

Aequus Pharmaceuticals Inc.

Consolidated Financial Statements

For the years ended December 31, 2016 and 2015



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Independent Auditor's Report

To the Shareholders of Aequus Pharmaceuticals Inc.

We have audited the accompanying consolidated financial statements of Aequus Pharmaceuticals Inc. and its subsidiary, which comprise the consolidated statements of financial position as at December 31, 2016 and December 31, 2015, and the consolidated statements of loss and comprehensive loss, changes in shareholders' equity, and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Aequus Pharmaceuticals Inc. and its subsidiary as at December 31, 2016 and December 31, 2015 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

"Crowe MacKay LLP"

**Chartered Professional Accountants
Vancouver, British Columbia
May 1, 2017**

Aequus Pharmaceuticals Inc.
Consolidated Statements of Financial Position
(Expressed in Canadian dollars)

	Note	December 31, 2016 \$	December 31, 2015 \$
ASSETS			
Current			
Cash and cash equivalents		473,242	1,163,812
Amounts receivable		190,114	94,309
Prepaid expenses and deposit		140,197	75,256
Deferred financing costs	8[b][iii]	—	51,563
		803,553	1,384,940
Property and equipment	5	45,958	6,535
Intangible assets	6	1,072,502	763,151
Deferred share-based payments	7	88,082	275,112
		1,206,542	1,044,798
Total assets		2,010,095	2,429,738
LIABILITIES AND SHAREHOLDERS' EQUITY			
LIABILITIES			
Current			
Accounts payable and accrued liabilities	9	744,411	1,145,077
Total liabilities		744,411	1,145,077
SHAREHOLDERS' EQUITY			
Share capital	8	12,606,882	7,582,240
Common share subscriptions received	8[b][iii]	—	719,575
Contributed surplus		2,522,737	2,034,726
Deficit		(13,863,935)	(9,051,880)
Total shareholders' equity		1,265,864	1,284,661
Total liabilities and shareholders' equity		2,010,095	2,429,738

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

Nature of operations and Going Concern [Note 1]
Commitments and Contingencies [Note 10]
Subsequent Events [Note 17]

These consolidated financial statements were approved for issue by the Board of Directors on May 1, 2017 and signed on its behalf by:

/s/ Douglas G. Janzen
Director

/s/ Chris Clark
Director

Aequus Pharmaceuticals Inc.
Consolidated Statements of Loss and Comprehensive Loss
(Expressed in Canadian dollars)

	Note	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Revenue		701,633	—
Expenses			
Research and development	12[a]	1,127,780	2,144,488
Sales and marketing	12[b]	1,767,364	555,177
General administration	12[c]	2,670,072	2,355,485
		5,565,216	5,055,150
Loss before other income		(4,863,583)	(5,055,150)
Other income (loss)			
Interest income		3,139	—
Government grant		—	84,141
Income tax credit		50,721	—
Foreign exchange loss		(2,332)	(40,396)
		51,528	43,745
Net loss and comprehensive loss		(4,812,055)	(5,011,405)
Basic and diluted loss per common share		(0.10)	(0.15)
Weighted average number of common shares outstanding		47,453,906	34,395,872

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

Aequus Pharmaceuticals Inc.
Consolidated Statements of Changes in Shareholders' Equity
(Expressed in Canadian dollars)

	Common Shares		Special Warrants		Subscriptions Received	Contributed Surplus	Deficit	Total
	Number	\$	Number	\$	\$	\$	\$	\$
Balance, December 31, 2014	25,975,347	2,029,127	8,044,301	3,599,524	-	1,333,221	(4,040,475)	2,921,397
Deemed exercise of special warrants <i>[note 8[b][i]]</i>	7,618,780	3,599,524	(8,044,301)	(3,599,524)	-	-	-	-
Issued for cash pursuant to exercise of options	125,000	81,273	-	-	-	(37,524)	-	43,749
Issued for cash pursuant to a public financing <i>[note 8[b][ii]]</i>	2,475,000	870,196	-	-	-	34,439	-	904,635
Issued for acquisition of intangible asset and services <i>[notes 6[a] and 7]</i>	3,360,000	1,002,120	-	-	-	-	-	1,002,120
Subscriptions received	-	-	-	-	719,575	-	-	719,575
Share-based payments <i>[note 8 [e]]</i>	-	-	-	-	-	704,590	-	704,590
Net loss for the year	-	-	-	-	-	-	(5,011,405)	(5,011,405)
Balance, December 31, 2015	39,554,127	7,582,240	-	-	719,575	2,034,726	(9,051,880)	1,284,661
Issued for cash pursuant to a non-brokered private placement and a non-brokered public offering <i>[note 8[b][iii]]</i>	5,297,422	2,515,177	-	-	(719,575)	-	-	1,795,602
Issued for cash pursuant to a public financing <i>[note 8[b][iv]]</i>	9,146,400	2,458,186	-	-	-	-	-	2,458,186
Shares issued for services <i>[note 8[b][v]]</i>	153,072	51,279	-	-	-	-	-	51,279
Share-based payments <i>[note 8 [e]]</i>	-	-	-	-	-	488,011	-	488,011
Net loss for the year	-	-	-	-	-	-	(4,812,055)	(4,812,055)
Balance, December 31, 2016	54,151,021	12,606,882	-	-	-	2,522,737	(13,863,935)	1,265,684

