, management has made estimates related to the valuation of Kneat Solutions Limited on the effective date of Transaction which impact the calculation of the listing fee recognized in the statement of loss and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016. The main estimates used in the valuation of Kneat Solutions Limited are in reference to the trading price of kneat.com on the Transaction date. A change in these estimates could have a significant impact on the listing expense and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 whereby a ten percent decrease in the valuation of Kneat Solutions Limited would decrease the listing expense and decrease the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 by approximately \$1,200,000. Conversely, if the valuation of Kneat Solutions Limited was increased by ten percent, the listing expense and the valuation of the shares issued to holders of kneat.com shares on June 24, 2016 would increase by approximately \$1,200,000.

Valuation and amortization of internally generated intangible asset

The Company capitalizes certain costs incurred for the development of its Kneat Gx computer software platform. Estimates are used in order to determine the point in time whereby the recognition criteria are met and the allocation and nature of costs to capitalize in accordance with IAS 38, *Intangible Assets*. The capitalized costs include the cost of direct labour and other costs directly attributable to preparing the intangible asset for its intended use. Management then estimates the expected term over which the Company will receive benefits from the software application, which is estimated to be five years. A change in these estimates would have a significant impact on the carrying value of the intangible asset and the amortization and expenses recognized in the statement of loss.

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Recovery of research and development tax credits

Amounts recorded for research and development tax credits are calculated based on the expected eligibility and tax treatment of qualifying research and experimental development expenditures recorded in the Company's consolidated financial statements. Estimates are used in determining the eligibility of expenditures incurred and may be subject to audit and further analysis by the tax authorities. A change in the estimates would have a significant impact on the carrying value of the research and development tax credit receivable balance, the research and development tax credit recovery in the statement of loss and the carrying value of the intangible asset.

Valuation of stock options

The fair value of the stock options granted by the Company is estimated by management using the Black-Scholes pricing model which incorporates several assumptions including the grant date, exercise price, share price on the grant date, volatility of the underlying stock, and the expected term of the stock options. The Company uses historical price data of comparable entities in the estimate of future volatilities. Changes in the assumptions can materially affect the fair value estimates, and therefore, may not necessarily provide a reliable estimate of the fair value of the related stock options.

4. ACCOUNTING FOR THE TRANSACTION

On June 27, 2016, kneat.com acquired 100% of the 794,254 issued and outstanding ordinary and A ordinary shares of Kneat Solutions Limited in exchange for 12,385,424 common shares of kneat.com. This resulted in 39,563,684 outstanding common shares of kneat.com. Previous shareholders of Kneat Solutions Limited held 68.7% or 27,178,260 common shares of kneat.com and previous shareholders of kneat.com held 31.3% or 12,385,424 common shares of kneat.com immediately following the Transaction.

As a consequence of the Transaction, the shareholders of Kneat Solutions Limited acquired control over the combined entity. kneat.com, after its spin-out of its resources properties to Spinco, does not meet the definition of a business as its assets consist only of cash, with no ability to generate outputs, therefore the transaction is outside the scope of IFRS 3 *Business Combinations*. The Transaction has therefore been accounted for under IFRS 2 *Share-based payment*. Under this basis of accounting, the consolidated entity is considered to be a continuation of Kneat Solutions Limited, with the net identifiable assets of kneat.com deemed to have been acquired by Kneat Solutions Limited on June 27, 2016.

All figures related to the common shares, as well as loss per share in these consolidated financial statements, have been retroactively restated to reflect the legal capital of kneat.com at an exchange ratio of one (1) Kneat Solutions Limited share to 34.2186 common shares of kneat.com as per the terms of the Transaction agreement. The number of Kneat Solutions Limited ordinary and A ordinary shares at June 30, 2015 and December 31, 2015 have been restated from 787,631 to 26,951,630 and 794,254 to 27,178,260 respectively.

As a result of the Transaction falling within the scope of IFRS 2, the Transaction was accounted for by Kneat Solutions Limited as the issuance of shares at fair value for the net assets of kneat.com and a listing expense, which reflects the difference between the fair value of the Kneat Solutions Limited deemed shares issued to kneat.com shareholders and kneat.com's net assets acquired. In accordance with IFRS 2, the excess of the fair value of the deemed shares issued over the acquired net assets is recognized in the statement of loss as a listing expense. The fair value of the 794,254 issued and outstanding ordinary and A ordinary shares of Kneat Solutions Limited was estimated to be \$25,275,782 based on management's estimates as described in Note 3 (c).

