HILL STREET BEVERAGE COMPANY INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE TWELVE-MONTH PERIOD ENDING JUNE 30, 2020

The following management's discussion and analysis ("**MD&A**") provides a review of the activities, results of operations and financial condition of Hill Street Beverage Company Inc. (the "**Company**" or "**Hill Street**") for the three months and year ended June 30, 2020 in comparison with the three months and year ended June 30, 2019. These comments should be read in conjunction with the audited financial statements for the years ended June 30, 2020 and June 30, 2019 and accompanying notes included therein, which have been prepared in accordance with International Financial Reporting Standards ("**IFRS**"). This MD&A has been prepared as of October 28, 2020. Additional information relating to Hill Street is available on SEDAR.

All amounts are stated in Canadian dollars unless otherwise identified.

FORWARD-LOOKING STATEMENTS

Except for the historical information contained herein, the discussion in this MD&A contains certain forward-looking statements that involve risks and uncertainties, such as statements of Hill Street's plans, objectives, strategies, expectations and intentions. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may", "will", "expect", "intend", "anticipate", "seek", "plan", "believe" or "continue" or the negatives of these terms or variations of them or similar terminology. Although Hill Street believes that the expectations and assumptions reflected in these forward-looking statements are reasonable, undue reliance should not be placed on these forward-looking statements. These forward-looking statements are not guarantees and reflect Hill Street's views as October 28, 2020 with respect to future events. Future events are subject to certain risks, uncertainties and assumptions, which may cause actual performance and financial results to differ materially from such forward-looking statements. The forward-looking statements, including the statements regarding expected volumes, operating efficiencies, and costs are based on, among other things, the following material factors and assumptions: sales volumes in the quarter will increase; no material changes in consumer preferences; brewing, blending, and packaging efficiencies will improve; the cost of input materials for brewing and blending will increase; competitive activity from other manufacturers will continue; foreign currency exchange rates will change; no material change to the regulatory environment in which Hill Street operates and no material supply, cost or quality control issues with vendors. Readers are urged to consider the foregoing factors and assumptions when reading the forward-looking statements and for more information regarding the risks, uncertainties and assumptions that could cause Hill Street's actual financial results to differ from the forward-looking statements, to also refer to the remainder of the discussion in this MD&A, Hill Street's various other public filings as and when released by Hill Street. The forward-looking statements included in this MD&A are made only as of October 28, 2020 and, except as required by applicable securities laws, Hill Street does not undertake to publicly update such forward-looking statements to reflect new information, future events or otherwise.

DESCRIPTION OF THE BUSINESS

The Company presently has one business segment, the marketing and distribution of alcohol-free beer and wine in Canada and, to a much lesser extent, the United States. Hill Street sells its products online and in thousands of branded retail chain stores through licensed distributors in Canada. It also provides direct to consumer and wholesale sales at www.hillstreetbeverages.com. In addition, the Company is preparing to launch Cannabis infused beverages and other cannabis products, including drink mixes, tablets, and infusion ingredients for the wholesale market, in late 2020 and early 2021.

HIGHLIGHTS FOR THE 2020 FISCAL YEAR END

In spite of the dramatic negative effects of the global novel coronavirus pandemic on both the Canadian and global economy, Hill Street managed to continue generating growth for the full fiscal year, increasing gross annual revenues year over year by 7% to $2,613,923. This included increased revenues of 23% for the fourth quarter versus the prior fiscal year, supported in part by a 242% increase in online sales. Hill Street believes this increase in online revenues is directly attributable to dramatically changing consumer behaviours and purchasing patterns resulting from the lockdown imposed by both Canadian and American governments. While fourth quarter sales reflected a 52% drop in revenues for the month of June 2020 vs June 2019, they did reflect a strengthening over the previous months as retailers restocked shelves after essentially shutting down sales in the first months of the lockdown. In response to the broad pullback in capital markets support for cannabis companies, the Company has been conserving its limited cash resources to focus on preparations for the launch of cannabis beverages later this year, and has reduced marketing support and investment in new listings to increase distribution of its alcohol free beverages. In spite of the broad-based economic headwinds, Hill Street finished the year with a 7% increase in sales versus the prior fiscal year, with reports from its major retail partners that Hill Street's brands have taken leading market share positions in the national branded alcohol-free wine category in their stores.

