

ParaZero Ltd.

**Financial Statements
As at December 31, 2017**

Financial Statements at of December 31, 2017

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Auditors' Report to the Shareholders of ParaZero Ltd.

We have audited the accompanying statements of financial position of ParaZero Ltd. (hereinafter "the Company") as at December 31, 2017, 2016 and January 1, 2016 and the related statements of comprehensive loss, statements of changes in equity and statements of cash flows, for the years ended December 31, 2017, 2016 and 2015. These financial statements are the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including standards prescribed by the Auditors Regulations (Manner of Auditor's Performance) - 1973. Such standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and by Management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as at December 31, 2017, 2016 and January 1, 2016 and its results of operations, changes in shareholder equity and cash flows, for the years ended on December 31, 2017, 2016 and 2015, in accordance with International Financial Reporting Standards (IFRS).

Without qualifying our opinion, we draw attention to Note 1A of the financial statements. The Company has limited capital resources, loss from operations, and accumulated deficit, all of which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters include continued development and marketing as well as seeking additional financing arrangements. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.


Somekh Chaikin
Certified Public Accountants (Isr.)

February 20, 2018

ParaZero Ltd.

Statements of Financial Position as at

		December 31 2017	December 31 2016	January 1 2016
	Note	USD thousands	USD thousands	USD thousands
Assets				
Cash and cash equivalents		54	483	*-
Trade receivables		40	9	-
Other receivables	4	82	19	34
Total current assets		176	511	34
Property and equipment	5	81	53	-
Total assets		257	564	34
Liabilities				
Credit and current maturities of long-term loans from banks	6	159	58	49
Trade payables		81	178	81
Other payables	7	276	195	56
Liability for Chief Office Scientist grants	8	119	37	15
Loans from related party	6	-	-	1,080
Total current liabilities		635	468	1,281
Long-term loans from bank	6	59	98	85
Liability for Chief Office Scientist grants	8	267	173	81
Convertible loans	9	2,962	1,645	-
Liabilities for employees severance benefit, net		-	24	8
Total non-current liabilities		3,288	1,940	174
Total liabilities		3,923	2,408	1,455
Shareholders' equity				
Share capital and share premium	10	*-	*-	*-
Capital reserves		1,537	884	-
Retained deficit		(5,203)	(2,728)	(1,421)
Total liabilities and shareholders' deficit		(3,666)	(1,844)	(1,421)
Total shareholders' equity		257	564	34

* Less than USD 1 thousand

DocuSigned by:

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 Director

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 Director

Date of approval of the financial statements: February 20, 2018

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

ParaZero Ltd.

Statements of Comprehensive Loss

		For the year ended December 31 2017	For the year ended December 31 2016	For the year ended December 31 2015
	Note	USD thousands	USD thousands	USD thousands
Revenues		540	442	125
Cost of sales		<u>(329)</u>	<u>(521)</u>	<u>(105)</u>
Gross profit (Loss)		211	(79)	20
Research and development expenses	11	(977)	(548)	(715)
General and administrative expenses	12	(792)	(334)	(46)
Selling and marketing expenses	13	<u>(404)</u>	<u>(240)</u>	<u>(129)</u>
Operating loss		(1,962)	(1,201)	(870)
Financing income		-	-	5
Financing expenses		<u>(513)</u>	<u>(106)</u>	<u>(11)</u>
Financing income (expenses), net	14	<u>(513)</u>	<u>(106)</u>	<u>(6)</u>
Loss for the year		<u>(2,475)</u>	<u>(1,307)</u>	<u>(876)</u>
Loss per Share				
Basic and Diluted loss per share (in USD)	16	<u>(2.08)</u>	<u>(0.13)</u>	<u>(0.88)</u>

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

ParaZero Ltd.

Statements of Changes in Shareholders' Equity

	<u>Share capital and share premium</u>	<u>Capital reserves</u>	<u>Retained deficit</u>	<u>Total</u>
	<u>USD thousands</u>	<u>USD thousands</u>	<u>USD thousands</u>	<u>USD thousands</u>
Balance as at January 1, 2015	* -	-	(545)	(545)
Loss for the year	-	-	(876)	(876)
Balance as at December 31, 2015	* -	-	(1,421)	(1,421)
Loan conversion	-	736	-	736
Compensation from shareholders	-	148	-	148
Loss for the year	-	-	(1,307)	(1,307)
Balance as at December 31, 2016	* -	884	(2,728)	(1,844)
Share-based compensation	-	341	-	341
Exercise of options	* -	-	-	-
Loan conversion	-	312	-	312
Loss for the year	-	-	(2,475)	(2,475)
Balance as at December 31, 2017	* -	1,537	(5,203)	(3,666)

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

ParaZero Ltd.

