



# ADVANTEX

**ADVANTEX® MARKETING INTERNATIONAL INC.**  
**Management's Discussion and Analysis of Operating Results**  
For the three month periods ended September 30, 2017 and 2016

This management's discussion and analysis ("MD&A") has been prepared based on information available to Advantex Marketing International Inc. ("Advantex" or "the company") as at November 29, 2017. MD&A is a narrative explanation to enable the reader to assess material changes in the financial condition and results of operations of the company during the three month period ended September 30, 2017 compared to the three month period ended September 30, 2016. This MD&A should be read in conjunction with the company's audited consolidated financial statements and the related notes for the twelve months ended June 30, 2017, and the interim consolidated financial statements and the related notes for the three months ended September 30, 2017 which are available on [www.sedar.com](http://www.sedar.com). All dollar amounts are stated in Canadian Dollars, which is the company's presentation and functional currency, unless otherwise noted. Certain dollar amounts have been rounded and may not tie directly to the interim and audited consolidated financial statements.

## **Overall Performance**

Advantex is a leader in the marketing services industry. The company develops and manages merchant based loyalty programs for its "Affinity partners", Canadian Imperial Bank of Commerce ("CIBC"), The Toronto Dominion Bank ("TD"), Aimia Inc. ("Aimia") and Caesars Entertainment Corporation ("Caesars"). The programs the company operates in partnership with CIBC and TD ("CIBC/TD program"), Aimia ("Aeroplan program") and Caesars ("Caesars program") enable holders of designated CIBC and TD credit cards, members of Aeroplan, and Caesars Towards Rewards (holders and members together "consumers") to accelerate earning frequent flyer miles and/or other rewards ("consumer rewards") on completing purchases at participating merchants. Under the umbrella of each program, Advantex markets participating merchants to consumers and on behalf of the merchants issues consumer rewards, provides merchants with business intelligence connected to the spending behaviour of consumers, and at its sole discretion provides merchants with working capital by the pre-purchase of their future sales.

On a combined basis, Advantex has contractual marketing access to millions of Canadian consumers with above-average personal and household income. The company's merchant partner base currently consists of about 1,025 merchants participating in the three programs and operating across Canada and the US in diverse business segments: restaurants; golf courses; independent inns, resorts and selected hotels; spas; retailers of men's and ladies fashion, footwear and accessories; retailers of sporting goods; florists and garden centres; health and beauty centres; dry cleaners; gift stores; and home décor, many of which are leaders in their respective business segment.

Advantex earns its revenue from merchants participating in its CIBC/TD program, in the form of an agreed marketing fee, for every purchase completed using an eligible CIBC and TD credit card at their establishments. Advantex earns its revenue in the Aeroplan program from selling consumer rewards (aeroplan miles), at an agreed price per consumer reward, to participating merchants. Merchants participating in the Caesars program pay an agreed monthly participation fee.

Advantex's common shares are traded on the Canadian Securities Exchange ("CSE") under the symbol ADX.

## **Summary – Three months ended September 30, 2017**

During the period the company's focus continued to be to stabilize operations in an environment where it had limited access to working capital. The limited access to working capital has for the past fifteen months hindered the company's ability to invest in resources necessary to influence new enrollment and retention of merchants participating in the CIBC/TD program. The resulting decline in merchant participation is reflected in the financial performance and financial position.

The company was able to secure agreement with the majority holder of its 12% non-convertible debentures payable to extend the original maturity date of September 30, 2016. The most recent extension took the maturity date to December 31, 2017.

In response to this situation the company has developed a financial restructuring plan ("Plan"). The Plan requires accommodations from the company's employees, its affinity partners and its financial backers. Successful implementation would enable the company to re-finance the new 12% debentures and provide working capital to support a gradual sustained recovery of its business. Some measures have been implemented while others are in process. The company expects the Plan to be fully implemented by December 31, 2017. The company believes implementing the Plan is the most effective way to transition to the next phase of recovery of its core business, during which it expects a gradual but sustained growth in its CIBC/TD program merchant base and related revenues. This transition will ultimately benefit all of its stakeholders.

The financial highlights for the three months ended September 30, 2017 ("Q1 Fiscal 2018") compared to three months ended September 30, 2016 ("Q1 Fiscal 2017") are summarized in the tabulation:

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>
	\$	\$
<b>Revenues</b>		
CIBC/TD program	\$ 1,708,296	\$ 2,121,992
Aeroplan program	287,967	471,022
Caesars program	9,906	11,223
Misc	-	33
	<u>\$ 2,006,169</u>	<u>\$ 2,604,270</u>
<b>Gross profit</b>	\$ 1,392,690	\$ 1,726,912
<b>Gross margin</b>	69.4%	66.3%
<b>Earnings from operations before depreciation, amortization and interest</b>	\$ 163,408	\$ 328,661
<b>Net loss and Comprehensive loss</b>	\$ (171,305)	\$ (149,405)

## **Income Statement – Q1 Fiscal 2018 compared to Q1 Fiscal 2017**

The \$598,101 drop in the company's revenues reflects mainly the decline in CIBC/TD revenues of \$413,696 (19.5%). CIBC/TD program accounts for a significant share of the company's revenues (over 80% in both fiscal periods). The decline primarily reflects lower merchant participation in the CIBC/TD program. The average merchant participation during Q1 Fiscal 2018 at 628 was 21.7% lower compared to Q1 Fiscal 2017. The decline in merchant participation is explained in the section Revenues in this document.

Gross profit decline of \$334,222 reflects mainly the \$284,164 decline in gross profit from CIBC/TD program.

CIBC/TD program accounts for a significant share of the company's gross profit (about 90% in both fiscal periods). The decline reflects lower CIBC/TD revenues offset by higher program margin, 74.0% for Q1 Fiscal 2018 compared to 72.9% for Q1 Fiscal 2017. Gross profit is reviewed in sections Direct expenses and Gross profit in this document.

SG&A expenses are \$168,969 lower compared to Q1 Fiscal 2017. The lower SG&A expenses reflect salary reduction of between 10% - 20% implemented mid-August 2017, lower headcount in G&A but a higher headcount in the CIBC/TD program sales organization. This increase is to enable the company to gradually ramp up merchant participation post the financial restructuring discussed above under Summary – Three months ended September 30, 2017. Excluding compensation for non-sales staff the G&A expenses were flat to Q1 Fiscal 2017 reflecting continued focus on cost management.

The decline of \$165,253 in earnings from operations before depreciation, amortization and interest reflect lower SG&A which partially offsets decline in gross profit.

Q1 Fiscal 2018 reflects a decrease in interest cost (\$73,399). The decrease reflects lower interest (\$13,598) paid on loan payable which is primarily consequent to lower utilization of loan payable on account of lower merchant participation. The non-cash interest (accretion charge for 12% Non-convertible debentures payable (“new 12% debentures”) for Q1 Fiscal 2018 was \$nil compared to \$60,227 for Q1 Fiscal 2017.

Depreciation and amortization expense was lower (\$69,954) compared to Q1 Fiscal 2017.

Q1 Fiscal 2018 net loss of \$171,305 is an increase of \$21,900 compared to Q1 Fiscal 2017. The increase reflects the above noted factors.

### **Balance Sheet – Q1 Fiscal 2018 compared to Q1 Fiscal 2017**

Transaction credits at September 30, 2017 of \$5,546,596 compared to \$6,252,747 at September 30, 2016. The change reflects decrease in transaction credits, net of provision for delinquent accounts, of \$706,151 which is primarily a reflection of a decrease in merchant participation. Transaction credits account for 87% of Q1 Fiscal 2018 total assets (Q1 Fiscal 2017 79%).

Cash and cash equivalents declined \$671,541 reflecting operational performance between October 1, 2016 and September 30, 2017, and the timing difference between the company's ongoing deployment and collection of transaction credits from merchants participating in its CIBC/TD program's APM product.

The capital assets decreased \$92,953. Decline of \$52,243 in intangible reflects amortization of amounts capitalized in prior periods related to operationalizing the TD agreement in Fiscal 2015 and enhancing the operability of the company's merchant based programs. The costs are amortized over the shorter of useful life of the software and term of Affinity partner agreement. Decline of \$40,710 in property, plant and equipment reflects both lower investment due to cash constraints and the company leasing equipment vs. purchasing. Lease costs are reflected in expenses.