The global outbreak of the novel coronavirus, COVID-19 had an impact on businesses through the restrictions put in place by the Canadian, provincial and municipal governments regarding travel, business operations and isolation/quarantine orders. The Company's operations were impacted by COVID-19 due to a slower growth in year over year sales than anticipated. At this time, it is unknown the extent of the impact the COVID-19 outbreak may have on the Company as this will depend on future developments that are highly uncertain and that cannot be predicted with confidence. These uncertainties arise from the inability to predict the ultimate geographic spread of the disease, and the duration of the outbreak, including the duration of travel restrictions, business closures or disruptions, and quarantine/isolation measures that are currently, or may be put, in place by Canada and other countries to fight the virus. While the extent of the impact is unknown, we anticipate this outbreak may cause reduced customer demand, supply chain disruptions, staff shortages, and increased government regulations, all of which may negatively impact the Company's business and financial condition.

The Company continued planning for its licensed cannabis operations at the Lucknow facility, strategically located near Pearson Airport in Mississauga, Ontario. Construction on the facility has been delayed as a result of shut downs imposed relating to COVID-19. The Company has continued preparations and planning to have the facility licensed for cannabis processing and sales for the Joint Manufacturing Partnership ("**JMP**") the Company formed with Lexaria Biosciences in June 2019. The Lucknow facility will also serve as a warehouse for cannabis infused products produced by the JMP for the consumer market, as well as the processing facility for the cannabis powder the Company plans to begin selling as an ingredient to cannabis 2.0 product manufacturers.

During the quarter, the Company began an extensive search for cannabis extraction partners to become resellers of its cannabis powder products, which we believe will add tremendous value to the cannabis oil extraction sector. Cannabis oil is an unstable product, declining in potency at a rate of 10-40% per year. The DehydraTECH process developed by Lexaria converts this unstable oil into a shelf stable ingredient, which can be used for any edible or topical form of product, including meat, fish, eggs, dairy, beverages, cocoa, coffee, tea, herbs, spices, sugar, salt, and flour-type products. The Company has identified several extraction companies who match the criteria we have established to act as resellers of cannabis powder and has entered negotiations with them to act in this capacity as soon as the Lucknow facility is operational. In addition, subsequent to the quarter, Hill Streetannounced that it signed a non-binding Term Sheet with Molecule Holdings Inc. ("**Molecule**") to produce select cannabis infused beverages for Hill Avenue Cannabis Co., the wholly owned subsidiary of Hill Street created to manage its business in the legal cannabis segment. The Notice of New Product Introduction to Health Canada was filed on October 1, 2020 for the first beverages to be produced by this partnership. This begins the sixty-day notice period wherein the two companies can begin arranging sales and distribution agreements with provincial regulators and independent retailers. It is anticipated that the definitive agreement with Molecule, which has not yet been executed, will contemplate a three (3) year term and will include both formulating and manufacturing beverage products using proprietary infusion technologies provided by Molecule or Hill Street, pursuant to the JMP, once the Lucknow facility is licensed by Health Canada under the Cannabis Act.

For the fiscal year ended June 30, 2020, the Company reports an increase in revenues of 7% versus the prior year. This increase can be attributed to drives by the Company to increase brand awareness of its products, increased distribution and availability of its alcohol-free brands. The Company continues to monitor sell through to determine consumer preferences for alcohol free products in order to better inform product selection of its future cannabis-infused products, and analyze industry trends of both alcohol free and cannabis 2.0 products. With COVID-19 having a profound effect on both business activities and consumer behaviour, the Company's revenues from alcohol free products resulted in slower than anticipated growth. In addition, in late Q4 the Company secured an important group of listings with Metro, the largest retailer in Quebec, representing over 30% of Quebec grocery sales. The Company hopes to use this initial relationship with Metro to expand nationally, which could increase Hill Street product availability in grocery stores nationally in Canada from approximately 65% to over 75%.

