

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended May 31, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from to

Commission File Number: 000-55418



**KUSH BOTTLES, INC.**

(Exact name of registrant as specified in its charter)

**Nevada**  
(State or other jurisdiction of  
incorporation or organization)

**46-5268202**  
(I.R.S. Employer  
Identification No.)

**1800 Newport Circle, Santa Ana, CA 92705**  
(Address of Principal Executive Offices) (Zip Code)

**(714) 243-4311**  
(Registrant's telephone number, including area code)

N/A

Former name, former address, and former fiscal year, if changed since last report

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated Filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated Filer	<input type="checkbox"/> (Do not check if smaller reporting company)	Smaller reporting company	<input checked="" type="checkbox"/>
Emerging growth company	<input checked="" type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 74,198,243 shares outstanding as of July 9, 2018.

## FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are subject to risks and uncertainties and are based on the beliefs and assumptions of management and information currently available to management. In some cases, you can identify forward-looking statements by words such as “anticipate,” “believe,” “contemplate,” “continue,” “could,” “estimate,” “expect,” “intend,” “may,” “plan,” “potential,” “predict,” “project,” “seek,” “should,” “target,” “will,” “would,” or the negative of these words or other comparable terminology.

The identification in this report of factors that may affect our future performance and the accuracy of forward-looking statements is meant to be illustrative and by no means exhaustive. All forward-looking statements should be evaluated with the understanding of their inherent uncertainty.

Factors that could cause our actual results to differ materially from those expressed or implied by forward-looking statements include, but are not limited to:

- Trends affecting our financial condition, results of operations or future prospects;
- Our business and growth strategies;
- Our financing plans and forecasts;
- The factors that we expect to contribute to our success and our ability to be successful in the future;
- Our business model and strategy for realizing positive results as sales increase;
- Competition, including our ability to respond to such competition and its expectations regarding continued competition in the market in which we compete;
- Our ability to meet our projected operating expenditures and the costs associated with development of new projects;
- Our ability to pay dividends or to pay any specific rate of dividends, if declared;
- The impact of new accounting pronouncements on our financial statements;
- That our cash flows from operating activities will be sufficient to meet our operating expenditures;
- Our market risk exposure and efforts to minimize risk;
- Development opportunities and our ability to successfully take advantage of such opportunities;
- Regulations, including anticipated taxes, tax credits or tax refunds expected;
- The outcome of various tax audits and assessments, including appeals thereof, timing of resolution of such audits, our estimates as to the amount of taxes that will ultimately be owed and the impact of these audits on our financial statements;
- Our overall outlook including all statements under *Management’s Discussion and Analysis of Financial Condition and Results of Operations*;
- That estimates and assumptions made in the preparation of financial statements in conformity with US GAAP may differ from actual results; and
- Our expectations as to future financial performance, cash and expense levels and liquidity sources.

Any forward-looking statements in this Quarterly Report on Form 10-Q reflect our current views with respect to future events or to our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Factors that may cause actual results to differ materially from current expectations include, among other things, those listed under Part II, Item 1A. “Risk Factors” in this Quarterly Report on Form 10-Q, Part I, Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended August 31, 2017 and our other filings with the SEC. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Except as required by law, we assume no obligation to update or revise these forward-looking statements for any reason, even if new information becomes available in the future.

Unless the context requires otherwise, references in this Quarterly Report on Form 10-Q to “we,” “us” and “our” refer to Kush Bottles, Inc., and its subsidiaries.

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**KUSH BOTTLES, INC.**  
**QUARTERLY REPORT ON FORM 10-Q**  
**FOR THE THREE MONTHS ENDED MAY 31, 2018**  
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## PART I - FINANCIAL INFORMATION

### Item 1. Unaudited Condensed Consolidated Financial Statements

**KUSH BOTTLES, INC.**  
Condensed Consolidated Balance Sheets  
(Unaudited)

	<u>May 31,</u> <u>2018</u>	<u>August 31,</u> <u>2017</u>
<b>ASSETS</b>		
Current assets:		
Cash	\$ 3,574,430	\$ 916,984
Accounts receivable, net of allowance	6,285,310	1,695,303
Prepaid expenses and other current assets	6,736,528	1,625,689
Inventory	10,059,200	3,754,171
Total current assets	<u>26,655,468</u>	<u>7,992,147</u>
Goodwill	51,281,279	34,247,344
Intangible assets, net	3,175,583	3,730,287
Deposits	621,723	50,235
Deferred tax asset	30,081	30,081
Property and equipment, net	2,778,796	931,763
Total Assets	<u>\$ 84,542,930</u>	<u>\$ 46,981,857</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 3,675,579	\$ 1,039,889
Accrued expenses and other current liabilities	2,494,794	993,186
Contingent cash consideration	2,150,000	1,820,000
Notes payable - current portion	145,413	689,450
Line of credit - current portion	2,433,907	-
Total current liabilities	<u>10,899,693</u>	<u>4,542,525</u>
Long-term liabilities:		
Deferred tax liability	1,151,536	1,424,173
Notes payable	185,772	34,513
Total long-term liabilities	<u>1,337,308</u>	<u>1,458,686</u>
Total liabilities	<u>12,237,001</u>	<u>6,001,211</u>
<b>Commitments and contingencies</b>		
<b>Stockholders' equity</b>		
Preferred stock, \$0.001 par value, 10,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$0.001 par value, 265,000,000 shares authorized, 66,389,529 and 58,607,066 shares issued and outstanding, respectively	66,389	58,607
Additional paid-in capital	75,838,222	41,529,283
Accumulated deficit	(3,598,682)	(607,244)
Total stockholders' equity	<u>72,305,929</u>	<u>40,980,646</u>
Total liabilities and stockholders' equity	<u>\$ 84,542,930</u>	<u>\$ 46,981,857</u>

See accompanying notes to the unaudited condensed consolidated financial statements

**KUSH BOTTLES, INC.**  
**Condensed Consolidated Statements of Operations**  
(Unaudited)

	For the three months ended		For the nine months ended	
	May 31,		May 31,	
	2018	2017	2018	2017
Revenue	\$ 12,904,609	\$ 4,719,477	\$ 32,113,100	\$ 10,161,813
Cost of goods sold	9,246,879	3,042,405	22,859,731	6,345,204
Gross profit	<u>\$ 3,657,730</u>	<u>\$ 1,677,072</u>	<u>\$ 9,253,369</u>	<u>\$ 3,816,609</u>
<b>Operating expenses:</b>				
Depreciation	258,837	28,816	666,409	48,294
Stock compensation expense	495,897	259,417	1,904,568	522,226
Selling, general and administrative	4,987,374	1,380,100	9,495,295	3,369,202
Total operating expenses	<u>5,742,108</u>	<u>1,668,333</u>	<u>12,066,272</u>	<u>3,939,722</u>
Income (loss) from operations	<u>(2,084,378)</u>	<u>8,739</u>	<u>(2,812,903)</u>	<u>(123,113)</u>
<b>Other income (expense)</b>				
Other expense	-	-	-	(23,944)
Interest expense	(81,362)	(2,620)	(112,357)	(4,488)
Total other expense	<u>(81,362)</u>	<u>(2,620)</u>	<u>(112,357)</u>	<u>(28,432)</u>
Income (loss) before income taxes	(2,165,740)	6,119	(2,925,260)	(151,545)
Provision for income taxes	-	-	66,178	-
<b>Net Income (Loss)</b>	<u><b>\$ (2,165,740)</b></u>	<u><b>\$ 6,119</b></u>	<u><b>\$ (2,991,438)</b></u>	<u><b>\$ (151,545)</b></u>
<b>Net Income (Loss) per Share:</b>				
Basic net income (loss) per common share outstanding	<u>\$ (0.03)</u>	<u>\$ -</u>	<u>\$ (0.05)</u>	<u>\$ -</u>
Diluted net income (loss) per common share outstanding	<u>\$ (0.03)</u>	<u>\$ -</u>	<u>\$ (0.05)</u>	<u>\$ -</u>
Basic weighted average number of common shares outstanding	<u>64,680,419</u>	<u>51,805,930</u>	<u>61,995,107</u>	<u>50,458,416</u>
Diluted weighted average number of common shares outstanding	<u>64,680,419</u>	<u>53,334,232</u>	<u>61,995,107</u>	<u>50,458,416</u>

See accompanying notes to the unaudited condensed consolidated financial statements

**KUSH BOTTLES, INC.**  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	<b>For the nine months ended May 31,</b>	
	<b>2018</b>	<b>2017</b>
<b>Cash flows from operating activities</b>		
Net loss	\$ (2,991,438)	\$ (151,545)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	666,410	142,814
Depreciation cost of goods sold	125,111	-
Stock compensation expense	1,904,568	522,226
Changes in operating assets and liabilities:		
Accounts receivable	(4,119,337)	(625,760)
Provisions for deferred taxes	(272,637)	-
Prepays	(3,715,284)	(213,436)
Inventory	(6,068,029)	(1,305,102)
Accounts payable	1,371,469	634,741
Accrued expenses and other current liabilities	869,209	94,603
<b>Net cash used in operating activities</b>	<b>(12,229,958)</b>	<b>(901,459)</b>
<b>Cash flows from investing activities</b>		
Acquisition of web domain	(9,321)	(150,000)
Security deposits	(571,488)	(28,379)
Acquisition of CMP Wellness, LLC	-	(1,500,000)
Purchase of property and equipment	(987,746)	(777,542)
Acquisition of Summit Innovations Gas, LLC, net of cash received	(945,218)	-
<b>Net cash used by investing activities</b>	<b>(2,513,773)</b>	<b>(2,455,921)</b>
<b>Cash flows from financing activities</b>		
Repayment of the car loans	(247,907)	-
Repayment of Summit loans	(711,896)	-
Payment of earn-out	(170,000)	-
Proceeds from note payable	-	24,785
Repayment of note payable	(583,441)	(21,614)
Proceeds from line of credit	2,433,907	-
Proceeds from stock option exercises	245,791	44,001
Proceeds from sale of stock	16,434,723	3,009,897
<b>Net cash provided by financing activities</b>	<b>17,401,177</b>	<b>3,057,069</b>
<b>Net increase (decrease) in cash</b>	<b>2,657,446</b>	<b>(300,311)</b>
<b>Cash at beginning of period</b>	<b>916,984</b>	<b>1,027,003</b>
<b>Cash at end of period</b>	<b>\$ 3,574,430</b>	<b>\$ 726,692</b>
<b>Supplemental Disclosures of Cash Flow Information:</b>		
Cash paid for:		
Interest	73,706	3,855
Income taxes	330,000	-
<b>Non-cash investing and financing activities</b>		
Services prepaid for in common stock	\$ 1,308,929	\$ 169,955
Shares issued for accounts payable	\$ 112,310	\$ -
Fair value of shares issued related to acquisition of business	\$ -	\$ 19,500,000
Fair value of shares issued related to acquisition of web domain	\$ -	\$ 466,000
Fair value of contingent equity consideration	\$ -	\$ 11,229,760
Reclass Summit tax payable from loan payable short term	\$ 274,363	\$ -
Purchase of property and equipment on credit	\$ 204,315	\$ -

See accompanying notes to the condensed consolidated financial statements

**KUSH BOTTLES, INC.**  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

**For the nine months ended May 31,**

	<b>2018</b>	<b>2017</b>
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**Supplemental Disclosures - Acquisition:**

Accounts receivable	\$	470,670
Prepaid expense and other current assets		86,626
Inventory		237,000
Property and equipment, net		648,770
Goodwill		17,033,935
Accounts payable		(1,376,531)
Accrued expenses		(358,035)
Notes payable		(986,816)
Stock consideration		(14,310,400)
Contingent cash consideration liability		(500,000)
Acquisition of Summit Innovations Gas, LLC	\$	945,218

See accompanying notes to the condensed consolidated financial statements

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(UNAUDITED)**

**NOTE 1 - NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES**

Nature of Business

Kush Bottles, Inc. (“the Company”) was incorporated in the state of Nevada on February 26, 2014. The Company provides customizable packaging products, vaporizers, hydrocarbon gases, solvents, accessories and branding solutions for the cannabis industry. Representative examples of the Company’s products include pop-top bottles, vaporizer cartridges and accessories, exit/barrier bags, tubes, and other small-sized containers. The Company’s wholly owned subsidiary Kim International Corporation (KIM), a California corporation, was originally incorporated as Hy Gro Economics Corporation (“Hy Gro”) on December 2, 2010. On October 30, 2012, Hy Gro amended its articles of incorporation to reflect a name change to KIM International Corporation (KIM). On March 4, 2014, the shareholders of KIM exchanged all 10,000 of their common shares for 32,400,000 shares of common stock of Kush Bottles, Inc. The operations of KIM became the operations of Kush after the share exchange and accordingly the transaction is accounted for as a recapitalization of KIM whereby the historical financial statements of KIM are presented as the historical financial statements of the combined entity. KIM was the acquiring entity in accordance with ASC 805, Business Combinations. The accumulated losses of KIM were carried forward after the completion of the share exchange. Operations prior to the share exchange were those of KIM.

Acquisition of CMP Wellness, LLC

On May 1, 2017, the Company entered into an agreement of merger agreement with Lancer West Enterprises, Inc. a California corporation, Walnut Ventures, a California corporation, Jason Manasse, an individual, and Theodore Nicols, an individual, pursuant to which each of Lancer West Enterprises, Inc. and Walnut Ventures were merged with and into Merger Sub, with Merger Sub as the surviving corporation, resulting in the Company’s indirect acquisition of CMP Wellness, LLC, a California limited liability company, which prior to the merger, was owned 100% by Lancer West Enterprises, Inc. and Walnut Ventures. CMP Wellness, LLC is a distributor of vaporizers, cartridges and accessories. See Note 2 for a further description of the CMP acquisition.

Acquisition of Summit Innovations, LLC

On May 2, 2018, the Company completed its acquisition of Summit Innovations, LLC (“Summit”), a leading distributor of hydrocarbon gases to the legal cannabis industry. Pursuant to the terms of the Agreement and Plan of Merger (the “Merger Agreement”), Summit merged with and into KCH Energy, LLC (“KCH”), a wholly-owned subsidiary of the Company, with KCH as the surviving entity. See Note 3 for a further description of the Summit acquisition.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements and related notes include the activity of the Company and its wholly owned subsidiaries and have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information. All intercompany balances and transactions have been eliminated. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. The Company’s operating results for the three and nine months period ended May 31, 2018 are not necessarily indicative of the results that may be expected for the fiscal year ended August 31, 2018, or for any other period. These unaudited condensed consolidated financial statements and notes should be read in conjunction with the Company’s audited consolidated financial statements and accompanying notes for the fiscal year ended August 31, 2017. The condensed consolidated balance sheet as of August 31, 2017 included herein was derived from the audited financial statements as of that date, but does not include all disclosures including notes required by GAAP. There have been no changes to the Company’s significant accounting policies described in its Annual Report on Form 10-K for the fiscal year ended August 31, 2017 that have had a material impact on our condensed consolidated financial statements and related notes.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amount of revenues and expenses during the reporting period.