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

Aequus Pharmaceuticals Inc.
Consolidated Statements of Cash Flows
(Expressed in Canadian dollars)

	Note	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
OPERATING ACTIVITIES			
Net loss for the year		(4,812,055)	(5,011,405)
Add items not affecting cash:			
Depreciation of property and equipment	5	2,812	1,984
Loss from sale of fixed assets		—	920
Depreciation of intangible assets	6	169,589	84,794
Share-based payments	7 & 8[e]	675,041	820,918
Shares issued for services		51,279	—
		(3,913,334)	(4,102,789)
Changes in non-cash working capital items relating to operations:			
Amounts receivable		(95,805)	(18,969)
Prepaid expenses and deposit		(64,941)	(66,006)
Accounts payable and accrued liabilities		(391,338)	349,007
Cash used in operating activities		(4,465,418)	(3,838,757)
INVESTING ACTIVITIES			
Purchase of property and equipment	5	—	(5,211)
Proceeds from sale of property and equipment	5	—	1,015
Purchase of intangible assets	6	(478,940)	(237,265)
Cash used in investing activities		(478,940)	(241,461)
FINANCING ACTIVITIES			
Issuance of common shares, net of issuance costs	8[b]	4,253,788	948,384
Subscriptions received	8[b]	—	719,575
Cash provided by financing activities		4,253,788	1,667,959
Decrease in cash and cash equivalents		(690,570)	(2,412,259)
Cash and cash equivalents, beginning of the year		1,163,812	3,576,071
Cash and cash equivalents, end of the year		473,242	1,163,812

Supplemental disclosure with respect to cash flow (Note 16)

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

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

Aequus Pharmaceuticals Inc. (the “**Company**”) was incorporated under the *Business Corporations Act* (British Columbia) on January 3, 2013. The Company is a specialty pharmaceutical company focused on developing and commercializing high quality and differentiated products. The Company’s registered and records office is located at Suite 2600, 595 Burrard Street, Vancouver, British Columbia, Canada, V7X 1L3 and its head office is located at Suite 2820, 200 Granville Street, Vancouver, British Columbia, Canada, V6C 1S4.

These consolidated financial statements (the “**Financial Statements**”) have been prepared under the assumption that the Company will continue as a going concern. The going concern basis of presentation assumes that the Company will be able to meet its obligations and continue its operations for the foreseeable future and be able to realize its assets and discharge its liabilities and commitments in the normal course of business. Realization values may be substantially different from the carrying values as shown, and these Financial Statements do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should the Company be unable to continue as a going concern.

The Company has incurred losses and negative operating cash flows since its inception. As of December 31, 2016, the Company has accumulated a deficit of \$13,863,935 (December 31, 2015 - \$9,051,880) and working capital of \$59,142 (December 31, 2015 - \$239,863). Subsequent to the year end, the Company completed a financing for gross proceeds of \$5,175,000 [note 17[b]].

The Company’s ability to meet its long term business strategy depends on its ability to obtain additional equity financing and to generate operational cash flow from the acquired business of TeOra Health Ltd. (“**TeOra**”). On July 28, 2015, the Company completed its acquisition of TeOra, a privately held Canadian specialty pharmaceutical company (the “**TeOra Acquisition**”) [note 6[a]]. The TeOra Acquisition provided the Company with sales and marketing capabilities, and an exclusive right to promote and market a branded generic ophthalmology product within Canada. On September 30, 2015, the Company further expanded this exclusive promotional right to include a transplant product called Tacrolimus IR. The Company will receive revenues based on agreed upon percentages of net sales. The Company started generating service revenue from Tacrolimus IR in the first quarter of 2016 and from ^{PR} Vistitan™ sales in the second quarter of 2016. The Company’s longer term business strategy for generating cash flow is to successfully develop its later stage product pipeline through marketing agreements or product commercialization profits and engaging in development and commercial partnerships for one or more of its development pipeline products which would generate licensing revenues for the Company from territories outside of Canada.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

2. BASIS OF PRESENTATION

[a] Statement of compliance

These Financial Statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”) effective for the year ended December 31, 2016.

These Financial Statements were approved by the Company’s Board of Directors on May 1, 2017.