Statements of Cash Flows

	For the year ended December 31 2017	For the year ended December 31 2016	For the year ended December 31 2015
	<u>USD thousands</u>	<u>USD thousands</u>	<u>USD thousands</u>
Loss for the year	(2,475)	(1,307)	(876)
Cash flows used in operating activities			
Adjustments for:			
Depreciation	14	*-	-
Share base compensation	341	-	-
Change in trade and other receivables	(94)	(145)	167
Change in trade and other payables	(87)	111	(13)
Change in liability for Chief Office Scientist grants	176	114	95
Change in liabilities for employee severance benefit, net	(24)	16	8
Change in other adjusting item	330	231	3
Interest paid in cash	5	4	4
Net cash used in operating activities	<u>(1,814)</u>	<u>(976)</u>	<u>(612)</u>
Cash flows from investing activities			
Acquisition of fixed assets	(42)	(54)	-
Net cash provided by (used in) investing activities	<u>(42)</u>	<u>(54)</u>	<u>-</u>
Cash flows from financing activities			
Receipt of loans from banks	-	78	129
Repayment of bank loans	(46)	(53)	(16)
Change in credit from banking institutions	93	(23)	(2)
Proceed loan from related party	-	920	499
Proceed from convertible loans	1,380	591	-
Net cash provided by financing activities	<u>1,427</u>	<u>1,513</u>	<u>610</u>
Net increase (decrease) in cash and cash equivalents	<u>(429)</u>	<u>483</u>	<u>(2)</u>
Cash and cash equivalents as at the beginning of the year	<u>483</u>	<u>*-</u>	<u>2</u>
Cash and cash equivalents as at the end of the year	<u>54</u>	<u>483</u>	<u>*-</u>

* Less than USD 1 thousand

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

Notes to the Financial Statements as at December 31, 2017

Note 1 - General**A. Reporting entity**

- (1) ParaZero Ltd. (hereinafter – “the Company”) was incorporated in Israel on June 30, 2013, the registered address of the Company's office is Dov Hoz 30, Kiryat Ono, Israel. The Company specializes in the development and manufacturing of drone safety systems for commercial drones. The Company's technology enables parachute deployment in fractions of a second using customized pyrotechnic devices that actively deploy the parachute to its full formation. Parazero's SafeAir™ system monitors the flight operation of the drone with the SmartAir™ control system, which in case of drone failure in flight, triggers a patented ballistic parachute to provide a controlled descent rate, warns bystanders and transmits the issue to the UTM (Unmanned Traffic System) under development by NASA.
- (2) The Company's operations involve a number of risks and uncertainties. Factors that could affect the Company's operating results and cause actual results to vary materially from expectations include, but are not limited to, rapid technological change, uncertainty of market acceptance of products and services, competition from substitute products and larger companies, protection of proprietary technology, strategic relationships and dependence on key individuals. The Company has limited capital resources, loss from operations, and accumulated deficit, all of which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters include continued development and marketing as well as seeking additional financing arrangements, see also Note 19. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

B. Definitions in these financial statements –

The Company – ParaZero Ltd.

Related party - Within its meaning in IAS 24 (2009), “Related Party Disclosures.

NIS – The Israeli currency is the New Israeli Shekel

Note 2 - Basis of Preparation**A. Statement of compliance**

Since January 1, 2016, the Company has adopted the International Financial Reporting Standards (IFRSs) and its interpretations adopted by the International Accounting Standards Board (“IASB”). The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and IFRS 1 “First-time-Adoption of International Financial Reporting” has been applied.

An explanation of how the transition to IFRS's has affected the reported financial position, financial performance and cash flows of the Company was not provided due to immaterial adjustments.

The financial statements were authorized for issue by the Company's Board of Directors on February 20, 2018.

Notes to the Financial Statements as at December 31, 2017

Note 2 - Basis of Preparation (cont'd)**B. Functional and presentation currency**

These financial statements are presented in USD, which is the Company's functional currency, and have been rounded to the nearest thousands, except when otherwise indicated. The USD is the currency that represents the principal economic environment in which the Company operates.

The dollar figures are determined as follows: transactions and balances originally denominated in dollars are presented at their original amounts. Balances in non-dollar currencies are translated into dollars using historical and current exchange rates for non-monetary and monetary balances, respectively. For non-dollar transactions reflected in the statement of operations, the exchange rates at transaction dates are used. Depreciation and other charges deriving from non-monetary items are based on historical exchange rates. The resulting translation gains or losses are recorded as financial income or expenses, as appropriate.

C. Use of estimates and judgments

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

The preparation of accounting estimates used in the preparation of the Group's financial statements requires management of the Company to make assumptions regarding circumstances and events that involve considerable uncertainty. Management of the Company prepares the estimates on the basis of past experience, various facts, external circumstances, and reasonable assumptions according to the pertinent circumstances of each estimate.

D. Operating cycle

The operating cycle of the Company is one year. Thus, current assets and current liabilities include items the realization of which is intended and anticipated to take place within one year.

Note 3 - Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements and in preparing the opening IFRS statement of financial position at January 1, 2016 for the purposes of the transition to IFRSs unless otherwise indicated.

A. Cash and cash equivalents

Cash and Cash Equivalents includes bank balances and bank deposits that were deposited for periods that do not exceed three months, and there are no contractual restrictions for their use.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**B. Financial instruments****(1) Non-derivative financial assets****Initial recognition of financial assets**

The Company initially recognizes receivables on the date that they are created. Non-derivative financial instruments include accounts receivable and cash and cash equivalents.