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(UNAUDITED)**

Significant estimates relied upon in preparing these unaudited condensed consolidated financial statements include revenue recognition, accounts receivable reserves, inventory and related reserves, valuations and purchase price allocations related to business combinations, expected future cash flows used to evaluate the recoverability of long-lived assets, estimated fair values of long-lived assets used to record impairment charges related to intangible assets and goodwill, amortization periods, accrued expenses, stock-based compensation, contingent liabilities and recoverability of the Company's net deferred tax assets and any related valuation allowance.

Although the Company regularly assesses these estimates, actual results could differ materially from these estimates. Changes in estimates are recorded in the period in which they become known. The Company bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the circumstances. Actual results may differ from management's estimates.

The Company is subject to a number of risks similar to those of other companies of similar size and having a focus of serving the cannabis industry, including, the development stage of certain products, competition, limited number of suppliers, integration of acquisitions, substantial indebtedness, government regulations, protection of proprietary rights, and dependence on key individuals.

Reclassification

Certain classifications have been made to the prior year financial statements to conform to the current year presentation. The reclassification had no impact on previously reported net income (loss) or accumulated deficit.

Segments

The Company operates as one operating segment. Operating segments are defined as components of an enterprise for which separate financial information is evaluated regularly by the chief operating decision maker, who is the chief executive officer, in deciding how to allocate resources and assessing performance. Over the past few years, the Company has completed a number of acquisitions. These acquisitions have allowed the Company to expand its offerings, presence and reach in the cannabis industry. While the Company has offerings in multiple geographic locations for its products for the cannabis industry, including as a result of the Company's acquisitions, the Company's business operates in one operating segment because the majority of the Company's offerings operate similarly, and the Company's chief operating decision maker evaluates the Company's financial information and resources and assesses the performance of these resources on a consolidated basis. Since the Company operates in one operating segment, all required financial segment information can be found in the unaudited condensed consolidated financial statements.

Accounts Receivable

Trade accounts receivable are carried at their estimated collectible amounts. Trade credit is generally extended on a short-term basis, thus trade receivables do not bear interest. Trade accounts receivables are periodically evaluated for collectability based on past credit history and their current financial condition. The Company's allowance for doubtful accounts was \$132,000 and \$25,000 as of May 31, 2018 and August 31, 2017, respectively.

Inventory

Inventories are stated at the lower of cost or net realizable value using the first-in first out (FIFO) method. The Company's inventory consists of finished goods of \$10,059,200 and \$3,754,171 as of May 31, 2018 and August 31, 2017, respectively.

Fair Value of Financial Instruments

The fair value of certain of the Company's financial instruments, including cash and cash equivalents, receivables, other current assets, accounts payable, accrued compensation and employee benefits, other accrued liabilities and notes payable, approximate their carrying amounts because of the short-term maturity of these instruments.

Valuation of Business Combinations and Acquisition of Intangible Assets

The Company records intangible assets acquired in business combinations and acquisitions of intangible assets under the purchase method of accounting. The Company accounts for acquisitions in accordance with FASB ASC Topic 805, *Business Combinations*. Amounts paid for each acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the dates of acquisition. The Company then allocates the purchase price in excess of the fair value of the net tangible assets acquired to identifiable intangible assets, including purchased intangibles based on detailed valuations that use information and assumptions provided by management. The Company allocates any excess purchase price over the fair value of the net tangible and intangible assets acquired to goodwill.

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(UNAUDITED)**

The Company uses the income approach, the relief from royalty method (both a market and income method), and the with and without method to determine the fair values of its purchased intangible assets. The Company uses the probability-weighted expected return method (an income approach) to determine the appropriate amount of contingent consideration to include in the purchase price for an acquisition. The Company bases its revenue assumptions on estimates of relevant market sizes, expected market growth rates, expected industry trends and expected product introductions by competitors. In arriving at the value. The Company bases the discount rate used to arrive at a present value as of the date of acquisition on the time value of money and cannabis industry investment risk factors. For the intangible assets acquired, the Company used risk-adjusted discount rates ranging from 19% to 26% to discount its projected cash flows. The Company believes that the estimated purchased intangible asset amounts so determined represent the fair value at the date of acquisition and do not exceed the amount a third party would pay for the projects.

The Company also used the income approach (probably weighted cash flow), as described above, to determine the estimated fair value of certain identifiable intangibles assets including domain names and tradenames. Domain names represent established relationships with customers, which provides a ready channel for the sale of additional products and services. Tradenames represent acquired product names that the Company intends to continue to utilize. The Company used the with and without method to ascertain the fair value of the non-competition agreement.

The company has not completed the valuation of Summit's assets acquired and liabilities assumed as of May 31, 2018.

Goodwill and Intangible Assets

Goodwill and intangible assets that have indefinite useful lives are not amortized but are evaluated for impairment annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The Company records intangible assets at historical cost. The Company amortizes its intangible assets that have finite lives using either the straight-line method or based on estimated future cash flows to approximate the pattern in which the economic benefit of the asset will be utilized. Amortization is recorded over the estimated useful lives ranging from four to six years. The Company reviews intangible assets subject to amortization quarterly to determine if any adverse conditions exist or a change in circumstances has occurred that would indicate impairment or a change in the remaining useful life. Conditions that would indicate impairment and trigger a more frequent impairment assessment include, but are not limited to, a significant adverse change in legal factors or business climate that could affect the value of an asset, or an adverse action or assessment by a regulator. If the carrying value of an asset exceeds its undiscounted cash flows, the Company will write-down the carrying value of the intangible asset to its fair value in the period identified. The Company generally calculates fair value as the present value of estimated future cash flows to be generated by the asset using a risk-adjusted discount rate. If the estimate of an intangible asset's remaining useful life is changed, the Company will amortize the remaining carrying value of the intangible asset prospectively over the revised remaining useful life.

Consistent with prior years, the Company conducted its annual impairment test of goodwill during the fourth quarter of fiscal 2018. The estimate of fair value requires significant judgment. Any loss resulting from an impairment test would be reflected in operating income in the Company's unaudited condensed consolidated statements of income. The annual impairment testing process is subjective and requires judgment at many points throughout the analysis. If these estimates or their related assumptions change in the future, the Company may be required to record impairment charges for these assets not previously recorded. The Company performed its goodwill impairment test as of June 1, 2018 and goodwill was not impaired.

Business Combinations

The Company uses its best estimates and assumptions to accurately assign fair value to the tangible and intangible assets acquired and liabilities assumed at the acquisition date. The Company's estimates are inherently uncertain and subject to refinement. During the measurement period, which may be up to one year from the acquisition date, the Company may record adjustments to the fair value of these tangible and intangible assets acquired and liabilities assumed, with the corresponding offset to goodwill. In addition, uncertain tax positions and tax-related valuation allowances are initially established in connection with a business combination as of the acquisition date. The Company continues to collect information and reevaluates these estimates and assumptions quarterly and records any adjustments to the Company's preliminary estimates to goodwill provided that the Company is within the measurement period. Upon the conclusion of the measurement period or final determination of the fair value of assets acquired or liabilities assumed, whichever comes first, any subsequent adjustments are recorded to the Company's condensed consolidated statements of operations.

Earnings (Loss) Per Share

The Company computes earnings per share under Accounting Standards Codification subtopic 260-10, "Earnings per Share" ("ASC 260-10"). Basic net income (loss) per common share is computed by dividing net loss by the weighted average number of shares of common stock. Diluted net loss per share is computed using the weighted average number of common and common stock equivalent shares outstanding during the period.

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Basic earnings per share are computed by dividing net earnings by the weighted average number of shares of common stock outstanding during the period. Diluted earnings per share are computed by dividing net earnings by the sum of (a) the weighted average number of shares of common stock outstanding during the period and (b) the potentially dilutive securities outstanding during the period. Stock options are potentially dilutive securities; and the number of dilutive options is computed using the treasury stock method. The effect of the contingent equity consideration relating to the acquisitions of CMP and Summit is also factored into the calculation of dilutive securities.

The following table sets forth the calculation of basic and diluted earnings per share:

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>May 31, 2018</b>	<b>May 31, 2017</b>	<b>May 31, 2018</b>	<b>May 31, 2017</b>
Net income	\$ (2,165,740)	\$ 6,119	\$ (2,991,438)	\$ (151,545)
Weighted average common shares outstanding:				
Basic	64,680,419	51,805,930	61,995,107	50,458,416
Net effect of dilutive options	-	1,528,302	-	-
Diluted	64,680,419	53,334,232	61,995,107	50,458,416
Earnings per share:				
Basic	\$ (0.03)	\$ -	\$ (0.05)	\$ -
Diluted	\$ (0.03)	\$ -	\$ (0.05)	\$ -

Potentially dilutive securities consisted of 7,231,042 and 4,695,000 stock options as of May 31, 2018 and 2017, respectively.

Additionally, the approximately 640,000 shares of Common Stock held back by the Company for a period of 15 months for potential post-closing working capital and/or indemnification claims relating to, among other things, breaches of representations, warranties and covenants contained in the Summit Merger Agreement and the potential earn-out consideration of up to an additional 1,280,000 shares of common stock, in the aggregate, based on the performance of the Summit business during a one-year period following the closing were not included in earnings per share because it is not certain that the shares will be issued.

Revenue Recognition

It is the Company's policy that revenues from product sales is recognized in accordance with ASC 605 "Revenue Recognition". Four basic criteria must be met before revenue can be recognized; (1) persuasive evidence of an arrangement exists; (2) delivery has occurred; (3) the selling price is fixed and determinable; and (4) collectability is reasonably assured. Determination of criteria (3) and (4) are based on management's judgments regarding fixed nature in selling prices of the products delivered and the collectability of those amounts. The Company has not implemented any specific rebate programs. Provisions for discounts to customers, estimated returns and allowances, and other adjustments are provided for in the same period the related sales are recorded. During the three-month period ended May 31, 2018 and 2017, the Company had no provisions for sales discounts of \$140,018 and \$40,806, respectively. The Company has not established a formal customer incentive program, but considers and accommodates discounts to certain customers on a case by case basis, including by way of example, for volume shipping or for certain new customers with orders over a specific discretionary dollar threshold. The Company classifies the reimbursement by customers of shipping and handling costs as revenue and the associated cost as cost of revenue.

As of May 31, 2018 and 2017, the Company had a refund allowance of nil, respectively. Consistent with ASC 605-15-25-1, the Company considers factors such as historical return of products, estimated remaining shelf life, price changes from competitors, and introductions of competing products in establishing a refund allowance. The Company recognizes revenues when and title to products transfers to the customer (which generally occurs at the time shipment is made), the sales price is fixed or determinable, and collectability is reasonably assured. The Company defers any revenue for which the product was not delivered or is subject to refund until such time that the Company and the customer jointly determine that the product has been delivered or no refund will be required.

Warranty Costs

The Company has not had any historical warranty related expenditures and so does not record a reserve for warranty costs.

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Fair Value of Financial Instruments

The Company adopted ASC 820 which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). The standard outlines a valuation framework and creates a fair value hierarchy in order to increase the consistency and comparability of fair value measurements and the related disclosures. Under this standard certain assets and liabilities must be measured at fair value, and disclosures are required for items measured at fair value.

The Company currently does not have non-financial assets or non-financial liabilities that are required to be measured at fair value on a recurring basis. The Company's financial assets and liabilities are measured using inputs from the three levels of the fair value hierarchy. The three levels are as follows:

Level 1 - Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date. The fair value of the Company's cash is based on quoted prices and therefore classified as Level 1.

Level 2 - Inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates, yield curves, etc.), and inputs that are derived principally from or corroborated by observable market data by correlation or other means (market corroborated inputs).

Level 3 - Unobservable inputs that reflect management's assumptions about the assumptions that market participants would use in pricing the asset or liability.

*Application of Valuation Hierarchy*

Financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The following is a description of the valuation methodology used to measure fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy.

The Company has a contingent consideration liability of \$2,150,000 which consists of contingent cash consideration of \$1,650,000 resulting from the acquisition of CMP and \$500,000 resulting from the acquisition of Summit. The contingent consideration liability is calculated based on the weighted average probability of meeting certain milestones. This liability is remeasured at each reporting period. The Company had no other financial assets or liabilities that are measured at fair value on a recurring basis as of May 31, 2018.

The following table summarizes, for assets or liabilities measured at fair value, the respective fair value and the classification by level of input within the fair value hierarchy:

Description	May 31, 2018	Fair Value Measurement at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Contingent consideration liability	\$ 2,150,000	\$ -	\$ -	\$ 2,150,000

The Company classifies its contingent consideration liability within Level 3 as the valuation inputs are based on quoted market prices and market observable data. During the nine months ended May 31, 2018, a payment of \$170,000 was made towards this liability, an increase of \$500,000 resulted from the Summit acquisition, resulting in a net liability of \$2,150,000. During the three months ended May 31, 2018, the Company did not recognize any change in the fair value of its contingent consideration liability of \$2,150,000.

Recently Issued Accounting Pronouncements

On December 22, 2017 the Securities and Exchange Commission ("SEC") staff issued Staff Accounting Bulletin 118 (SAB 118), which provides guidance on accounting for the tax effects of the Tax Cuts and Jobs Act (the TCJA). SAB 118 provides a measurement period that should not extend beyond one year from the enactment date for companies to complete the accounting under ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the TCJA for which the accounting under ASC 740 is complete. To the extent that a company's accounting for certain income tax effects of the TCJA is incomplete but for which they are able to determine a reasonable estimate, it must record a provisional amount in the financial statements. Provisional treatment is proper in light of anticipated additional guidance from various taxing authorities, the SEC, the FASB, and even the Joint Committee on Taxation. If a company cannot determine a provisional amount to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the TCJA. The Company is still in the process of estimating the tax impact and is expected to apply this guidance at year end.

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In September 2017, the Financial Accounting Standards Board “FASB” issued Accounting Standards Update (ASU) No. 2017-13, “*Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017 EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments.*” The amendments in ASU No. 2017-13 amends the early adoption date option for certain companies related to the adoption of ASU No. 2014-09 and ASU No. 2016-02. The Company may still adopt using the public company adoption guidance in the related ASUs, as amended. The effective date is the same as the effective date and transition requirements for the amendments for ASU 2014-09 and ASU 2016-02.