[b] Basis of measurement

These Financial Statements have been prepared on a historical cost basis, except for the revaluation of certain financial assets and financial liabilities to fair value.

[c] Functional and foreign currency

These Financial Statements are presented in Canadian dollars, which is the Company’s functional currency. Foreign currency transactions are translated into Canadian dollars using the exchange rates at the date of the transactions. Foreign exchange gains or losses resulting from the settlement of transactions and from the translation at year-end rate of monetary assets and liabilities denominated in foreign currencies are recognized in net income or loss.

[d] Significant accounting estimates and judgments

The preparation of these Financial Statements requires management to make certain estimates, judgments and assumptions that affect the reported amounts of assets and liabilities at the date of the Financial Statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. These Financial Statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the Financial Statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. These estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Company reviews its estimates and underlying assumptions on an ongoing basis.

Critical Judgments

The following are critical judgments that management has made in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the Financial Statements:

- i. Research costs are recognized as an expense when incurred but development costs may be capitalized as intangible assets if certain conditions are met as described in IAS 38, *Intangible Assets*. Management has determined that development costs do not meet the conditions for capitalization under IAS 38 and all research and development costs have been expensed.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

Critical Judgments (continued)

- ii. Management is required to assess the functional currency of the Company. In concluding that the Canadian dollar is the functional currency of the Company, management considered the currency that mainly influences the operating expenditures in the jurisdiction in which the Company operates.
- iii. The determination of categories of financial assets and financial liabilities has been identified as an accounting policy which involves judgments or assessments made by management.
- iv. Management is required to determine whether or not the going concern assumption is appropriate for the Company at the end of each reporting period. Considerations taken into account include available information about the future including the availability of financing and revenue projection, as well as current working capital balance and future commitments of the Company.

Estimation Uncertainty

The following are key assumptions concerning the future and other key sources of estimation uncertainty that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year:

- i. Provisions for income taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxation authorities. Where the final outcome of these tax-related matters is different from the amounts that were originally recorded, such differences will affect the tax provisions in the period in which such determination is made.
- ii. The fair value of accrued liabilities at the time of initial recognition is made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors.
- iii. Intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses. Amortization is calculated using management's best estimate of the useful life of the intangible assets. Determination of impairment loss is subject to management's assessment if there is any indication of a possible write-down; and if so, the determination of recoverable value based on discounted future cash flows of the intangible assets. The carrying amount of intangible assets does not necessarily reflect present or future value and the ultimate amount recoverable will be dependent upon the successful commercialization of products based on these underlying technologies.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

2. BASIS OF PRESENTATION (CONTINUED)

[d] Significant accounting estimates and judgments (continued)

iv. Revenues are recognized based on a calculation of estimated profits using actual third party sales figures. Changes in estimates of revenues are recognized prospectively as adjustments to revenue and amounts receivable. When an uncertainty arises about the collectability of an amount already included in revenue, the uncollectible amount, or the amount in respect of which recovery has ceased to be probable, is recognized as an expense. At each reporting period the entity reviews and, when necessary, revises the estimates of revenue as services are performed.

3. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied in the preparation of these Financial Statements are set out below which have been applied to all the years presented, unless otherwise stated.

[a] Consolidation

These Financial Statements include the accounts of the Company's wholly-owned subsidiary: TeOra Health Ltd. incorporated under the Business Corporations Act (Ontario). All significant intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

[b] Financial instruments

Financial assets and liabilities are initially recognized at fair value when the Company becomes party to the contracts that give rise to them. Subsequent measurement depends on whether the financial instrument is classified as fair value through profit and loss ("FVTPL"), available-for-sale, held-to-maturity, loans and receivables, or other liabilities. Financial instruments classified as (i) FVTPL are measured at fair value with unrealized gains and losses recognized in net income or loss; (ii) available-for-sale are measured at fair value with unrealized gains and losses recognized in other comprehensive income or loss; and (iii) held-to-maturity, loans and receivables, and other liabilities are measured at amortized cost. Transaction costs in respect of FVTPL financial instruments are recognized in net income or loss at the transaction date whereas transaction costs in respect of other financial instruments are included in the initial fair value measurement of the financial instruments.

The Company has designated its cash and cash equivalents as FVTPL, which is measured at fair value. Amounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities, which are measured at amortized cost.

[c] Cash and cash equivalents

Cash and cash equivalents consists of cash, term deposits and guaranteed investment certificates that are readily convertible to known amounts of cash within 90 days of purchase.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[d] Property and equipment

Property and equipment are recorded at cost less accumulated depreciation and accumulated impairment losses. Initial acquisition cost is based on the fair value of the consideration paid or payable and includes expenditures that are directly attributable to the acquisition of the asset. Where an item of property and equipment is comprised of major components with different useful lives, each component is accounted and depreciated for as a separate item.

