



California Nanotechnologies Corp.
Consolidated Financial Statements
For the years ended February 28, 2018 and 2017
(in United States Dollars)

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Independent Auditors' Report

To the Shareholders of California Nanotechnologies Corp.

We have audited the accompanying consolidated financial statements of California Nanotechnologies Corp., which comprise the consolidated statements of financial position as at February 28, 2018 and February 28, 2017, the consolidated statements of loss and comprehensive loss, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of California Nanotechnologies Corp. as at February 28, 2018 and February 28, 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 2 in the consolidated financial statements which describes matters and conditions that indicate the existence of a material uncertainty, which may cast significant doubt about California Nanotechnologies Corp.'s ability to continue as a going concern.

June 26, 2018
Calgary, Alberta

MNP LLP
Chartered Professional Accountants

California Nanotechnologies Corp.
Consolidated Statements of Financial Position
United States Dollars

As at	Note	February 28, 2018	February 28, 2017
ASSETS			
Current assets			
Cash		\$ 36,192	\$ 18,257
Accounts receivable		50,126	67,356
Inventory		39,084	-
Equipment deposit		-	64,240
Prepaid expenses and deposits		19,920	5,781
Total current assets		145,322	155,634
Equipment	6	712,504	48,455
Intangible assets	7	38,890	52,224
Other assets	7	8,615	6,235
Total assets		\$ 905,331	\$ 262,548
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities		\$ 166,816	\$ 88,071
Income taxes payable		3,200	2,400
Interest payable		13,963	3,380
Finance lease obligation – current portion	9	897	822
Bank indebtedness	8	349,825	165,000
Advances from related parties	5	1,045,522	1,045,522
Share purchase warrants	12(b)	11	69,014
Total current liabilities		1,580,234	1,374,209
Bank indebtedness	8	450,175	-
Finance lease obligation – long-term	9	810	1,707
Total liabilities		2,031,219	1,375,916
Shareholders' deficit			
Share capital	12	2,902,277	2,902,277
Contributed surplus	14	280,961	246,167
Deficit		(4,309,126)	(4,261,812)
Total shareholders' deficit		(1,125,888)	(1,113,368)
Total liabilities and shareholders' deficit		\$ 905,331	\$ 262,548
Going concern	2		

“signed” David Grant
Director

“signed” Roger Dent
Director

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

California Nanotechnologies Corp.
Consolidated Statements of Loss and Comprehensive Loss
United States Dollars
For the years ended February 28, 2018 and 2017

	Note	2018	2017
Revenue		\$ 548,575	\$ 543,534
Cost of goods sold		186,470	236,506
Gross margin		362,105	307,028
Expenses			
Advertising and promotion		25,704	36,257
Depreciation and amortization - equipment and intangible assets	6, 7	64,135	22,365
Consulting		27,030	36,081
Office		27,840	28,299
Professional fees		49,342	36,815
Repairs and maintenance		4,521	11,522
Research and development		17,858	23,430
Salaries, wages and benefits		116,543	252,927
Supplies		49,657	26,311
Travel and entertainment		11,455	4,284
Share-based compensation	12(c)	34,794	24,313
		428,879	502,604
Loss from operations		(66,774)	(195,576)
Other income (expense)			
Foreign exchange loss		(566)	(1,257)
Interest expense		(48,177)	(24,079)
Unrealized gain (loss) on share purchase warrants	12(b)	69,003	(48,051)
Loss before income taxes		(46,514)	(268,963)
Provision for income taxes	10	800	800
Net loss and comprehensive loss		\$ (47,314)	\$ (269,763)
Loss per share - basic	13	\$ -	\$ (0.01)
- diluted	13	-	(0.01)
Weighted average shares outstanding - basic	13	31,430,296	31,368,378
- diluted	13	31,430,296	31,368,378

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

California Nanotechnologies Corp.
Consolidated Statements of Changes in Equity
United States Dollars
For the years ended February 28, 2018 and 2017

	Note	Share capital	Contributed surplus	Deficit	Total
Balance at February 29, 2016		\$ 2,889,969	\$ 226,469	\$ (3,992,049)	\$ (875,611)
Shares issued upon option exercise	12(b)	12,308	(4,615)	-	7,693
Share-based compensation	12(c)	-	24,313	-	24,313
Net loss and comprehensive loss		-	-	(269,763)	(269,763)
Balance at February 28, 2017		\$ 2,902,277	\$ 246,167	\$ (4,261,812)	\$ (1,113,368)
Share-based compensation	12(c)	-	34,794	-	34,794
Net loss and comprehensive loss		-	-	(47,314)	(47,314)
Balance at February 28, 2018		\$ 2,902,277	\$ 280,961	\$ (4,309,126)	\$ (1,125,888)

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

California Nanotechnologies Corp.
Consolidated Statements of Cash Flows
United States Dollars
For the years ended February 28, 2018 and 2017