The decline in transaction credits and cash are the primary reasons for decline in current assets of \$1,377,257, and together with the change in capital assets the primary reasons for decline in total assets of \$1,470,210.

The amount due on the loan payable decreased \$179,957 reflecting decrease in merchant participation which in turn reflects decrease in transaction credits and the timing difference between the company's ongoing deployment and collection of transaction credits from merchants participating in its CIBC/TD program's APM product.

Accounts payable and accrued liabilities decreased \$62,006 reflecting lower activity level, settlement of affinity partner dues under payment plans, and accrued and unpaid interest and fees payable to new 12% debentures (Q1 Fiscal 2018 \$566,218 compared to \$284,168 at end of Q1 Fiscal 2017).

A detailed look at the results for Q1 Fiscal 2018 compared to Q1 Fiscal 2017 is set out in the following sections.

## Outlook

The company continues to maintain the outlook noted in the management discussion and analysis for fiscal year ended June 30, 2017.

The company's assets are its Affinity partnerships with CIBC, TD, Aimia and Caesars, its merchant portfolio and its unique product offerings which seamlessly connect, through the company's proprietary technology, merchants to consumers. The company believes that it has a unique product, working capital and loyalty marketing at affordable prices, for the small independent merchant space. The company's systems and processes can rapidly onboard new affinity partners and the business is scalable. Loyalty marketing is a multi-billion dollar business in North America and the company is well positioned to gain a wider share of this market with its proprietary technology and its outstanding partners. But to do so it needs access to working capital.

The company has had partnership and competitive challenges since early Fiscal 2014. The financial cost in terms of righting its business deprived it of working capital to maintain and support the growth of the business. This is reflected in declining merchant participation levels since Fiscal 2013, the most recent year the company was profitable. Furthermore, the company's new 12% debentures mature December 31, 2017 and will have to be re-financed.

In response to this situation the company has developed a financial restructuring plan ("Plan"). The Plan requires accommodations from the company's employees, its affinity partners and its financial backers. Successful implementation would enable the company to re-finance the new 12% debentures and provide working capital to support a gradual sustained recovery of its business. Some measures have been implemented while others are in process. The company expects the Plan to be fully implemented by December 31, 2017. The company believes implementing the Plan is the most effective way to transition to the next phase of recovery of its core business, during which it expects a gradual but sustained growth in its CIBC/TD program merchant base and related revenues. This transition will ultimately benefit all of its stakeholders.

## Results of Operations

	Q1 Fiscal 2018	Q1 Fiscal 2017
	\$	\$
<b>Revenues</b>	<b>\$ 2,006,169</b>	<b>\$ 2,604,270</b>
Direct Expenses - Cost of cardholder rewards and marketing merchants to cardholders	481,575	697,764
Direct Expenses - Expense for provision against delinquent accounts	131,904	179,594
<b>Gross profit</b>	<b>\$ 1,392,690</b>	<b>\$ 1,726,912</b>
Selling and General & Administrative	1,229,282	1,398,251
<b>Earnings from operations before depreciation, amortization and interest</b>	<b>\$ 163,408</b>	<b>\$ 328,661</b>
Cash interest on loan payable and debentures	325,822	338,994
<b>Loss from operations before depreciation, amortization and non-cash interest on debentures (accretion charges)</b>	<b>\$ (162,414)</b>	<b>\$ (10,333)</b>
Depreciation and amortization	8,891	78,845
Non-cash interest expense on debentures	-	60,227
<b>Net loss and Comprehensive loss</b>	<b>\$ (171,305)</b>	<b>\$ (149,405)</b>
<b>Basic and Diluted loss per share</b>	<b>\$ (0.00)</b>	<b>\$ (0.00)</b>

Extract from the Statement of Financial Position

	At September 30, 2017	At June 30, 2017	Increase/ (Decrease)
	\$	\$	\$
Current assets	\$ 6,345,660	\$ 6,215,037	\$ 130,623
Total assets	\$ 6,409,832	\$ 6,288,100	\$ 121,732
Shareholders' deficiency	\$ (6,750,760)	\$ (6,579,455)	\$ 171,305

The current assets and total assets at September 30, 2017 are flat compared to June 30, 2017 reflecting a stability in the CIBC/TD program at September 30, 2017 relative to June 30, 2017.

The movement in the shareholders' deficit reflects net loss during Q1 Fiscal 2018.

Extracts from the Statement of Cash Flow

	Q1 Fiscal 2018	Q1 Fiscal 2017	Change
	\$	\$	\$
Net loss	\$ (171,305)	\$ (149,405)	\$ (21,900)
Adjustments for non cash expenses	8,891	139,072	(130,181)
Loss after adjustments for non cash expenses	\$ (162,414)	\$ (10,333)	\$ (152,081)
Changes in working capital	69,518	1,174,546	(1,105,028)
Net cash provided by (used in) financing activities supporting working capital	151,915	(724,974)	876,889
Net cash provided by operations and financing activities	\$ 59,019	\$ 439,239	\$ (380,220)
Increase in cash and cash equivalents	59,019	\$ 439,239	\$ (380,220)
Cash and cash equivalents at start of period	\$ 367,357	\$ 658,678	\$ (291,321)
Cash and cash equivalents at end of period	\$ 426,376	\$ 1,097,917	\$ (671,541)

*Changes in working capital.* Transaction credits, accounts receivable, accounts payable and accrued liabilities and other working capital items. During Q1 Fiscal 2018 the change reflects nominal movement in the various working capital items. This reflects stability in the CIBC/TD program during Q1 Fiscal 2018 relative to balance sheet at June 30, 2017. During Q1 Fiscal 2017 the changes reflect decrease in transaction credits, net of provision for delinquent accounts, of \$1,099,515 which is a reflection of a decrease in merchant participation. Decrease in accounts receivable of \$212,268 reflects lower accounts receivable (\$111,715) from merchants participating in the Aeroplan program primarily reflecting collection efforts and receipt of amounts due from Affinity partners (\$114,855) both of which are reflected in higher cash balance. Decrease in accounts payable and accrued liabilities reflects payments, per payment plan, to an affinity partner.

*Financing activities.* During Q1 Fiscal 2018 and Q1 Fiscal 2017 movement in loan payable reflects changes in merchant participation and the timing difference between the company's ongoing deployment and collection of transaction credits from merchants participating in its CIBC/TD program's APM product. Merchant participation is discussed in the section Revenue.

*Investing activities.* The company expects to secure lease arrangements for significant expenditures during Fiscal year ending June 30, 2018. The financial commitments on existing leases is provided in the section Contractual Obligations in this document. The lease costs are reflected in expenses. The company expects capital expenditures for Fiscal 2018 to be higher compared to Fiscal 2017 and Fiscal 2016.

*The presentations in Results of Operations section are not set out in accordance with International Financial Reporting Standards (“IFRS”). The presentations are extracts from the interim consolidated financial statement for the three months ended September 30, 2017, and have been included to provide additional analysis for the reader.*

## **Revenue**

The company’s revenue is derived from merchants participating in its Retail programs which currently consist of the CIBC/TD program, the Aeroplan program and Caesars program.

The Retail programs have four business products. APM, Marketing Only, Re-seller and Participation fee which are described later in this section.

The CIBC/TD program operates the APM, and Marketing Only business products.

The Aeroplan program operates the Re-seller product.

The Caesars program operates the Participation fee product.

The nature of the company’s products is as follows:

**Advance Purchase Marketing (“APM”):** The company acquires the rights to cash flow from future designated CIBC and TD credit card transactions at a discount from participating merchants (transaction credits on consolidated statement of financial position) and promotes the merchant by way of targeted marketing to holders of designated CIBC/TD credit cards, issues consumer rewards to consumers when they complete purchases at participating merchants, and provides merchants with business intelligence connected to the spending behaviour of consumers. The company’s revenue is from the purchases completed at the participating merchants using designated CIBC and TD credit cards, net of the company’s costs to acquire the transaction credits. Proceeds from the amount spent on above noted CIBC/TD credit cards at participating merchants are received by the company and a predetermined portion is applied to reduce the transaction credit balance.