Depreciation is provided using the straight-line method over the estimated useful lives of the property and equipment. One-half of the depreciation is recognized in the year of acquisition. Office furniture and equipment is amortized over 5 years. Leasehold improvement is amortized over the expected term of the lease. Website cost is amortized over 3 years.

[e] Intangible assets

Intangible assets consist of contractual rights to commercialize, market and promote certain pharmaceutical products. The cost of intangible assets acquired in a business combination is its fair value at the date of acquisition. Following its initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses.

Intangible assets are amortized on a straight-line basis over the useful economic life of five years and assessed for indicators of impairment at the end of each reporting period. The amortization period is reviewed at least annually.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[f] Impairment of assets

Financial assets and non-financial assets of the Company are reviewed at the end of each reporting period or when facts and circumstances suggest their carrying values have been impaired. The Company considers assets to be impaired if the carrying values exceed the recoverable amount, being the higher of the value in use and the fair value less costs to sell.

Financial assets include cash and cash equivalents carried at fair value and amounts receivable measured at amortized cost. Amounts receivable consist of primarily of goods and services taxes due from the Government of Canada and revenue from customers for promotional marketing services performed. The Company considers the recoverable amounts of its financial assets to approximate their carrying values.

Non-financial assets consist of property and equipment and intangible assets. In assessing value in use for a non-financial asset, the estimated future cash flows associated with the non-financial asset are discounted to their present value using a risk adjusted pre-tax discount rate. If the recoverable amount is estimated to be less than its carrying amount, the carrying amount is reduced to its recoverable amount with the impairment immediately recognized in net income or loss. Where an impairment subsequently reverses, the carrying amount is increased to the revised estimate, subject to the amount not exceeding the carrying amount that would have been determined had impairment loss not been recognized for the asset in prior periods. Any reversal of impairment is recognized immediately in net income or loss.

[g] Research and development costs

Research costs, including costs for new patents and patent applications, are expensed in the period in which they are incurred. Development costs are expensed in the period in which they are incurred unless certain criteria, including technical feasibility, commercial feasibility, intent and ability to develop and use the technology, are met for deferral and amortization. No development cost has been deferred to date.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[h] Share-based payments

The Company grants stock options to directors, officers and consultants pursuant to a stock option plan described in *note 8[e]*. The Company uses the fair value method to account for all share-based awards granted, modified or settled, and the Black-Scholes option pricing model to determine the fair value of stock options granted. As such, a share-based payment is recorded based on the estimated fair value of options with a corresponding credit to contributed surplus. Any consideration received plus the amounts recognized in contributed surplus will be transferred to share capital on the exercise of stock options. Stock options with graded vesting schedules are accounted for as separate grants with different vesting periods and fair values. Changes to the estimated number of share options that will eventually vest are accounted for prospectively. Options issued to non-employees are valued based on the fair value of the options issued as the fair value of the services provided cannot be measured reliably.

[i] Income taxes

The Company follows the liability method of accounting for income taxes. Under this method, deferred income taxes are recognized for the future income tax consequences attributable to differences between carrying values of assets and liabilities and their respective income tax bases, unused tax losses and other income tax deductions. Deferred income tax assets are recognized for deductible temporary differences, unused tax losses and other income tax deductions to the extent that it is probable the Company will have taxable income against which those deductible temporary differences, unused tax losses and other income tax deductions can be utilized. The Company reassesses the extent to which tax benefits may be realized at the end of each reporting period.

Deferred income tax assets and liabilities are measured using the enacted or substantively enacted tax rates expected to apply when the related tax assets are realized or the liabilities are settled. The measurement of deferred income tax assets and liabilities reflect the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover and settle the carrying amounts of its assets and liabilities, respectively. The effect on deferred income tax assets and liabilities of a change in tax rates is recognized in the period in which the change is substantively enacted.

Current and deferred income tax expense or recovery are recognized in net income or loss except when they arise as a result of items recognized in other comprehensive income or loss, or directly in equity in the current or prior periods, in which case the related current and deferred income taxes are also recognized in other comprehensive income or loss, or in equity, respectively.

[j] Investment tax credit

Investment tax credits are recorded as either a reduction of the cost of applicable assets or credited in net income or loss depending on the nature of the expenditures which gave rise to the credits. Claims for tax credits are recorded upon the Company receiving cash from the Canada Revenue Agency.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[k] Government assistances

Government assistances consist of grants received under the Industrial Research Assistance Program (“**IRAP**”) and refundable scientific research and experimental development tax credits (“**SR&ED**”). Government assistances are recorded in net income or loss upon cash receipt and when reasonable assurance exists that the Company has complied with the terms and conditions of the IRAP program.