	Note	2018	2017
Cash provided by (used for) the following activities			
Operating activities			
Net loss and comprehensive loss		\$ (47,314)	\$ (269,763)
Depreciation and amortization - equipment and intangible assets	6,7	64,135	22,365
Unrealized (gain) loss on share purchase warrants	12(b)	(69,003)	48,051
Share-based compensation	12(c)	34,794	24,313
		<u>(17,388)</u>	<u>(175,034)</u>
Changes in working capital accounts			
Accounts receivable		17,230	(20,496)
Inventory		(39,084)	
Prepaid expenses and deposits		(14,139)	1,701
Income taxes payable		800	800
Accounts payable and accrued liabilities		78,745	(8,480)
Interest payable		10,583	3,380
Net cash provided by (used for) operating activities		36,747	(198,129)
Financing activities			
Issue of shares upon option exercise	12(b)	-	7,693
Repayment of finance lease obligation	9	(822)	(754)
Advances from credit line	8	85,000	195,000
Repayments to credit line		-	(30,000)
Advances from equipment loan	8	550,000	-
Net cash provided by financing activities		634,178	171,939
Investing activities			
Deposits for equipment	6	-	(64,240)
Purchase of equipment	6	(650,610)	-
Deposits for patent		(2,380)	-
Net cash used for investing activities		(652,990)	(64,240)
Increase (decrease) in cash resources		17,935	(90,430)
Cash, beginning of year		18,257	108,687
Cash, end of year		\$ 36,192	\$ 18,257

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

California Nanotechnologies Corp.
Notes to the Consolidated Financial Statements
United States Dollars

For the years ended February 28, 2018 and February 28, 2017

1. Incorporation and operations

Veritek Technologies Inc. was incorporated under the laws of the Province of Alberta on May 19, 2002. On February 1, 2007, the Company changed its name to California Nanotechnologies Corp. (the “Company”) in connection with the reverse takeover with California Nanotechnologies Inc. The consolidated financial statements of the Company for the year ended February 28, 2018 include the accounts of the Company and its wholly-owned subsidiaries. Its head office, research and development, and production operations are located at 17220 Edwards Road, Cerritos, California, U.S.A, 90703. A corporate, registered office is located at 900 - 517 - 10th Avenue S.W., Calgary, Alberta T2R 0A8. Since the date of the reverse takeover, the Company has been devoted to the development of nanocrystalline materials through grain size reduction. The advantages of these materials include improved strength and ductility. The Company's target markets are Aerospace, Defense, Automotive, Medical and Sports and Recreation. Since the most significant portion of the Company's operations is located in the United States and its functional currency is denominated in United States dollars, these consolidated financial statements are presented in United States dollars. The Company is listed for trading on the TSX Venture Exchange under the symbol CNO and in the United States on the OTCQB under the symbol CANOF. These consolidated financial statements were authorized for issue in accordance with a resolution by the Board of Directors on June 26, 2018.

2. Going concern

These consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due.

The Company has a net loss and comprehensive loss for the year of \$47,314 (2017 - \$269,763). In addition, the Company has an accumulated deficit of \$4,309,126 (2017 - \$4,261,812). These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern.

The Company's ability to continue as a going concern is dependent upon its ability to attain profitable operations and generate funds there from, and to continue to obtain equity investment and borrowings sufficient to meet current and future obligations and/or restructure the existing debt and payables. The related party will provide support for any deficits in the realization of assets and the payment of liabilities in the ordinary course of business. These consolidated financial statements do not reflect the adjustments or reclassification of assets and liabilities which would be necessary if the Company were unable to continue its operations that could be material.

3. Significant accounting policies

These consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and the International Financial Reporting Interpretations Committee (“IFRIC”) in effect at March 1, 2017. The principal accounting policies are set out below.

Any standards and interpretations that have been issued but are not yet effective, and that are available for early application, have not been applied by the Company in these consolidated financial statements. The impact of these standards and interpretations on the Company is still to be assessed.

The preparation of consolidated financial statements requires management to make estimates and judgments that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. The consolidated financial statements have, in management's opinion, been properly prepared using careful judgment with reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

California Nanotechnologies Corp.
Notes to the Consolidated Financial Statements
United States Dollars

For the years ended February 28, 2018 and February 28, 2017

3. Significant accounting policies – continued

(a) Consolidation

The Company has consolidated the assets, liabilities, revenues and expenses of the subsidiaries after the elimination of intercompany transactions and balances. These consolidated financial statements include the accounts of the Company, and its wholly owned subsidiaries, California Nanotechnologies Inc. and White Roof Solutions, Inc.

(b) Basis of measurement

These consolidated financial statements have been prepared on a going concern basis, using the historical cost convention except for share-based compensation and certain financial instruments assets classified as fair value through profit or loss or available-for-sale which are measured at fair value. In addition, they have been prepared on an accrual basis of accounting except for cash flow information.

(c) Inventory

Inventories are carried at the lower of cost and net realizable value. Cost is determined using the first-in, first-out method. The cost of finished goods and work-in-progress comprises raw materials, direct labour, and other direct costs (based on normal operating capacity) but excludes borrowing costs.

(d) Revenue recognition

Revenue is recognized when obligations under the terms of a contract with our customer have been satisfied; generally this occurs with the transfer of our parts or services. Revenue and related cost is measured and the amount of consideration we expect to receive in exchange for the transfer of goods or providing services can be reasonably assured.

The Company recognizes revenue and profits from services on the percentage of completion basis, and accordingly costs are expensed as incurred and revenue is recognized only to the extent of contract costs incurred that will be recoverable. Expected losses are recognized immediately when it is probable that total contract costs will exceed total contract revenue.

(e) Cash

Cash includes balances with banks. Any cheques issued in excess of cash are covered with the Company's overdraft protection in the amount of \$30,000 within three months of their issuance.