Cash and cash equivalents include cash balances available for immediate use and call deposits. Cash equivalents include short-term highly liquid investments (with original maturities of three months or less) that are readily convertible into known amounts of cash and are not exposed to significant risks of change in value.

(2) Non-derivative financial liabilities

Non-derivative financial liabilities include trade and other payables.

Initial recognition of financial liabilities

Financial liabilities are recognized initially on the trade date at which the Company becomes a party to the contract creating the obligation.

Financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, financial liabilities are measured at amortized cost using the effective interest method.

Derecognition of financial liabilities

Financial liabilities are derecognized when the obligation of the Company, as specified in the agreement, expires or when the obligation is discharged or cancelled.

(3) Change in terms of debt instruments

An exchange of debt instruments having substantially different terms, between an existing borrower and lender is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability at fair value. Furthermore, a substantial modification of the terms of the existing financial liability or part of it, is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

In such cases the entire difference between the amortized cost of the original financial liability and the fair value of the new financial liability is recognized in profit or loss as financing income or expense.

The terms are substantially different if the discounted present value of the cash flows according to the new terms, including any commissions paid, less any commissions received and discounted using the original effective interest rate, is different by at least ten percent from the discounted present value of the remaining cash flows of the original financial liability.

If a shareholder forgives the debt, then it is likely that the shareholder is acting in the capacity of a shareholder and that the forgiveness of debt should be treated as a capital transaction. The outstanding financial liability should be reclassified to equity and no gain or loss should be recognized.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**B. Financial instruments (cont'd)****(4) Share capital**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of the shares are recognized as a deduction from equity, net of any tax effects.

C. Property and equipment

Property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalized net within "other income" or other expenses" as relevant in profit or loss.

Depreciation is a systematic allocation of the depreciable amount of an asset over its useful life. The depreciable amount is the cost of the asset, or other amount substituted for cost, less its residual value.

Gains and losses on disposal of a fixed asset item are determined by comparing the net proceeds from disposal with the carrying amount of the asset, and are recognized in profit or loss.

An asset is depreciated from the date it is ready for use, meaning the date it reaches the location and condition required for it to operate in the manner intended by management. Depreciation is recognized in profit or loss on a straight-line basis over the estimated useful life of each part of the property and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

The cost of replacing part of a fixed asset item and other subsequent expenses are capitalized if it is probable that the future economic benefits associated with them will flow to the Group and their cost can be measured reliably. The carrying amount of the replaced part of a fixed asset item is derecognized. The costs of day-to-day servicing are recognized in profit or loss as incurred.

The estimated useful lives for the current and comparative periods are as follows:

- Furniture and office equipment 3-17 years
- Computers 3 years
- Leasehold improvements The shorter of the lease term and the useful life

Depreciation methods and useful lives are reviewed at the end of each reporting year and adjusted if appropriate.

D. Impairment of non-financial assets

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use.

No impairment losses were recorded during 2017.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**E. Revenue Recognition**

Revenue from the sale of goods in the ordinary course of business is measured at the fair value of the consideration received or receivable. When the credit period is short and constitutes the accepted credit in the industry, the future consideration is not discounted.

Revenue is recognized when persuasive evidence exists (usually in the form of an executed sales agreement) that the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably.

Transfer of risks and rewards occurs when the goods are transferred to the customer.

F. Research and development expenses

Research and development expenses are recognized in profit or loss when incurred. An intangible asset arising from a development project or from the development phase of an internal project is recognized if the Company can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale; the Company's intention to complete the intangible asset; and the Company's ability to measure reliably the expenditure attributable to the intangible asset during its development. Since the Company's research and development projects are often subject to regulatory approval procedures and other uncertainties, the conditions for the capitalization of costs incurred before receipt of approvals are not normally satisfied, and, therefore, research and development expenses are recognized in profit or loss when incurred.

As of December 31, 2017, no development expenditures have met the recognition criteria and thus the Company expensed all of its development expenditures as incurred.

G. Income taxes

Income tax includes current and deferred tax. Current tax is the expected tax payable (or receivable) on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date.

A provision for uncertain tax positions, or reduction in deferred tax asset, is recognized when it is more probable than not that the Company will have to use its economic resources to pay the obligation.

Deferred tax is recognized for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. A deferred tax asset is recognized for unused tax losses, tax benefits and deductible temporary differences, to the extent that it is probable that there will be future taxable profits against which such tax benefits can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**G. Income taxes (cont'd)**

As of December 31, 2017, no deferred tax assets have been recorded since it is not probable that the Company will have future taxable income against which any tax losses, benefits or deductible temporary differences can be utilized.

H. Employee benefits**(1) Post-employment benefits**

The Company's liability for severance pay is pursuant to Section 14 of the Israeli Severance Compensation Act, 1963 ("Section 14"). The majority of the Company's employees are included under this section and are entitled only to monthly deposits made in the employee's name with insurance companies at a rate of 8.33% of an employee's monthly salary. Payments in accordance with Section 14 release the Company from any future severance payments in respect of those employees. The funds deposited are made available to the employee at the time the employer-employee relationship is terminated, regardless of cause of termination. The severance pay liabilities and deposits under Section 14 are accounted for as defined contribution benefits and accordingly are not reflected in the balance sheet, as the severance pay risks have been irrevocably transferred to the severance funds.