[l] Loss per common share

Basic loss per common share is computed using the weighted average number of common shares outstanding during the period. Diluted loss per common share is equivalent to the basic loss per common share as the effects of outstanding warrants and options disclosed in Note 8 are anti-dilutive for all periods presented.

[m] Equity and share capital

Share capital represents the value of shares that have been issued. Transaction costs directly attributable to the issuance of common shares are recognized as a deduction from equity, net of any tax effects. The Company may issue units consisting of common shares and common share purchase warrants. The Company estimates the fair value of the common shares based on their market price on the announcement date. The residual difference, if any, between the unit price and the fair value of each common share represents the fair value attributable to each warrant.

[n] Revenue recognition

The Company earns service revenues based on a proportion of a third party’s net product sales. The Company recognizes service revenues when the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the entity, the stage of completion of the transaction at the end of the reporting period can be measured reliably and the costs incurred for the transaction and the costs to complete the transaction can be measured reliably. Service revenue is recognized based on actual third party sales of products for the reporting period when collectability is certain. Service revenues recognized are estimated based on actual third party sales for the period net of estimated costs multiplied by the contractual proportionate allocation.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

4. RECENT ACCOUNTING PRONOUNCEMENTS

New Standards Recently Adopted

The following is an overview of new accounting standards that the Company adopted effective January 1, 2016:

- **IFRS 7 *Financial Instruments*** - The amendment clarifies the applicability of the amendments to *IFRS 7 Disclosure - Offsetting Financial Assets and Financial Liabilities* to condensed interim financial statements. This amendment is effective for reporting periods beginning on or after January 1, 2016.
- **IAS 34 *Interim Financial Reporting*** - The amendment clarifies the meaning of disclosure of information 'elsewhere in the interim financial report' and requires a cross reference. This amendment is effective for reporting periods beginning on or after January 1, 2016.
- **IAS 38 *Intangible Assets (Amendment)*** - This new standard provides guidance on revaluation methods for intangible assets. The standard is effective for annual periods beginning on or after January 1, 2016.

The adoption of the above standards did not have a material impact on the Financial Statements.

New Standards Not Yet Effective

The following is an overview of new accounting standards that the Company will be required to adopt in future years. The Company does not expect to adopt any of these standards before their effective dates. The Company continues to evaluate the impact of these standards on its Financial Statements.

IAS 7 *Disclosure Initiative (Amendments to IAS 7 Statement of Cash Flows)* - These amendments require that the following changes in liabilities arising from financing activities are disclosed (to the extent necessary): (i) changes from financing cash flows; (ii) changes arising from obtaining or losing control of subsidiaries or other businesses; (iii) the effect of changes in foreign exchange rates; (iv) changes in fair values; and (v) other changes. One way to fulfil the new disclosure requirement is to provide a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities. Finally, the amendments state that changes in liabilities arising from financing activities must be disclosed separately from changes in other assets and liabilities. These amendments are effective for reporting periods beginning on or after January 1, 2017.

- **IFRS 9 *Financial Instruments*** - This standard provides added guidance on the classification and measurement of financial liabilities. The standard is effective for annual periods beginning on or after January 1, 2018.
- **IFRS 15 *Revenue from Contracts with Customers*** - This standard covers principles for reporting about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. IFRS 15 is effective for annual periods beginning or after January 1, 2018.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

4. RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

New Standards Not Yet Effective (continued)

- **IFRS 2 *Classification and Measurement of Share-based Payment Transactions*** – This standard was issued in June 2016. The amendments provide requirements on accounting for the effect of vesting and non-vesting conditions on the measurement of cash settled share-based payments, share-based transactions with a net settlement feature for withholding tax obligations and a modification to the terms and conditions of a share-based payment that changes the classification of the transactions from cash-settled to equity-settled. This standard is effective for reporting periods beginning on or after January 1, 2018.
- **IFRS 16 *Leases*** - This standard was issued in January 2016 and specifies how an IFRS reporter will recognize, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17. This standard is effective for reporting periods beginning on or after January 1, 2019.

5. PROPERTY AND EQUIPMENT

	Office Furniture and Equipment \$	Website Costs \$	Leasehold Improvement \$	Total \$
Office Furniture and Equipment				
Cost:				
Balance, December 31, 2014	7,491	—	—	7,491
Addition	1,000	—	4,211	5,211
Disposition	(2,977)	—	—	(2,977)
Balance, December 31, 2015	5,514	—	4,211	9,725
Addition	—	42,235	—	42,235
Balance, December 31, 2016	5,514	42,235	4,211	51,960
Accumulated depreciation:				
Balance, December 31, 2014	2,248	—	—	2,248
Depreciation	1,002	—	982	1,984
Disposition	(1,042)	—	—	(1,042)
Balance, December 31, 2015	2,208	—	982	3,190
Depreciation	1,128	—	1,684	2,812
Balance, December 31, 2016	3,336	—	2,666	6,002
Net book value:				
As of December 31, 2015	3,306	—	3,229	6,535
As of December 31, 2016	2,178	42,235	1,545	45,958