(f) Business combinations

The Company uses the acquisition method of accounting to account for business combinations. The consideration transferred is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Company. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date.

(g) Equipment

Equipment is carried at historical cost less accumulated depreciation. Depreciation is provided using the straight-line method and is calculated over the estimated useful life of the assets, which has been estimated as seven years for nanotechnology equipment and three years for roof coating equipment. Borrowing costs are capitalized that are directly attributable to the construction of equipment are capitalized. The Company reviews the criteria for capitalization and the useful life of its equipment on an on-going basis considering changes in circumstances.

3. Significant accounting policies – continued

(g) Equipment-continued

When the cost of a part of an item of equipment is significant in relation to the total cost of an item and the items have different useful lives, they are accounted for as separate items (significant components) of equipment. The costs of day-to-day servicing of equipment are recognized in direct operating expenses. Gains or losses on disposal of an item of equipment is determined by comparing the proceeds from disposal with the carrying amount of equipment, and are recognized net within net loss in the consolidated statements of loss and comprehensive loss. Depreciation methods, useful lives and residual values are reviewed at the end of each reporting period and adjusted if appropriate.

(h) Leased assets

Leases in terms of which the Company assumes substantially all of the risks and rewards of ownership are classified as finance leases and are capitalized at the commencement of the lease term at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset. Other leases are operating leases and are not recognized on the Company's consolidated statement of financial position.

(i) Intangible assets

Intangible assets are comprised of customer relationships, trade secrets, use of operating rights and contract intangibles. Intangible assets are recorded at cost less any accumulated amortization and/or impairment losses. Intangible assets are amortized on a straight-line basis over their estimated useful life of 15 years and are assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization method and period of an intangible asset is reviewed at least annually.

Patents are recorded at cost and are amortized on a straight-line basis over a period of ten years based on management's analysis of the market and competition. Patents represent accumulated costs and are not intended to reflect present or future values. The recoverability of these amounts is dependent upon future profitable operations.

(j) Impairment of non-financial assets

The Company assesses, at the end of each reporting period, whether there is an indication that an asset group may be impaired. If any indication of impairment exists, the Company estimates the recoverable amount of the asset group. External triggering events include, for example, changes in customer or industry dynamics, other technologies and economic declines. Internal triggering events for impairment include lower profitability or planned restructuring. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets, cash generating units ("CGU").

If the carrying amount of the asset, or its respective CGU, exceeds its estimated recoverable amount, the difference is recognized as an impairment charge. The Company's corporate assets, which do not generate separate cash inflows, are allocated to the CGUs on a reasonable basis for impairment testing purposes.

The Company's impairment tests compare the carrying amount of the asset or CGU to its recoverable amount. The recoverable amount is the higher of fair value less costs of disposal ("FVLCD") and value in use ("VIU"). FVLCD is the amount obtainable from the sale of an asset or CGU in an arm's length transaction of similar assets or observable market prices, less the costs of disposal. The determination of VIU requires the estimation and discounting of cash flows which involves key assumptions that consider all information available on the respective testing date. Management uses its judgment, considering past and actual performance as well as expected developments in the respective markets and in the overall macro-economic environment and economic trends to model and discount future cash flows.

California Nanotechnologies Corp.
Notes to the Consolidated Financial Statements
United States Dollars

For the years ended February 28, 2018 and February 28, 2017

3. Significant accounting policies – continued

(k) Provisions

Provisions cover risks resulting from legal disputes and proceedings. In order to determine the amount of the provisions, the facts related to each case, the size of the claim, awards in similar cases, the expected timing of such possible awards, insurance coverage and deductibles and independent expert advice are considered along with assumptions regarding the probability of a successful claim and the range of possible awards. The actual costs can deviate from these estimates.

A provision is recognized in the consolidated financial statements when the Company has a material obligation, whether existing or potential, as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the obligation is determined to be material, then the estimated amount of the provision is determined by discounting the expected future cash outflows. At February 28, 2018 and February 28, 2017 there were no provisions recognized in the consolidated financial statements.

(l) Income taxes

Income tax expense for the year consists of current and deferred tax. Deferred tax is recognized in the consolidated statement of loss and comprehensive loss, except to the extent that it relates to a business combination or items recognized in other comprehensive loss (“OCL”) or directly in equity.

Taxable income differs from income as reported in the consolidated statements of loss and comprehensive loss. As a result, current tax is the expected tax due on taxable income less adjustments to prior periods using tax rates enacted, or substantively enacted as at the reporting date in jurisdictions where the Company operates.

In general, deferred taxes are recognized based on temporary differences arising between the tax value of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax liabilities are not recognized and are not accounted for if they arise from the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable income. Deferred taxes are calculated on the basis of the tax laws enacted or substantively enacted as at the reporting date and apply to when the related deferred tax asset is realized or the deferred tax liability is settled.

Current and deferred tax assets and liabilities are offset when there is a legally enforceable right to settle on a net basis and when such assets and liabilities relate to income taxes imposed by the same taxation authority.

(m) Foreign exchange

These consolidated financial statements have been presented in United States (U.S.) dollars, the functional currency of the Company's operations. Monetary assets and liabilities denominated in foreign currencies are translated into U.S. dollars at the foreign exchange rate in effect at the statement of financial position date. Revenue and expense transactions in foreign currencies are translated to the appropriate functional currency at the foreign exchange rate on the date of the transaction with all consequential exchange differences recognized in net loss and comprehensive loss.