In addition, as a result of the COVID-19 pandemic, the Company's has seen a dramatic uptick in revenues from ecommerce, especially in sales to the US market. Ecommerce revenues increased 242% during the fourth quarter of the fiscal year. The Company plans on leveraging this new shift in consumer buying behaviour from bricks and mortar to ecommerce by opening additional sales channels through US digital retailers such as Amazon.com and NABeverages.com, in advance of launching its products formally in US retailers, and securing partnerships with major US beverage distributors.

Social media activity and consumer sentiment towards the Company's brands has trended higher with increased positive reviews and mentions from a number of key social media influencers. While the online segment remains a small fraction of the Company's sales volume, it is a much higher margin business segment when consumers order a case of six bottles of wine or more. Both distribution and retail partners costs are eliminated from the transaction, being replaced by the cost of home delivery services and fulfillment centres. Average daily net dollar sales increased 47.3% from July 2019 to June 2020 and sales to the US market continue to show great promise, as consumer awareness and demand for high quality alternatives to alcohol increases. Subsequent to the end of the fiscal year, the Company participated in a major social media virtual party and sampling promotion, organized by For All Drinks, a company focused on driving demand for adult alternatives to alcohol. Over 1500 participants from all aspects of the industry, including restaurant and bar owners, mixologists, and social media influencers attended a virtual launch. As a result of this initiative and others, the Company expects to see continued demand and growth from the US ecommerce market for its products.

INNOVATIVE PRODUCTS AND ADDRESSABLE MARKETS

Product Innovation

Hill Street's largest retail customer has indicated that the Company has a long reputation for innovation and providing category leadership. The expanded interest in this category by consumers has driven the major retailers to look to expand their offerings. Hill Street's considers itself well positioned to accommodate this expansion, and in its annual business review meetings with the retailers, Hill Street was urged to fuel sector innovation and growth. Plans for 2021 include addressing this interest via monitoring trends, consumer buying behaviours and share of wallet exercises to determine the best path to meeting these expectations.

In the cannabis-infused market, Hill Street continued to progress the plans with securing the proper manufacturing environment for edibles and other 2.0 offerings. By keeping closely abreast of industry announcements, monitoring competitive introductions and harvesting data, Hill Street is well-positioned to bring a suite of innovations to the cannabis market as licensing permits.

Addressable Market

Given the changing market conditions owing to the COVID-19 realities, the Direct-to-Consumer (D2C) model gained increasing importance in the distribution model. By offering all of the products in a variety of buying formats online, Hill Street was able to assess which "hot buttons" activated a higher dollar value cart. This in turn allowed the Company to analyze consumer segmentation to understand the buying demographics of its consumers. Utilizing this information, the Company was able to formulate a strategy that it hopes improve reach, cart size and frequency rates. Armed with this knowledge, the Company believes it is now positioned well to unlock the ecommerce opportunity in a more meaningful way in upcoming quarters.

MARKETING

As reported in late January 2020, the Company anticipated a sales decline for the third quarter, and a decision was taken to focus marketing efforts on building the Company's online presence, at the expense of more traditional marketing activities. The objective was to drive more organic social media interactions, steward influencers and to facilitate genuine customer reviews.

Additionally, a few key US alcohol-free partners were established, complete with a back-end support to enable seamless ordering and fulfillment of orders. This backend support included a complete strategic sales strategy that includes a broker model for sales into the U.S. Owing to the size and the complexity of the US market, considerable time and thought had to be devoted to ensuring a smooth roll out of this element. Final touches are being made to this new opportunity and it is anticipated that this platform will be completed in the near-term.