**Marketing Only:** The company does not acquire transaction credits. In all other respects Marketing Only is similar to APM. Revenue is earned in the form of an agreed marketing fee for every purchase completed using CIBC/TD credit card (as defined under APM) at participating merchants.

**Re-seller:** The company sells aeroplan miles to small and mid-sized retailers and service providers. Revenue is recognized, at the agreed price per aeroplan mile, when the participating merchant issues aeroplan miles to an Aeroplan member completing a qualifying transaction at the merchant.

**Participation fee:** The company markets participating merchants to Caesars Total Rewards members and the merchant issues total rewards loyalty points to Total Rewards members completing a qualifying transaction at the merchant. The merchant pays an agreed monthly fee to Advantex.

The drivers for revenues from the CIBC/TD program are:

1. Number of participating merchants;
2. Market penetration of the CIBC/TD credit cards;
3. Economic environment;
4. Mix of merchants in terms of their volume of CIBC/TD credit card transactions; and
5. Participation levels in APM and Marketing Only. The fees that a merchant would pay for participation in the APM product is higher compared to Marketing Only.

The revenues from the Re-seller product reflect the number of participating merchants, traffic of aeroplan members completing purchases at participating merchants and the level of engagement of participating merchants in the program.

The revenues from the Caesars program are dependent on the number of participating merchants. The program expansion was launched in February 2015 in the Philadelphia market. About 60 merchants are participating in the program as of date hereof.

The company believes the primary driver of revenues across all programs is the number of merchants participating in the programs.

The revenue trends are provided in the tabulation.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./Dec)</u>	<u>Inc./Dec)</u>
<b>Avg. # of merchants participating during the periods</b>				
CIBC/TD program	628	803		-21.7%
Aeroplan program	373	544		-31.4%
	₤	₤	₤	
<b>Revenues</b>				
CIBC/TD program	\$ 1,708,296	\$ 2,121,992	\$ (413,696)	-19.5%
Aeroplan program	287,967	471,022	(183,055)	-38.9%
Caesars program	9,906	11,223	(1,317)	
Misc	-	33	(33)	
	<u>\$ 2,006,169</u>	<u>\$ 2,604,270</u>	<u>\$ (598,101)</u>	<u>-23.0%</u>

#### CIBC/TD program

The lower merchant participation during Q1 Fiscal 2018 compared to Q1 Fiscal 2017 is the primary reason for decline in revenues.

Towards the middle of March 2017 the company started to fill vacant sales positions. Due to the deficiency in working capital this re-building process is taking longer than expected. Due to the lack of an optimal sales organization and because the company does not have sufficient working capital to pre-purchase future sales from new merchants wishing to enroll in the company's APM product the merchant participation during Q1 Fiscal 2018 is lower compared to Q1 Fiscal 2017. Although the company was able to stabilize merchant participation during Q1 Fiscal 2018 relative to June 30, 2017 it expects a delay in bounce back of merchant participation until the optimal sales team is in place and it has sufficient working capital to pre-purchase future sales from merchants wishing to enroll in the company's APM product.

#### Aeroplan program

The decline in revenues primarily reflects decline in merchant participation.

#### **Direct Expenses**

In the CIBC/TD program, direct expenses include costs of consumer rewards which the company purchases from CIBC and TD, the cost of marketing and advertising on behalf of merchants, cost of sales related to sale of aeronotes, cost of sales of digital marketing services and provision against receivables.

In the Aeroplan program, direct expenses are primarily costs of consumer rewards which the company purchases from Aimia. Other costs include cost of marketing and advertising on behalf of merchants and provision against receivables.

Caesars program direct expenses are costs of consumer rewards which the company purchases from Caesars.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
<b>Revenues</b>			
CIBC/TD program	\$ 1,708,296	\$ 2,121,992	-19.5%
Aeroplan program	287,967	471,022	-38.9%
Caesars program	9,906	11,223	-11.7%
Misc	-	33	
	<u>\$ 2,006,169</u>	<u>\$ 2,604,270</u>	<b>-23.0%</b>
<b>Direct expenses</b>			
CIBC/TD program	\$ 444,895	\$ 574,427	-22.5%
Aeroplan program	162,918	294,244	-44.6%
Caesars program	5,666	8,687	-34.8%
	<u>\$ 613,479</u>	<u>\$ 877,358</u>	<b>-30.1%</b>

➤ CIBC/TD program

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
Avg. # of merchants participating during the periods	628	803	-21.7%
Revenue	\$ 1,708,296	\$ 2,121,992	-19.5%
Direct expenses			
Consumer rewards	\$ 296,546	\$ 347,781	-14.7%
Marketing and advertising	66,445	103,052	-35.5%
Marketing support by Affinity partners	(50,000)	(50,000)	0.0%
Expense for delinquent accounts	131,904	173,594	-24.0%
	<u>\$ 444,895</u>	<u>\$ 574,427</u>	-22.5%

The Q1 Fiscal 2018 decline in cost of consumer rewards primarily reflects decline in merchant population.

The Q1 Fiscal 2018 decrease in marketing and advertising costs relative to merchant participation and revenues primarily reflects timing of marketing expenditures which vary in a fiscal year. Timing is driven by marketing needs of the merchant portfolio and the marketing calendars of Affinity partners.

The Q1 Fiscal 2018 expense for delinquent accounts – at 7.7% of revenues – is to expectations and tracks Fiscal 2017 trend. Delinquencies are discussed in the section Critical Accounting Estimates – Credit Risk.

➤ Aeroplan program.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
Avg. # of merchants participating during the periods	373	544	-31.4%
Revenue	\$ 287,967	\$ 471,022	-38.9%
Direct expenses			
Consumer rewards	162,918	288,244	-43.5%
Misc., including expense for delinquent accounts	<u>-</u>	<u>6,000</u>	-100.0%
	<u>\$ 162,918</u>	<u>\$ 294,244</u>	-44.6%

The decrease in Q1 Fiscal 2018 direct expenses primarily reflects decline in revenues.

### Gross Profit

Gross margins of Q1 Fiscal 2018 compared to Q1 Fiscal 2017 are tabulated.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>
CIBC/TD program	74.0%	72.9%
Aeroplan program	43.4%	37.5%

Improvement in Q1 Fiscal 2018 CIBC/TD program gross margin reflects lower direct expenses which are explained in section Direct Expenses in this document.

Q1 Fiscal 2017 Aeroplan margin reflects revenues from a wholesale account (Q1 Fiscal 2018 \$nil). Wholesale accounts carry lower margin. This is the primary reason for improvement in Q1 Fiscal 2018 gross margin.

The company gross profit was lower in Q1 Fiscal 2018 compared to Q1 Fiscal 2017 reflecting primarily a decline in revenues offset by margin improvement of CIBC/TD program and Aeroplan program.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
CIBC/TD program	\$ 1,263,401	\$ 1,547,565	-18.4%
Aeroplan program	\$ 125,049	176,778	-29.3%
Caesars program	\$ 4,240	2,536	67.2%
Misc	<u>\$ -</u>	<u>33</u>	
	<u>\$ 1,392,690</u>	<u>\$ 1,726,912</u>	-19.4%

### Selling Expenses

Selling expenses include expenses arising from remuneration of sales staff, transaction processing and other selling activities. The significant component is cost of sales staff.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
<b>Revenues</b>			
CIBC/TD program	\$ 1,708,296	\$ 2,121,992	-19.5%
Aeroplan program	287,967	471,022	-38.9%
Caesars program	9,906	11,223	-11.7%
Misc	-	33	0.0%
	<u>\$ 2,006,169</u>	<u>\$ 2,604,270</u>	<b>-23.0%</b>
<b>Selling expenses</b>			
CIBC/TD program	\$ 444,155	\$ 445,590	-0.3%
Aeroplan program	5,018	30,550	-83.6%
Caesars program	31,025	29,567	4.9%
	<u>\$ 480,198</u>	<u>\$ 505,707</u>	<b>-5.0%</b>
Remuneration of sales staff	\$ 440,083	\$ 453,096	
Remuneration as % of selling expenses	91.6%	89.6%	

#### CIBC/TD program

The higher selling costs during Q1 Fiscal 2018 reflect higher headcount consequent to gradual re-build of the sales organization partially offset by company-wide salary reduction of between 10% and 20% implemented from mid- August 2017. The salary reduction is a component of the restructuring the company expects to close by end of December 2017.