In March 2017, the FASB issued ASU 2017-08, “*Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities*”. This update shortens the amortization period of a callable security that is held at a premium to the earliest call date of that security instead of the contractual life of the security. Although the Company does not currently hold any callable securities at a premium, it may do so in the future. Unless such securities are purchased by the Company, the Company does not believe that ASU 2017-08 will have an impact its consolidated financial statements effective beginning January 1, 2019.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04, *Simplifying the Test for Goodwill Impairment* (“ASU 2017-04”). ASU 2017-04 simplifies the accounting for goodwill impairment by removing Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation. ASU 2017-04 is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019 and should be applied on a prospective basis. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not anticipate the adoption of ASU 2017-04 will have a material impact on its consolidated financial statements.

In January 2017, the FASB issued Accounting Standards Update No. 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business* (ASU 2017-01), which revises the definition of a business and provides new guidance in evaluating when a set of transferred assets and activities is a business. This guidance will be effective for the Company in the first fiscal quarter of 2018 on a prospective basis, and early adoption is permitted. The Company does not expect the standard to have a material impact on its consolidated financial statements. The Company adopted this standard on March 1, 2018 and the adoption did not have a material on its consolidated financial statements.

In August, 2016, the FASB issued Accounting Standards Update No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)* (“ASU 2016-15”). The amendments in ASU 2016-15 address eight specific cash flow issues and apply to all entities that are required to present a statement of cash flows under ASC Topic 230, *Statement of Cash Flows*. The amendments in ASU 2016-15 are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption during an interim period. The Company has not yet completed the analysis of how adopting this guidance will affect its consolidated financial statements.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, “*Revenue from Contracts with Customers (Topic 606)*” (“ASU 2014-09”), and subsequently issued modifications or clarifications in ASU No. 2015-14, “*Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date,*” ASU 2016-08, “*Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net),*” ASU No. 2016-10, “*Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing,*” and ASU No. 2016-12, “*Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients.*” The revenue recognition principle in ASU 2014-09 and the related guidance is that an entity should recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 prescribes a five-step process for evaluating contracts and determining revenue recognition. In addition, new and enhanced disclosures are required. Companies may adopt the new standard either using the full retrospective approach, a modified retrospective approach with practical expedients, or a cumulative effect upon adoption approach. The Company has not yet determined whether the impact that this new guidance will be material to its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. The amendments in this update change existing guidance related to accounting for employee share-based payments affecting the income tax consequences of awards, classification of awards as equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within those annual periods, with early adoption permitted. The Company adopted this standard on September 1, 2017 and the adoption did not have a material on its consolidated financial statements.

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In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the consolidated balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the consolidated income statement. ASU 2016-02 is effective for annual periods beginning after December 15, 2018, including interim periods within those annual periods, with early adoption permitted. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the potential impact of the adoption of this standard.

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this update revise the accounting related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. The amendments are effective for annual reporting periods after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the potential impact of the adoption of this standard.

Other Accounting standards that have been issued or proposed by FASB that do not require adoption until a future date are not expected to have a material impact on the consolidated financial statements upon adoption. The Company does not discuss recent pronouncements that are not anticipated to have an impact on or are unrelated to its financial condition, results of operations, cash flows or disclosures.

**NOTE 2 – ACQUISITION OF CMP WELLNESS, LLC**

On May 1, 2017 (“Merger Date”), the Company and KBCMP, Inc., a Delaware corporation and newly formed wholly-owned subsidiary of the Company (“Merger Sub”), entered into an Agreement of Merger (the “Merger Agreement”) with Lancer West Enterprises, Inc. a California corporation and Walnut Ventures, a California corporation, pursuant to which each of Lancer West Enterprises, Inc. and Walnut Ventures were merged with and into Merger Sub, with Merger Sub as the surviving corporation, resulting in the Company’s indirect acquisition of CMP Wellness, LLC (“CMP”), a California limited liability company, which prior to the merger, was owned 100% by Lancer West Enterprises, Inc. and Walnut Ventures. Membership interest in CMP was the sole and only asset of Lancer West Enterprises, Inc. and Walnut Ventures. As a result, CMP became a wholly-owned subsidiary of the Company. CMP is a distributor of vaporizers, cartridges and accessories. The Company’s Directors believed the acquisition of CMP and the product offerings of CMP leveraged the Company’s existing product development program and provided the Company with the possibility of generating near term revenue and operating cash flow, as well as establishing a commercial platform whereby other cannabis industry-support products may be accessed in the future. Going forward, the existing product offering and other product licensing opportunities, will be the basis of the Company’s long-term product portfolio.

The acquisition consideration consisted of a cash payment of \$1,500,000, unsecured promissory notes in the aggregate principal amount of approximately \$770,820, having a one-year maturity, and an aggregate of 7,800,000 restricted shares of the Company’s common stock (equal to 12% of the Company’s common stock outstanding as of May 31, 2018). During the one-year period following the closing, the two sellers of CMP may become entitled to receive up to an additional \$1,905,000 in cash, in the aggregate, and 4,740,960 shares of common stock of the Company, in the aggregate, based on the gross profit generated by CMP product line for the period from May 1, 2017 to April 30, 2018. Per the terms of the Merger Agreement, post-closing adjustments to CMP’s working capital is directly offset to the unsecured promissory notes payable. Management has estimated that the post-closing working capital adjustments amounted to \$104,032, which management estimates will result in a decrease of the unsecured promissory notes payable from \$770,820 to \$666,788. In accordance with ASC 805, management has evaluated the estimated fair value of the contingent consideration based a probability-weighted assessment of the occurrence of CMP reaching certain gross profit earnout targets. The Company initially recorded a contingent liability for the contingent cash consideration of \$1,735,375 and recorded contingent equity consideration of \$10,763,760. Based on information obtained during the fourth fiscal quarter, the Company revised its estimate of the contingent cash consideration from \$1,735,375 to \$1,905,000, and its estimate of the contingent equity consideration from \$10,763,760 to \$11,852,400. A payment of \$85,000 was made towards this liability during the year ended August 31, 2017, resulting in a net liability of \$1,820,000. During the six months ended February, a payment of \$170,000 was made towards this liability, resulting in a net liability of \$1,650,000. During the three months ended May 31, 2018, the Company did not recognize any change in the fair value of its contingent consideration liability of \$1,650,000.

CMP’s assets acquired and liabilities assumed are recorded at their acquisition-date fair values. As part of the purchase price allocation, all intangible assets that were a part of the acquisition were identified and valued. It was determined that only non-competition agreements and trade name had separately identifiable values. Trade name represents the CMP product names that the Company intends to continue to use. The deferred income tax liability relates to the tax effect of acquired identifiable intangible assets as such amounts are not deductible for tax purposes. For the acquisition discussed above, goodwill represents the excess of the purchase price over the net identifiable tangible and intangible assets acquired. The Company determined that the acquisition of CMP resulted in the recognition of goodwill primarily because of synergies unique to the Company and the strength of its acquired workforce.

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The results of operations of CMP were consolidated beginning on the date of the merger. Acquisition-related transaction costs are not included as a component of consideration transferred, but are accounted for as an expense in the period in which the costs are incurred. Any excess of the acquisition consideration over the fair value of tangible and intangible assets acquired and liabilities assumed is allocated to goodwill. The amount of contingent consideration was recorded at its estimated fair value as of the acquisition date. The subsequent accounting for contingent consideration depends on whether the contingent consideration is classified as a liability or equity. The portion of contingent consideration classified as equity is not remeasured in subsequent accounting periods. However, contingent consideration classified as a liability is remeasured to its fair value at the end of each reporting period and the change in fair value is reflected in income or expense during that period. Any changes within the measurement period resulting from facts and circumstances that existed as of the acquisition date may result in retrospective adjustments to the provisional amounts recorded at the acquisition date.

The equity consideration received by CMP members was calculated based on the negotiated price per share of common stock of the Company of \$2.50, which approximated the quoted market price on the acquisition date. The contingent equity consideration (number of common shares) was also calculated based on the negotiated price per share of common stock of the Company of \$2.50, which approximated the quoted market price. The total preliminary acquisition consideration used in preparing the consolidated financial statements is as follows:

**Acquisition Consideration:**

	<b>May 1, 2017</b> <b>(As initially</b> <b>reported)</b>	<b>Measurement</b> <b>Period</b> <b>Adjustments (1)</b>	<b>August 31,</b> <b>2017</b> <b>(As adjusted)</b>
Cash	\$ 1,500,000	\$ —	\$ 1,500,000
Fair value of common shares issued to CMP members	19,500,000	—	19,500,000
Promissory notes	660,216	6,572	666,788
Estimated fair value contingent cash consideration	1,735,375	169,625	1,905,000
Estimated fair value contingent equity consideration	10,763,760	1,088,640	11,852,400
Total estimated acquisition consideration	<u>\$ 34,159,351</u>	<u>\$ 1,264,837</u>	<u>\$ 35,424,188</u>

- (1) As of August 31, 2017, the Company revised its estimate of the contingent cash consideration from \$1,735,375 to \$1,905,000, and the Company revised its estimate of the contingent equity consideration from \$10,763,760 to \$11,852,400, to reflect the increased probability of the sellers of CMP reaching the maximum earnouts available. An additional post-closing adjustment of \$6,572 was recorded, which resulted in an increase of the promissory notes from \$660,216 to \$666,788. The balance of the note payable at May 31, 2018 reflects principal payments of \$583,440 made to the sellers of CMP. The balance of the contingent cash consideration \$1,650,000 as of May 31, 2018, reflects a decrease of \$255,000 due to cash payments made to the sellers of CMP.

**NOTE 3 - ACQUISITION OF SUMMIT INNOVATIONS, LLC**

On May 2, 2018, the Company completed its acquisition of Summit, a leading distributor of hydrocarbon gases to the legal cannabis industry. Pursuant to the terms of the Merger Agreement with Summit, Summit merged with and into KCH, a wholly-owned subsidiary of the Company, with KCH as the surviving entity.

The acquisition was accounted for using the acquisition method of accounting in accordance with ASC 805, Business Combinations. The consideration paid to the Members of Summit at the closing included the Cash Consideration, consisting of an aggregate of \$1.4 million in cash, net of cash received and the Share Consideration, consisting of an aggregate of 1,280,000 shares common stock. \$500,000 of the Cash Consideration and approximately 640,000 shares of common stock from the Share Consideration were held back by the Company for a period of 15 months for potential post-closing working capital and/or indemnification claims relating to, among other things, breaches of representations, warranties and covenants contained in the Merger Agreement. The Members may become entitled to receive earn-out consideration of up to an additional 1,280,000 shares of common stock, in the aggregate, based on the net revenue performance of the Summit business during a one-year period following the closing.

The Company estimated the probability of the contingent consideration at 100% and recorded the earn-out consideration of the additional 1,280,000 shares of common stock in stockholders' equity.

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The preliminary total purchase price (based on the \$5.59 May 2, 2018 closing price) was as follows:

	<b>Shares</b>	<b>Dollars</b>
Company stock	640,000	\$ 3,577,600
Company stock held back	640,000	3,577,600
Contingent company stock consideration	1,280,000	7,155,200
Cash, net of cash received	-	945,218
Cash held back	-	500,000
<b>Total purchase price</b>	<b><u>2,560,000</u></b>	<b><u>\$15,755,618</u></b>

The following table summarizes the allocation of the preliminary purchase price to the assets acquired and liabilities assumed:

Accounts receivable	\$ 470,670
Prepaid expense and other current assets	86,626
Inventory	237,000
Property and equipment, net	648,770
Goodwill	17,033,935
Accounts payable	(1,376,531)
Accrued expenses	(358,035)
Notes payable	(986,816)
<b>Total purchase price</b>	<b><u>\$15,755,618</u></b>

The following unaudited pro forma financial data assumes the acquisition had occurred at September 1, 2016. Pro forma results have been prepared by adjusting the Company's historical results to include Summit's results of operations. The unaudited pro forma results presented do not necessarily reflect the results of operations that would have resulted had the acquisition been completed at September 1, 2016, nor do they indicate the results of operations in future periods. Additionally, the unaudited pro forma results do not include the impact of possible business model changes, nor do they consider any potential impacts of current market conditions or revenues, reduction of expenses, asset dispositions, or other factors. The impact of these items could alter the following pro forma results (\$ in thousands):

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	<b>Three Months Ended</b>	<b>Three Months Ended</b>
	<b>May 31, 2018</b>	<b>May 31, 2017</b>
	<b>Unaudited</b>	<b>Unaudited</b>
Total revenues	\$ 13,860,746	\$ 4,735,295
Net income (loss)	\$ (2,778,867)	\$ (83)
Loss per share:		
Basic	\$ (0.04)	\$ (0.00)
Diluted	\$ (0.04)	\$ (0.00)

	<b>Nine Months Ended</b>	<b>Nine Months Ended</b>
	<b>May 31, 2018</b>	<b>May 31, 2017</b>
	<b>Unaudited</b>	<b>Unaudited</b>
Total revenues	\$ 35,249,655	\$ 10,177,631
Net income (loss)	\$ (4,285,427)	\$ (157,747)
Loss per share:		
Basic	\$ (0.07)	\$ (0.00)
Diluted	\$ (0.07)	\$ (0.00)

**NOTE 4 - CONCENTRATIONS OF RISK**

Supplier Concentrations

The Company purchases inventory from various suppliers and manufacturers. For the nine months ended May 31, 2018 and 2017, two vendors, Transpring And Shenzhen Buddy Technology Co. Ltd., accounted for approximately 14% and 22%, respectively, of total inventory purchases.

Customer Concentrations

During the nine months ended May 31, 2018 there was no customer which represented over 10% of the Company's revenues there were no such customers for the same period ended May 31, 2017. As of May 31, 2018, there were two customers who represented 8% of accounts receivable. As of May 31, 2017, there was one customer that accounted for over 10% of accounts receivable.

**NOTE 5 - RELATED-PARTY TRANSACTIONS**

The Company leases its California and Colorado facilities from related parties. During the nine months ended May 31, 2018 and 2017, the Company made rent payments of \$161,100 and \$152,100, respectively, to these related parties.

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**NOTE 6 - PROPERTY AND EQUIPMENT**

The major classes of fixed assets consist of the following as of May 31, 2018 and August 31, 2017:

	<b>May 31, 2018</b>	<b>August 31, 2017</b>
Machinery and equipment	\$1,422,523	\$ 886,608
Vehicles	378,543	144,845
Office Equipment	219,123	118,387
Leasehold improvements	800,120	71,545
Gas Tanks - Summit	593,974	-
	<u>3,414,283</u>	<u>1,221,385</u>
Accumulated Depreciation	<u>(635,487)</u>	<u>(289,622)</u>
	<u>\$2,778,796</u>	<u>\$ 931,763</u>

Depreciation expense was \$113,258 and \$ 51,297 for the three months ended May 31, 2018 and 2017, respectively. Of the \$113,258 of depreciation expense, \$70,885 is included in depreciation and amortization expense and \$42,373 is included in cost of goods sold on the consolidated statements of operations.