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

6. INTANGIBLE ASSETS

[a] On July 28, 2015, the Company acquired all issued and outstanding shares of TeOra for its sales and marketing capabilities, and a right to promote and market ^{PR} Vistitan™, an ophthalmology product within Canada. In exchange for these assets and services of TeOra shareholders [Note 7], the Company issued 3,360,000 common shares of the Company valued at \$1,002,120, repaid TeOra's liabilities of \$154,817 in cash and incurred transaction costs of \$82,448 for a total acquisition cost of \$1,239,385. Of the 3,360,000 common shares issued, 420,000 common shares were released to TeOra shareholders upon closing, and the remaining 2,940,000 common shares were held in escrow for release over time for services performed and upon achievement of certain milestones [Note 8[b]].

The Company accounted for this transaction as an acquisition of an asset and services, and allocated \$847,945 and \$391,440 of the acquisition costs to intangible assets and deferred share-based payments [Note 7], respectively. The acquisition cost of intangible assets is amortized over a five-year period using a straight-line method with one half of the amortization recognized in the year of acquisition.

[b] On February 12, 2016, the Company entered into a licensing agreement with Supernus Pharmaceuticals, Inc. for Canadian commercial rights to Topiramate XR and Oxcarbazepine XR, two branded products for the treatment of epilepsy (the "Supernus Agreement"). Pursuant to the terms of the Supernus Agreement, the Company paid an upfront fee of \$478,940 (US\$350,000) and is further obligated to pay additional licensing milestone fees of US\$5.15 million, a 15% royalty fee on sales and a final sales milestone payment as described in Note 10[c]. Amortization of licensing fees will be recognized following the receipt of regulatory approval from Health Canada and upon commencement of commercial activities of the underlying products.

As of December 31, 2016, the net book value of intangible assets are as follows:

	TeOra Assets \$	Supernus Licensing Fee \$	Total \$
Cost:			
Balance, December 31, 2014			
Acquisition cost	847,945	—	847,945
Balance, December 31, 2015	847,945	—	847,945
Initial advance for license	—	478,940	478,940
Balance, December 31, 2016	847,945	478,940	1,326,885
Accumulated amortization:			
Balance, December 31, 2014	—	—	—
Amortization of intangible assets	84,794	—	84,794
Balance, December 31, 2015	84,794	—	84,794
Amortization of intangible assets	169,589	—	169,589
Balance, December 31, 2016	254,383	—	254,383
Net book value:			
As of December 31, 2015	763,151	—	763,151
As of December 31, 2016	593,562	478,940	1,072,502

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

7. DEFERRED SHARE-BASED PAYMENTS

On July 28, 2015, the Company acquired all of the issued and outstanding shares of TeOra for its sales and marketing capabilities, and a right to promote and market ^{PR} Vistitan™, an ophthalmology product within Canada [Note 6[a]]. Share-based payment for services of TeOra shareholders was recognized up front as a deferred asset and is expensed using the graded-vesting approach. During the year ended December 31, 2016, the Company recognized share-based payment expense of \$187,030 (2015 – \$116,328) related to the acquisition of TeOra. As of December 31, 2016, the net book value of the services acquired were as follows:

	Deferred share-based payments
	\$
Cost:	
Balance, December 31, 2014	—
Acquisition cost	391,440
Balance, December 31, 2015 & 2016	391,440
Accumulated amortization:	
Balance, December 31, 2014	—
Amortization of deferred share-based payments	116,328
Balance, December 31, 2015	116,328
Amortization of deferred share-based payments	187,030
Balance, December 31, 2016	303,358
Net book value:	
As of December 31, 2015	275,112
As of December 31, 2016	88,082

8. SHARE CAPITAL

[a] Preferred shares

The authorized share capital of the Company consists of an unlimited number of Class A preferred shares without par value. As of December 31, 2016 and 2015, there were no preferred shares issued and outstanding.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