(2) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided or upon the actual absence of the employee when the benefit is not accumulated. A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably. The employee benefits are classified, for measurement purposes, as short-term benefits or as other long-term benefits depending on when the Company expects the benefits to be wholly settled.

(3) Termination benefits

Termination benefits are recognized as an expense when the Company is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment before the normal retirement date.

(4) Share based compensation

The grant date fair value of share-based compensation awards granted to employees is recognized as a salary expense, with a corresponding increase in equity, over the period that the employees become unconditionally entitled to the awards. The amount recognized as an expense in respect of share-based compensation awards that are conditional upon meeting service and non-market performance conditions, is adjusted to reflect the number of awards that are expected to vest. In respect of other service providers, where the fair value of the goods or services received as consideration of equity instruments cannot be measured reliably, they are measured by reference to the fair value of the equity instruments granted.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**I. Government grants**

Government grants are recognized when there is reasonable assurance that they will be received and the Company will comply with the conditions associated with the grant.

Grants received from the Chief Scientist in Israel are recognized as a liability on the date of their receipt if there is reasonable assurance that the research activity will lead to sales entitling the State to royalties.

The liability in respect of the loan is initially recognized at fair value and discounted according to the market rate.

The difference between the amount of the grant received and the fair value of the liability is accounted for as a government grant and is offset from the research and development expenses. Subsequent to initial recognition, the liability is measured at amortized cost using the effective interest method. Amounts paid as royalties are recognized as settlement of the liability. When economic benefits are not expected from the research activity, the grants received are recognized as a deduction from the corresponding research and development expenses. In such a case the liability for the payment of royalties is accounted for as a contingent liability in accordance with IAS 37.

Each reporting date the company examines whether there is reasonable assurance that the liability that was recognized, all or part, will not be settled (since the Company will not be required to pay royalties) based on the best estimate of future sales using the original effective interest rate, and if there is reasonable assurance the appropriate liability is derecognized against a decrease in research and development expenses. Amounts paid as royalties are recognized as settlement of the liability.

J. Financing income and expenses

Financing expense includes bank charges, changes in foreign currency losses change in fair value of derivatives and interest expenses.

Foreign currency gains and losses on financial assets and financial liabilities are reported on a net basis as either financing income or financing expenses, depending on whether foreign currency movements are in a net gain or net loss position.

K. Loss per share

The Company presents basic and diluted earnings or loss per share ("LPS") data for its ordinary shares. Basic LPS is calculated by dividing the loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the year, which includes, inter alia, ordinary shares issuable for little or no consideration. There is no difference between basic and diluted LPS since there are no dilutive potential ordinary shares.

L. Segment reporting

The Company does not present segment information as the Company currently operates in a single segment.

Notes to the Financial Statements as at December 31, 2017

Note 3 - Significant Accounting Policies (cont'd)**M. New standards and interpretations not yet adopted****(1) IFRS 15, Revenue from Contracts with Customers (hereinafter – “IFRS 15”)**

IFRS 15 replaces the current guidance regarding recognition of revenues and presents a comprehensive framework for determining whether revenue should be recognized and when and at what amount.

IFRS 15 is applicable for annual periods beginning on or after January 1, 2018 and earlier application is permitted.

The Company has examined the effects of applying IFRS 15, and in its opinion the effect on the financial statements will be immaterial.

(2) IFRS 9 (2014), Financial Instruments (hereinafter – “IFRS 9 (2014)”)

IFRS 9 (2014) replaces the current guidance in IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 (2014) includes revised guidance on the classification and measurement of financial instruments, a new ‘expected credit loss’ model for calculating impairment for most financial assets, and new guidance and requirements with respect to hedge accounting. IFRS 9 (2014) is effective for annual periods beginning on or after January 1, 2018 with early adoption being permitted. The Company has examined the effects of applying IFRS 9 (2014), and in its opinion the effect on the financial statements will be immaterial.

(3) IFRS 16, Leases

IFRS 16 replaces IAS 17, *Leases* and its related interpretations. For lessees, the standard presents a unified model for the accounting treatment of most leases according to which the lessee has to recognize an asset and liability in respect of the lease in its financial statements. IFRS 16 is applicable for annual periods as of January 1, 2019, with the possibility of early adoption, so long as the company has also early adopted IFRS 15, *Revenue from Contracts with Customers*.

The Company has examined the effects of applying IFRS 17, and in its opinion the effect on the financial statements will be immaterial.