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Under IFRS 2, the capital transaction is measured at the fair value of the shares deemed to have been issued by Kneat Solutions Limited such that the kneat.com shareholders held 31.3% of the combined entity. The fair value of the deemed shares of Kneat Solutions Limited issued to kneat.com shareholders is based on the fair value of Kneat Solutions Limited on the effective date of the Transaction and is estimated to be \$11,518,443 and has been allocated as follows:

	\$
Net assets of kneat.com on the Transaction date (consisting of approximately \$8.2 million in cash and \$0.2 million in accounts payable)	8,036,534
Fair value of 31.3% of the equity of the combined entity based on the estimated fair value	(11,518,443)
Fair value of warrants (Note 10)	(67,424)
Fair value of options (Note 10)	(250,477)
	<hr/>
Listing expense	(3,799,810)
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The listing expense is expensed through the statement of loss. The consideration and allocation reflects the best estimates and assumptions of the management of the Company after taking in to account all available information.

Certain former Kneat Solutions Limited shareholders took part in an employment and investment incentive scheme (“EIS”) under Part 16 of the Irish Taxes Consolidation Act 1997, pursuant to which they availed of income tax relief on their investment in Kneat Solutions Limited. As a result of the Transaction, a claw back of this relief from these shareholders may occur. Only those former Kneat Solutions Limited shareholders who have held their EIS shares for less than three years up to June 27, 2016 should be affected by this claw back. kneat.com and Kneat Solutions Limited formulated a proposal whereby kneat.com would make a payment to the Irish Revenue Commissioners that would be equivalent to or less than the amount of the tax relief as a result of the Transaction. Any payment to any shareholder pursuant to this proposal would only be made after kneat.com has been provided with satisfactory documentary evidence of the loss of tax relief. As at June 30, 2016, the estimated cost that may be incurred as a result of the Transaction is \$436,616. This figure is management’s best estimate based on supporting evidence received from former Kneat Solutions Limited shareholders to date and is subject to change pending final annual tax filings by former Kneat Solutions Limited shareholders which is expected to be finalized in the fourth quarter of 2016.

5. ACCOUNTS RECEIVABLE AND OTHER

	June 30 2016	December 31 2015
	<hr/>	<hr/>
Current		
	\$	\$
Research and development tax credit receivable	308,779	324,509
Trade debtors	44,346	230,280
Other debtors	1,453	33,486
Unpaid share capital	-	20,455
Value-added tax receivable	37,714	13,344
Prepayments	25,070	11,326
	<hr/>	<hr/>
	417,362	633,400
Non-current		
Research and development tax credit receivable	586,105	389,614
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	\$1,003,467	\$1,023,014
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Notes to the Unaudited Condensed Interim Consolidated Financial Statements**6. PROPERTY AND EQUIPMENT**

Cost	Property and equipment	Leasehold improvements	Total
As at January 1, 2015	\$161,129	\$217,374	\$378,503
Additions	120,691	-	120,691
Effect of movements in exchange rates	19,793	15,605	35,398
As at December 31, 2015	301,613	232,979	534,592
Additions	46,778	-	46,778
Effect of movements in exchange rates	(15,984)	(11,293)	(27,277)
As at June 30, 2016	<u>\$332,407</u>	<u>\$221,686</u>	<u>\$554,093</u>
Accumulated depreciation	Property and equipment	Leasehold improvements	Total
As at January 1, 2015	\$70,101	\$ -	\$70,101
Depreciation charge	34,008	-	34,008
Effect of movements in exchange rates	7,350	-	7,350
As at December 31, 2015	111,459	-	111,459
Depreciation charge	21,523	14,278	35,801
Effect of movements in exchange rates	(6,039)	(420)	(6,459)
As at June 30, 2016	<u>\$126,943</u>	<u>\$13,858</u>	<u>\$140,801</u>
Carrying amount	Property and equipment	Leasehold improvements	Total
Balance, December 31, 2015	<u>\$190,154</u>	<u>\$232,979</u>	<u>\$423,133</u>
Balance, June 30, 2016	<u>\$205,464</u>	<u>\$207,828</u>	<u>\$413,292</u>

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements**7. INTANGIBLE ASSETS**