Depreciation expense was \$227,496 and \$124,393 for the nine months ended May 31, 2018 and 2017, respectively. Of the \$227,496 of depreciation expense, \$102,385 is included in depreciation and amortization expense and \$125,111 is included in cost of goods sold on the consolidated statements of operations.

**NOTE 7 - INTANGIBLE ASSETS AND GOODWILL**

Intangible assets consist of the following as of May 31, 2018 and August 31, 2017:

<b>Acquisition</b>	<b>Description</b>	<b>Weighted Average Estimated Useful Life</b>	<b>As of May 31, 2018</b>		<b>As of August 31, 2017</b>	
			<b>Gross Carrying Value</b>	<b>Accumulated Amortization</b>	<b>Gross Carrying Value</b>	<b>Accumulated Amortization</b>
Roll-Uh-Bowl	Domain name	5 years	\$ 598,605	\$ (136,910)	\$ 589,284	\$ (47,886)
CMP Wellness, LLC	Trade name	6 years	2,600,000	(469,444)	2,600,000	(144,444)
	Non-compete agreement	4 years	800,000	(216,667)	800,000	(66,667)
			<u>\$ 3,998,605</u>	<u>\$ (823,022)</u>	<u>\$ 3,989,284</u>	<u>\$ (258,997)</u>

The activity in the goodwill balance for the nine months ended May 31, 2018 was as follows:

Balance - August 31, 2017	\$34,247,344
Summit acquisition (Note 2)	17,033,935
Balance - May 31, 2018	<u>\$51,281,279</u>

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**NOTE 8 - ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accrued expenses and other current liabilities consist of the following as of May 31, 2018 and August 31, 2017:

	<b>May 31, 2018</b>	<b>August 31, 2017</b>
Customer deposits	\$ 750,950	\$ 319,492
Accrued compensation	388,342	245,975
Income tax payable	1,774	219,082
Credit card liabilities	198,709	142,157
Deferred revenue	476,384	-
Deferred rent	25,301	25,881
Sales tax payable	364,601	17,182
Other accrued expenses	288,734	23,417
	<u>\$2,494,794</u>	<u>\$ 993,186</u>

**NOTE 9 - NOTES PAYABLE**

Notes payable – current portion consists of unsecured promissory notes relating to the CMP acquisition with a principal balance of \$83,348 and vehicle loans with an aggregate principal balance of \$62,065 for the sum of \$145,413, as described below.

As partial consideration for the acquisition of CMP, the Company issued the sellers unsecured promissory notes totaling \$770,820. Management has estimated that the post-closing working capital adjustments amounted to \$104,032, which resulted in a decrease of the unsecured promissory notes payable from \$770,820 to \$666,788. The promissory notes matured on May 1, 2018 (however, this note payable remains outstanding as of July 9, 2018) and bear interest at an annual rate of 1.15%. The notes and accrued and unpaid interest are payable in quarterly installments beginning August 1, 2017. As of May 31, 2018, management has accrued for \$0 of interest expense on the promissory notes, which is included in accrued expenses and other current liabilities. The principal balance of \$83,348 is recognized in the current portion of notes payable in the consolidated balance sheet as of May 31, 2018. Principal payments of \$583,441 were made during the nine months ended May 31, 2018.

Automobile Contracts Payable

The Company has entered into purchase contracts for its vehicles. The loans are secured by the vehicles and bear interest at an average interest rate of approximately 6% per annum. Future principal payments on these automobile contracts payable is summarized in the table below:

<b>May 31, 2018</b>	<b>Principal Due</b>
2018	\$ 62,247
2019	59,351
2020	52,730
2021	46,812
2022	30,906
	<u>\$ 252,045</u>

**NOTE 10 - LOAN AGREEMENT**

On November 16, 2017, the Company and KIM as borrowers, and all of the Company's other subsidiaries, as credit parties, entered into a Loan and Security Agreement (the "Loan Agreement") with Gerber Finance Inc., as lender ("Gerber"), effective as of November 6, 2017. The Loan Agreement provides a secured revolving credit facility (the "Revolving Line") in an aggregate principal amount of up to \$2.0 million at any time outstanding (subsequently increased to \$4.0 million), of which \$2,433,907 including accrued interest was outstanding on May 31, 2018. Under the original terms of the Loan Agreement, the principal amount of loans, plus the face amount of any outstanding letters of credit, at any time outstanding cannot exceed up to 85% of the Company's eligible receivables minus reserves. Under the terms of the Loan Agreement, the Company may also request letters of credit from Gerber. The proceeds of the loans under the Loan Agreement will be used for working capital and general corporate purposes. The Revolving Line has a maturity date of November 6, 2019. Borrowings under the Revolving Line accrues interest at a rate based on the prime rate as customarily defined, plus a margin of 3.0%. On March 8, 2018, the Company and KIM entered into an amendment to the Loan Agreement with Gerber. Pursuant to this amendment, the aggregate principal amount of the Revolving Line at any time outstanding was increased to \$4.0 million and the principal amount of loans, plus the face amount of any outstanding letters of credit, at any time outstanding cannot exceed the lesser of (i) 40% of the value of certain inventory and (ii) 50% of certain accounts receivable.

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
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**NOTE 11 - STOCKHOLDERS' EQUITY**

Preferred Stock

The authorized preferred stock is 10,000,000 shares with a par value of \$0.001. As of May 31, 2018, and August 31, 2017, the Company has no shares of preferred stock issued or outstanding.

Common Stock

The authorized common stock is 265,000,000 shares with a par value of \$0.001. As of May 31, 2018, and August 31, 2017, 66,389,529 and 58,607,066 shares were issued and outstanding, respectively.

During the nine months ended May 31, 2018, the Company sold 5,877,415 shares of its common stock to investors in exchange for cash of \$16,404,723.

During the nine months ended May 31, 2018, the Company received \$30,000 from an investor but the shares were not issued as of May 31, 2018.

Share-based Compensation

The Company recorded stock compensation expense of \$495,897 and \$259,418 for the three month periods ended May 31, 2018 and 2017, respectively, in connection with the issuance of shares of common stock and options to purchase common stock.

The Company recorded stock compensation expense of \$1,904,568 and \$522,226 for the nine month periods ended May 31, 2018 and 2017, respectively, in connection with the issuance of shares of common stock and options to purchase common stock.

During the nine month period ended May 31, 2018, the Company issued 368,624 shares of common stock to consultants in exchange for \$1,794,828 of services, of which \$485,899 was service rendered and \$1,308,929 of prepaid services.

During the nine month period ended May 31, 2018, the Company entered into a separation agreement dated as of January 12, 2018 with one employee. The Company issued 100,000 restricted common shares as part of the separation agreement to this employee, which valued at \$667,000 and was recorded as share-based compensation during the nine months ended May 31, 2018.

Stock Options

The Company's 2016 Stock Incentive Plan (the Plan) was adopted on February 9, 2016. The Plan permits the grant of share options and shares to its employees and directors for up to 5,000,000 shares of common stock. The Company believes that such awards better align the interests of its employees with those of its shareholders. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the date of grant; those option awards generally vest based on three years of continuous service and have 10-year contractual terms.

The Company estimates the fair value of share-based compensation utilizing the Black-Scholes option pricing model, which is dependent upon several variables such as the expected option term, expected volatility of the Company's stock price over the expected option term, expected risk-free interest rate over the expected option term, expected dividend yield rate over the expected option term, and an estimate of expected forfeiture rates. The Company believes this valuation methodology is appropriate for estimating the fair value of stock options granted to employees and directors which are subject to ASC Topic 718 requirements. These amounts are estimates and thus may not be reflective of actual future results, nor amounts ultimately realized by recipients of these grants. The Company recognizes compensation on a straight-line basis over the requisite service period for each award. The following table summarizes the assumptions the Company utilized to record compensation expense for stock options granted during the nine months ended May 31, 2018 and 2017:

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
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	<b>May 31, 2018</b>	<b>February 28, 2017</b>
Expected term (years)	1-4	1-4
Expected volatility	60%	60%
Weighted-average volatility	60%	60%
Risk-free interest rate	0.67%-2.81%	0.85%-1.57%
Dividend yield	0%	0%
Expected forfeiture rate	33%	33%

The expected life is computed using the simplified method, which is the average of the vesting term and the contractual term. The expected volatility is based on management's analysis of historical volatility for comparable companies. The risk-free interest rate is based on the U.S. Treasury yields with terms equivalent to the expected term of the related option at the time of the grant. While the Company believes these estimates are reasonable, the compensation expense recorded would increase if the expected life was increased, a higher expected volatility was used, or if the expected dividend yield increased.

During the nine months ended May 31, 2018 and 2017, the Company issued 4,096,000 and 2,940,000 stock options, respectively, pursuant to the Company's 2016 Stock Incentive Plan. A summary of the Company's stock option activity during the nine month period ended May 31, 2018 is presented below:

	<b>No. of Options</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Term</b>	<b>Aggregate Intrinsic Value</b>
Balance Outstanding, August 31, 2017	5,275,500	\$ 1.73	8.0 years	\$ 917,610
Granted	4,098,500	\$ 4.42	9.7 years	-
Exercised	834,459	\$ 0.56	-	-
Forfeited	1,579,375	\$ 2.60	-	-
Balance Outstanding, May 31, 2018	<u>6,960,166</u>	<u>\$ 3.25</u>	<u>8.7 years</u>	<u>23,250,945</u>
Exercisable, May 31, 2018	<u>2,135,549</u>	<u>\$ 1.74</u>	<u>7.5 years</u>	<u>16,093,825</u>

The weighted-average grant-date fair value of options granted during the nine months ended May 31, 2018 and 2017, was \$4.42 and \$0.96, respectively. The weighted-average grant-date fair value of options forfeited during the nine months ended May 31, 2018 was \$2.61.

During the nine months ended May 31, 2018, the Company issued 796,425 shares of common stock pursuant to exercises of stock options and received cash of \$245,791.

As of May 31, 2018, there was \$14,500,580 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Plan. That cost is expected to be recognized over a weighted-average period of 8.7 years. The total fair value of shares vested during the nine month period May 31, 2018 is \$939,420. This amount is included in stock compensation expense on the consolidated statements of operations.

**NOTE 12- COMMITMENTS AND CONTINGENCIES**

Lease

The Company's corporate head-quarters and primary distribution center is located in Santa Ana, California. In July 2017, the Company entered into a facility lease in Garden Grove, California. The Garden Grove facility lease expires on August 1, 2022 and requires escalating monthly payments that range between \$24,480 and \$28,379. As part of the acquisition of CMP on May 1, 2017, the Company assumed the lease for CMP's facility located in Lawndale, California. The lease expires in January 2019, and requires escalating monthly payments that range between \$4,031 and \$4,143. On April 1, 2016, the Company entered into a sublease agreement for a facility located in Woodinville, Washington. The lease commenced on July 15, 2016 and expires on January 31, 2020, and requires escalating monthly payments that range between \$14,985 and \$16,022. Effective April 10, 2015, the Company assumed the facility lease in Denver, Colorado, which is the headquarters of operations for its wholly-owned subsidiary, Dank. On September 1, 2016, the Colorado facility lease was amended to include additional office space. The lease runs through March 31, 2020 and requires escalating monthly payments, ranging between \$4,800 and \$7,300. During the nine months ended May 31, 2018 and 2017, the Company recognized \$601,938 and \$288,789, respectively, of rental expense, related to its office, retail and warehouse space. The increase is the result of the addition of the CMP Wellness facility as well as expenses related to the Company's new headquarters in Garden Grove, CA.

**KUSH BOTTLES, INC. AND SUBSIDIARIES**  
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Additionally, Summit has several short-term operating leases in several states, which expire at various dates during 2018.

Other Commitments

In the ordinary course of business, the Company may enter into contractual purchase obligations and other agreements that are legally binding and specify certain minimum payment terms. The Company had no such agreements as of May 31, 2018.

Litigation

The Company may be subject to legal proceedings and claims which arise in the ordinary course of its business. Although occasional adverse decisions or settlements may occur, the Company believes that the final disposition of such matters should not have a material adverse effect on its financial position, results of operations or liquidity. The Company had no pending legal proceedings or claims as of May 31, 2018.

**NOTE 13 - SUBSEQUENT EVENTS**

On June 7, 2018, the Company entered into a securities purchase agreement (the "Purchase Agreement") with certain accredited investors (the "Purchasers") pursuant to which the Company agreed to issue and sell an aggregate of 7,500,000 shares of its common stock and warrants to purchase 3,750,000 shares of common stock in a registered direct offering (the "Offering"). The securities were offered by the Company pursuant to its shelf registration statement on Form S-3 (File No. 333-221910). Subject to certain ownership limitations, the warrants are immediately exercisable at an exercise price equal to \$5.28 per share of common stock. The warrants are exercisable for five years from the date of issuance. The combined per share purchase price for a share of common stock and half of a warrant was \$4.80.

The Company completed the Offering on June 12, 2018 for aggregate gross proceeds of \$36.0 million and net proceeds, after deducting the placement agent fees and other estimated offering expenses, of approximately \$32.9 million. A.G.P./Alliance Global Partners (the "Placement Agent") acted as the placement agent for the Offering. The Company agreed to pay the Placement Agent an aggregate cash fee equal to 7% of the aggregate gross proceeds raised in the Offering. The Company also agreed to reimburse the Placement Agent for up to \$120,000 of certain of its expenses with respect to the Offering and to pay the Placement Agent a non-accountable expense allowance equal to 1% of the aggregate gross proceeds raised in the Offering.

## **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

### **Cautionary Statement Concerning Forward-Looking Statements**

The following discussion and analysis should be read in conjunction with our audited consolidated financial statements and related notes included in this report. This report contains “forward-looking statements.” The statements contained in this report that are not historic in nature, particularly those that utilize terminology such as “may,” “will,” “should,” “expects,” “anticipates,” “estimates,” “believes,” or “plans” or comparable terminology are forward-looking statements based on current expectations and assumptions.

Various risks and uncertainties could cause actual results to differ materially from those expressed in forward-looking statements. The forward-looking events discussed in this report, the documents to which we refer you and other statements made from time to time by us or our representatives, may not occur, and actual events and results may differ materially and are subject to risks, uncertainties, and assumptions about us. For these statements, we claim the protection of the “bespeaks caution” doctrine. All forward-looking statements in this document are based on information currently available to us as of the date of this report, and we assume no obligation to update any forward-looking statements. Forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause the actual results to differ materially from any future results, performance, or achievements expressed or implied by such forward-looking statements.

### **Overview**

We provide customizable packaging products, vaporizers, hydrocarbon gases, solvents, accessories and branding solutions for the cannabis industry. Representative examples of our products include pop-top bottles, vaporizer cartridges and accessories, exit/barrier bags, tubes, and other small-sized containers. We sell our solutions predominantly to businesses operating in jurisdictions that have some form of cannabis legalization. These businesses include medical and recreational dispensaries, large and small scale processors, and packaging re-distributors.