Note 4 - Other Receivable

	December 31 2017	December 31 2016	January 1 2016
	<u>USD thousands</u>	<u>USD thousands</u>	<u>USD thousands</u>
Government institutions	82	-	22
Prepaid expenses and others	*-	19	12
	<u>82</u>	<u>19</u>	<u>34</u>

* Less than USD 1 thousand

Notes to the Financial Statements as at December 31, 2017**Note 5 - Property and Equipment, net**

	Leasehold Improvement USD thousands	Office furniture and equipment USD thousands	Computers USD thousands	Total USD thousands
Cost				
Balance as at January 1, 2015	-	-	-	-
Additions	46	8	-	54
Balance as at December 31, 2016	46	8	-	54
Additions	40	1	1	42
Balance as at December 31, 2017	85	9	1	95
Depreciation				
Balance as at January 1, 2015	-	-	-	-
Additions	(1)	*-	-	(1)
Balance as at December 31, 2016	(1)	*-	-	(1)
Additions	(12)	(1)	*-	(14)
Balance as at December 31, 2017	(13)	(1)	*-	(14)
Property and equipment, net				
As at December 31, 2016	45	8	*-	53
As at December 31, 2017	72	8	1	81

* Less than USD 1 thousand

Note 6 - Loans and Credit from Banks

	December 31 2017 USD thousands	December 31 2016 USD thousands	January 1 2016 USD thousands
Current liabilities			
Bank credit	93	-	21
Current maturities of long term loan (1)	66	58	28
Loan from related parties (2)	-	-	1,080
	159	58	1,129
Non-current liabilities			
Loans from banks (1)	59	98	85
	59	98	85
	218	156	1,214

Notes to the Financial Statements as at December 31, 2017**Note 6 - Loans and Credit from Banks (cont'd)**

- (1) In January 2015 the Company entered into loan agreements with a bank in the total amount of \$ 128 thousand. According to the agreement, the loan will be repaid as from June 28, 2015 in 55 monthly installments bearing fixed interest at the rate of 3.25%.
In March 2016 the Company entered into an additional loan agreement in the total amount of \$ 39 thousand. According to the agreement, the loan will be repaid as from May 25, 2016 in 36 monthly installments bearing interest at the prime rate plus 4.1%.
In December 2016 the Company entered into an additional loan agreement in the total amount of \$ 39 thousand. According to the agreement, the loan will be repaid as from January 25, 2017 in 28 monthly installments bearing interest at the prime rate plus 4.1%.
- (2) As from the date of its incorporation, the Company is financed by a loan from its principal shareholder that bears interest at the rate of 4% and has no fixed date of repayment. In December 2016 it was decided that \$ 0.7 million of the balance of the loan and interest accrued until that date would be converted into a Share Premium. In December 2017 it was decided that the balance of the loan and interest accrued until that date would be converted into a convertible loan other than an amount of \$ 0.3 million that will be converted into a Share Premium. The convertible loan will be at the same terms indicated in Note 9 except for the interest rate as the convertible loan will not bear interest. As a result of the aforesaid change in terms, the company recognized compensation related to the loan from its shareholder in the amount of US\$148 thousand recorded in capital reserve. In the financial statements as at December 31, 2015 the loan and the interest accrued on it are presented in current liabilities. In the financial statements as at December 31, 2017 and 2016 the loan is presented as part of the convertible loans in non-current liabilities, see also Note 9.

Note 7 - Other Payables

	December 31 2017	December 31 2016	January 1 2016
	USD thousands	USD thousands	USD thousands
Government authorities	-	27	14
Payroll and related accruals	108	77	39
Accrued expenses and others	168	91	3
	276	195	56

Note 8 - Liabilities in respect of Chief Scientist Grants

	December 31 2017	December 31 2016	January 1 2016
	USD thousands	USD thousands	USD thousands
Balance as at January 1	210	96	-
Grants received during the year	210	152	132
Payments made during the year	(2)	-	-
Amounts recognized in profit or loss	(32)	(38)	(36)
Balance at the end of the year	386	210	96

Notes to the Financial Statements as at December 31, 2017

Note 8 - Liabilities in respect of Chief Scientist Grants (cont'd)

ParaZero Ltd received from the National Authority for Technology and Innovation (hereinafter "the Chief Scientist") grants for participation in research and development and in return it undertook to pay royalties at the rate of 3%-3.5% of the sales resulting from the research and development financed as aforesaid, in an amount of up to 100% of the grants received. The grants that were received are linked to the dollar and bear interest at the Libor rate. As at December 31, 2017 ParaZero has recognized a liability in respect of all the grants that were received.

In the calculation of the liability to the Chief Scientist, Parazero used the guidance of IAS 20(R) and accordingly, the cash flows were discounted using the Company's cost of capital of 15%, which in the opinion of management of the Company, reflects the Company's level of risk in each of the years.

Note 9 - Convertible Loans

In December 2016 the Company entered into a convertible loan agreement in the amount of US\$ 590 thousand with an investor (hereinafter: "Agreement A") that bears interest of 12% p.a. of which half is payable every half year and half is added to the loan's principal. According to the provisions of the agreement, the loan is convertible into shares when certain conditions are met and at a discount of 25% and in the case of raising an amount of US\$ 3 million, however, the price per share shall not exceed a price per share determined according to a Company pre-money valuation of US\$ 8,000,000, on a fully diluted basis.

In April 2017 the Company entered into a convertible loan agreement in the amount of US\$ 100 thousand with an investor (hereinafter: "Agreement B") that bears interest of 12% p.a. of which half is payable every half year and half is added to the loan's principal. According to the provisions of the agreement, the loan is convertible into shares when certain conditions are met and at a discount of 25% and in the case of raising an amount of \$ 3 million, however, the price per share shall not exceed a price per share determined according to a Company pre-money valuation of US\$ 8,000,000, on a fully diluted basis.