Non-monetary assets that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transactions. All resulting exchange differences from translation of the functional currency into a different reporting currency are recognized as a separate component of OCL.

3. Significant accounting policies – continued

(n) Share-based compensation plan

The Company provides equity-settled share-based payments in the form of a share option plan to its employees, officers, directors and consultants. The Company accounts for these share options using the fair value method of accounting for share-based compensation. Under this method, the associated compensation expense is charged to net loss and comprehensive loss with a corresponding increase to contributed surplus less an estimated forfeiture rate over each vesting period (tranches) of the options granted. The forfeiture rate is based on past experience of actual forfeitures. Each tranche is treated as a separate share option grant, and subsequently valued at the start of each tranche's vesting period.

Share-based compensation transactions with non-employees are measured at the fair value of the goods or services recovered. However, if the fair value cannot be estimated reliably, the share-based compensation transaction is measured at the fair value of the equity instruments granted at the date the non-employee provides the goods or services.

(o) Per share amounts

Basic loss per share is calculated using the weighted average number of shares outstanding during the period. The Company follows the treasury stock method for the computation of diluted per share amounts. This method assumes the proceeds from the exercise of dilutive options and warrants are used to purchase common shares at the weighted average market price during the period.

(p) Research and development expenses

Expenses related to research and development activities that do not meet generally accepted criteria for deferral are expensed as incurred, net of related tax credits and government grants. Development expenses that meet generally accepted criteria for deferral, in accordance with the IAS 38, "Intangible Assets", are capitalized, net of related tax credits and government grants, and are amortized against net loss and comprehensive loss over the estimated benefit period. The Company assesses, at the end of each reporting period, whether there is an indication the assets may be impaired. If any indication of impairment exists, the Company estimates the recovery amount of the assets. Research and development expenses are mainly comprised of salaries and related expenses, material costs as well as fees paid to third party consultants.

(q) Financial instruments

All financial instruments are required to be measured at fair value on initial recognition of the instrument. Measurement in subsequent periods depends on whether the financial instrument has been classified as "fair value through profit or loss", "available-for-sale", "held-to-maturity", "loans and receivables", or "other financial liabilities" as defined by the standard.

Financial assets and financial liabilities at "fair value through profit or loss" are measured at fair value with changes in fair value recognized in net loss and comprehensive loss. Financial assets classified as "available-for-sale" are measured at fair value, with changes in fair value recognized in OCL. Transaction costs related to financial assets and liabilities recorded at fair value are included in net loss and comprehensive loss when incurred. Financial assets classified as "held-to-maturity", "loans and receivables" and financial liabilities classified as "other financial liabilities" are initially recorded at fair value plus transaction costs and are subsequently measured at amortized cost using the effective interest method of amortization.

3. Significant accounting policies – continued

(q) Financial instruments - continued

Cash and share purchase warrants are designated as "fair value through profit or loss". Accounts receivable are designated as "loans and receivables". Accounts payable and accrued liabilities, bank indebtedness, and advances from related parties are designated as "other liabilities".

Financial instruments measured at fair value on the consolidated statement of financial position require classification into one of the following levels of the fair value hierarchy:

- Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 - Inputs other than quoted prices listed in Level 1 that are observable for the asset or liability either directly or indirectly;
- Level 3 - Inputs that are not based on observable market data.

The fair value hierarchy level at which a fair value measurement is categorized is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

A financial asset, except for those classified as "fair value through profit or loss," is assessed at each reporting date to determine whether it is impaired based on objective evidence indicating that one or more events have had a negative effect on the estimated future cash flows of that asset. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the net present value of the estimated future cash flows discounted at the original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognized in net loss and comprehensive loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized.

(r) Significant accounting estimates and judgments

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and judgments that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent assets and liabilities at the reporting date. On an ongoing basis, management evaluates its judgments and estimates in relation to revenue, expenses, assets and liabilities. Management uses historical experience and various other factors it believes to be reasonable under the given circumstances as the basis for its judgments and estimates. Actual outcomes may differ from these estimates under different assumptions and conditions.

The following are the most significant accounting judgments and estimates made by the Company in applying accounting policies:

Judgments

Determining CGU's

For the purpose of assessing impairment of tangible and intangible assets, assets are grouped at the lowest level of separately identified cash inflows which make up the CGU. Determination of what constitutes a CGU is subject to management judgment. The asset composition of a CGU can directly impact the recoverability of assets included within the CGU. In assessing the recoverability of tangible and intangible assets, each CGU's carrying value is compared to the greater of its FVLCD and VIU.

3. Significant accounting policies – continued

(r) Significant accounting estimates and judgments - continued

Deferred taxes

Uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable earnings will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable earnings together with future tax planning strategies.

Estimates

Valuation of loans and receivables

Loans and receivables are reviewed on a regular basis to estimate recoverability of balances. Loans and receivables are stated after evaluation as to their collectability and an appropriate allowance for doubtful accounts is provided where considered necessary.

Inventory

Inventories are carried at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and any applicable variable selling expenses.