New labelling for our existing lineup of products will have a flash call-out to our philanthropic activities. As this is viewed favorably by our customers, the decision was taken to incorporate this into new label productions. These should begin to appear on-pack in the FY 2021- Q2 timeframe in a slow roll out as new inventories are secured.

SOCIAL RESPONSIBILITY

Hill Street and its wholly owned subsidiary company, Hill Avenue Cannabis, remains committed to discovering ways to mitigate excess packaging, reduce overall waste and to find solutions that align with its mission to make an impactful difference in the lives of its customers. As the plans for the introduction for the suite of Cannabis 2.0 products evolve, deep research into the various packaging methods to deliver these in a manner that encourages environmental responsibility continues. The Company also continues to reinforce our concept of a distributed team which allows each team member to function from their remote locations and limit face to face meetings to respond to the pandemic safety measures as well as commit to reducing our carbon footprint in as many ways as possible.

The Company continues to remain steadfast in donations to charitable causes affected by alcohol. Hill Street has now surpassed the $2 Million mark in historical donations, which is viewed very favorably by our customers. When a small sample was surveyed, they indicated that their buying preference was at least in part influenced by this important contribution. As such, as mentioned in the marketing commentary, future labels will reflect this position more prominently to encourage on-shelf purchasing decisions.

SELECTED ANNUAL INFORMATION

The following table summarizes certain financial information of the Company for the years ended June 30, 2018, 2019 and 2020.

RESULTS OF OPERATIONS

The following table summarizes certain financial information of the Company for the twelve months ended June 30, 2020, June 30, 2019 and June 30, 2018. Gross revenues for the year ended June 30, 2020 increased by 7% compared to the year ended June 30, 2019.

Results for the Year Ended	June 30, 2020	June 30, 2019	June 30, 2018
Gross Revenue	$2,613,923	$2,432,094	$1,511,311
Chargebacks and listing fees	-$883,068	-$1,151,894	-$840,429
Net Revenue	$1,730,855	$1,280,200	$670,882
Direct Costs	-$1,004,806	-$848,373	-$584,500
Gross profit	**$726,049**	**$431,827**	**$86,382**
Ordinary Operating Expenses	**$2,453,642**	**$3,430,203**	**$2,039,727**
One-time Expenses	**$1,242,075**	**$1,136,338**	**$148,220**
Non-Cash Expenses	**$676,940**	**$875,666**	**$895**
Loss before other Income (Expense)	**-$3,646,608**	**-$5,010,380**	**-$2,188,842**
Other income (Expenses)			
Foreign exchange (loss) gain	-$7,975	-$17,240	-$709
Loss on legal settlement			-$215,930
Write-off of inventory	-$80,445	-$7,298	-$242,399
Write-off of equipment			-6,936
Write-off of intangibles	-$8,000		
Charges relating to public company listing		-$918,345	
Gain On favourable interest rate	$17,939		
Gain on Settlement of Liability	$43,217		
Other Income	$194	$9,411	$1,830
Income (Loss) and comprehensive Income (loss) for the period	**-$3,861,679**	**-$5,943,852**	**-$2,652,986**
Basic and diluted income (loss) per common share	**-$0.04**	**-$0.07**	**-$0.07**
Weighted average number of common shares outstanding	**104,401,665**	**85,543,433**	**40,229,986**

REVENUES

During the twelve months ended June 30, 2020, gross revenues were $2,613,923 compared to $2,432,094 for the same period in 2019, representing an increase of 7%. The increase was driven by improved run rates at retail as consumers become more aware of the brand and its benefits

Net revenues for the twelve months ended June 30, 2020 were $1,730,855 compared to $1,280,200 in the twelve months ended June 30, 2019, representing an increase of 35% driven by lower listing fees.