#### Aeroplan program

The lower selling costs during Q1 Fiscal 2018 reflect lower headcount, aligning sales organization to expected medium term activity levels.

### **General and Administrative Expenses (“G&A”)**

G&A expenses include compensation for all non-sales staff, professional fees, head office premises costs, shareholder and public relations costs, office overheads, capital and income taxes, and foreign exchange gains/(losses).

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
<b>Change in revenues</b>			<b>-23.0%</b>
<b>G&amp;A</b>			
Compensation for non-sales staff	\$ 452,301	\$ 609,437	-25.8%
All other G&A expenses	296,783	283,107	
	<u>\$ 749,084</u>	<u>\$ 892,544</u>	<b>-16.1%</b>

### Compensation

While both periods reflect the staffing adequate to handle the existing and expected medium term activity levels, Q1 Fiscal 2018 reflects lower headcount and a company-wide salary reduction of between 10% and 20% implemented mid-August 2017. The salary reduction is a component of the restructuring the company expects to close by end of December 2017.

### All other expenses

Both periods reflect focus on cost management.

### **Interest Expense**

The interest expense is tabulated:

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	<u>\$</u>	<u>\$</u>	<u>%</u>
Stated ("Cash") interest expense			
Loan payable	\$ 169,780	\$ 183,378	-7.4%
new 12% debentures	<u>156,042</u>	<u>155,616</u>	
	\$ 325,822	\$ 338,994	-3.9%
Non cash interest (accretion charge) on new 12% debentures	<u>\$ -</u>	<u>\$ 60,227</u>	
	<b>\$ 325,822</b>	<b>\$ 399,221</b>	<b>-18.4%</b>

The company deployed the funds available to it under loan payable and new 12% debentures with merchants activated under its CIBC/TD program's APM product. The funds deployed are reflected as transaction credits on the consolidated statement of financial position. The funds available under the new 12% debentures were also used for other working capital purposes.

Stated interest expense on loan payable reflects the utilization of funds under this line of credit facility and prime rate which determines the facility interest rate (prime rate of a certain Canadian bank plus 11.5%). Average month end utilization of loan payable during Q1 Fiscal 2018 was \$4,542,207 compared to \$5,028,093 during Q1 Fiscal 2017, a lower utilization of 9.7%. During Q1 Fiscal 2018 prime rate was 0.5% higher as compared to Q1 Fiscal 2017.

The new 12% debentures in the principal amount of \$5,159,000 carry a coupon of 12%. The equity component of the new 12% debentures was fully accreted by the original maturity date of September 30, 2016 and hence there is no accretion charge for Q1 Fiscal 2018.

## Net Loss

Highlights of Q1 Fiscal 2018 compared to Q1 Fiscal 2017 are tabulated:

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>	<u>Inc./ (Dec)</u>
	\$	\$	\$
Revenues	\$ 2,006,169	\$ 2,604,270	\$ (598,101)
Gross margin	69.4%	66.3%	
Gross profit	\$ 1,392,690	\$ 1,726,912	\$ (334,222)
Earnings from operations before depreciation, amortization and interest	\$ 163,408	\$ 328,661	\$ (165,253)
Net loss and Comprehensive loss	\$ (171,305)	\$ (149,405)	\$ (21,900)
Basic and Diluted loss per share	\$ (0.00)	\$ (0.00)	

The \$598,101 drop in the company's revenues reflects mainly the decline in CIBC/TD revenues of \$413,696 (19.5%). CIBC/TD program accounts for a significant share of the company's revenues (over 80% in both fiscal periods). Gross profit decline of \$334,222 reflects mainly the \$284,164 decline in gross profit from CIBC/TD program. CIBC/TD program accounts for a significant share of the company's gross profit (about 90% in both fiscal periods). The decline of \$165,253 in earnings from operations before depreciation, amortization and interest reflect lower SG&A of \$168,969 which partially offsets decline in gross profit. Q1 Fiscal 2018 reflects a decrease in interest cost (\$73,399). The decrease reflects lower interest (\$13,598) paid on loan payable which is primarily consequent to lower utilization of loan payable on account of lower merchant participation. Depreciation and amortization expense was lower (\$69,954) compared to Q1 Fiscal 2017. Q1 Fiscal 2018 net loss of \$171,305 is an increase of \$21,900 compared to Q1 Fiscal 2017. The increase reflects the above noted factors and these are explained in the respective sections earlier in this document.

## Working Capital and Liquidity Management

	Q1 Fiscal 2018	Q1 Fiscal 2017
	\$	\$
<b>Funds available to expand the CIBC/TD programs APM product (Transaction credits on the balance sheet) and meet working capital needs</b>		
Net loss	\$ (171,305)	\$ (149,405)
Adjustments for non cash expenses	8,891	139,072
Profit (Loss) after adjustment for non cash expenses	(162,414)	(10,333)
Cash balances at start of the period	367,357	658,678
Inc / (Dec) in loan payable	151,915	(724,974)
(Inc) / Dec in accounts receivable	(71,640)	212,268
	<b>\$ 285,218</b>	<b>\$ 135,639</b>
<b>Utilization of funds</b>		
Cash balances at end of period	\$ 426,376	\$ 1,097,917
(Dec) in transaction credits	(3,116)	(1,099,515)
(Inc) / Dec. in accounts payable and accrued liabilities	(141,122)	121,716
Changes in all other working capital items	3,080	15,521
Capital expenditures	-	-
	<b>\$ 285,218</b>	<b>\$ 135,639</b>

The cash and cash equivalents, and accounts receivable at September 30, 2016 include \$192,202 of amounts received/receivable from our Affinity partners CIBC and TD to be invested in marketing the program (at June 30, 2017 \$nil and at September 30, 2017 \$nil). Accounts payable and accrued liabilities at September 30, 2016 reflect the corresponding liability.

The company believes that increasing the amount of the transaction credits deployed with merchants under the CIBC/TD program's APM product will result in higher revenue and, consequently, improve the company's financial results and cash flows. Generally, the change in transaction credits partially reflects the change in the number of merchants participating in the APM product, as well as the amount of transaction credits deployed with its existing merchants.

Changes in working capital. Transaction credits, accounts receivable, accounts payable and accrued liabilities and other working capital items. During Q1 Fiscal 2018 the change reflects nominal movement in the various working capital items. This reflects stability in the CIBC/TD program during Q1 Fiscal 2018 relative to balance sheet at June 30, 2017. During Q1 Fiscal 2017 the changes reflect decrease in transaction credits, net of provision for delinquent accounts, of \$1,099,515 which is a reflection of a decrease in merchant participation. Decrease in accounts receivable of \$212,268 reflects lower accounts receivable (\$111,715) from merchants participating in the Aeroplan program primarily reflecting collection efforts and receipt of amounts due from Affinity partners (\$114,855) both of which are reflected in higher cash balance. Decrease in accounts payable and accrued liabilities reflects payments, per payment plan, to an affinity partner.

Financing activities. During Q1 Fiscal 2018 and Q1 Fiscal 2017 movement in loan payable reflects changes in merchant participation and the timing difference between the company's ongoing deployment and collection of transaction credits from merchants participating in its CIBC/TD program's APM product. Merchant participation is discussed in the section Revenue.

Investing activities. The company expects to secure lease arrangements for significant expenditures during Fiscal year ending June 30, 2018. The financial commitments on existing leases is provided in the section Contractual Obligations in this document. The lease costs are reflected in expenses. The company expects capital expenditures for Fiscal 2018 to be higher compared to Fiscal 2017 and Fiscal 2016.

From time to time the company enters into payment plans to settle its dues. As of date hereof there are payment plans with an affinity partner and certain vendors. The company had a payment plan with CIBC to settle outstanding amounts by July 31, 2017 and these were settled by the due date.

While, generally the cash balances at the end of a quarter / year reflect cash generated /(used) by operations [profit (loss) before depreciation of property, plant and equipment, and amortization of intangible assets; and non-cash interest on debentures], the timing difference between the company's ongoing collection of transaction credits from merchants participating in its CIBC/TD program's APM product and deploying advances to existing and new merchants, the following are the additional considerations:

As at September 30, 2016, as noted earlier in this section, also included in cash and cash equivalents are funds totaling \$192,202 provided by Affinity partners CIBC and TD. At September 30, 2017 \$nil.