Share-based compensation and share purchase warrants

The Corporation uses an option pricing model to determine the fair value of share-based compensation and share purchase warrants. Inputs to the model are subject to various estimates about volatility, interest rates, dividend yields, forfeiture rates and expected life of the units issued. Fair value inputs are subject to market factors as well as internal estimates. The Company considers historic trends together with any new information to determine the best estimate of fair value at the date of grant.

Depreciation and amortization

The consolidated financial statements include estimates of the useful economic life of equipment and intangible assets. Due to varying assumptions required to be made with regards to future recoverability of these assets, the depreciation and amortization recorded by management is based on their best estimate in this regard and may be significantly different from those determined based on future operational results.

(s) New accounting policies

For the twelve months ended February 28, 2018, the Company did not adopt any new IFRS standards.

(t) Recent accounting pronouncements

In May 2014, the IASB issued IFRS 15 “Revenue from Contracts with Customers”, which replaces International Accounting Standard (“IAS”) 18 “Revenue”, IAS 11 “Construction Contracts”, and related interpretations. The standard is required to be adopted either retrospectively or using a modified transition approach for fiscal years beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 15 will be applied by the Company on March 1, 2018 and the Company is currently evaluating the impact of the standard on its consolidated financial statements.

California Nanotechnologies Corp.
Notes to the Consolidated Financial Statements
United States Dollars

For the years ended February 28, 2018 and February 28, 2017

3. Significant accounting policies – continued

(t) Recent accounting pronouncements - continued

In July 2014, the IASB completed the final elements of IFRS 9 “Financial Instruments”. The standard supersedes earlier versions of IFRS 9 and completes the IASB’s project to replace IAS 39 “Financial Instruments: Recognition and Measurement”. IFRS 9, as amended, includes a principle-based approach for classification and measurement of financial assets, a single ‘expected loss’ impairment model and a substantially reformed approach to hedge accounting. The standard will come into effect for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. IFRS 9 will be applied on a retrospective basis by the Company on March 1, 2018 and the Company is currently evaluating the impact of the standard on its consolidated financial statements.

In January 2016, the IASB issued IFRS 16 “Leases”, which replaces IAS 17 “Leases”. For lessees applying IFRS 16, a single recognition and measurement model for leases would apply, with required recognition of assets and liabilities for most leases. The standard will come into effect for annual periods beginning on or after January 1, 2019, with earlier adoption permitted if the entity is also applying IFRS 15 “Revenue from Contracts with Customers”. IFRS 16 will be applied by the Company on March 1, 2019 and the Company is currently evaluating the impact of the standard on its consolidated financial statements.

4. Inventory

The major components of inventory are classified as follows:

	February 28, 2018	February 28, 2017
Raw materials	\$ 37,228	-
Finished goods	1,855	-
	\$ 39,084	-

The cost of finished goods inventories recognized as expense and included in cost of goods sold was \$7,874 (2017 - \$nil). There were no recurring inventory write-downs included in cost of goods sold.

5. Related party transactions

Advances from related parties are from a related entity that owns 18% of the Company’s shares. The advances bear interest at 2% per annum and is due upon demand. There are no set terms for repayment and the loan is secured by all the assets of the Company. Interest was paid in the amount of \$3,727 (2017 - \$17,619) on the advances with accrued interest in the amount of \$158,167 (2017 – \$140,921). The current year amount is included in accounts payable. This related entity also engaged with the Company for revenue of \$31,158 (2017 – \$166,456) and incurred expenses of \$48,479 (2017 – \$50,960). The transactions are considered to be in the normal course of operations and are initially recognized at their fair value.

	February 28, 2018	February 28, 2017
Advances from related parties	\$ 1,045,522	\$ 1,045,522

California Nanotechnologies Corp.
Notes to the Consolidated Financial Statements
United States Dollars

For the years ended February 28, 2018 and February 28, 2017

5. Related party transactions - continued

Significant subsidiaries:

The table below provides information relative to California Nanotechnologies Corp.'s significant subsidiaries, including the entity's name, its jurisdiction of incorporation/formation, the percentage of securities directly or indirectly owned by California Nanotechnologies Corp., and the market areas served, if applicable.

Company (Jurisdiction of Incorporation/ Formation)	Percentage of ownership by California Nanotechnologies Corp.	Overview	Market Area
California Nanotechnologies Inc. (California, USA)	100%	Wholly-owned subsidiary of California Nanotechnologies Corp. which was formed and incorporated on February 4, 2005. It is the head office which conducts research and development, and materials processing.	USA
White Roof Solutions Inc. (California, USA)	100%	Wholly-owned subsidiary of California Nanotechnologies Inc. which was formed and incorporated on May 21, 2012. It conducts sales and the application of white solar reflective roof coatings.	USA

6. Equipment

	Nanotechnology equipment	Roof coating equipment	Totals
Cost			
At February 29, 2016 and February 28, 2017	\$ 961,940	\$ 8,520	\$ 970,460
Additions	714,850	-	714,850
At February 28, 2018	\$ 1,676,790	\$ 8,520	\$ 1,685,310
Accumulated depreciation			
At February 29, 2016	\$ 904,453	\$ 8,520	\$ 912,973
Depreciation	9,032	-	9,032
At February 28, 2017	913,485	8,520	922,005
Depreciation	50,801	-	50,801
At February 28, 2018	\$ 964,286	\$ 8,520	\$ 972,806
Net book value			
At February 28, 2017	48,455	-	48,455
At February 28, 2018	\$ 712,504	-	\$ 712,504

Nanotechnology equipment includes equipment with a cost of \$4,084 (2017 - \$4,084) and a net book value of \$2,236 (2017 - \$2,820) under finance lease obligation (See note 9). During the year, the Company added a production SPS system with a cost of \$675,750.