For the twelve months ended June 30, 2020, chargebacks and listing fees represented 34% of gross revenues compared to 47% for the twelve months ended June 30, 2019. Chargebacks are fees charged by retailers and distributors for program money and discounts. The decrease was driven by listing fees for the twelve months ended June 30, 2020. Listing fees were $48,000, for the twelve months ended June 30, 2020 and $446,303 for the twelve months ended June 30, 2019.

COST OF SALES/DIRECT COSTS

Direct costs were $1,004,806 or 38% of gross revenue for the twelve months ended June 30, 2020 and $848,373 or 35% of gross revenue for the twelve months ended June 30, 2019. This is a 3% percentage point increase over the twelve months ended June 30, 2019. The increase is primarily driven by the clearing of near dated product to liquidators at lower sale prices.

OPERATING EXPENSES - ORDINARY

Ordinary operating expenses include selling & marketing expenses, employee expenses, donations, dues & licenses, professional fees, and other general and administrative expenses. For the twelve months ended June 30, 2020, ordinary operating expenses totaled $2,453,642 compared to $3,430,203 for the twelve months ended June 30, 2019. The principal driver of the $976,562 decrease in operating expenses was a reduction in marketing expenses, which decreased by $853,070. Marketing expenses were $258,186 or 10% of gross revenue for the twelve months ended June 30, 2020 and $1,222,155 or 50% of gross revenue for the twelve months ended June 30, 2019.

OPERATING EXPENSES – ONE TIME

In addition to ordinary operating expenses, the Company incurred a number of one-time expenses. For the twelve months ended June 30, 2020, one-time expenses totaled $1,242,075 relating to M&A, severance payments to former executives, investor relations, cannabis investment, and finder's fees. For the twelve months ended June 30, 2019 one-time expenses totaled $1,136,338 relating to M&A, investor relations, and cannabis investment

OPERATING EXPENSES - NON-CASH

For the twelve months ended June 30, 2020 the Company incurred non-cash expenses totaled $676,940, these include expenses related to the severance, stock options, accretion, depreciation and the expense of warrants issued in exchange for marketing services. For the twelve months ended June 30, 2019 the Company incurred non-cash expenses of $875,666 related to depreciation and stock options.

OTHER EXPENSES

For the twelve months ended June 30, 2020, the Company incurred other expenses totaling $35,070. This included $80,445 for inventory write off which was offset largely by the gain on settlement of a severance liability of $43,217.

For the twelve months ended June 30, 2019, the Company incurred other expenses totaling $933,472. This included: $918,345 for non-cash charges related to Public Company Listing charges. These are expenses related to shares issued in relation to the completion of the Company's Reverse Take Over (RTO) qualifying transaction completed July 24, 2018. The Inventory write off was $7,298 for the twelve months ended June 30, 2019, this was driven by product written off due to an error in nutritional product labelling and offset by replacement product received. For the twelve months ended June 30, 2019 the Company received $9,411 in interest income.

NET EARNINGS

The Company recorded a net loss of $3,681,679 for the year ended June 30, 2020 driven by expenses relating to professional fees for M&A and employee expenses, compared to a loss of $5,943,852 in the twelve months ended June 30, 2019. The improvement in net loss was primarily driven by the one time non cash expense of $918,345 for the public company listing for twelve months ended June 30, 2019 and a year over year decrease in marketing expenses of $853,070.

The basic and diluted loss per share for the twelve months ended June 30, 2020 was $0.04 per share. The basic and diluted loss per share for the twelve months ended June 30, 2019 was also $0.07 per share.