Cost	<u>Software application</u>
As at January 1, 2015	\$1,662,327
Additions	962,481
Effect of movements in exchange rates	184,938
As at December 31, 2015	<u>2,809,746</u>
Additions	617,992
Effect of movements in exchange rates	(154,452)
As at June 30, 2016	<u>\$3,273,286</u>
 Accumulated amortization	
As at January 1, 2015	\$472,843
Amortization charge	526,087
Effect of movements in exchange rates	69,804
As at December 31, 2015	<u>1,068,734</u>
Amortization charge	306,392
Effect of movements in exchange rates	(60,854)
As at June 30, 2016	<u>\$1,314,272</u>
 Carrying amount	
Balance, December 31, 2015	<u>\$1,741,012</u>
Balance, June 30, 2016	<u>\$1,959,014</u>

8. ACCOUNTS PAYABLE, ACCRUED LIABILITIES AND DEFERRED INCOME

	<u>June 30 2016</u>	<u>December 31 2015</u>
Current		
Accruals	\$805,758	\$256,683
Social insurance cost payable	54,866	137,488
Other payables	387,756	161,836
Lease incentives	8,889	33,126
	<u>1,257,269</u>	<u>589,133</u>
Non-current		
Lease incentives	195,251	186,086
	<u>\$1,452,520</u>	<u>\$775,219</u>

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9. LOAN PAYABLE AND ACCRUED INTEREST

On June 27, 2016, Enterprise Ireland and kneat.com executed a loan agreement whereby Enterprise Ireland agreed to exchange its cumulative redeemable convertible preference shares in Kneat Solutions Limited, comprised of 232,000 convertible preference shares and 300,000 A convertible preference shares plus accrued interest, for a loan payable to Enterprise Ireland on the third anniversary of the Merger effective date, being June 27, 2019. The interest rate is 3% on the principal balance of €532,000, not compounded and payable annually. Management has determined that the underlying terms of the loan payable do not differ substantially from the terms of the cumulative redeemable convertible preference shares and thus it has been accounted for as a modification of the original financial liability. As at June 30, 2016 the loan payable and accrued interest balance on the statement of financial position was comprised of a principal balance of \$766,729 and accrued interest of \$170,813 (December 31, 2015 – principal balance of \$805,788 and accrued interest of \$167,462).

10. SHARE CAPITAL

a) Common Shares

Authorized share capital of the Company consists of an unlimited number of fully paid common shares without par value.

	Number of shares	Amount
Outstanding, January 1, 2015	23,314,877	\$8,815,352
Shares issued during the period	3,863,383	2,459,952
Outstanding, December 31, 2015	27,178,260	11,275,304
Shares issued pursuant to the Transaction	12,385,424	11,518,443
Outstanding, June 30, 2016	39,563,684	\$22,793,747

Shares issued pursuant to the Transaction

Pursuant to the Transaction completed on June 27, 2016, the Company issued 12,385,424 common shares (Note 4).

As at June 30, 2016, 17,048,720 common shares of the Company are subject to an escrow agreement pursuant to the terms of the Transaction and will be released over a time period of 18 months from the effective date of the Transaction.

b) Warrants

Pursuant to the Transaction, 267,857 warrants were issued, valued at \$67,424. The fair value of the 267,857 warrants issued has been estimated at the grant date using the Black-Scholes option pricing model. The weighted-average assumptions used in the pricing model for warrants issued during the period ended June 30, 2016 are as follows:

Risk-free interest rate	0.53%
Expected life	0.76 years
Expected volatility	75.2%
Expected dividend per share	\$0.00
Weighted average fair value	\$0.25

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As at June 30, 2016, 267,857 common share purchase warrants are outstanding, exercisable at \$0.90 into common shares of the Company and expiring on April 1, 2017.

e) Stock Option Plan

The Company has adopted a stock option plan, providing the Board of Directors with the discretion to issue an equivalent number of options of up to 10% of the issued and outstanding share capital of the Company. Stock options are granted with an exercise price of not less than the closing share price the date preceding the date of grant.

As per the terms of the Transaction, all Kneat Solutions Limited stock options were cancelled and 1,045,635 stock options in kneat.com were granted to former holders of Kneat Solutions Limited stock options. In accordance with IFRS 2, *Share-based payment*, the 1,045,635 stock options granted to former Kneat Solutions Limited option holders are treated as though the options were modified although they are legally new options in kneat.com. These kneat.com options have an exercise price of \$0.90, a term of 5 years and vest over varied periods. The incremental value of \$11,654 related to the modification of these options that are fully vested was recorded as an expense in the current period.

In connection with the Transaction, 666,667 kneat.com stock options were granted to former holders of options in Fortune Bay Corp. These options were granted with an exercise price of \$0.90 per share and are fully vested with expiration dates ranging from September 25, 2016 to November 10, 2020.