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7. Intangible assets

	Trade secrets	Use of operating rights	Customer list	Customer contract	Total
Cost					
At February 29, 2016, February 28, 2017, and February 28, 2018	\$ 100,000	\$ 50,000	\$ 27,000	\$ 23,000	\$ 200,000
Accumulated amortization					
At February 29, 2016	\$ 67,224	33,610	18,150	\$ 15,459	134,443
Amortization	6,667	3,333	1,800	1,533	13,333
At February 28, 2017	\$ 73,891	\$ 36,943	\$ 19,950	\$ 16,992	\$ 147,776
Amortization	6,666	3,334	1,800	1,534	13,334
At February 28, 2018	\$ 80,557	\$ 40,277	\$ 21,750	\$ 18,526	\$ 161,110
Net book value					
At February 28, 2017	\$ 26,109	\$ 13,057	\$ 7,050	\$ 6,008	\$ 52,224
At February 28, 2018	\$ 19,443	\$ 9,723	\$ 5,250	\$ 4,474	\$ 38,890

Included in other assets are deposits in expectation of a patent in the amount of \$8,615, which was subsequently issued on April 17, 2018.

8. Bank indebtedness

Effective September 2016, the Company established a new long-term primary credit facility (the "Credit Agreement") with total credit facilities of up to \$250,000, comprised of a commercial advance line in the amount of \$250,000, bearing interest at the prime rate plus one-half of one percent (0.50%) maturing on May 31, 2018. Subsequent to year-end, the maturity date was extended to June 30, 2018. The Credit Agreement is secured by all the accounts, inventory, equipment, and general intangibles of the Company and guaranteed by a related party.

Effective February 2017, the Company increased the long-term primary credit facility up to \$800,000, adding an equipment advance line in the amount of \$550,000, bearing interest at the prime rate plus one-half of one percent (0.50%) maturing on May 31, 2023, with monthly principal payments commencing March 31, 2018 for a period of 60 months.

Less: current portion

	February 28, 2018	February 28, 2017
	\$ 250,000	\$ 165,000
	550,000	-
	<u>(349,825)</u>	<u>(165,000)</u>
	\$ 450,175	\$ -

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8. Bank indebtedness –continued

Interest of \$26,435 (2017 - \$nil) related to the long-term credit facilities has been recorded as interest expense in the consolidated statements of net loss and comprehensive loss for the fiscal year ended February 28, 2018.

Future minimum payments related to the long-term credit facilities are as follows:

2018-9	\$ 375,810
2019-20	125,810
2020-21	125,810
2021-22	125,810
Thereafter	<u>125,810</u>
	879,050
Less: interest	<u>(79,050)</u>
	800,000
Less: current portion	<u>(349,825)</u>
	<u>\$ 450,175</u>

9. Finance lease obligation

Equipment under a finance lease payable in equal month installments of \$84 which includes implied interest of 8.7%. The lease matures on December 16, 2019 and is secured against the equipment under finance lease with a net book value of \$2,236 (2017 - \$2,820).

February 28, 2018 February 28, 2017

The lease matures on December 16, 2019 and is secured against the equipment under finance lease with a net book value of \$2,236 (2017 - \$2,820).

\$ **1,707** \$ 2,529

Less: current portion

(897) (822)

\$ **810** \$ 1,707

Interest of \$189 (2017 - \$282) related to the finance lease has been recorded as interest expense in the consolidated statements of loss and comprehensive loss for the year ended February 28, 2018.

Future minimum lease payments related to obligations under finance lease are as follows:

2018-9	\$ 1,011
2019	<u>843</u>
	1,854
Less: implied interest	<u>(147)</u>
	1,707
Less: current portion	<u>(897)</u>
	<u>\$ 810</u>

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10. Income taxes

	<u>February 28, 2018</u>	<u>February 28, 2017</u>
Statutory tax rate	27.00%	27.00%
Income taxes recovery at the statutory rate	\$ (12,559)	\$ (72,620)
Share-based compensation	9,394	6,565
Other	(18,523)	(12,390)
Change in deferred tax asset not recognized	22,488	79,245
	<u>\$ 800</u>	<u>\$ 800</u>

Principal components of deferred tax asset (liability) are:

	<u>February 28, 2018</u>	<u>February 28, 2017</u>
Deferred tax:		
Unused tax losses carry forward - US (1)	\$ 1,538	\$ 2,101
Equipment - US	(1,538)	(2,101)
	<u>\$ -</u>	<u>\$ -</u>

Details of the unrecognized deductible temporary differences are as follows:

	<u>February 28, 2018</u>	<u>February 28, 2017</u>
Deferred tax:		
Unused tax losses carry forward - US (1)	\$ 3,618,248	\$ 3,572,815
Unused tax losses carry forward - Canada (1)	763,497	812,663
Share issuance costs	-	8,228
Disallowed interest - US	16,694	16,694
	<u>\$ 4,398,439</u>	<u>\$ 4,410,400</u>

(1) Consists of U.S. Federal and State tax losses in the approximate amount of \$3,606,000 expiring at various dates commencing 2025. Canadian tax losses in the approximate amount of \$826,000 expiring at varying dates commencing 2017.