The company's operations are funded by debt – loan payable and new 12% debentures (see sections Loan Payable and 12% Non-Convertible Debentures Payable in this document). To continue its current operations and fund growth beyond Q1 Fiscal 2018, the company requires continued access to its existing levels of debt and access to additional working capital in the form of debt and or equity to meet operational needs including payments to its partners CIBC, TD and Aimia, meet debenture interest payments, and to support the growth of the company, including the APM product, as described under the section General Risks and Uncertainties in this document.

At present, the need for capital to expand the APM product is partially satisfied by the loan payable (facility credit limit of \$8.5 million and utilization at September 30, 2017 and June 30, 2017 of \$4.6 million and \$4.5 million respectively). However, there are limitations including; a credit limit of \$8.5 million; it is a demand facility; it requires the company to co-fund 15% of the transaction credits deployed with merchants under the APM product and the company's restricted cash position limits its ability to do so; and is only available to expand the APM product. The loan payable agreement expires in December 2018.

The new 12% debentures were issued by the company on December 30, 2013 in the principal amount of \$5,159,000 with an initial maturity date of September 30, 2016. At June 30, 2016 the company was in breach of all its financial covenants. Recognizing that the company does not have the ability to repay the debentures on maturity the company commenced discussions with the debenture holders. In September 2016 the company secured a waiver to the breach of all its financial covenants at June 30, 2016. In addition, the company and the debenture holders agreed to extend the maturity of the new 12% debentures to December 31, 2016 from September 30, 2016. In December 2016 the company secured an extension of the maturity date to March 31, 2017. In March 2017 the company secured an extension of the maturity date to June 30, 2017. In June 2017 the company secured an extension of the maturity date to September 30, 2017. In September 2017 the company secured an extension of the maturity date to October 31, 2017. In October 2017 the company secured an extension of the maturity date to December 31, 2017 but not a waiver to the breach of financial covenants at September 30, 2017. The company has been in breach of all its financial covenants since September 2016. The new 12% debentures are secured by a general security interest over the assets of the company and its subsidiaries. If the company breaches a financial covenant or is unable to pay either interest or its debts as they came due, it would be in default under the new 12% debentures agreement and, as a result, the new 12% debentures holders would have the right to waive the event of default, demand immediate payment of the new 12% debentures in full or modify the terms and conditions of the new 12% debentures including key terms such as repayment terms, interest rates and security. If the company is unable to secure alternative financing to pay interest or repay the new 12% debentures, the new 12% debentures holders would have the right to realize upon a part or all of the security held by them. The company has a decade + relationship with the primary holder (about 60%) of the new 12% debentures – a Toronto based firm investing on behalf of its managed accounts. Related parties holdings at September 30, 2017 of the new 12% debentures were about \$1.2 million (about 24% of the new 12% debentures), see section Related party transactions in this document. The primary holder of the new 12% debentures is also the primary shareholder of the company as it beneficially owns or exercises control

or direction through about 15% of the company's common shares (as of November 20, 2017) held on behalf of its managed accounts.

The company is seeking to re-finance its new 12% debentures and secure additional capital to continue its operations and execute its expansion plans. While in the past the company has been successful in obtaining waivers and debt amendments, and refinancing its debentures, there can be no assurance these initiatives will continue to be successful.

Except for the leasing arrangements the company does not participate in off balance sheet financing arrangements.

The consolidated financial statements for three months ended September 30, 2017 have been prepared in accordance with accounting principles applicable to a going concern which contemplates that the company will be able to realize its assets and settle its liabilities in the normal course as they come due during the normal course of operations for the foreseeable future. When a company is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern, the entity is required to disclose those uncertainties. The company has a shareholders' deficiency of \$6,750,760 and negative working capital of \$6,814,932 as at September 30, 2017. There is uncertainty surrounding:

1. The re-financing of the new 12% debentures maturing December 31, 2017; and
2. The access to existing and additional working capital in the form of debt and or equity to meet operational needs including payments to its partners CIBC, TD and Aimia, payment of new 12% debentures interest for period January 1, 2017 to maturity and to support the growth of the company.

As a result, this may cast significant doubt on the validity of going concern assumption and the company's ability to continue as a going concern after September 30, 2017 and hence the ultimate use of accounting principles applicable to a going concern.

The company's future success is dependent on retaining its existing relationships with CIBC, TD, and Aimia; continued access to its existing levels of debt capital; additional capital in the form of debt or equity; ensuring profitability; and generating positive cash flows from operations. The company's business plan includes renewal of its agreements with CIBC, TD, and Aimia; refinancing of its current loans; the receipt of waivers or agreement amendments where breaches occur; and raise of additional capital. While in the past the company has been successful in renewal of its agreement with CIBC, TD, and Aimia, refinancing its debentures and loan payable, obtaining waivers or agreement amendments, there can be no assurance these initiatives will continue to be successful. In addition, there can be no assurance the company will be successful in securing additional capital which is required to meet operational needs including payments to its partners CIBC, TD and Aimia, payment of new 12% debentures interest for period January 1, 2017 to maturity and to support the growth of the company.

The consolidated financial statements do not include any adjustments or disclosures that may result from the company's ability to continue as a going concern. If the going concern assumption were not appropriate for the consolidated financial statements, adjustments may be necessary in the carrying values of assets and liabilities and the reported expenses and balance sheet classifications; and such adjustments could be material.

The company has had partnership and competitive challenges since early Fiscal 2014. The company has had declining merchant participation levels since Fiscal 2013 and the company's new 12% debentures mature December 31, 2017 and will have to be re-financed.

In response to this situation the company has developed a financial restructuring plan ("Plan"). The Plan requires accommodations from the company's employees, its affinity partners and its financial backers. Successful implementation would enable the company to re-finance the new 12% debentures and provide working capital to support a gradual sustained recovery of its business. Some measures have been implemented while others are in process. The company expects the Plan to be fully implemented by December 31, 2017. The company believes implementing the Plan is the best way to ensure it is able to transition to the next phase of recovery of its business.

## Contractual Obligations

Contractual obligations as at September 30, 2017 were due as follow:

	<u>Total</u>	<u>Less than 1 year</u>	<u>1 to 3 years</u>	<u>4 to 5 years</u>
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Loan payable	\$ 4,628,336	\$ 4,628,336	\$ -	\$ -
New 12% debentures	\$ 5,159,000	\$ 5,159,000	\$ -	\$ -
Operating leases	\$ 447,575	\$ 125,740	\$ 172,862	\$ 148,973
	<b>\$ 10,234,911</b>	<b>\$ 9,913,076</b>	<b>\$ 172,862</b>	<b>\$ 148,973</b>

In addition, new 12% debenture interest of \$619,080 is payable for the period January 1, 2017 to maturity on December 31, 2017. The company also has a liability for \$103,180 to the holders of the new 12% debentures respecting fee charged by the holders for waiving breach of financial covenants at March 31, 2016.

The expense related to above leases is expensed in selling and marketing, and general and administrative expenses in the consolidated statements of income.

In August 2017 the company renewed its lease for the company's head office for five year term ending August 31, 2022.

### Loan Payable

The loan payable is a line of credit facility ("facility") with Accord to be used exclusively to fund the merchants participating in the APM product in the business segments available to the company under its agreements with CIBC, TD and Aimia. As security, the provider has first charge to all transaction credits funded from the facility.

The facility was established in December 2007. The current term of the loan payable expires in December 2018.

The facility has a limit of \$8.5 million. Interest is calculated daily on the amount outstanding and charged monthly at an interest rate equivalent to prime rate of a certain Canadian bank plus 11.5% per annum. In certain circumstances the loan payable amount is repayable on demand to Accord.

The Company had utilized \$4.6 million of the facility as at September 30, 2017 (as at June 30, 2017 \$4.5 million).

In addition to loan payable, since February 2017 Accord has given the company access to a \$100,000 overdraft facility. The facility is used for working capital needs. The interest rate on the overdraft facility and loan payable is the same. The term of this facility expires December 31, 2017. It is repayable on demand.