8. SHARE CAPITAL (CONTINUED)

[b] Common shares

	Number of Shares	Amount \$
Authorized		
Unlimited number of common shares without par value		
Issued and Outstanding		
Balance, December 31, 2014	25,975,347	2,029,127
Issued for deemed exercise of special warrants <i>[note 8 [b][i]]</i>	7,618,780	3,599,524
Issued for cash pursuant to exercise of options	125,000	81,273
Issued for purchase of intangible assets <i>[note 6[a]]</i>	3,360,000	1,002,120
Issued for cash pursuant to a public financing <i>[note 8 [b][ii]]</i>	2,475,000	870,196
Balance, December 31, 2015	39,554,127	7,582,240
Issued for cash pursuant to a non-brokered private placement and a non-brokered public offering <i>[note 8[b][iii]]</i>	5,297,422	2,515,177
Issued for cash pursuant to a public financing <i>[note 8[b][iv]]</i>	9,146,400	2,458,186
Issue for services <i>[note 8[b][v]]</i>	153,072	51,279
Balance, December 31, 2016	54,151,021	12,606,882
	Number of	Percentage of
Held in Escrow Accounts	Shares	Escrowed
		Shares
<i>(i) Pursuant to listing requirements of the TSX Venture Exchange</i>		
Balance, December 31, 2014	—	
Shares subject to escrow in accordance to regulations of the TSX Venture Exchange	20,387,125	100.00%
Release on the listing date of March 17, 2015	(2,038,712)	(10.00%)
Release on September 17, 2015	(3,058,069)	(15.00%)
Balance, December 31, 2015	15,290,344	75.00%
Release on March 17, 2016	(3,058,069)	(15.00%)
Release on September 17, 2016	(3,058,069)	(15.00%)
Balance, December 31, 2016	9,174,206	45.00%
<i>(ii) Pursuant to the terms of the TeOra Acquisition [note 17[c]]</i>		
Balance, December 31, 2014	—	
Shares subject to escrow in terms of the TeOra acquisition	3,360,000	100.00%
Release on the closing of the TeOra acquisition	(420,000)	(12.50%)
Balance, December 31, 2015	2,940,000	87.50%
Release on closing date anniversary of the TeOra acquisition	(420,000)	(12.50%)
Release on achievement of performance milestones	(1,344,000)	(40.00%)
Balance, December 31, 2016	1,176,000	35.00%
Balance, December 31, 2015	18,230,344	
Balance, December 31, 2016	10,350,206	

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

8. SHARE CAPITAL (CONTINUED)

[b] Common shares (continued)

As of December 31, 2016, the Company had 10,350,206 common shares, representing 19.11% of its issued and outstanding shares, held in escrow accounts. Subsequent to December 31, 2016, an additional 3,058,069 shares were released from escrow.

- [i] On November 20, 2014, the Company issued a total of 7,618,780 special warrants at a price of \$0.55 per special warrant for total gross proceeds of \$4,190,329 (“**Offering**”). Each special warrant entitles the holder to acquire, upon exercise or deemed exercise and for no additional consideration, one unit consisting of one common share in the capital of the Company and one-half of one common share purchase warrant, which expired unexercised on November 20, 2016. The Company obtained a receipt for a final long form prospectus on February 19, 2015 and listed its common shares on the TSX Venture Exchange on March 17, 2015.

In connection to the Offering, the Company incurred \$248,270 cash commissions and issued 425,521 agents’ special warrants, which expired unexercised on November 20, 2016, valued at \$122,963. The Company has allocated \$219,572 of professional fees and other related financing costs to this Offering and recorded a total issuance cost of \$590,805 including cash commissions.

- [ii] On October 30, 2015, the Company closed a public financing and issued 2,475,000 common shares at a price of \$0.50 per share for total gross proceeds of \$1,237,500 (the “**2015 Financing**”). The public offering was made through Richardson GMP Limited. In connection to this financing, the Company issued 123,750 broker warrants valued at \$34,439, paid broker commissions and corporate finance fees of \$92,813 and \$25,000, respectively, and reimbursed \$83,786 of legal expenses. The Company also incurred \$131,266 of professional fees and other related financing costs to this financing.
- [iii] On January 12, 2016, the Company closed a non-brokered private placement in the United States of 1,797,422 common shares and a non-brokered public offering in Canada of 3,500,000 common shares at a price of \$0.50 per share for total gross proceeds of \$2,648,711. Of these proceeds, \$719,575 were collected and recorded as common share subscription received during the year ended December 31, 2015. In connection to this financing, the Company paid professional fees and other related financing costs of \$133,534. Of these issuance costs, \$51,563 were incurred and recorded as deferred financing costs at December 31, 2015.
- [iv] On September 13, 2016, the Company closed a public financing and issued 9,146,400 common shares at a price of \$0.30 per share for total gross proceeds of \$2,743,920. The public offering was co-led by Cormark Securities Inc. and Canaccord Genuity Corp. In connection to this financing, the Company paid commissions of \$192,074, legal and professional fees of \$79,940 and filing fees of \$13,720.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

8. SHARE CAPITAL (CONTINUED)

[b] Common shares (continued)

[v] On October 19, 2016, the Company issued 153,072 common shares as part of a service agreement entered into with Camargo Pharmaceutical Services, LLC for regulatory consulting services. Under the terms of the agreement, Camargo will be compensated with a split of cash and common shares of the Company for the services provided. The fair value of the shares is \$51,279, which makes up a portion of the non-refundable start-up fee.