In July 2017 the Company entered into additional convertible loans with several investors (hereinafter: "Agreement C") in the total amount of \$ 1.28 million. The loans bear interest of 12% p.a. of which half is payable every half year and half is added to the loan's principal. According to the provisions of the agreements, the loans are convertible into shares when certain conditions are met and at a discount of 30% in the case of raising an amount of US\$ 4 million, however, the price per share shall not exceed a price per share determined according to a Company pre-money valuation of US\$ 7,000,000, on a fully diluted basis.

In addition, the Company amended Agreement A and Agreement B such that the conversion terms will be the same as those terms in Agreement C.

The consideration for the convertible loans was split for measurement purposes into a conversion component, which is accounted for as a derivative measured at fair value through profit or loss and accordingly measured on a fair value basis on every date of the statement of financial position, with the changes in fair value being recognized in profit or loss, and the balance of the consideration that was not attributed to the conversion component was attributed to a liability component and accounted for according to the amortized cost method using the effective interest inherent in it that was calculated on the date of its issuance as aforesaid.

The convertible loan and the derivatives were classified as a non-current financial liability since the Company is or may be obliged to deliver a variable number of its own equity instruments.

Notes to the Financial Statements as at December 31, 2017

Note 10 - Shareholders' Equity

A. Share capital – composition

	Number of shares	Number of shares	Number of shares
	December 31 2017	December 31 2016	January 1 2016
Ordinary shares of NIS 0.01 par value authorized	10,000,000	10,000,000	10,000,000
Ordinary shares of NIS 0.01 par value issued and paid	102,736	100,000	100,000

B. Share-based compensation

(1) Expense recognized in the statement of loss is as follows:

The expense that was recognized for services received from employees and service providers is as follows:

	Year ended December 31 2017 USD thousands
Research and development	76
Sales and Marketing	27
General and administrative	238
Total share-based compensation	341

(2) Share based compensation plans for employees and consultants:

The Company has reserved for issuance as share options plan for employees limited options to purchase ordinary shares. Any options, which are forfeited or not exercised before expiration, become available for future grants.

Options granted under the Company's 2017 Israeli Share Option Plan (hereinafter- "Plan") are exercisable in accordance with the terms of the Plan, within 10 years from the date of grant, against payment of an exercise price. The options for employees vest over a period of two to six years.

The cost of the benefits in the options granted as aforementioned, based on the grant date fair value amounted to \$398 thousands. This amount will be amortized in the statement of loss over the vesting period of each portion.

Notes to the Financial Statements as at December 31, 2017**Note 10 - Shareholders' Equity (cont'd)****B. Share-based compensation (cont'd)****(3) Option grants during 2017:**

1. In July 2016, the Company granted 18,141 options to purchase ordinary shares under the plan for an exercise price of NIS 0.01 per share to its consultants.
2. In March 2017, the Company granted 7,468 options to purchase ordinary shares under the Plan for an exercise price of NIS 0.01 per share to its employees and consultants.
3. In May 2017, the Company granted 2,337 options to purchase ordinary shares under the Plan for an exercise price of NIS 0.01 per share to its employees and consultants.
4. In September 2017, the Company granted 283 options to purchase ordinary shares under the Plan for an exercise price of NIS 0.01 per share to its employees and consultants.
5. In December 2017, the Company granted 1,093 options to purchase ordinary shares under the Plan for an exercise price of NIS 0.01 per share to its consultant

(4) The number and weighted average exercise prices of options are as follows:

	Weighted average exercise price 2017 U.S. Dollar	Number of options 2017
Outstanding at January 1	-	-
Expired and forfeited	0.003	(616)
Exercised during the year	0.003	(2,736)
Granted during the year	0.003	29,322
Outstanding at December 31	0.003	25,970

Note 11 - Research and Development Costs

	For the year ended December 31 2017 USD thousands	For the year ended December 31 2016 USD thousands	For the year ended December 31 2015 USD thousands
Payroll and related expenses	566	261	277
Materials and Subcontractors	279	170	416
Rent & Maintenance	86	58	-
Other expenses	78	97	58
Less – Chief Office Scientist participation	(32)	(38)	(36)
	977	548	715

Notes to the Financial Statements as at December 31, 2017**Note 12 - General and Administrative Expenses**

	For the year ended December 31 2017	For the year ended December 31 2016	For the year ended December 31 2015
	USD thousands	USD thousands	USD thousands
Payroll and related expenses	329	117	28
Rent and office maintenance	43	46	9
Professional services	217	105	7
Other expenses	203	66	2
	<u>792</u>	<u>334</u>	<u>46</u>

Note 13 - Selling and Marketing Expenses

	For the year ended December 31 2017	For the year ended December 31 2016	For the year ended December 31 2015
	USD thousands	USD thousands	USD thousands
Payroll and related expenses	246	131	46
Rent & Maintenance	43	-	-
Professional services	26	-	-
Other expenses	89	109	83
	<u>404</u>	<u>240</u>	<u>129</u>