### 12% Non-Convertible Debentures Payable

On December 30, 2013, the company completed a refinancing by way of a private placement of 12% non-convertible debentures ("new 12% debentures") in the principal amount of \$5,159,000.

The new 12% debentures were issued as units. Each unit comprised (i) \$1,000 face value secured non-convertible debentures of the company bearing interest at 12% per annum, payable semi-annually, and with an initial maturity date of September 30, 2016, and (ii) 8,150 common shares in the capital of the company. The company issued 5,159 units and 42,045,850 common shares.

Under the agreement, the proceeds of the new 12% debentures are to be used for working capital purposes.

The new 12% debentures are secured by a general security interest over the assets of the company and its subsidiaries. The significant financial covenants of the new 12% debentures require the company to meet on a quarterly basis a defined level of designated current assets, and interest coverage.

At June 30, 2016 the company was in breach of all its financial covenants. In September 2016 the company secured a waiver to the breach of all its financial covenants at June 30, 2016 and extension of the maturity date to December 31, 2016. In December 2016 the company secured an extension of the maturity date to March 31, 2017. In March 2017 the company secured an extension of the maturity date to June 30, 2017. In June 2017 the company secured an extension of the maturity date to September 30, 2017. In September 2017 the company secured an extension of the maturity date to October 31, 2017. In October 2017 the company secured an extension of the maturity date to December 31, 2017 but not a waiver to the breach of financial covenants at September 30, 2017.

The company has been in breach of all its financial covenants since September 2016.

The new 12% debentures are secured by a general security interest over the assets of the company and its subsidiaries. If the company were to breach a financial covenant or were unable to pay its debts as they came due, it would be in default under the new 12% debentures agreement and, as a result, the new 12% debentures holders would have the right to waive the event of default, demand immediate payment of the new 12% debentures in full or modify the terms and conditions of the new 12% debentures including key terms such as repayment terms, interest rates and security. If the company is unable to secure alternative financing to repay the new 12% debentures, the new 12% debentures holders would have the right to realize upon a part or all of the security held by them.

### Summary of Quarterly Results

<u>12 month period ended September 30, 2017</u>					
	Q2	Q3	Q4	Q1	Total
	Dec 31, 2016	Mar 31, 2017	Jun 30, 2017	Sep 30, 2017	
	\$	\$	\$	\$	\$
Revenues	2.4	1.9	2.3	2.0	8.6
% of annual revenues	27.9%	22.1%	26.7%	23.3%	100.0%
Net Loss	(0.2)	(0.5)	(0.4)	(0.2)	(1.3)
Loss per share - Basic and Diluted	-	-	-	-	(0.01)
<u>12 Month period ended September 30, 2016</u>					
	Q2	Q3	Q4	Q1	Total
	Dec 31, 2015	Mar 31, 2016	Jun 30, 2016	Sep 30, 2016	
	\$	\$	\$	\$	\$
Revenues	3.1	2.4	2.8	2.6	10.9
% of annual revenues	28.4%	22.0%	25.7%	23.9%	100.0%
Net Loss	-	(0.5)	(0.3)	(0.1)	(0.9)
Loss per share - Basic and Diluted	-	-	-	-	(0.01)

The fluctuations in the company's quarterly revenues from its Retail programs reflect seasonal consumer behavior at merchants participating in the Retail programs, as well as the other factors described under section Revenue in this document.

The fluctuations in the company's quarterly results reflect revenues and the costs to earn the revenues.

## **Capital Resources**

There were no expenditures during Q1 Fiscal 2017 and Q1 Fiscal 2018.

The company expects to secure lease arrangements for significant expenditures during Fiscal year ending June 30, 2018. The financial commitments on existing leases is provided in the section Contractual Obligations in this document. The lease costs are reflected in expenses. The company expects capital expenditures for Fiscal 2018 to be higher compared to Fiscal 2017 and Fiscal 2016.

There are no material commitments for capital expenditures as of the date hereof.

## **Critical Accounting Estimates**

The preparation of the company's consolidated financial statements, in accordance with IFRS, requires the company's management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the interim and annual consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The company's significant accounting policies are disclosed in note 4 to the audited consolidated financial statements for year ended June 30, 2017.

### *Contingent liabilities*

A significant amount of estimation is applied in evaluating the company's uncertain tax provision with the Canada Revenue Agency (CRA), as described in note 14 to the audited consolidated financial statements for year ended June 30, 2017, and in the final paragraph in the General Risks and Uncertainties section of this document, and whether a tax provision is required.

From time to time, the company is party to legal proceedings arising out of the normal course of business. The results of these litigations cannot be predicted with certainty, and management is of the opinion that the outcome of these types of proceedings is generally not determinable. Any loss resulting from these proceedings will be charged to operations in the period the loss is determined.

### *Going concern*

The company tests the going concern assumption on a quarterly basis. The company determines this from its financial forecasts that are prepared on its expectation regarding continuation of its agreement with CIBC and TD, continuation of its agreement with Aimia, continued access to existing sources of debt, obtaining waivers and debt amendments, ability to re-finance its new 12% debentures on their maturity, ability to access additional sources of debt, growth of its existing business, and development of new lines of business.

The company's audited consolidated financial statements for year ended June 30, 2017 and interim consolidated financial statements for three months ended September 30, 2017 carry a going concern note (note 2b).

### *Financial instruments – fair value*

The carrying value of accounts receivable, transaction credits, accounts payable and accrued liabilities, loan payable and new 12% debentures approximate their fair values due to the short-term maturity of these instruments.

### *Credit risk*

The company has certain business risks linked to the collection of its transaction credits. Under the APM product the company generally acquires the rights to cash flow from future designated credit card transactions ("future sales") at a discount from participating merchants ("transaction credits" on consolidated statement of financial position). These transaction credits are estimated to be fully extinguishable within 30 – 210 days. Until these transaction credits have been extinguished through designated cardholder spend at participating

merchants, there is a credit risk, and an increase in credit risk associated with the longer time frame approaching and/or exceeding 210 days. In the event of default, the company has set up escalating collection measures, and an allowance is determined on specifically identified transaction credit balances that are delinquent and amount of the specific provision is determined based on whether the account has been referred to collection agency, for legal action, whether the company's attempt to debit the merchant's bank account for payments due to the company has been rejected, the underlying reason for the rejections, and the company's historical experience on recoveries.

The maximum exposure to credit risk is the balance, net of provision for impaired accounts, of the transaction credits, and accounts receivable.

The accounts receivable, transaction credits, and the allowance is as follows:

	At September 30, 2017	At June 30, 2017
	\$	\$
Transaction credits	\$ 6,201,032	\$ 6,078,872
Accounts receivable	253,411	181,771
Allowance	<u>(655,690)</u>	<u>(530,414)</u>
Per statement of financial position	\$ <u>5,798,753</u>	\$ <u>5,730,229</u>
Maximum exposure to credit risk	\$ 5,798,753	\$ 5,730,229

The transaction credits that are considered impaired and the related allowance is as follows:

	At September 30, 2017	At June 30, 2017
	\$	\$
Impaired transaction credits	\$ 699,140	\$ 613,754
Allowance	<u>(654,436)</u>	<u>(529,160)</u>
Impaired transaction credits not allowed for	\$ <u>44,704</u>	\$ <u>84,594</u>

## Stock Options

The company has a stock option plan for directors, officers, employees and consultants. The stock options are non-assignable; the stock option price is to be fixed by the Board of Directors but may not be less than the regulations of the stock exchange on which the company's common shares are listed; the term of the stock options may not exceed five years, and payment for the optioned shares is required to be made in full on the exercise of the stock options. The stock options are subject to various vesting provisions, determined by the Board of Directors, ranging from immediate to four years.

Movement during Q1 Fiscal 2018 and Q1 Fiscal 2017 is tabulated.

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>
	<u>Number of options</u>	
Outstanding at start of the period	1,490,000	4,100,000
Expired	-	-
Forfeited	-	-
Outstanding at end of the period	<u>1,490,000</u>	<u>4,100,000</u>

The number of stock options available for future issuance at September 30, 2017 compared to September 30, 2016 is as follows:

	<u>Q1 Fiscal 2018</u>	<u>Q1 Fiscal 2017</u>
	<u>Number of options</u>	
Maximum number of shares reserved for issuance	16,688,546	16,688,546
Less: outstanding at end of period	<u>(1,490,000)</u>	<u>(4,100,000)</u>
Number of options available for future issuance	<u>15,198,546</u>	<u>12,588,546</u>

There was no stock based compensation expense during Q1 Fiscal 2018 and Q1 Fiscal 2017.