11. Compensation of Key Management Personnel

The remuneration of key management personnel during the year was as follows:

	<u>February 28, 2018</u>	<u>February 28, 2017</u>
Remuneration	\$ 67,712	\$ 61,819

Key management personnel of the Company include the CEO and COO. For the fiscal year ended February 28, 2018, the Company did not pay the current Chief Executive Officer (2017 - \$nil). It is management's estimate that the fair value salary would approximate \$150,000. Due to the lack of independent evidence with respect to the fair value of these services, this transaction has been recorded at the carrying amount of \$nil.

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12. Share capital

(a) Authorized:

Unlimited number of Class "A" Common shares, without nominal or par value.

(b) Issued:

	Number	Amount
Total issued and outstanding, February 29, 2016	31,230,296	\$ 2,889,969
Issued upon exercise of options	200,000	12,308
Total issued and outstanding, February 28, 2017 and February 28, 2018	31,430,296	\$ 2,902,277

On June 17, 2016, 200,000 options were exercised for total proceeds of \$7,693. The fair value of the options exercised was \$0.04 per option, resulting in a total charge to share capital of \$12,308 and a charge to contributed surplus of \$4,615.

On April 9, 2014, the Company completed a private placement of 5,290,296 units at \$0.135 Canadian Dollars ("CAD") per unit for total proceeds of \$714,190 CAD. Each unit was comprised of one common share and one-half of one common share purchase warrant exercisable at \$0.225 CAD per common share until April 9, 2015. The ascribed values of the warrants were determined using the Black-Scholes fair value pricing model based on a risk free rate of 1.06%, expected volatility of 167.9% and an expected life of one year.

Since April 9, 2014 various extensions of the warrants' expiration date have been approved by the TSV Venture Exchange with a current extension of the share purchase warrants to April 8, 2018, which have expired subsequent to the report date. As the exercise price of the share purchase warrants are fixed in Canadian dollars and the functional currency of the Company is the U.S. dollar, the warrants are considered a derivative, as a variable amount of cash in the Company's functional currency will be received on exercise. At February 28, 2018, the fair value of share purchase warrants issued and outstanding with Canadian dollar exercise prices was \$11 (2017 - \$69,014). The share purchase warrants are re-measured at fair value at each statement of financial position date with the change in fair value recorded in net loss and comprehensive loss during the period of change. The fair value of share purchase warrants is reclassified to equity upon exercise. The ascribed values of the warrants were determined using the Black-Scholes fair value pricing model based on a risk free rate of 1.74%, expected volatility of 108% and expected life of 0.1 years.

Warrants

	Number	Amount
Total issued and outstanding, February 29, 2016	2,645,148	\$ 20,963
Unrealized loss on share purchase warrants	-	48,051
Total issued and outstanding, February 28, 2017	2,645,148	\$ 69,014
Unrealized gain on share purchase warrants	-	(69,003)
Total issued and outstanding, February 28, 2018	2,645,148	\$ 11

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12. Share capital - continued

(c) Options - Directors, Officers, Employees and Consultants

The Company has a stock option plan for directors, officers, employees and consultants. Stock options can be issued up to a maximum number of common shares equal to 10% of the issued and outstanding common shares of the Company. The exercise price of options granted is not less than the market price of the common shares traded and along with the vesting period, is determined by the Board of Directors. Options granted have a term of up to 5 years.

	Number of Options	Weighted Average price (CAD)
Balance, February 29, 2016	2,580,000	\$ 0.08
Granted	1,625,000	0.08
Forfeited	(200,000)	0.05
Expired	(805,000)	0.08
Forfeited	(750,000)	0.08
Balance, February 28, 2017	2,450,000	\$ 0.07
Granted	25,000	0.14
Expired	(25,000)	0.10
Forfeited	(175,000)	0.07
Balance, February 28, 2018	2,275,000	\$ 0.07

During the year ended February 28, 2018, the Company recorded \$34,794 in share-based compensation expense (2017 - \$24,313). The weighted average fair value of the options granted during the year was \$0.08 (2017 - \$0.07), and was estimated using the Black Scholes option-pricing model with the following assumptions:

Risk free interest rate (%)	1.1
Expected term (years)	1-3
Expected volatility (%)	145-156
Dividend per share	-
Forfeiture rate (%)	10.67

California Nanotechnologies Corp.
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12. Share capital - continued

(c) Options - Directors, Officers, Employees and Consultants - continued

The following tables summarize information about stock options outstanding at February 28, 2018:

Options Outstanding			Options Exercisable		
Exercise Price	Number of options	Weighted Average of Remaining Contractual Life (years)	Weighted Average Exercise Price (CAD)	Number of Options	Weighted Average Exercise Price (CAD)
\$ 0.06 - 0.14	2,275,000	2.3	\$ 0.07	1,299,992	\$ 0.07

The following tables summarize information about stock options outstanding at February 28, 2017:

Options Outstanding			Options Exercisable		
Exercise Price	Number of options	Weighted Average of Remaining Contractual Life (years)	Weighted Average Exercise Price (CAD)	Number of Options	Weighted Average Exercise Price (CAD)
\$ 0.05 - 0.12	2,450,000	3.4	\$ 0.07	974,999	\$ 0.06

13. Loss per share

The basic loss per common share is calculated by dividing net loss and comprehensive loss by the weighted-average number of common shares outstanding. The diluted loss per common share is calculated using net loss and comprehensive loss divided by the weighted-average number of diluted common shares outstanding during the year.