Note 14 - Financial income (expenses), net

	For the year ended December 31 2017	For the year ended December 31 2016	For the year ended December 31 2015
	USD thousands	USD thousands	USD thousands
Financial income			
Exchange rate differences	-	-	5
	<u>-</u>	<u>-</u>	<u>5</u>
Financial expenses			
Interest and bank fees	(90)	(70)	(7)
Revaluation of derivatives	(48)	(3)	-
Interest expenses on convertible loans	(243)	(3)	-
Exchange rate differences	(132)	(31)	-
Other expenses	-	-	(4)
	<u>(513)</u>	<u>(107)</u>	<u>(11)</u>
Financial income (expenses), net	<u>(513)</u>	<u>(107)</u>	<u>(11)</u>

Notes to the Financial Statements as at December 31, 2017

Note 15 - Income Tax**Corporate tax rate**

- (1) Presented hereunder are the tax rates relevant to the Company:

2015 – 26.5%
 2016 – 25%
 2017 – 24%
 2018 – 23%

- (2) On January 4, 2016 the Knesset plenum passed the Law for the Amendment of the Income Tax Ordinance (Amendment 216) - 2016, by which, inter alia, the corporate tax rate would be reduced by 1.5% to a rate of 25% as from January 1, 2016.

As a result of the reduction in the tax rate to 25%, the deferred tax balances as at January 4, 2016 were calculated according to the new tax rate specified in the Law for the Amendment of the Income Tax Ordinance, at the tax rate expected to apply on the date of reversal.

Furthermore, on December 22, 2016 the Knesset plenum passed the Economic Efficiency Law (Legislative Amendments for Achieving Budget Objectives in the Years 2017 and 2018) – 2016, by which, inter alia, the corporate tax rate would be reduced from 25% to 23% in two steps. The first step will be to a rate of 24% as from January 2017 and the second step will be to a rate of 23% as from January 2018.

As of December 31, 2017, no deferred tax balances were recognized. Therefore, no impact on the balances is expected due to the reduction in tax rate as detailed above.

- (3) On January 12, 2012 Amendment 188 to the Income Tax Ordinance (New Version) – 1961 (hereinafter – “the Ordinance”) was published in the Official Gazette. The amendment amended Section 87A to the Ordinance, and provides a temporary order whereby Accounting Standard No. 29 “Adoption of International Financial Reporting Standards (IFRS)” that was issued by the Israel Accounting Standards Board shall not apply when determining the taxable income for the tax years 2010-2011 even if this standard was applied when preparing the financial statements (hereinafter – “the Temporary Order”). On July 31, 2014 Amendment 202 to the Ordinance was issued, by which the Temporary Order was extended to the 2012 and 2013 tax years.

Tax losses

As at December 31, 2017, 2016 and January 1, 2016 the Company has carryforward tax losses of approximately US\$4,762 thousand, US\$2,609 thousand and US\$1,190 thousand, respectively. The Company did not create deferred tax assets against such loss, as it does not foresee utilization of such losses in the near future.

Note 16 - Loss Per Share**Basic and Diluted loss per share**

Basic and Diluted loss per share is calculated by dividing the loss of the Company by the weighted average number of the issued and outstanding ordinary shares during the year, including warrants and options to purchase ordinary shares which were granted with an exercise price of par value (2017 - 19,141).

Notes to the Financial Statements as at December 31, 2017

Note 16 - Loss Per Share (cont'd)

	For the year ended December 31 2017	For the year ended December 31 2016	For the year ended January 1 2016
Loss for the year (US\$ thousands)	(2,475)	(1,307)	(876)
Number of Issued ordinary shares (In NIS; 0.01 NIS par value)	119,141	100,000	100,000
Basic and diluted loss per ordinary share (in US\$)	(2.08)	(1.30)	(0.88)

Note 17 - Financial Instruments

A. Overview

The Company has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This note presents quantitative and qualitative information about the Company's exposure to each of the above risks, and the Company's objectives, policies and processes for measuring and managing risk. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework.

B. Credit risk

The Company's revenues are derived from sales to customers mainly worldwide. The Company's Management regularly monitors the customers' balances and includes, when necessary, specific provisions for doubtful debts in the financial statements that adequately reflect, in the opinion of management, the loss inherent in debts the collection of which is doubtful.

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting dates was:

	December 31		
	2017	2016	2015
	Carrying amount		
	USD thousands	USD thousands	USD thousands
Cash and cash equivalents	54	483	*-
Trade accounts receivable	40	9	-
Other accounts receivable	82	19	34
	176	511	34

Notes to the Financial Statements as at December 31, 2017**Note 17 - Financial Instruments (cont'd)****C. Liquidity risk**

The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

Convertible loans have not presented as part of the contractual maturities of financial liability since the Company is or may be obliged to deliver a variable number of its own equity instruments.