### **Outstanding Share Data**

As of June 30, 2017, September 30, 2017 and the date hereof, the number of issued and outstanding common shares of the company is 139,071,218. The number of common shares is provided by the company's transfer agent AST Trust Company.

### **Potentially Dilutive Securities**

As of date hereof, the company was committed to issuing 1,490,000 additional common shares pursuant to the company's stock option plan.

## Related party transactions

### Directors and Officers

In December 2013 the following related parties purchased new 12% debentures, on terms and conditions applicable to the other subscribers (section 12% Non-Convertible Debentures Payable in this document). The holdings of debentures are tabulated:

	At September 30, 2017	At June 30, 2017
	\$	\$
Director, Chief Executive Officer - K. Ambrose	\$ 500,000	\$ 500,000
Director, Chairman of the Board of Directors - S. Burns	\$ 50,000	\$ 50,000
Director - W. Polley	\$ 50,000	\$ 50,000
Director - M. Lavine	\$ 500,000	\$ 500,000
Chief Financial Officer - M. Sabharwal	\$ 115,000	\$ 115,000
	<b>\$ 1,215,000</b>	<b>\$ 1,215,000</b>

### Trapeze Capital Corp. and Trapeze Asset Management Inc. (together "Trapeze")

Trapeze may have been considered, at the time of the purchase of new 12% debentures, to be a related party of the company by virtue of their holding of \$4,446,062 old 12% debentures, \$1,296,000 14% debentures, and 65,475,823 common share purchase warrants, issued with old 12% debentures and 14% debentures, of the company, on behalf of their respective managed accounts.

## Economic Dependence

A significant portion of the company's current revenue is dependent upon its value-added loyalty program agreement with CIBC and TD under which consumer rewards are awarded to holders of designated CIBC and TD credit cards when they complete purchases at merchants participating in Advantex's CIBC/TD program. The significance to the company of the CIBC and TD agreements can best be assessed by comparing its revenues from its relationship with CIBC and TD with that of other programs as tabulated at the end of this section.

The company's relationship with CIBC has been in place for about two decades and has been through several multi-year renewal terms. The current agreement was renewed effective September 1, 2016 and prior to its expiry on September 30, 2017 it was extended to March 31, 2018. The company and CIBC are in discussions on a renewal. If CIBC does not renew the agreement or exercises its right to terminate the existing agreement upon at least six months prior notice or retains a competing service provider the company could be materially and adversely affected.

In June 2014, the company entered into an agreement with TD. The agreement with TD had an initial term of two years. The agreement renews automatically for additional one year terms unless TD provides notice not to renew. The current term of the agreement expires in June 2018. If TD does not renew the agreement or exercises its right to terminate the agreement upon at least four months prior notice or retains a competing service provider the company could be materially and adversely affected.

The company's revenue from the CIBC/TD programs is dependent on the number of merchants participating in the CIBC/TD program, dollar spending by holders of designated CIBC credit cards and TD aeroplan credit cards at participating merchants and the economic environment. Since the dollar spending by holders of designated CIBC and TD aeroplan credit cards is dependent upon the banks credit card portfolio, the company believes that the agreements with two banks mitigate the risk of dependence on one partner.

Illustration of economic dependence on CIBC/TD program. Revenue and Gross profit are tabulated.

	Q1 Fiscal 2018		Q1 Fiscal 2017	
	\$	% of company Total	\$	% of company Total
CIBC/TD program revenues	\$ 1,708,296	85.2%	\$ 2,121,992	81.5%
CIBC/TD program gross profit	\$ 1,263,401	90.7%	\$ 1,547,565	89.6%

## General Risks and Uncertainties

As indicated in the Economic Dependence section of this document a significant portion of the company's current revenue is dependent on its value-added loyalty agreement with CIBC. The company's relationship with CIBC has been in place for about two decades and has been through several multi-year renewal terms. The current agreement was renewed effective September 1, 2016 and prior to its expiry on September 30, 2017 it was extended to March 31, 2018. The company and CIBC are in discussions on a renewal. If CIBC does not renew the agreement or exercises its right to terminate the existing agreement upon at least six months prior notice or retains a competing service provider the company could be materially and adversely affected.

In September 2013, CIBC, TD, and Aimia announced they had come to a tripartite arrangement effective January 2014, and under which CIBC sold a significant part of its Aeroplan portfolio to TD. In June 2014, the company entered into an agreement with TD. The agreement with TD had an initial term of two years. The agreement renews automatically for additional one year terms unless TD provides notice not to renew. The current term of the agreement expires in June 2018. If TD does not renew the agreement or exercises its right to terminate the agreement upon at least four months prior notice the company could be materially and adversely affected.

The company's revenue from the CIBC/TD programs is dependent on the number of merchants participating in the CIBC/TD program, dollar spending by holders of designated CIBC credit cards and TD aeroplan credit cards at participating merchants and the economic environment. Since the dollar spending by holders of designated CIBC and TD credit cards is dependent upon the banks credit card portfolio, the company believes that the agreements with two banks mitigate the risk of dependence on one partner.

The company's working capital needs are currently partially provided by debt in the form of new 12% debentures maturing December 31, 2017 and loan payable. The company's relationship with the new 12% debentures holders, and providers of loan payable facility span a decade. The term of the loan payable expires in December 2018. At September 30, 2017 there is about \$4.0 million room on the loan payable and the need for capital to expand the APM product is partially satisfied by the loan payable. The loan payable credit facility requires the company to co-fund 15% of the transaction credits deployed with merchants under the APM product and the company has limited ability to co-fund the 15%. To be able to operate and advance its business the company needs to be able to access the loan payable facility and have funds to co-fund. The loan payable is a demand facility. The new 12% debentures carry financial covenants. The company does not have the ability to repay the new 12% debentures maturing December 31, 2017 and the accrued and unpaid interest – since January 1, 2017 - thereon. The company is in breach of all its financial covenants at September 30, 2017. The new 12% debentures are secured by a general security interest over the assets of the company and its subsidiaries. If the company were to breach a financial covenant or were unable to pay its debts as they came due, it would be in default under the new 12% debentures agreement and, as a result, the new 12% debentures holders would have the right to waive the event of default, demand immediate payment of the new 12% debentures in full or modify the terms and conditions of the new 12% debentures including key terms such as repayment terms, interest rates and security. If the company is unable to secure alternative financing to repay the new 12% debentures, the new 12% debentures holders would have the right to realize upon a part or all of the security held by them; see section Working Capital and Liquidity Management in this document for a fuller discussion of the risks. Consequently, general market conditions or the financial status of the company in terms of its profitability, cash flows and strength of its consolidated balance sheet may eliminate or limit access to existing sources of debt, and / or may limit access to additional financing and / or alternative funding to replace existing debt, or the terms of accessible debt may be uneconomic and this could materially and adversely affect the company.

The company believes that increasing the amount of the transaction credits deployed with merchants under its CIBC/TD program's APM product will result in higher revenue and, consequently, improve the company's financial results and cash flows. The company requires additional debt financing and or equity to scale its ability in this area. If the company is not successful in raising additional debt financing and equity, its ability to expand its merchant base and increase revenue may be impeded, resulting in reduced growth in cash flows from operations. This could affect the company's liquidity and working capital position. Any debt structure would need to recognize the general security interest over the company's assets held by the new 12% debentures holders.