We believe that we have created one of the largest product libraries in the cannabis industry, allowing us to be a comprehensive solutions provider to our customers. Our extensive knowledge of the regulatory environment applicable to the cannabis industry allows us to quickly adapt to our customers' packaging requirements. We maintain the flexibility to enter the markets of decriminalized regions by establishing re-distributor partnerships or opening new facilities. We also have the flexibility to introduce new products and services to our vast customer network. We have no supplier purchase commitments and no take or pay arrangements. In addition to these factors, we believe that we offer competitive pricing, prompt deliveries, and excellent customer service. We expect continued growth as we take measures to expand into new markets, invest in our systems and personnel, forge strategic alliances and invest in our own molds and intellectual property.

### **Acquisitions**

On May 1, 2017 (“Merger Date”), the Company and KBCMP, Inc., a Delaware corporation and newly formed wholly-owned subsidiary of the Company (“Merger Sub”), entered into an Agreement of Merger (the “Merger Agreement”) with Lancer West Enterprises, Inc., a California corporation and Walnut Ventures, a California corporation, pursuant to which each of Lancer West Enterprises, Inc. and Walnut Ventures were merged with and into Merger Sub, with Merger Sub as the surviving corporation, resulting in our indirect acquisition of CMP Wellness, LLC (“CMP”), a California limited liability company. Prior to the merger, CMP was owned 100% by Lancer West Enterprises, Inc. and Walnut Ventures. Membership interest in CMP was the sole asset of Lancer West Enterprises, Inc. and Walnut Ventures. As a result, CMP became our wholly-owned subsidiary. CMP is a distributor of vaporizers, cartridges and accessories. Our Board of Directors believed the acquisition of CMP and the product offerings of CMP leveraged our existing product development program and provided us with the possibility of generating near term revenue and operating cash flow, as well as establishing a commercial platform whereby other cannabis industry-support products may be accessed in the future. Going forward, the existing product offering and other product licensing opportunities will be the basis of our long-term product portfolio. The operational results discussed below include the activity of CMP during the three and nine months ended May 31, 2018.

The purchase price for CMP consisted of an aggregate of \$1,500,000 in cash, unsecured promissory notes in the aggregate principal amount of approximately \$770,820 having a one-year maturity, and an aggregate of 7,800,000 restricted shares of the Company’s common stock. The purchase price is subject to customary post-closing adjustments with respect to confirmation of the levels of working capital and cash held by CMP as of the closing. During the one-year period following the closing, the former owners of CMP may become entitled to receive up to an additional approximately \$1,650,000 in cash, in the aggregate, and approximately 4,740,960 shares of our common stock, in the aggregate, based on the future performance of CMP.

In May 2017, we acquired intellectual property, domain name, and inventory from RUB Acquisition, LLC. The purchase price for the intellectual property and inventory was \$150,000 in cash and 200,000 shares of our common stock having an estimated fair value of \$466,000. We are amortizing the cost of the domain name over six years.

On May 2, 2018, we completed our acquisition of Summit Innovations, LLC (“Summit”), a leading distributor of hydrocarbon gases to the legal cannabis industry. Pursuant to the terms of the Agreement and Plan of Merger (the “Merger Agreement”), Summit merged with and into KCH Energy, LLC (“KCH”), our wholly-owned subsidiary, with KCH as the surviving entity.

The consideration we paid to the members of Summit (the “Members”) at the closing included an aggregate of \$3.2 million in cash (the “Cash Consideration”), as adjusted to reflect estimated working capital, indebtedness and transaction expenses as of the closing date, and an aggregate of 1,280,000 shares (the “Share Consideration”) of our common stock. \$500,000 of the Cash Consideration and approximately 640,000 shares of common stock were held back by us for a period of 15 months for potential post-closing working capital and/or indemnification claims relating to, among other things, breaches of representations, warranties and covenants contained in the Merger Agreement. The Members may become entitled to receive earn-out consideration of up to an additional 1,280,000 shares of common stock, in the aggregate, based on the performance of the Summit business during a one-year period following the closing.

## **Results of Operations - Comparison for the three-month periods ended May 31, 2018 and 2017**

### **Revenue**

For the three months ended May 31, 2018, our revenue increased to \$12,904,609, compared to \$4,719,477 for the comparable period in 2017, which represents an increase of \$8,185,132 or 173%. We experienced solid organic growth across all markets, namely in California following the adoption of adult use cannabis sales from January 1st, 2018. In addition, vaping product related sales remained strong as this sector of the cannabis industry continues to perform well. In addition, we witnessed strong growth of its custom branded product business as customers seek differentiated brand building solutions in line with regulatory requirements.

### **Gross Profit**

Gross profit for the three months ended May 31, 2018 was \$3,657,730, or 28% of revenue, compared to \$1,677,072, or 36% of revenue, for the three months ended May 31, 2017. The decrease in gross margin percentage is primarily attributable to discounting focused on gaining market share strategy and the mix of products sold, driven by vaporizers and cartridges sales that carry lower margins than the rest of the product portfolio.

### **Operating Expenses**

Our operating expenses for the three months ended May 31, 2018 increased to \$5,742,108, or 44% of total revenue, from \$1,668,333, or 35% of total revenue, for the three months ended May 31, 2017. The increase is due to the expansion of the business, primarily attributed to increased personnel cost, insurance, professional and facility expenses. We will continue to make significant investments in infrastructure and supply chain to scale efficiently.

### **Income (Loss) from Operations**

Loss from operations for the three months ended May 31, 2018 was \$2,084,378 compared to income from operations of \$8,739 for the three months ended May 31, 2017. The decrease is primarily attributable to acquisition related closing cost, one-time operating expenses, increased marketing expenses and investment in infrastructure and personnel to scale the expanding business..

### **Interest and Other Income (Expense), Net**

Interest and Other Income (Expense), net during the three months ended May 31, 2018 was expense of \$81,362, as compared to an expense of \$2,620 for the three months ended May 31, 2017. The increase is attributed interest expense related to the recently established credit line.

### **Income Tax Provision**

The provision for income taxes was \$0 for both the three-month periods ended May 31, 2018 and 2017.

### **Net Income (Loss)**

Our net result for the three months ended May 31, 2018 was a net loss of \$2,165,740 or \$0.03 per share, compared to net income of \$6,119 or \$0.00 per share, for the three months ended May 31, 2017.

## Results of Operations - Comparison for the nine-month periods ended May 31, 2018 and 2017

### Revenue

For the nine months ended May 31, 2018, our revenue increased to \$32,113,100, compared to \$10,161,813 for the comparable period in 2017, which represents an increase of \$21,951,287 or 216%. We experienced solid organic growth across all markets, namely in California following the adoption of adult use cannabis sales from January 1st, 2018. In addition, vaping product related sales remained strong as this sector of the cannabis industry continues to perform well. In addition, we witnessed strong growth of its custom branded product business as customers seek differentiated brand building solutions in line with regulatory requirements.

### Gross Profit

Gross profit for the nine months ended May 31, 2018 was \$9,253,369, or 29% of revenue, compared to \$3,816,609 or 38% of revenue, for the nine months ended May 31, 2017. The decrease in gross margin percentage is primarily attributable to discounting focused on gaining market share strategy and the mix of products sold, driven by vaporizers and cartridges sales that carry lower margins than the rest of the product portfolio.

### Operating Expenses

Our operating expenses for the nine months ended May 31, 2018 increased to \$12,066,272, or 38% of total revenue, from \$3,939,722, or 39% of total revenue, for the nine months ended May 31, 2017. The increase is due to the expansion of the business, primarily attributed to increased personnel cost, insurance, professional and facility expenses. We will continue to make significant investments in infrastructure and supply chain to scale efficiently.

### Income (Loss) from Operations

Loss from operations for the nine months ended May 31, 2018 was \$2,812,903 compared to a loss from operations of \$123,113 for the nine months ended May 31, 2017. The decrease is primarily attributable to acquisition related closing cost, one-time operating expenses, increased marketing expenses and investment in infrastructure and personnel to scale the expanding business...

### Interest and Other Income (Expense), Net

Interest and Other Income (Expense), net during the nine months ended May 31, 2018 was expense of \$112,357, as compared to an expense of \$28,432 for nine months ended May 31, 2017. The increase is attributed interest expense related to the recently established credit line.

### Income Tax Provision

The provision for income taxes was \$66,178 for the nine month period ended May 31, 2018 and \$0 for the nine months ended May 31, 2017.

### Net Income (Loss)

Our net loss for the nine months ended May 31, 2018 was \$2,991,438 or \$0.05 per share, compared to a net loss of \$151,545 or \$0.00 per share, for the nine months ended May 31, 2017.

### Liquidity and Capital Resources

At May 31, 2018, we had cash of \$3,574,430 and a working capital surplus of \$15,755,775 compared to cash of \$916,984 and working capital of \$3,449,622 as of August 31, 2017. Working capital increased by \$12,306,153 or 357%. The increase is due to cash from the sale of our common stock in private placements and inventory.

#### *Cash Flows from Operating Activities*

For the nine months period ended May 31, 2018, net cash used in operating activities was \$12,229,958 compared to \$901,459 in net cash used in operating activities for the nine months ended 2017. The change is primarily attributed to an increase in inventory, including related prepayments and accounts receivable.

#### *Cash Flows from Investing Activities*

Net cash used in investing activities increased from \$2,455,921 for the nine months ended May 31, 2018 to \$2,513,773 for the nine months ended May 31, 2017. The aggregate of our acquisition activity, property and equipment purchases and security deposits for the nine months ended May 31, 2018 exceeded similar activity for the nine months ended May 31, 2017.

### *Cash Flows from Financing Activities*

Net cash provided by financing activities increased from \$3,057,069 to \$17,401,177 for the nine months ended May 31, 2017 and May 31, 2018, respectively. The increase is primarily attributed to the increase of cash received from sale of shares of the Company's common stock compared to the nine months ended May 31, 2017.

We manage our liquidity and financial position in the context of our overall business strategy. We continually forecast and manage our cash, working capital balances, and capital structure to meet the short-term and long-term obligations of our business while seeking to maintain liquidity and financial flexibility.

As of May 31, 2018, we have historically funded our operations primarily through the issuance of equity. We had a net loss of \$2,991,438 for the nine months ended May 31, 2018 and had an accumulated deficit of \$3,598,682 as of May 31, 2018. For the nine months ended May 31, 2017, we had net loss of \$151,545, and an accumulated deficit of \$828,253 as of May 31, 2017.

On June 12, 2018, we completed a public offering of 7,500,000 shares of common stock and warrants to purchase 3,750,000 shares of common stock. Subject to certain ownership limitations, the warrants are immediately exercisable at an exercise price equal to \$5.28 per share of common stock. The warrants are exercisable for five years from the date of issuance. The combined per share purchase price for a share of common stock and half of a warrant was \$4.80. The aggregate gross proceeds from the offering were \$36.0 million and net proceeds, after deducting the placement agent fees and other estimated offering expenses, were approximately \$32.9 million.

We believe that income generated from operations are adequate to fund existing obligations and introduce new products for at least the next twelve months. We may elect to raise additional funds, through debt or equity financings, for the purposes of expanding current operations, making capital acquisitions, or consummating strategic transactions. Additional equity or debt financing may not be available when needed, on terms favorable to us or at all.

### *Off-Balance Sheet Arrangements*

We do not currently have, and did not have during the periods presented, any off-balance sheet arrangements, as defined under SEC rules.

### **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the U.S. The preparation of the condensed consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, accounts receivable reserves, inventory and related reserves, valuations and purchase price allocations related to business combinations, expected cash flows used to evaluate the recoverability of long-lived assets, estimated fair values of long-lived assets used to record impairment charges related to intangible assets and goodwill, amortization periods, accrued expenses, stock-based compensation, contingent liabilities, and recoverability of our net deferred tax assets and any related valuation allowance. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

There have been no material changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates described in our Annual Report on Form 10-K for the fiscal year ended August 31, 2017.

### **Item 3. Quantitative and Qualitative Disclosure About Market Risk**

We do not use derivative financial instruments in our investment portfolio and have no foreign exchange contracts. Our financial instruments consist of cash and cash equivalents. We consider investments that, when purchased, have a remaining maturity of ninety (90) days or less to be cash equivalents. We do not believe that a notional or hypothetical 10% change in interest rate percentages would have a material impact on the fair value of our investment portfolio or our interest income.

### **Item 4. Controls and Procedures**

#### **Management's Evaluation of our Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our Chief Executive Officer and the Chief Financial Officer, we are responsible for conducting an evaluation of the effectiveness of the design and operation of our internal controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the fiscal quarter covered by this report. Disclosure controls and procedures means that the material information required to be included in our SEC reports is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms relating to our company, including any consolidating subsidiaries, and was made known to us by others within those entities, particularly during the period when this report was being prepared. Based on this evaluation, our principal executive officer and principal financial officer concluded as of the evaluation date that our disclosure controls and procedures were not effective as of May 31, 2018.

The material weaknesses that existed on August 31, 2017 are described in Part II, Item 9A - Controls and Procedures in our most recent Annual Report on Form 10-K, filed on November 29, 2017. Due to a lack of financial resources and size, we are not able to take any action to immediately remediate these material weaknesses. We will implement further controls as circumstances, cash flow, and working capital permit. Notwithstanding the assessment that our disclosure controls and procedures were not effective and that there were material weaknesses as identified in this report, we believe that our financial statements fairly present our financial position, results of operations and cash flows for the periods covered thereby in all material respects.

We have taken steps to enhance our internal control over financial reporting and plan to take additional steps to remediate the material weaknesses. Specifically:

- (i) We appointed additional independent members with public company board experience to our board of directors, such that our board of directors is now composed of a majority of independent directors;
- (ii) On March 9, 2018, our board of directors formed an Audit Committee composed entirely of independent directors that will, among other things, assist the board of directors in its oversight of the integrity of our financial statements and our financing reporting processes and systems of internal control;
- (iii) We have adopted a Code of Business Conduct and Ethics and a whistleblower policy;
- (iv) We added staff to our finance team, and outsourced to third party the assessment of certain complex transactions under US GAAP; and
- (v) In January 2018, we hired a controller with public company experience

We believe that the measures described above will strengthen our internal control over financial reporting. We expect that our efforts, including design, implementation and testing will continue throughout fiscal year 2018.

#### **Changes in Internal Control over Financial Reporting**

There has been no change in our internal control over financial reporting identified in connection with our evaluation we conducted of the effectiveness of our internal control over financial reporting as of May 31, 2018, that occurred during our second fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

To the best of the Company's knowledge and belief, no material legal proceedings are currently pending or threatened.