14. Contributed surplus

	February 28, 2018	February 28, 2017
Balance, beginning of year	\$ 246,167	\$ 226,469
Share-based compensation (12(c))	34,794	24,313
Exercise of options (12(b))	-	(4,615)
Balance, end of year	<u>\$ 280,961</u>	<u>\$ 246,167</u>

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15. Financial instruments

Financial instruments of the Company consist of cash, accounts receivable, share purchase warrants, accounts payable and accrued liabilities, finance lease obligation, bank indebtedness and advances from related parties.

	February 28, 2018		February 28, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
At fair value through profit or loss				
Cash	\$ 36,192	\$ 36,192	\$ 18,257	\$ 18,257
Share purchase warrants	11	11	69,014	69,014
Loans and receivables				
Accounts receivable	50,126	50,126	67,356	67,356
Other liabilities				
Accounts payable and accrued liabilities	166,816	166,816	88,071	88,071
Finance lease obligation	1,707	1,707	2,529	2,529
Bank indebtedness	800,000	800,000	165,000	165,000
Advances from related parties	1,045,522	1,045,522	1,045,522	1,045,522

The table below sets out fair value measurements using fair value hierarchy.

	Total	Level 1	Level 2	Level 3
Assets				
Cash	\$ 36,192	\$ 36,192	\$ -	\$ -
Share purchase warrants	11	-	11	-

There have been no transfers during the period between Levels 1, 2 and 3.

The carrying values of accounts receivable, accounts payable and accrued liabilities, advances from related parties, current portion of the finance lease obligation and current portion of the bank indebtedness approximate their fair value due to their short-term nature.

The fair value of the Company's finance lease obligation approximate its fair values due to the interest rates applied to these instruments, which approximate market interest rates.

As disclosed above, the Company holds various forms of financial instruments. The nature of these instruments and the Company's operations expose the Company to various risks. The Company manages its exposure to these risks by operating in a manner that minimizes its exposure to the extent practical. The Company does not use off statement of financial position contracts to manage these risks.

Liquidity Risk

The Company defines liquidity risk as the financial risk that the Company will encounter difficulties meeting its obligations associated with financial liabilities. The Company's objective for managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. This risk is mitigated by managing the cash flow by controlling receivables and payables to vendors and related parties. At February 28, 2018, the Company had a working capital deficiency of \$1,434,912 (2017 – \$1,218,575) (Note 2).

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15. Financial instruments - continued

Foreign currency risk

A portion of the Company's operations are located outside of the U.S. and, accordingly, the related financial assets and liabilities are subject to fluctuations in exchange rates.

The Company manages its exposure to foreign currency fluctuations by maintaining foreign currency bank accounts and receivables to offset foreign currency payables and planned expenditures. At February 28, 2018, the Company had the following balances denominated in Canadian dollars. The balances have been translated into U.S. currency in accordance with the Company's foreign exchange accounting policy.

	U.S. Dollar February 28, 2018	U.S. Dollar February 28, 2017
Cash/(bank overdraft)	\$ 1,581	\$ (26)
Accounts payable and accrued liabilities	36,947	32,744

The Company operates with a U.S. dollar functional currency which gives rise to currency exchange rate risk on the Company's Canadian dollar denominated monetary assets and liabilities, such as Canadian dollar bank accounts and accounts payable, as follows:

	Impact on Net Loss
U.S. Dollar Exchange Rate – 10% increase	\$ 4,935
U.S. Dollar Exchange Rate – 10% decrease	(4,935)

Credit risk

The Company manages credit risk by dealing with financially sound customers, based on an evaluation of the customer's financial condition. For the year ended February 28, 2018, the Company was engaged in contracts for products with two (2017 – three) customers in excess of 10% of revenue, which accounted for \$264,014 (2017 - \$284,246) or 48% (2017 – 52%) of the Company's total revenue. The maximum exposure to credit risk is the carrying value of accounts receivable and cash. Three (2017 - two) customers had outstanding balances in excess of 10% of accounts receivable, which accounted for \$37,443 (2017 - \$51,480) or 78% (2017 – 79%) of the Company's total accounts receivable balance. No allowance for doubtful accounts was recorded. The table below provides an analysis of our current and past due but not impaired accounts receivables.

	Total	Current	≤ 30 days	> 30 days ≤ 60 days	>60 days ≤ 90 days	> 90 days
February 28, 2018	\$ 50,126	\$ 43,468	\$ 5,463	\$ -	\$ 1,195	\$ -
February 28, 2017	\$ 67,356	\$ 63,542	\$ 3,016	\$ 494	\$ -	\$ 304

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16. Capital disclosures

The Company manages its capital to maintain its ability to continue as a going concern and to provide returns to shareholders and benefits to other stakeholders. The capital structure of the Company consists of cash, and equity comprised of issued capital, contributed surplus and deficit.

The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share issues or by undertaking other activities as deemed appropriate under the specific circumstances.

The Company is not subject to externally imposed capital requirements and the Company's overall strategy with respect to capital risk management remains unchanged from the year ended February 28, 2018.