SELECTED QUARTERLY INFORMATION

The following table summarizes certain financial information of the Company for the quarters indicated below:

	June 30, 2020	Mar 31, 2020	Dec 31, 2019	Sep 30, 2019	June 30, 2019	Mar 31, 2019	Dec 31, 2018	Sep 30, 2018
Gross Revenue	$623,450	$502,997	$973,710	$513,766	$506,721	$603,854	$527,652	$793,867
Net Revenue	$323,604	$388,536	$689,276	$329,439	$55,100	$428,355	$395,356	$511,589
Direct Costs	$231,176	$226,366	$395,228	$152,036	$164,193	$219,736	$169,569	$294,875
Gross Profit	$92,428	$162,710	$294,048	$177,403	$219,293	$208,619	$225,787	$216,714
Net Loss (-gain)	$456,685	$796,425	$882,658	$1,509,913	-$6,711,371	$1,074,283	$1,443,020	$2,134,396
Total Assets	$2,016,673	$1,594,737	$2,225,062	$1,908,157	$3,004,909	$2, 216,288	$2,997,226	$4,506,261
Total Liabilities	$1,831,278	$1,242,007	$1,198,761	$882,662	$627,141	$829,799	$743,463	$1,069,283
Shareholder Equity	$185,395	$352,730	$1,026,301	$1,025,495	$2,377,768	$1,386,489	$2,253,763	$3,436,978

LIQUIDITY AND CAPITAL RESOURCES

FINANCIAL POSITION

The Company's principal capital needs are for operating expenses related to employee and marketing expenses. Additional investments are being made to support the cannabis infused beverages market, including the build of the cannabis. Since its formation, the Company has financed its additional cash requirements through revenues generated from operations, issuance of securities and borrowing from shareholders and other lenders.

The Company has positive working capital and will continue to focus on cost management and revenue growth. However, it is likely the Company will need to raise capital through debt or equity financings in the near future.

WORKING CAPITAL

Working capital represents current assets less current liabilities. As of June 30, 2020, the Company had a working capital of $571,611 compared to a working capital of $1,880,164 for the twelve months and ended June 30, 2019.

CASH FLOWS

During the twelve months ended June 30, 2020, Hill Street had negative cash flows from operations of $1,930,439 compared to negative cash flow of $5,367,269 during the twelve months ended June 30, 2019. The amount of cash (used) in investing activities in the twelve months ended June 30, 2020 was $9,497 compared to $243,578 in the twelve months ended June 30, 2019. The amount of cash provided by financing activities in during the twelve months ended June 30, 2020 was $1,571,755 compared to $4,568,413 in the twelve months ended June 30, 2019.

CONTRACTUAL OBLIGATIONS

A summary of the Company's contractual obligations for future periods is as follows:

	Payments due by Period					
Contractual Obligations	**FY2021**	**FY2022**	**FY2023**	**FY2024**	**FY2025**	**Total**
Contractual Royalty Obligations	$77,000	$77,000	$77,000	$77,000	$77,000	$385,000
Operating Leases & TMI	$30,165	$30,656	$20,656	$0	$0	$81,477
Purchase Obligations	$130,667	$66,750	$0	$0	$0	$197,417
Total	$237,832	$174,406	$97,656	$77,000	$77,000	$663,893

SHARE CAPITAL

The Company is authorized to issue an unlimited number of Common Shares of which 112,060,380 Common Shares are issued and outstanding as of the date hereof.

CAPITAL RESOURCES

As of June 30, 2020, the Company did not have commitments for capital expenditures.

OFF BALANCE SHEET ARRANGEMENTS

Hill Street does not have any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on the financial performance or financial condition of the Company.

TRANSACTIONS WITH RELATED PARTIES

The Company considers its executive officers and directors to be key management personnel. The Company incurred the following amounts to related parties during the respective periods for key management personnel compensation:

	$	**$**
During year ended June 30,	**2020**	**2019**
Total salaries, benefits and management fees	856,646	749,892
Stock-based compensation	283,735	808,264
Total salaries and other short-term benefits	1,140,381	1,558,156

Included in accounts payable as at June 30, 2020 is $337,682 (June 30, 2019: $86,438) payable to Directors and Officers of the Company for management wages. The amount is non-interest bearing and unsecured.

On December 23, 2019, management and board members participated in a non-brokered private placement financing of units ("**Units**") for gross proceeds of $250,000 at a price of $0.06 per Unit. Each

Unit consists of one common share and one warrant, with each warrant entitling the holder thereof to purchase one common share in the capital of the Company at a price of $0.13 per share for a period of two years from closing, subject to acceleration.