### **Item 1A. Risk Factors.**

Item 1A of Part I of our Annual Report on Form 10-K for the year ended August 31, 2017, filed with the SEC on November 28, 2017 and Item 1A of Part II of our Quarterly Report on Form 10-Q for the quarter ended November 30, 2017, filed with the SEC on January 16, 2018, contain risk factors identified by the Company. Our operations could also be affected by additional factors that are not presently known to us or by factors that we currently consider immaterial to our business. To our knowledge and except to the extent additional factual information disclosed in this Quarterly Report on Form 10-Q relates to such risk factors, there have been no material changes in the risk factors described in "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended August 31, 2017 and Item 1A of Part II of our Quarterly Report on Form 10-Q for the quarter ended November 30, 2017.

### **Item 2. Unregistered Sales of Equity Securities.**

In addition to the Share Consideration issued in connection with the acquisition of Summit, during the three months ended May 31, 2018, we sold 1,251,119 shares of our common stock to investors in exchange for cash of \$5,017,719.

During the three months ended May 31, 2018, we granted 312,000 shares of our common stock for services pursuant to contracts, with an aggregate fair market value of \$1,632,000.

These securities were issued without registration under the Securities Act in reliance on registration exemptions contained in Section 4(a) (2) of the Securities Act and Regulation D as transactions by an issuer not involving any public offering. The recipients of securities in each such transaction represented their intention to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof, and appropriate legends were affixed to the share certificates and other instruments issued in such transactions. The sales of these securities were made without general solicitation or advertising.

**Item 3. Default Upon Senior Securities.**

None.

**Item 4. Mine Safety Disclosures.**

Not applicable.

**Item 5. Other Information.**

None.

**Item 6. Exhibits**

The following exhibits are filed as part of this Current Report on Form 10-Q. Where such filing is made by incorporation by reference to a previously filed document, such document is identified.

Exhibit Number	Description of Exhibit
<a href="#"><u>2.1<sup>(1)</sup></u></a>	<a href="#"><u>Agreement and Plan of Merger, dated April 10, 2018, by and among Kush Bottles, Inc., KCH Energy, LLC, Summit Innovations, LLC and Mark Driver.</u></a>
<a href="#"><u>2.2<sup>(2)</sup></u></a>	<a href="#"><u>Amendment to Agreement and Plan of Merger, dated May 2, 2018, by and among Kush Bottles, Inc., KCH Energy, LLC, Summit Innovations, LLC and Mark Driver.</u></a>
<a href="#"><u>4.1<sup>(3)</sup></u></a>	<a href="#"><u>Form of Warrant dated as of June 12, 2018.</u></a>
<a href="#"><u>10.1#*</u></a>	<a href="#"><u>Kush Bottles, Inc. 2016 Stock Option Plan, as amended.</u></a>
<a href="#"><u>10.2<sup>(4)</sup></u></a>	<a href="#"><u>First Amendment to Loan and Security Agreement dated as of March 8, 2018 by and among Gerber Finance Inc., Kush Bottles, Inc. and Kim International Corporation.</u></a>
<a href="#"><u>10.3<sup>(3)</sup></u></a>	<a href="#"><u>Form of Securities Purchase Agreement, dated June 7, 2018.</u></a>
<a href="#"><u>10.4<sup>(3)</sup></u></a>	<a href="#"><u>Placement Agency Agreement, dated June 7, 2018, by and between Kush Bottles, Inc. and A.G.P./Alliance Global Partners.</u></a>
<a href="#"><u>31.1*</u></a>	<a href="#"><u>Certification of principal executive officer pursuant to Rules 13a-15(e) and 15d-15(e), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>31.2*</u></a>	<a href="#"><u>Certification of principal financial and accounting officer pursuant to Rules 13a-15(e) and 15d-15(e), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>32.1**</u></a>	<a href="#"><u>Certification of principal executive officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>32.2**</u></a>	<a href="#"><u>Certification of principal financial and accounting officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.

- (1) Previously filed as an exhibit to the Company's Current Report on Form 8-K (filed April 10, 2018) and incorporated by reference thereto.  
(2) Previously filed as an exhibit to the Company's Current Report on Form 8-K (filed May 3, 2018) and incorporated by reference thereto.  
(3) Previously filed as an exhibit to the Company's Current Report on Form 8-K (filed June 8, 2018) and incorporated by reference thereto.  
(4) Previously filed as an exhibit to the Company's Quarterly Report on Form 10-Q (filed April 13, 2018) and incorporated by reference thereto.

\* Filed herewith.

\*\* This certification shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section, nor shall it be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.

# Management contract or compensatory plan or arrangement.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**KUSH BOTTLES, INC.**

Date: July 13, 2018

By: /s/ Nicholas Kovacevich  
Nicholas Kovacevich  
Chairman and Chief Executive Officer  
(Principal executive officer)

Date: July 13, 2018

By: /s/ James McCormick  
James McCormick  
Chief Financial Officer and Chief Operating Officer  
(Principal financial and accounting officer)

**KUSH BOTTLES, INC. 2016 STOCK INCENTIVE PLAN**

Adopted February 9, 2016, amended on May 8, 2018

**THIS KUSH BOTTLES, INC. 2016 STOCK INCENTIVE PLAN** (the “**Plan**”) is designed to retain directors, executives, officers, selected employees, and consultants and reward them for making contributions to the success of the Company. These objectives are accomplished by making long-term incentive awards under the Plan thereby providing Participants with a proprietary interest in the growth and performance of the Company.

**1. Definitions**

(a) “**Board**” – The Board of Directors of the Company.

(b) “**Change in Control**” – Means, and shall be deemed to have occurred upon the occurrence of, any one of the following events:

i. The acquisition in one transaction by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d) (2) of the Exchange Act) (a “**Person**”) of beneficial ownership (within the meaning of Rule 13d-3 promulgated under the Exchange Act) of shares or other securities (as defined in Section 3(a)(10) of the Exchange Act) representing 51% or more of outstanding Stock of the Company; provided, however, that a Change in Control as defined in this clause (1) shall not be deemed to occur in connection with any acquisition by the Company, an employee benefit plan of the Company or any Person who immediately prior to the effective date of this Plan is a holder of Stock (a “**Current Stockholder**”) so long as such acquisition does not result in any Person other than the Company, such employee benefit plan or such Current Stockholder beneficially owning shares or securities representing 51% or more of the outstanding; or

ii. Any election has occurred of persons as directors of the Company that causes two-thirds or more of the Board to consist of persons other than (i) persons who were members of the Board on the effective date of this Plan and (ii) persons who were nominated by the Board for election as members of the Board at a time when at least two-thirds of the Board consisted of persons who were members of the Board on the effective date of this Plan; provided, however, that any person nominated for election by the Board when at least two-thirds of the members of the Board are persons described in sub clause (i) or (ii) and persons who were themselves previously nominated in accordance with this clause (2) shall, for this purpose, be deemed to have been nominated by a Board composed of persons described in sub clause (ii); or

iii. Approval by the stockholders of the Company of a reorganization, merger, consolidation or similar transaction (a “**Reorganization Transaction**”), in each case, unless, immediately following such Reorganization Transaction, more than 50% of, respectively, the outstanding shares of common stock (or similar equity security) of the corporation or other entity resulting from or surviving such Reorganization Transaction and the combined voting power of the securities of such corporation or other entity entitled to vote generally in the election of directors, is then beneficially owned, directly or indirectly, by the individuals and entities who were the respective beneficial owners of the outstanding Stock immediately prior to such Reorganization Transaction in substantially the same proportions as their ownership of the outstanding Stock immediately prior to such Reorganization Transaction; or

iv. Approval by the stockholders of the Company of (i) a complete liquidation or dissolution of the Company or (ii) the sale or other disposition of all or substantially all of the assets of the Company to a corporation or other entity, unless, with respect to such corporation or other entity, immediately following such sale or other disposition, more than 50% of, respectively, the outstanding shares of common stock (or similar equity security) of such corporation or other entity and the combined voting power of the securities of such corporation or other entity entitled to vote generally in the election of directors, is then beneficially owned, directly or indirectly, by the individuals and entities who were the respective beneficial owners of the outstanding Stock immediately prior to such sale or disposition in substantially the same proportions as their ownership of the outstanding Stock immediately prior to such sale or disposition.

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(c) “**Code**” – The Internal Revenue Code of 1986, as amended from time to time.

(d) “**Committee**” – The Compensation Committee of the Company's Board, or such other committee of the Board that is designated by the Board to administer the Plan.

(e) “**Company**” – Kush Bottles, Inc. and its subsidiaries, including subsidiaries of subsidiaries.

(f) “**Exchange Act**” – The Securities Exchange Act of 1934, as amended from time to time.

(g) “**Fair Market Value**” – The fair market value of the Company's issued and outstanding Stock based on the closing price on the day of any grant or award of stock under the Plan.

(h) “**Grant**” – The grant of any form of stock option, stock award, or stock purchase offer, whether granted singly, in combination, or in tandem, to a Participant pursuant to such terms, conditions and limitations as the Committee may establish in order to fulfill the objectives of the Plan.

(i) “**Grant Agreement**” – An agreement between the Company and a Participant that sets forth the terms, conditions and limitations applicable to a Grant.

(j) “**Option**” – Either an Incentive Stock Option, in accordance with Section 422 of Code, or a Nonstatutory Option, to purchase the Company's Stock that may be awarded to a Participant under the Plan. A Participant who receives an award of an Option shall be referred to as an “**Optionee**”.

(k) “**Participant**” – A director, officer, employee, or consultant of the Company to whom an Award has been made under the Plan.

(l) “**Restricted Stock Purchase Offer**” – A Grant of the right to purchase a specified number of shares of Stock pursuant to a written agreement issued under the Plan.

(m) “**Securities Act**” – The Securities Act of 1933, as amended from time to time.

(n) “**Stock**” – Authorized and issued or unissued shares of common stock of the Company.

(o) “**Stock Award**” – A Grant made under the Plan in stock or denominated in units of stock for which the Participant is not obligated to pay additional consideration.

**2. Administration.** The Plan shall be administered by the Board, provided however, that the Board may delegate such administration to the Committee. Subject to the provisions of the Plan, the Board and/or the Committee shall have authority to (a) grant, in its discretion, Incentive Stock Options in accordance with Section 422 of the Code, or Nonstatutory Options, Stock Awards or Restricted Stock Purchase Offers; (b) determine the Fair Market Value of the Stock covered by any Grant; (c) determine which eligible persons shall receive Grants and the number of shares, restrictions, terms and conditions to be included in such Grants; (d) construe and interpret the Plan; (e) promulgate, amend and rescind rules and regulations relating to its administration, and correct defects, omissions and inconsistencies in the Plan or any Grant; (f) consistent with the Plan and with the consent of the Participant, as appropriate, amend any outstanding Grant or amend the exercise date or dates thereof; (g) determine the duration and purpose of leaves of absence which may be granted to Participants without constituting termination of their employment for the purpose of the Plan or any Grant; and (h) make all other determinations necessary or advisable for the Plan's administration. The interpretation and construction by the Board of any provisions of the Plan or selection of Participants shall be conclusive and final. No member of the Board or the Committee shall be liable for any action or determination made in good faith with respect to the Plan or any Grant made thereunder.

### **3. Eligibility.**

(a) **General:** The persons who shall be eligible to receive Grants shall be directors, officers, employees or consultants to the Company. The term consultant shall mean any person, other than an employee, who is engaged by the Company to render services and is compensated for such services. An Optionee may hold more than one Option. Any issuance of a Grant to an officer or director of the Company subsequent to the first registration of any of the securities of the Company under the Exchange Act shall comply with the requirements of Rule 16b-3.

(b) Incentive Stock Options: Incentive Stock Options may only be issued to employees of the Company. Incentive Stock Options may be granted to officers or directors, provided they are also employees of the Company. Payment of a director's fee shall not be sufficient to constitute employment by the Company.

(c) The Company shall not grant an Incentive Stock Option under the Plan to any employee if such Grant would result in such employee holding the right to exercise for the first time in any one calendar year, under all Incentive Stock Options granted under the Plan or any other plan maintained by the Company, with respect to shares of Stock having an aggregate fair market value, determined as of the date the Option is granted, in excess of \$100,000. Should it be determined that an Incentive Stock Option granted under the Plan exceeds such maximum for any reason other than a failure in good faith to value the Stock subject to such option, the excess portion of such option shall be considered a Nonstatutory Option. To the extent the employee holds two (2) or more such Options which become exercisable for the first time in the same calendar year, the foregoing limitation on the exercisability of such Option as Incentive Stock Options under the Federal tax laws shall be applied on the basis of the order in which such Options are granted. If, for any reason, an entire Option does not qualify as an Incentive Stock Option by reason of exceeding such maximum, such Option shall be considered a Nonstatutory Option.

(d) Nonstatutory Option: The provisions of the foregoing Section 3(b) shall not apply to any Option designated as a "Nonstatutory Option" or which sets forth the intention of the parties that the Option be a Nonstatutory Option.

(e) Stock Awards and Restricted Stock Purchase Offers: The provisions of this Section 3 shall not apply to any Stock Award or Restricted Stock Purchase Offer under the Plan.

#### **4. Stock**

(a) Authorized Stock: Stock subject to Grants may be either unissued or reacquired Stock

(b) Number of Shares: Subject to adjustment as provided in Section 5(i) of the Plan, the total number of shares of Stock which may be purchased or granted directly by Options, Stock Awards or Restricted Stock Purchase Offers, or purchased indirectly through exercise of Options granted under the Plan shall not exceed fifteen million (15,000,000). If any Grant shall for any reason terminate or expire, any shares allocated thereto but remaining unpurchased upon such expiration or termination shall again be available for Grants with respect thereto under the Plan as though no Grant had previously occurred with respect to such shares. Any shares of Stock issued pursuant to a Grant and repurchased pursuant to the terms thereof shall be available for future Grants as though not previously covered by a Grant.

(c) Reservation of Shares: The Company shall reserve and keep available at all times during the term of the Plan such number of shares as shall be sufficient to satisfy the requirements of the Plan. If, after reasonable efforts, which efforts shall not include the registration of the Plan or Grants under the Securities Act, the Company is unable to obtain authority from any applicable regulatory body, which authorization is deemed necessary by legal counsel for the Company for the lawful issuance of shares hereunder, the Company shall be relieved of any liability with respect to its failure to issue and sell the shares for which such requisite authority was so deemed necessary unless and until such authority is obtained.

(d) Application of Funds: The proceeds received by the Company from the sale of Stock pursuant to the exercise of Options or rights will be used for general corporate purposes.

(e) No Obligation to Exercise: The issuance of a Grant shall impose no obligation upon the Participant to exercise any rights under such Grant.

**5. Terms and Conditions of Options.** Options granted hereunder shall be evidenced by agreements between the Company and the respective Optionees, in such form and substance as the Board or Committee shall from time to time approve. Option agreements need not be identical, and in each case may include such provisions as the Board or Committee may determine, but all such agreements shall be subject to and limited by the following terms and conditions:

(a) Number of Shares: Each Option shall state the number of shares to which it pertains.