The following are the contractual maturities of financial liabilities based on the actual rates at the reporting date excluding interest payments:

	December 31, 2017				
	Carrying amount	Contractual cash flows	Less than 12 months	1-2 years	More than 2 years
	\$ thousands				
Credit and current maturities of long-term					
loans from banks	218	218	159	59	-
Trade payables	81	81	81	-	-
Other payables	276	276	276	-	-
Liabilities for Chief Office Scientist grants	386	386	119	267	-
	<u>961</u>	<u>961</u>	<u>635</u>	<u>326</u>	<u>-</u>

	December 31, 2016				
	Carrying amount	Contractual cash flows	Less than 12 months	1-2 years	More than 2 years
	\$ thousands				
Credit and current maturities of long-term					
loans from banks	156	156	58	98	-
Trade payables	178	178	178	-	-
Other payables	195	195	195	-	-
Liabilities for Chief Office Scientist grants	210	210	37	89	84
	<u>739</u>	<u>739</u>	<u>468</u>	<u>187</u>	<u>84</u>

	January 1, 2016				
	Carrying amount	Contractual cash flows	Less than 12 months	1-2 years	More than 2 years
	\$ thousands				
Credit and current maturities of long-term					
loans from banks	134	134	49	56	29
Trade payables	81	81	81	-	-
Other payables	56	56	56	-	-
Loans from related party	1,080	11,080	1,080	-	-
Liabilities for Chief Office Scientist grants	96	96	15	21	60
	<u>1,447</u>	<u>1,447</u>	<u>1,281</u>	<u>77</u>	<u>89</u>

Notes to the Financial Statements as at December 31, 2017

Note 17 - Financial Instruments (cont'd)

D. Market risk

Market risk is the risk that changes in market prices, mainly foreign exchange rates, will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

Foreign currency risk

The Company is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than its respective functional currency, primarily the NIS.

The exposure to foreign currency risk

The Company's exposure to foreign currency risk was as follows based on notional amounts:

	December 31, 2017		
	NIS	U.S. Dollar	Total
Current assets:			
Cash and cash equivalents	1	53	54
Trade and other receivables	82	40	122
Current liabilities:			
Credit and current maturities of long-term loans from banks	159	-	159
Trade payables	73	8	81
Other payables	276	-	276
Liabilities for Chief Office Scientist grants	119	-	119
Non-current liabilities:			
Long-term loans from bank	59	-	59
Liabilities for Chief Office Scientist grants	267	-	267
Convertible loan	-	2,962	2,962
	1,036	3,063	4,099

Notes to the Financial Statements as at December 31, 2017

Note 17 - Financial Instruments (cont'd)

D. Market risk (cont'd)

Foreign currency risk (cont'd)

	December 31, 2016		
	NIS	U.S. Dollar	Total
Current assets:			
Cash and cash equivalents	231	252	483
Trade and other receivables	19	9	28
Current liabilities:			
Credit and current maturities of long-term loans from banks	58	-	58
Trade payables	178	-	178
Other payables	195	-	195
Liabilities for Chief Office Scientist grants	37	-	37
Non-current liabilities:			
Long-term loans from bank	98	-	98
Liabilities for Chief Office Scientist grants	173	-	173
Convertible loan	-	1,645	1,645
Liabilities for employees severance benefit, net	24	-	24
	<u>1,013</u>	<u>1,906</u>	<u>2,919</u>
	January 1, 2016		
	NIS	U.S. Dollar	Total
Current assets:			
Cash and cash equivalents	*_	-	*_
Trade and other receivables	28	6	34
Current liabilities:			
Credit and current maturities of long-term loans from banks	49	-	49
Trade payables	73	8	81
Other payables	56	-	56
Liabilities for Chief Office Scientist grants	15	-	15
Loans from related party	1,080	-	1,080
Non-current liabilities:			
Long-term loans from bank	85	-	85
Liabilities for Chief Office Scientist grants	81	-	81
Liabilities for employees severance benefit, net	8	-	8
	<u>1,475</u>	<u>14</u>	<u>1,489</u>

Notes to the Financial Statements as at December 31, 2017**Note 17 - Financial Instruments (cont'd)****D. Market risk (cont'd)**Foreign currency risk (cont'd)

Information regarding significant exchange rates:

	Year ended December 31		
	2017	2016	2015
	Rate of change		
	NIS		
1 U.S. Dollar	<u>3,467</u>	<u>3,845</u>	<u>3,902</u>

Information regarding significant changes exchange rates:

	Year ended December 31		
	2017	2016	2015
	Rate of change		
	%		
1 U.S. Dollar	<u>(9.83)</u>	<u>(1.46)</u>	<u>0.33</u>

Note 18 - Balances and Transactions with Related and Interested Parties

Details of transactions with related and interested parties are presented below:

	For the year ended December 31 2017 <u>USD thousands</u>	For the year ended December 31 2016 <u>USD thousands</u>	For the year ended January 1 2016 <u>USD thousands</u>
Trade receivables	<u>-</u>	<u>19</u>	<u>5</u>
Compensation and benefits to key management (including share-based compensation)	<u>398</u>	<u>158</u>	<u>77</u>

(*) With respect to loans from related party and convertible loans from shareholders, see Note 6(2) and 9, respectively.

Note 19- Subsequent Events

In December 2017, the Company signed a binding term sheet with a broker company to assist the Company in performing an initial public offering. The Company is currently negotiating a definitive agreement with said broker company, following the execution of which (and subject thereto) the broker company will commence the process of the initial public offering.