As at June 30, 2020, the company had $770,485 of related party convertible debt related to a private placement financing on May 4, 2020 for gross proceeds of $1,022,500 at a price of $1.00 per Unit. Each Unit is comprised of $1.00 principal amount of secured convertible debentures and 20 common share purchase.

FOURTH QUARTER

The following table summarizes certain financial information of the Company for the three months ended June 30, 2019 and June 30, 2020.

Results for the Quarter ended	June 30, 2020	June 30, 2019
Gross Revenue	$623,450	$506,721
Chargebacks and listing fees	-$299,846	-$561,821
Net Revenue	$323,604	-$55,100
Direct Costs	-$231,176	-$164,193
Gross profit	**$92,428**	**-$219,293**
Ordinary Operating Expenses	**$395,349**	**$668,452**
One-time Expenses	**$107,965**	**$475,195**
Non Cash Expenses	**$41,859**	**$175,609**
Loss before other Income (Expense)	**-$452,745**	**-$1,319,256**
Other income (Expenses)		
Foreign exchange (loss) gain	-$8,310	-$2,690
Loss on legal settlement	$0	$0
Write-off of inventory	-$56,979	$54,771
Write-off of equipment	$0	$0
Charges relating to public company listing	$0	$8,003,524
Gain on favourable interest rate	$17,939	$0
Other Income	$194	-$24,978
Income (Loss) and comprehensive Income (loss) for the period	**-$456,685**	**$6,711,371**

REVENUES

During the three months ended June 30, 2020, gross revenues were $623,450 compared to $506,721 for the three months ended June 30, 2019, representing an increase of 23% driven by timing of distributor sales from the three months ended April 30, 2020.

Net revenues for the three months ended June 30, 2020 were $323,604 compared to -$55,100 in the same period year ago. Net revenues are calculated by deducting from gross revenues the costs of chargebacks and listing fees. Chargebacks are fees charged by retailers and distributors for program money and discounts. Listing fees represent the fees charged by retailers to have product available for sale in such retail establishments. The decrease in net revenues was driven by the change in accounting for store listing fees. For the three months ended June 30, 2019 listing fees of $431,467 for the full year were charged to the P&L compared to $12,500 for listing fees for the three months ended June 30, 2020. For the three months ended June 30, 2020, chargebacks and listing fees represented 48% of gross revenues compared to 111% for the three months ended June 30, 2019.

COST OF SALES/DIRECT COSTS

Direct costs were $231,176 or 37% of gross revenue for the three months ended June 30, 2020 compared to $164,193 or 32% for the three months ended June 30, 2019. The year over year increase of 5 percentage points is driven by the clearance of near dated product to liquidators.

OPERATING EXPENSES - ORDINARY

Operating expenses include selling & marketing expenses, employee expenses, donations, dues & licenses, professional fees, and other general and administrative expenses. For the three months ended June 30, 2020, operating expenses totaled $395,349 compared to $668,452 for the three months ended June 30, 2019 representing a decline of $273,103 driven by a decline in marketing expenses.

OPERATING EXPENSES - ONE TIME

In addition to ordinary operating expenses, the Company incurred a number of one-time expenses. For the three months ended June 30, 2020, one-time expenses totaled $107,965 relating to cannabis investment, M&A, investor relations, warrants expense for services, severance and legal fees. For the three months ended June 30, 2019, one-time expenses totaled $475,195 relating to, M&A and cannabis investment.

OPERATING EXPENSES - NON-CASH

For the three months ended June 30, 2020 the Company incurred non-cash expenses totaling $41,859 these include the expense related to depreciation, accretion, warrant expense for services and severance expense. The expenses were offset by a year-end adjusting entry for stock options to reflect canceled options. For the three months ended June 30, 2019 the Company incurred non-cash expenses totaling $175,609 these include the expense related to depreciation and stock options.