The company has certain business risks linked to the collection of its transaction credits. Under the CIBC/TD program's APM product the company acquires the rights to cash flow from future designated credit card transactions ("future sales") at a discount from participating merchants ("transaction credits" on consolidated statement of financial position). These transaction credits are generally estimated to be fully extinguishable within 30 – 210 days of the funds being deployed with the merchant. Management has implemented review and monitoring procedures to assess the creditworthiness and ongoing eligibility of merchants if they wish to benefit from larger purchases of their future sales. Until these transaction credits have been extinguished through designated cardholder spend at participating merchants there is a credit risk, and an increase in credit risk associated with the longer time frame approaching and/or exceeding 210 days. In the event of default, the company has set up escalating collection measures, and an allowance is determined on specifically identified transaction credit balances that are delinquent and amount of the specific provision is determined based on whether the account has been referred to a collection agency, for legal action, whether the company's attempt to debit the merchant's bank account for payments due to the company has been rejected, the underlying reason for the rejections, and the company's historical experience on recoveries. Deterioration in either the credit environment or the company's monitoring processes and a resulting increase in bad debts would adversely impact the financial status of the company thereby affecting its attractiveness as a borrower and its ability to access existing or additional or alternative debt or debt at economic terms and this could materially and adversely affect the company.

The company's activities are funded by two sources of debt. The new 12% debentures has a fixed interest rate, and loan payable which carries a floating interest rate. While the company is not exposed to interest rate risk on account of new 12% debentures, its future cash flows are exposed to interest risk from the floating interest rate payable, calculated as prime rate of a certain Canadian bank plus 11.5%, on loan payable. While the company does not use derivative instruments to reduce its exposure to interest rate risk, it believes it can pass on, to merchants participating in its programs, a portion of a significant adverse interest rate movement on its loan payable. As disclosed under the section Interest Expense in this document, for the three months ended September 30, 2017, the company incurred interest expense of \$169,780 on utilization of loan payable. Had the interest rate, for the three months ended September 30, 2017, been 10% higher the interest expense on loan payable would have been \$186,758 an increase of \$16,978.

The company's operations are dependent on the abilities, experience and efforts of its management and highly skilled workforce. While the company has entered into employment agreements with key management personnel and other employees, and each of these agreements includes confidentiality and non-competition clauses, the business prospects of the company could be adversely affected if any of these people were unable or unwilling to continue their employment with the company.

The merchant based loyalty programs that the company develops and manages for CIBC, TD and Aimia, are dependent upon ongoing consumer interest in accumulating frequent flyer miles for the purpose of obtaining reward air travel on designated airlines. Due to the security difficulties being experienced by the airline industry overall, and in general continuous devaluation of frequent flyer miles, there is a risk that the underlying frequent flyer currencies used in these programs could become unavailable to the company, or that consumer interest in accumulating these awards could decline. This, in turn, may result in difficulties in acquiring and retaining merchants and may adversely affect the company's revenue and direct costs.

The company provides marketing services to retail organizations and, in more general terms, the company could be considered competitive with other advertising and promotional programs for a portion of a client's total marketing budget. If client promotional spending levels decrease, this could have a material adverse effect on the company's revenue. In addition, there are additional operators of either loyalty programs or merchant cash advance in Canada, targeting the same merchant base as the company. In the past, other companies have attempted to develop similar merchant-based coalitions on their own and failed, making the company, with its established merchant coalition and proven loyalty systems, a reputable outsourced partner in the Canadian

marketplace. The company believes its substantial client equity, proprietary systems, breadth of in-house services and significant Affinity partner contracts provide a strong platform for the company to compete effectively in the North American marketplace and respond to competition in Canada.

In addition to economic factors, factors noted in the Working Capital and Liquidity Management section, and those factors noted above, the profitability of the company is also subject to a number of additional risk factors including: continuation of partnership with Affinity partners CIBC, TD and Aimia; continued access to loan payable line of credit facility; continued access to the new 12% debentures; ability to refinance the new 12% debentures maturing December 31, 2017; ability to raise additional capital in the form of either debt or equity which is needed to meet future operational and expansion requirements; ability to negotiate payment plans with its vendors; competition; changes in regulations - including taxation - affecting the company's activities; consumer spending behavior; and continued demand for the company's programs by merchants.

In the ordinary course of business, the company is subject to ongoing audits by tax authorities. While the company believes that its tax filing positions are appropriate and supportable, from time to time, certain matters are reviewed and challenged by the tax authorities. The company regularly reviews the potential for adverse outcomes in respect of tax matters and believes that any ultimate disposition of a reassessment will not have a material adverse impact on its liquidity, consolidated financial position or results of operations due to adequate provisioning for these tax matters. Should an outcome materially differ from existing provisions, the company's effective tax rate, its earnings, and its liquidity and working capital position could be affected positively or negatively in the period in which matters are resolved.

### **Forward-Looking Information**

This Management's Discussion and Analysis contains certain "forward-looking information". All information, other than information comprised of historical fact, that addresses activities, events or developments that the company believes, expects or anticipates will or may occur in the future constitutes forward-looking information. Forward-looking information is typically identified by words such as: anticipate, believe, expect, goal, intend, plan, will, may, should, could and other similar expressions. Such forward-looking information relates to, without limitation, information regarding the company's: belief it has a unique product for the small independent merchant market; expectations from its processes and systems and belief the business is scalable; expectation of the size of the loyalty marketing market; belief in its ability to gain a share of the market; expectations from expansion outside Canada; estimation of the amount of working capital required to expand operations; belief in its ability to implement the Plan; expectation of timeline for implementation of the Plan; belief Plan is most effective way forward; expectation of outcomes for the business and stakeholders and their timing upon implementation of the Plan; belief it has the support of its partners and staff; expectation of capital expenditures during fiscal year ending June 30, 2018; expectation of securing lease arrangements for significant capital expenditures; belief the primary driver of revenues is merchant participation; expectation of bounce-back in merchant participation and its timing; belief an increase in transaction credits will positively effect financial performance and cash flows; expectation of and from finalizing the restructuring of the commercial terms of agreement with Aimia and the timing of finalization; belief in its ability to retain and expand its merchant base; belief agreements with CIBC and TD mitigate the risk of dependence on one partner; ability to manage credit and collection risk; expectations of delinquency expense during fiscal year ending June 30, 2018; belief current G&A staffing is adequate to handle current and medium term activity levels; expectation of adverse interest rate increase it can pass onto merchants; expectation of its ability to compete; belief in the appropriateness of its tax filings; and other information regarding financial and business prospects and financial outlook is forward-looking information.

Forward-looking information reflects the current expectations or beliefs of the company based on information currently available to the company, including certain assumptions and expectations of Management. With respect to the forward-looking information contained in this Management Discussion and Analysis, the company has made assumptions regarding, among other things, continued Affinity partner participation; continued support from its provider of loan payable and holders of new 12% debentures; its ability to re-finance new 12% debentures maturing December 31, 2017; its ability to close the Plan, the timeline to its close and the impact of the same on its business; its ability to access additional working capital in the form of debt and or equity to meet operational needs including payments to its partners CIBC, TD and Aimia and to support the growth of the company; its ability to manage risks connected to collection of transaction credits; current and future economic and market conditions and the impact of same on its business; ongoing consumer interest in

accumulating frequent flyer miles; the size of the market for its programs; its ability to increase merchant participation in its programs; ongoing and future Affinity partnerships and revenue sources; future business levels, and the cost structure, capital expenditures and working capital required to operate at those levels; future interest rates; and the appropriateness of its tax filing position.

Forward-looking information is subject to a number of risks, uncertainties and assumptions that may cause the actual results of the company to differ materially from those discussed in the forward-looking information, and even if such actual results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on the company. Factors that could cause actual results or events to differ materially from current expectations include, among other things, those listed under “Working Capital and Liquidity Management”, “General Risks and Uncertainties” and “Economic Dependence” in this Management Discussion and Analysis.

All forward-looking information speaks only as of the date on which it is made and, except as may be required by applicable securities laws, the company disclaims any intent or obligation to update any forward-looking information, whether as a result of new information, future events or results or otherwise. Although the company believes that the assumptions inherent in the forward-looking information are reasonable, forward-looking information is not a guarantee of future performance and accordingly undue reliance should not be put on such information due to the inherent uncertainty therein.

### **Disclosure Controls and Procedures, and Internal Controls Over Financial Reporting**

Management is responsible for external reporting. The company maintains appropriate processes to ensure that relevant and reliable financial information is produced.

### **Additional Information**

Additional information relating to the company is available at [www.sedar.com](http://www.sedar.com), and may also be obtained by request by telephone or facsimile or at the company’s website at [www.advantex.com](http://www.advantex.com).

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