The following are the weighted-average assumptions used in calculating the value of the stock options granted during the period ended June 30, 2016:

	June 30
	2016
Risk-free interest rate	0.55%
Expected life	1.56 years
Expected volatility	92%
Expected dividend per share	0%
Weighted-average fair value per option	\$0.38

For the six-month period ended June 30, 2016, the estimated value of options earned during the period and recorded in the unaudited condensed interim consolidated statement of loss was \$17,669 (six-month period ended June 30, 2015- \$13,191). The estimated value of options earned during the six-month period ended June 30, 2016 and recorded as an addition to the intangible asset was \$3,983 (six-month period ended June 30, 2015 - \$8,215).

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements**11. EXPENSES BY NATURE**

	Three-month period ended June 30, 2016	Three-month period ended June 30, 2015	Six-month period ended June 30, 2016	Six-month period ended June 30, 2015
	\$	\$	\$	\$
Included in administrative expenses:				
Employee salaries and wages	103,352	98,901	202,202	196,725
Other administrative cost	96,728	53,799	191,159	163,212
Professional fees	296,838	58,686	455,722	115,071
Director and key management salaries	47,550	42,415	95,169	87,397
Social insurance costs	54,065	30,282	100,955	60,791
Software development cost	58,685	28,004	106,955	44,484
Consultancy fees	39,624	52,166	68,454	100,189
Rent and rates	16,274	19,856	26,289	36,971
Regulatory fees	16,000	-	16,000	-
Audit fees	8,919	1,697	40,106	6,194
Depreciation of plant and equipment	17,586	7,761	35,801	12,806
Share-based compensation	14,661	8,962	17,669	13,191
Defined contribution pension cost	2,317	2,122	4,633	4,298
Foreign exchange loss	67,001	-	70,482	-
Research and development tax credit	(41,970)	(103,765)	(73,962)	(187,251)
Total administrative expenses	\$797,630	\$300,886	\$1,357,634	\$654,078

12. INCOME TAXES

The provision for income taxes reported differs from the amounts computed by applying the cumulative Canadian federal and provincial income tax rates to the net loss before tax provision due to the following:

	June 30 2016	June 30 2015
	\$	\$
Loss before income taxes	(5,905,409)	(519,759)
Statutory rate	12.50%	12.50%
Tax recovery at statutory rate	(738,176)	(64,970)
Expense for losses and deductible temporary differences not recognized in current and prior years	198,157	63,321
Permanent differences and other	540,019	1,649
Income tax recovery	-	-

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements**13. SUPPLEMENTAL CASH FLOW INFORMATION**

Net changes in non-cash operating working capital items are as follows:

	Six-months ended June 30 2016	Six-months ended June 30 2015
Accounts receivable and other	\$ 194,905	\$ (39,634)
Directors' current account	(89,105)	(22,047)
Accounts payable, accrued liabilities and deferred income	411,574	(63,643)
	<u>\$ 517,374</u>	<u>\$ (125,324)</u>

14. RELATED PARTY TRANSACTIONS

Amounts payable to officers and directors were \$160,111 as at June 30, 2016 (year-ended December 31, 2015 - \$259,146). During the six-month period ended June 30, 2016, the Company repaid Directors' current account balances of \$89,105 (year-ended December 31, 2015 - \$75,866).

During the period ended June 30, 2015, a Director of Kneat Solutions Limited was granted 2,727 shares of Kneat Solutions Limited valued at \$55,119 as compensation for consulting fees.

Key management of the Company previously included the Board of Directors, the Chief Executive Officer, Director of Research and Development and the Director of Quality. Effective June 27, 2016, key management also includes the Chief Financial Officer.

15. FAIR VALUE OF FINANCIAL INSTRUMENTS AND RISK MANAGEMENT**a) Capital Management**

The Company manages its capital to ensure that it will be able to continue as a going-concern while maximizing the return to stakeholders through the optimization of the debt and equity balance.

The capital of the Company consists of items included in equity, net of cash, as follows:

	June 30 2016	December 31 2015
Equity	\$ 8,126,145	\$ 2,243,068
Less: cash	(7,300,545)	(1,063,524)
	<u>\$ 825,600</u>	<u>\$ 1,179,544</u>

The Company manages its capital structure and makes adjustments in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may issue equity or return capital to shareholders. No changes were made in the objectives, policies or processes for managing capital during the period ended June 30, 2016.