OTHER EXPENSES

For the three months ended June 30, 2020, the Company had other expense totaling $21,878. The overall expense was driven by the inventory write-off of $56,979 which was offset largely by other income from the gain on settlement of liability of $43,217. For the three months ended June 30, 2019, the Company had other income totaling $8,030,627. This income is driven by the change in reporting the non-cash cost of listing the Company on the stock exchange. The credit of $54,771 in the three months ended June 30, 2019 was driven by replacement product for a nutritional labelling error that was received in this quarter.

NET EARNINGS

The Company recorded a net loss of $456,685 the three months ended June 30, 2020, compared to a net income of $6,711,371 for the three months ended June 30, 2019 which was driven by the change in reporting the non-cash cost of listing the Company on the stock exchange.

LEGAL PROCEEDINGS

There are no legal proceedings material to Hill Street to which Hill Street is a party to or of which any of its property is the subject matter, and there are no such proceedings known to Hill Street to be contemplated.

CRITICAL ACCOUNTING ESTIMATES

The determination of income tax is inherently complex and requires making certain estimates and assumptions about future events. While income tax filings are subject to audits and reassessments, the Company has adequately provided for all income tax obligations. However, changes in facts and circumstances as a result of income tax audits, reassessments, jurisprudence and any new legislation may result in an increase or decrease in the provision for income taxes.

Calculation of the net book value of machinery and equipment requires Management to make estimates of the useful economic life of the assets, residual value at the end of the asset's useful economic life, method of depreciation and whether impairment in value has occurred. Residual values of the assets, estimated useful lives and depreciation methodology are reviewed annually with prospective application of any changes, if deemed appropriate. Changes to estimates could be caused by a variety of factors, including changes to the physical life of the assets. A change in any of the estimates would result in a change in the amount of depreciation and, as a result, a charge to net income recorded in the period in which the change occurs, with a similar change in the carrying value of the asset on the balance sheet.

The amortization of the Company's intangible assets involves estimates of their useful lives. Such estimates may change as more experience is obtained or as general market conditions change, thereby impacting the value of the Company's intangible assets.

When valuing options, management uses judgment to determine the inputs to the Black-Scholes option pricing model including the expected plan lives, underlying share price volatility and forfeiture rates. Volatility is estimated by considering peer companies historic share price volatility over similar periods to the expected life of the awards under consideration. Changes in these assumptions will impact the calculation of fair value and the amount of compensation expense recognized in the consolidated statements of loss and comprehensive loss.

When valuing warrants, similar to other stock-based compensation, management uses judgment to determine the inputs to the Black-Scholes option pricing model including the expected life, and underlying share price volatility. Volatility is estimated by considering peer companies historic share price volatility over similar periods to the expected life of the warrants. Changes in these assumptions will impact the calculation of fair value and the value attributed to the warrants.

When the Company enters into leases as a lessee and where the interest rate implicit in a lease cannot be readily determined, the Company determines its incremental borrowing rate in order to measure its lease liability. The incremental borrowing rate is the rate of interest that a lessee would have to pay to borrow over a similar term, and with similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. In estimating its incremental borrowing rate, the Company considers the term of the lease, the nature of the leased asset, and its level of indebtedness with reference to market risk-free interest rates.

When determining the discount rate used to estimate the fair value of the debt component of the convertible debenture and the fair value of the CEBA loan, the Company considers market conditions and other internal and external factors. The Company estimates its credit rating and benchmarks the discount rate to certain fixed income indices.

In some contracts, the Company transfers control of a product to distributors and grants the distributors the right to return the product for a full or partial refund in the scenario that products are to expire in the hands of the distributor. To account for the transfer of products with a right of return, the Company recognises revenue for the transferred products in the amount of consideration to which the Company expects to be entitled to (therefore, revenue would not be recognised for the products expected to be returned). The expected consideration to be received is determined based on a combination of historical, current and forecasted information available to the entity at the end of each reporting period.