(b) Exercise Price: Each Incentive Stock Option shall state the exercise price, which shall be determined as follows:

(i) Any Incentive Stock Option granted to a person who at the time the Option is granted owns (or is deemed to own pursuant to Section 424(d) of the Code) stock possessing more than ten percent (10%) of the total combined voting power or value of all classes of stock of the Company ("**Ten Percent Holder**") shall have an exercise price of no less than 110% of the Fair Market Value of the Stock as of the date of grant; and

(ii) Incentive Stock Options granted to a person who at the time the Option is granted is not a Ten Percent Holder shall have an exercise price of no less than 100% of the Fair Market Value of the Stock as of the date of grant.

For the purposes of this Section 5(b), the Fair Market Value shall be as determined by the Board in good faith, which determination shall be conclusive and binding; provided however, that if there is an active public market for such Stock, the Fair Market Value per share shall be the closing price if such stock is listed on such public market on the date of grant of the Option, or if listed on a stock exchange, the closing price on such exchange on such date of grant.

The exercise price of each Nonstatutory Stock Option shall be determined at the discretion of the Board of Directors of the Corporation.

(c) Medium and Time of Payment: The exercise price shall become immediately due upon exercise of the Option and shall be paid in cash or check made payable to the Company. Should the Company's outstanding Stock be registered under Section 12(g) of the Exchange Act at the time the Option is exercised, then the exercise price may also be paid as follows:

(i) in shares of Stock held by the Optionee for the requisite period necessary to avoid a charge to the Company's earnings for financial reporting purposes and valued at Fair Market Value on the exercise date, or

(ii) through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable written instructions (a) to a Company designated brokerage firm to effect the immediate sale of the purchased shares and remit to the Company, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable Federal, state and local income and employment taxes required to be withheld by the Company by reason of such purchase and (b) to the Company to deliver the certificates for the purchased shares directly to such brokerage firm in order to complete the sale transaction.

(iii) At the discretion of the Board, exercisable either at the time of Option grant or of Option exercise, the exercise price may also be paid (i) by Optionee's delivery of a promissory note in form and substance satisfactory to the Company and permissible under applicable securities rules and bearing interest at a rate determined by the Board in its sole discretion, but in no event less than the minimum rate of interest required to avoid the imputation of compensation income to the Optionee under the Federal tax laws, or (ii) in such other form of consideration permitted by the Nevada Revised Statutes as may be acceptable to the Board.

(d) Term and Exercise of Options: Any Option granted to an employee of the Company shall become exercisable over a period of no longer than ten (10) years. In no event shall any Option be exercisable after the expiration of ten (10) years from the date it is granted, and no Incentive Stock Option granted to a Ten Percent Holder shall, by its terms, be exercisable after the expiration of ten (10) years from the date of the Option. Unless otherwise specified by the Board or the Committee in the resolution authorizing such Option, the date of grant of an Option shall be deemed to be the date upon which the Board or the Committee authorizes the granting of such Option.

Each Option shall be exercisable to the nearest whole share, in installments or otherwise, as the respective Option agreements may provide. During the lifetime of an Optionee, the Option shall be exercisable only by the Optionee and shall not be assignable or transferable by the Optionee, and no other person shall acquire any rights therein. To the extent not exercised, installments (if more than one) shall accumulate, but shall be exercisable, in whole or in part, only during the period for exercise as stated in the Option agreement, whether or not other installments are then exercisable.

(e) Termination of Status as Employee, Consultant or Director: If Optionee's status as an employee shall terminate for any reason other than Optionee's disability or death, then Optionee (or if the Optionee shall die after such termination, but prior to exercise, Optionee's personal representative or the person entitled to succeed to the Option) shall have the right to exercise the portions of any of Optionee's Incentive Stock Options which were exercisable as of the date of such termination, in whole or in part, within 90 days after such termination (or, in the event of "*termination for good cause*" as that term is defined in Nevada case law related thereto, or by the terms of the Plan or the Option Agreement or an employment agreement, the Option shall automatically terminate as of the termination of employment as to all shares covered by the Option).

With respect to Nonstatutory Options granted to employees, directors or consultants, the Board may specify such period for exercise, not less than 90 days (except that in the case of "*termination for cause*" or removal of a director), the Option shall automatically terminate as of the termination of employment or services as to shares covered by the Option, following termination of employment or services as the Board deems reasonable and appropriate. The Option may be exercised only with respect to installments that the Optionee could have exercised at the date of termination of employment or services. Nothing contained herein or in any Option granted pursuant hereto shall be construed to affect or restrict in any way the right of the Company to terminate the employment or services of an Optionee with or without cause.

(f) Disability of Optionee: If an Optionee is disabled (within the meaning of Section 22(e)(3) of the Code) at the time of termination, the ninety (90) day period set forth in Section 5(e) shall be a period, as determined by the Board and set forth in the Option, of not less than six months nor more than one year after such termination.

(g) Death of Optionee: If an Optionee dies while employed by, engaged as a consultant to, or serving as a Director of the Company, the portion of such Optionee's Option which was exercisable at the date of death may be exercised, in whole or in part, by the estate of the decedent or by a person succeeding to the right to exercise such Option at any time within (i) a period, as determined by the Board and set forth in the Option, of not less than six (6) months nor more than one (1) year after Optionee's death, which period shall not be more, in the case of a Nonstatutory Option, than the period for exercise following termination of employment or services, or (ii) during the remaining term of the Option, whichever is the lesser. The Option may be so exercised only with respect to installments exercisable at the time of Optionee's death and not previously exercised by the Optionee.

(h) Nontransferability of Option: No Option shall be transferable by the Optionee, except by will or by the laws of descent and distribution.

(i) Recapitalization: Subject to any required action of shareholders, the number of shares of Stock covered by each outstanding Option, and the exercise price per share thereof set forth in each such Option, shall be proportionately adjusted for any increase or decrease in the number of issued shares of Stock of the Company resulting from a stock split, stock dividend, combination, subdivision or reclassification of shares, or the payment of a stock dividend, or any other increase or decrease in the number of such shares affected without receipt of consideration by the Company; provided, however, the conversion of any convertible securities of the Company shall not be deemed to have been "*effected without receipt of consideration*" by the Company.

In the event of a proposed dissolution or liquidation of the Company, a merger or consolidation in which the Company is not the surviving entity, or a sale of all or substantially all of the assets or capital stock of the Company (collectively, a "**Reorganization**"), unless otherwise provided by the Board, this Option shall terminate immediately prior to such date as is determined by the Board, which date shall be no later than the consummation of such Reorganization. In such event, if the entity which shall be the surviving entity does not tender to Optionee an offer, for which it has no obligation to do so, to substitute for any unexercised Option a stock option or capital stock of such surviving entity, as applicable, which on an equitable basis shall provide the Optionee with substantially the same economic benefit as such unexercised Option, then the Board may grant to such Optionee, in its sole and absolute discretion and without obligation, the right for a period commencing thirty (30) days prior to and ending immediately prior to the date determined by the Board pursuant hereto for termination of the Option or during the remaining term of the Option, whichever is the lesser, to exercise any unexpired Option or Options without regard to the installment provisions of Paragraph 6(d) of the Plan; provided, that any such right granted shall be granted to all Optionees not receiving an offer to receive substitute options on a consistent basis, and provided further, that any such exercise shall be subject to the consummation of such Reorganization.

Subject to any required action of shareholders, if the Company shall be the surviving entity in any merger or consolidation, each outstanding Option thereafter shall pertain to and apply to the securities to which a holder of shares of Stock equal to the shares subject to the Option would have been entitled by reason of such merger or consolidation.

In the event of a change in the Stock of the Company as presently constituted, which is limited to a change of all of its authorized shares without par value into the same number of shares with a par value, the shares resulting from any such change shall be deemed to be the Stock within the meaning of the Plan.

To the extent that the foregoing adjustments relate to stock or securities of the Company, such adjustments shall be made by the Board, whose determination in that respect shall be final, binding and conclusive. Except as expressly provided in this Section 5(i), the Optionee shall have no rights by reason of any subdivision or consolidation of shares of stock of any class or the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class, and the number or price of shares of Stock subject to any Option shall not be affected by, and no adjustment shall be made by reason of, any dissolution, liquidation, merger, consolidation or sale of assets or capital stock, or any issue by the Company of shares of stock of any class or securities convertible into shares of stock of any class.

The Grant of an Option pursuant to the Plan shall not affect in any way the right or power of the Company to make any adjustments, reclassifications, reorganizations or changes in its capital or business structure or to merge, consolidate, dissolve, or liquidate or to sell or transfer all or any part of its business or assets.

(j) Rights as a Shareholder: An Optionee shall have no rights as a shareholder with respect to any shares covered by an Option until the effective date of the issuance of the shares following exercise of such Option by Optionee. No adjustment shall be made for dividends (ordinary or extraordinary, whether in cash, securities or other property) or distributions or other rights for which the record date is prior to the date such stock certificate is issued, except as expressly provided in Section 5(i) hereof.

(k) Modification, Acceleration, Extension, and Renewal of Options: Subject to the terms and conditions and within the limitations of the Plan, the Board may modify an Option, or, once an Option is exercisable, accelerate the rate at which it may be exercised, and may extend or renew outstanding Options granted under the Plan or accept the surrender of outstanding Options (to the extent not theretofore exercised) and authorize the granting of new Options in substitution for such Options, provided such action is permissible under Section 422 of the Code and applicable state securities laws. Notwithstanding the provisions of this Section 5(k), however, no modification of an Option shall, without the consent of the Optionee, alter to the Optionee's detriment or impair any rights or obligations under any Option theretofore granted under the Plan.

(l) Exercise Before Exercise Date: At the discretion of the Board, the Option may, but need not, include a provision whereby the Optionee may elect to exercise all or any portion of the Option prior to the stated exercise date of the Option or any installment thereof. Any shares so purchased prior to the stated exercise date shall be subject to repurchase by the Company upon termination of Optionee's employment as contemplated by Section 5(n) hereof prior to the exercise date stated in the Option and such other restrictions and conditions as the Board or Committee may deem advisable.

(m) Other Provisions: The Option agreements authorized under the Plan shall contain such other provisions, including, without limitation, restrictions upon the exercise of the Options, as the Board or the Committee shall deem advisable. Shares shall not be issued pursuant to the exercise of an Option, if the exercise of such Option or the issuance of shares thereunder would violate, in the opinion of legal counsel for the Company, the provisions of any applicable law or the rules or regulations of any applicable governmental or administrative agency or body, such as the Code, the Securities Act, the Exchange Act, applicable state securities laws, the corporate law of the state of Nevada, and the rules promulgated under the foregoing or the rules and regulations of any exchange upon which the shares of the Company are listed. Without limiting the generality of the foregoing, the exercise of each Option shall be subject to the condition that if at any time the Company shall determine that (i) the satisfaction of withholding tax or other similar liabilities, or (ii) the listing, registration or qualification of any shares covered by such exercise upon any securities exchange or under any state or federal law, or (iii) the consent or approval of any regulatory body, or (iv) the perfection of any exemption from any such withholding, listing, registration, qualification, consent or approval is necessary or desirable in connection with such exercise or the issuance of shares thereunder, then in any such event, such exercise shall not be effective unless such withholding, listing registration, qualification, consent, approval or exemption shall have been effected, obtained or perfected free of any conditions not acceptable to the Company.

(n) Repurchase Agreement: The Board may, in its discretion, require as a condition to the Grant of an Option hereunder, that an Optionee execute an agreement with the Company, in form and substance satisfactory to the Board in its discretion (“**Repurchase Agreement**”), (i) restricting the Optionee's right to transfer shares purchased under such Option without first offering such shares to the Company or another shareholder of the Company upon the same terms and conditions as provided therein; and (ii) providing that upon termination of Optionee's employment with the Company, for any reason, the Company (or another shareholder of the Company, as provided in the Repurchase Agreement) shall have the right at its discretion (or the discretion of such other shareholders) to purchase and/or redeem all such shares owned by the Optionee on the date of termination of his or her employment at a price equal to: (A) the fair value of such shares as of such date of termination; or (B) if such repurchase right lapses at 20% of the number of shares per year, the original purchase price of such shares, and upon terms of payment permissible under the applicable state securities laws; provided that in the case of Options or Stock Awards granted to officers, directors, consultants or affiliates of the Company, such repurchase provisions may be subject to additional or greater restrictions as determined by the Board or Committee.

## **6. Stock Awards and Restricted Stock Purchase Offers.**

### **(a) Types of Grants.**

(i) Stock Award. All or part of any Stock Award under the Plan may be subject to conditions established by the Board or the Committee, and set forth in the Stock Award Agreement, which may include, but are not limited to, continuous service with the Company, achievement of specific business objectives, increases in specified indices, attaining growth rates and other comparable measurements of Company performance. Such Awards may be based on Fair Market Value or other specified valuation.

(ii) Restricted Stock Purchase Offer. A Grant of a Restricted Stock Purchase Offer under the Plan shall be subject to such (i) vesting contingencies related to the Participant's continued association with the Company for a specified time and (ii) other specified conditions as the Board or Committee shall determine, in their sole discretion, consistent with the provisions of the Plan.

(b) Conditions and Restrictions. Shares of Stock which Participants may receive as a Stock Award under a Stock Award Agreement or Restricted Stock Purchase Offer under a Restricted Stock Purchase Offer may include such restrictions as the Board or Committee, as applicable, shall determine, including restrictions on transfer, repurchase rights, right of first refusal, and forfeiture provisions. When transfer of Stock is so restricted or subject to forfeiture provisions it is referred to as “**Restricted Stock**.” Further, with Board or Committee approval, Stock Awards or Restricted Stock Purchase Offers may be deferred, either in the form of installments or a future lump sum distribution. The Board or Committee may permit selected Participants to elect to defer distributions of Stock Awards or Restricted Stock Purchase Offers in accordance with procedures established by the Board or Committee to assure that such deferrals comply with applicable requirements of the Code including, at the choice of Participants, the capability to make further deferrals for distribution after retirement. Any deferred distribution, whether elected by the Participant or specified by the Stock Award Agreement, Restricted Stock Purchase Offers or by the Board or Committee, may require the payment be forfeited in accordance with the provisions of Section 6(c). Dividends or dividend equivalent rights may be extended to and made part of any Stock Award or Restricted Stock Purchase Offers denominated in Stock or units of Stock, subject to such terms, conditions and restrictions as the Board or Committee may establish.