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Notes to the Unaudited Condensed Interim Consolidated Financial Statements

b) Fair Values of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The carrying amounts reported in the statement of financial position for cash, accounts receivable, accounts payable, accrued liabilities and Directors' current account approximate their fair values based on the immediate or short-term maturities of these financial instruments. In addition, non-current accounts receivable, non-current accounts payable, accrued liabilities and the loan payable, although not due in the current year, do not have fair values that differ significantly from their carrying values.

c) Financial Risk Management Objectives

The Company examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include market risk, credit risk, liquidity risk, currency risk, interest rate risk, and commodity price risk. Where material, these risks are reviewed and monitored.

d) Credit Risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company. The carrying amounts of financial assets best represent the maximum credit risk exposure at the reporting date. At June 30, 2016 and December 31, 2015, the Company's financial assets exposed to credit risk amounted to the following:

	June 30, 2016	December 31, 2015
	\$	\$
Cash	7,300,545	1,063,524
Accounts receivable	1,003,467	1,023,014

During the periods ended June 30, 2016 and December 31, 2015, the Company did not hold any financial assets that were past due or impaired. Trade debtors of \$44,346 are included in accounts receivable as at June 30, 2016 (December 31, 2015 - \$230,280). Trade debtors are monitored on a regular basis in order to minimize material aging and to ensure adequate collection.

Cash is held with reputable banks in Ireland and Canada.

e) Liquidity Risk

Liquidity risk is the risk that the Company will not meet its financial obligations as they become due. The Company has a planning and budgeting process to monitor operating cash requirements, including amounts projected for capital expenditures, which are adjusted as input variables change. These variables include, but are not limited to, the ability of the Company to generate revenue from current and prospective customers, general and administrative requirements of the Company and the availability of capital markets. As these variables change, liquidity risks may necessitate the need for the Company to issue equity or obtain debt financing.

The Company is currently negotiating contracts with several customers and is pursuing financing alternatives. There can be no assurance that additional customer revenues will be generated or additional future financings will be available on acceptable terms or at all. If the Company is unable to obtain additional financing when required, the Company may have to substantially reduce or eliminate planned expenditures.

Accounts payables and accrued liabilities are paid in the normal course of business generally according to their terms.

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In the normal course of business, the Company enters into contracts that give rise to commitments for future minimum payments. The following table summarizes the remaining contractual maturities of the Company's financial liabilities.

	Payments due by period as of June 30, 2016				Total
	Within 1 year	2-3 years	4-5 years	Over 5 years	
	\$	\$	\$	\$	\$
Directors' current account	160,111	-	-	-	160,111
Loan payable	-	937,542	-	-	937,542
Accounts payable and accrued liabilities	1,248,379	-	-	-	1,248,379
	1,408,490	937,542	\$-	\$-	2,346,032

f) Currency Risk

Currency risk is the risk that the fair value or future flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Currency risk exposure arises from the Company entering into transactions which are denominated in currencies other than its functional currency.

The Company is exposed to currency risk on its cash balances, accounts receivable, and accounts payable and accrued liabilities that held in currencies that are not in its functional currency, in addition to certain of its operating costs. For the period ended June 30, 2016, the sensitivity of the Company's net loss due to charges in the exchange rate between the functional currency and foreign currencies would not have significantly impacted the statement of loss. The Company currently does not hedge its currency risk.

g) Interest Risk

Interest risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market interest rates.

An immaterial amount of interest rate exposure exists in respect of cash balances and the loan payable on the consolidated statement of financial position. The Company holds a loan payable with a fixed interest rate. These are privately-issued, with no secondary market. They are measured at amortized cost and bear a fixed interest rate. As a result, the Company is not exposed to the cash flow interest rate risk on its loan payable.

h) Fair Value Measurements Recognized in the Statement of Financial Position

The fair value hierarchy establishes three levels to classify the inputs to valuation techniques used to measure fair value. Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

At June 30, 2016 and December 31, 2015, the Company had no financial instruments that were measured and recognized on the unaudited condensed interim consolidated statement of financial position at fair value. In addition, there were no transfers between levels during the period.

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16. COMMITMENTS AND CONTINGENCIES

The Company is from time to time involved in various claims, legal proceedings and complaints arising in the ordinary course of business. The Company does not believe that adverse decisions in any pending or threatened proceedings related to any matter, or any amount which it may be required to pay by reason thereof, will have a material effect on the financial conditions or future results of operations of the Company.

17. SUBSEQUENT EVENT

On July 4, 2016, the Company granted 300,000 kneat.com stock options to former directors and officers of Kneat Solutions Limited. The options are exercisable at a price of \$0.90 per share and expire on July 4, 2021.