(c) Cancellation and Rescission of Grants. Unless the Stock Award Agreement or Restricted Stock Purchase Offer specifies otherwise, the Board or Committee, as applicable, may cancel any unexpired, unpaid, or deferred Grants at any time if the Participant is not in compliance with all other applicable provisions of the Stock Award Agreement or Restricted Stock Purchase Offer, the Plan and with the following conditions:

(i) A Participant shall not render services for any organization or engage directly or indirectly in any business which, in the judgment of the chief executive officer of the Company or other senior officer designated by the Board or Committee, is or becomes competitive with the Company, or which organization or business, or the rendering of services to such organization or business, is or becomes otherwise prejudicial to or in conflict with the interests of the Company. For Participants whose employment has terminated, the judgment of the chief executive officer shall be based on the Participant's position and responsibilities while employed by the Company, the Participant's post-employment responsibilities and position with the other organization or business, the extent of past, current and potential competition or conflict between the Company and the other organization or business, the effect on the Company's customers, suppliers and competitors and such other considerations as are deemed relevant given the applicable facts and circumstances. A Participant who has retired shall be free, however, to purchase as an investment or otherwise, stock or other securities of such organization or business so long as they are listed upon a recognized securities exchange or traded over-the-counter, and such investment does not represent a substantial investment to the Participant or a greater than ten percent (10%) equity interest in the organization or business.

(ii) A Participant shall not, without prior written authorization from the Company, disclose to anyone outside the Company, or use in other than the Company's business, any confidential information or material, relating to the business of the Company, acquired by the Participant either during or after employment with the Company.

(iii) A Participant shall disclose promptly and assign to the Company all right, title and interest in any invention or idea, patentable or not, made or conceived by the Participant during employment by the Company, relating in any manner to the actual or anticipated business, research or development work of the Company and shall do anything reasonably necessary to enable the Company to secure a patent where appropriate in the United States and in foreign countries.

(iv) Upon exercise, payment or delivery pursuant to a Grant, the Participant shall certify on a form acceptable to the Committee that he or she is in compliance with the terms and conditions of the Plan. Failure to comply with all of the provisions of this Section 6(c) prior to, or during the six months after, any exercise, payment or delivery pursuant to a Grant shall cause such exercise, payment or delivery to be rescinded. The Company shall notify the Participant in writing of any such rescission within two years after such exercise, payment or delivery. Within ten days after receiving such a notice from the Company, the Participant shall pay to the Company the amount of any gain realized or payment received as a result of the rescinded exercise, payment or delivery pursuant to a Grant. Such payment shall be made either in cash or by returning to the Company the number of shares of Stock that the Participant received in connection with the rescinded exercise, payment or delivery.

(d) Nonassignability.

(i) Except pursuant to Section 6(e)(iii) and except as set forth in Section 6(d)(ii), no Grant or any other benefit under the Plan shall be assignable or transferable, or payable to or exercisable by, anyone other than the Participant to whom it was granted.

(ii) Where a Participant terminates employment and retains a Grant pursuant to Section 6(e)(ii) in order to assume a position with a governmental, charitable or educational institution, the Board or Committee, in its discretion and to the extent permitted by law, may authorize a third party (including but not limited to the trustee of a "blind" trust), acceptable to the applicable governmental or institutional authorities, the Participant and the Board or Committee, to act on behalf of the Participant with regard to such Awards.

(e) Termination of Employment. If the employment or service to the Company of a Participant terminates, other than pursuant to any of the following provisions under this Section 6(e), all unexercised, deferred and unpaid Stock Awards or Restricted Stock Purchase Offers shall be cancelled immediately, unless the Stock Award Agreement or Restricted Stock Purchase Offer provides otherwise:

(i) Retirement Under a Company Retirement Plan. When a Participant's employment terminates as a result of retirement in accordance with the terms of a Company retirement plan, the Board or Committee may permit Stock Awards or Restricted Stock Purchase Offers to continue in effect beyond the date of retirement in accordance with the applicable Grant Agreement and the exercisability and vesting of any such Grants may be accelerated.

(ii) Rights in the Best Interests of the Company. When a Participant resigns from the Company and, in the judgment of the Board or Committee, the acceleration and/or continuation of outstanding Stock Awards or Restricted Stock Purchase Offers would be in the best interests of the Company, the Board or Committee may (i) authorize, where appropriate, the acceleration and/or continuation of all or any part of Grants issued prior to such termination and (ii) permit the exercise, vesting and payment of such Grants for such period as may be set forth in the applicable Grant Agreement, subject to earlier cancellation pursuant to Section 9 or at such time as the Board or Committee shall deem the continuation of all or any part of the Participant's Grants are not in the Company's best interest.

(iii) Death or Disability of a Participant.

1. In the event of a Participant's death, the Participant's estate or beneficiaries shall have a period up to the expiration date specified in the Grant Agreement within which to receive or exercise any outstanding Grant held by the Participant under such terms as may be specified in the applicable Grant Agreement. Rights to any such outstanding Grants shall pass by will or the laws of descent and distribution in the following order: (a) to beneficiaries so designated by the Participant; if none, then (b) to a legal representative of the Participant; if none, then (c) to the persons entitled thereto as determined by a court of competent jurisdiction. Grants so passing shall be made at such times and in such manner as if the Participant were living.

2. In the event a Participant is deemed by the Board or Committee to be unable to perform his or her usual duties by reason of mental disorder or medical condition which does not result from facts which would be grounds for termination for cause, Grants and rights to any such Grants may be paid to or exercised by the Participant, if legally competent, or a committee or other legally designated guardian or representative if the Participant is legally incompetent by virtue of such disability.

3. After the death or disability of a Participant, the Board or Committee may in its sole discretion at any time (1) terminate restrictions in Grant Agreements; (2) accelerate any or all installments and rights; and (3) instruct the Company to pay the total of any accelerated payments in a lump sum to the Participant, the Participant's estate, beneficiaries or representative; notwithstanding that, in the absence of such termination of restrictions or acceleration of payments, any or all of the payments due under the Grant might ultimately have become payable to other beneficiaries.

4. In the event of uncertainty as to interpretation of or controversies concerning this Section 6, the determinations of the Board or Committee, as applicable, shall be binding and conclusive.

**7. Change in Control** . Unless otherwise provided in the applicable Grant Agreement, in the event of a Change in Control, 50% of the vesting restrictions applicable to each Participant's Grant(s) shall terminate fully and the Participant shall immediately have the right to the delivery of share certificates or exercise of Options, i.e. to the extent that a Participant's Option(s) are unvested, 50% of such unvested portion shall vest.

**8. Investment Intent** All Grants under the Plan are intended to be exempt from registration under the Securities Act provided by Rule 701 thereunder. Unless and until the granting of Options or sale and issuance of Stock subject to the Plan are registered under the Securities Act or shall be exempt pursuant to the rules promulgated thereunder, each Grant under the Plan shall provide that the purchases or other acquisitions of Stock thereunder shall be for investment purposes and not with a view to, or for resale in connection with, any distribution thereof. Further, unless the issuance and sale of the Stock have been registered under the Securities Act, each Grant shall provide that no shares shall be purchased upon the exercise of the rights under such Grant unless and until (i) all then applicable requirements of state and federal laws and regulatory agencies shall have been fully complied with to the satisfaction of the Company and its counsel, and (ii) if requested to do so by the Company, the person exercising the rights under the Grant shall (A) give written assurances as to knowledge and experience of such person (or a representative employed by such person) in financial and business matters and the ability of such person (or representative) to evaluate the merits and risks of exercising the Option, and (B) execute and deliver to the Company a letter of investment intent and/or such other form related to applicable exemptions from registration, all in such form and substance as the Company may require. If shares are issued upon exercise of any rights under a Grant without registration under the Securities Act, subsequent registration of such shares shall relieve the purchaser thereof of any investment restrictions or representations made upon the exercise of such rights.

**9. Amendment, Modification, Suspension or Discontinuance of the Plan**. The Board may, insofar as permitted by law, from time to time, with respect to any shares at the time not subject to outstanding Grants, suspend or terminate the Plan or revise or amend it in any respect whatsoever, except that without the approval of the shareholders of the Company, no such revision or amendment shall (i) increase the number of shares subject to the Plan, (ii) decrease the price at which Grants may be granted, (iii) materially increase the benefits to Participants, or (iv) change the class of persons eligible to receive Grants under the Plan; provided, however, no such action shall alter or impair the rights and obligations under any Option, or Stock Award, or Restricted Stock Purchase Offer outstanding as of the date thereof without the written consent of the Participant thereunder. No Grant may be issued while the Plan is suspended or after it is terminated, but the rights and obligations under any Grant issued while the Plan is in effect shall not be impaired by suspension or termination of the Plan.

In the event of any change in the outstanding Stock by reason of a stock split, stock dividend, combination or reclassification of shares, recapitalization, merger, or similar event, the Board or the Committee may adjust proportionally (a) the number of shares of Stock (i) reserved under the Plan, (ii) available for Incentive Stock Options and Nonstatutory Options and (iii) covered by outstanding Stock Awards or Restricted Stock Purchase Offers; (b) the Stock prices related to outstanding Grants; and (c) the appropriate Fair Market Value and other price determinations for such Grants. In the event of any other change affecting the Stock or any distribution (other than normal cash dividends) to holders of Stock, such adjustments as may be deemed equitable by the Board or the Committee, including adjustments to avoid fractional shares, shall be made to give proper effect to such event. In the event of a corporate merger, consolidation, acquisition of property or stock, separation, reorganization or liquidation, the Board or the Committee shall be authorized to issue or assume stock options, whether or not in a transaction to which Section 424(a) of the Code applies, and other Grants by means of substitution of new Grant Agreements for previously issued Grants or an assumption of previously issued Grants.

**10. Tax Withholding**. The Company shall have the right to deduct applicable taxes from any Grant payment and withhold, at the time of delivery or exercise of Options, Stock Awards or Restricted Stock Purchase Offers or vesting of shares under such Grants, an appropriate number of shares for payment of taxes required by law or to take such other action as may be necessary in the opinion of the Company to satisfy all obligations for withholding of such taxes. If Stock is used to satisfy tax withholding, such stock shall be valued based on the Fair Market Value when the tax withholding is required to be made. Each Participant understands that such Participant (and not the Company) shall be responsible for the Participant's own tax liability that may arise as a result of an award or grant of options or Shares. Participant represents that Participant has consulted any tax consultants Participant deems advisable in connection with the receipt of the options or Shares and that Participant is not relying on the Company or the Company's counsel for any tax advice. The Company intends to report the value of the options or Shares received, if applicable, to appropriate tax authorities. The Company has the authority to require Participant to remit to the Company an amount sufficient to satisfy all federal, state, and local taxes required by law to be withheld with respect to any taxable event arising as a result of the receipt of the Shares.

**11. Availability of Information**. During the term of the Plan and any additional period during which a Grant granted pursuant to the Plan shall be exercisable, the Company shall make available, not later than one hundred and twenty (120) days following the close of each of its fiscal years, such financial and other information regarding the Company as is required by the bylaws of the Company and applicable law to be furnished in an annual report to the shareholders of the Company.

**12. Notice**. Any written notice to the Company required by any of the provisions of the Plan shall be addressed to the chief financial officer or to the chief executive officer of the Company, and shall become effective when it is received by the office of the chief financial officer or the chief executive officer.

**13. Indemnification of Board.** In addition to such other rights or indemnifications as they may have as directors or otherwise, and to the extent allowed by applicable law, the members of the Board and the Committee shall be indemnified by the Company against the reasonable expenses, including attorneys' fees, actually and necessarily incurred in connection with the defense of any claim, action, suit or proceeding, or in connection with any appeal thereof, to which they or any of them may be a party by reason of any action taken, or failure to act, under or in connection with the Plan or any Grant granted thereunder, and against all amounts paid by them in settlement thereof (provided such settlement is approved by independent legal counsel selected by the Company) or paid by them in satisfaction of a judgment in any such claim, action, suit or proceeding, except in any case in relation to matters as to which it shall be adjudged in such claim, action, suit or proceeding that such Board or Committee member is liable for negligence or misconduct in the performance of his or her duties; provided that within sixty (60) days after institution of any such action, suit or Board proceeding the member involved shall offer the Company, in writing, the opportunity, at its own expense, to handle and defend the same.

**14. Governing Law.** The Plan and all determinations made and actions taken pursuant hereto, to the extent not otherwise governed by the Code or the securities laws of the United States, shall be governed by the law of the State of California and construed accordingly.

**15. Termination Dates.** The Plan shall terminate ten years following the initial adoption of the Plan by the Board of Directors, subject to earlier termination by the Board pursuant to Section 9.

The foregoing 2016 Stock Incentive Plan was duly adopted and approved by the Board of Directors as of February 9, 2016, and the first amendment thereto was duly adopted and approved by the Board of Directors as of March 9, 2018.

**Certification**

I, Nicholas Kovacevich, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Kush Bottles, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 13, 2018

/s/ Nicholas Kovacevich  
Nicholas Kovacevich  
Chairman and Chief Executive Officer  
(principal executive officer)

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**Certification**

I, Jim McCormick, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Kush Bottles, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 13, 2018

/s/ Jim McCormick

Jim McCormick

Chief Financial Officer and Chief Operating Officer

(principal accounting and financial officer)

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**CERTIFICATION OF PERIODIC FINANCIAL REPORT  
PURSUANT TO 18 U.S.C. SECTION 1350**

The undersigned officer of Kush Bottles, Inc. (the “Company”) hereby certifies to his knowledge that the Company’s Quarterly Report on Form 10-Q for the three months ended May 31, 2018 (the “Report”) to which this certification is being furnished as an exhibit, as filed with the Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company. This certification is provided solely pursuant to 18 U.S.C. Section 1350 and Item 601(b)(32) of Regulation S-K (“Item 601(b)(32)”) promulgated under the Securities Act of 1933, as amended (the “Securities Act”), and the Exchange Act. In accordance with clause (ii) of Item 601(b)(32), this certification (A) shall not be deemed “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and (B) shall not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the Company specifically incorporates it by reference.

Date: July 13, 2018

/s/ Nicholas Kovacevich

Nicholas Kovacevich  
Chairman and Chief Executive Officer  
(principal executive officer)

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**CERTIFICATION OF PERIODIC FINANCIAL REPORT  
PURSUANT TO 18 U.S.C. SECTION 1350**

The undersigned officer of Kush Bottles, Inc. (the "Company") hereby certifies to his knowledge that the Company's Quarterly Report on Form 10-Q for the three months ended May 31, 2018 (the "Report") to which this certification is being furnished as an exhibit, as filed with the Securities and Exchange Commission on the date hereof, fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company. This certification is provided solely pursuant to 18 U.S.C. Section 1350 and Item 601(b)(32) of Regulation S-K ("Item 601(b)(32)") promulgated under the Securities Act of 1933, as amended (the "Securities Act"), and the Exchange Act. In accordance with clause (ii) of Item 601(b)(32), this certification (A) shall not be deemed "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and (B) shall not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the Company specifically incorporates it by reference.

Date: July 13, 2018

/s/ Jim McCormick

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Jim McCormick

Chief Financial Officer and Chief Operating Officer

(principal financial and accounting officer)

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