[c] Common share purchase warrants

Common share purchase warrant transactions and the number of common share purchase warrants outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2014	510,390	0.75
Issued	3,809,388	0.75
Balance, December 31, 2015	4,319,778	0.75
Expired	(4,319,778)	(0.75)
Balance, December 31, 2016	Nil	Nil

[d] Agents' special warrants and broker's warrants

In connection with the Offering and the 2015 Financing, the Company issued 425,521 Agents' Warrants and 123,750 broker warrants, respectively:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2014	—	—
Issued in connection with the Offering <i>[note 8 [b][i]]</i>	425,521 ^[i]	0.55
Issued in connection with the 2015 Financing <i>[note 8 [b][ii]]</i>	123,750 ^[ii]	0.50
Balance, December 31, 2015	549,271	0.54
Expired	(425,521)	(0.55)
Balance, December 31, 2016	123,750	0.50

[i] Each Agents' Warrant entitles the holder to acquire one unit consisting of one common share in the capital of the Company and one-half of one common share purchase warrant at an exercise price of \$0.55 per Agents' Warrant until November 20, 2016. Each whole warrant entitles the holder to acquire an additional common share at a purchase price of \$0.75 per warrant for a period of 24 months following the date of issuance of the Agents' Warrant. These warrants expired unexercised.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

8. SHARE CAPITAL (CONTINUED)

[d] Agents' special warrants and broker's warrants (continued)

- [ii] Each broker warrant entitles the holder to acquire one common share in the capital of the Company at an exercise price of \$0.50 per common share until October 30, 2017.

[e] Stock options

On December 10, 2014, the Company adopted a stock option plan (the "Stock Option Plan") providing the granting of options to employees, officers, directors, consultants and scientific advisory board members. The Stock Option Plan was subsequently amended on February 4, 2015 to meet the listing requirements of the TSX Venture Exchange. On June 15, 2015 and August 19, 2016, the Company further amended its Stock Option Plan (the "Amended and Restated Stock Option Plan").

The maximum number of common shares issuable under the Amended and Restated Stock Option Plan is fixed at 8,970,308 common shares. Under the Amended and Restated Stock Option Plan, the maximum number of common shares that may be optioned in favour of any single individual will not exceed 5% of the issued and outstanding common shares at the date of grant. The maximum number of common shares that may be optioned in favour of directors and senior officers under the Stock Option Plan is 10% of the issued and outstanding common shares at the date of grant. The options can be granted for a maximum term of 10 years.

During the fiscal years ended December 31, 2016 and 2015, the Company recorded share-based payments of \$488,011 and \$704,590, respectively. The fair values of share options granted during the fiscal years ended December 31, 2016 and 2015 are estimated using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2016	2015
Risk-free interest rate	0.63%	1.29%
Estimated annualized volatility based on comparable companies	87%	103%
Expected life	5.49 years	8 years
Expected dividend yield	0%	0%
Exercise price	\$0.38	\$0.55
Fair value	\$0.26	\$0.49
Share price	\$0.38	\$0.56

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

8. SHARE CAPITAL (CONTINUED)

[e] Stock options (continued)

Stock option transactions and the number of stock options outstanding are summarized below:

	Number	Weighted Average Exercise Price \$
Balance, December 31, 2014	2,597,337	0.35
Exercised ^[i]	(125,000)	(0.35)
Cancelled, expired or forfeited	(230,000)	(0.35)
Granted	1,695,000	0.55
Balance, December 31, 2015	3,937,337	0.44
Cancelled, expired or forfeited	(662,000)	(0.55)
Granted	1,950,000	0.38
Balance, December 31, 2016	5,225,337	0.40

[i] No options were exercised during the year ended December 31, 2016. Average trading price when options exercised in the year ended December 31, 2015 was \$0.58 per share.

Date of Expiry	Exercise Price	Number of Options Outstanding	Number of Options Exercisable
November 23, 2018	\$0.31	400,000	200,000
December 2, 2019	\$0.27	500,000	250,000
May 31, 2020	\$0.25	1,124,337	1,124,337
December 12, 2021	\$0.35	565,000	565,000
December 1, 2022	\$0.55	50,000	37,500
December 18, 2022	\$0.55	350,000	350,000
March 6, 2023	\$0.55	465,000	377,500
July 9, 2023	\$0.57	300,000	225,000
September 30, 2023	\$0.55	421,000	268,500
April 21, 2024	\$0.47	900,000	410,000
July 22, 2024	\$0.35	150,000	37,500
Balance, December 31, 2016	\$0.40	5,225,337	3,845,337

As of December 31, 2016, the weighted average remaining life for outstanding options was 5.09 years (2015 - 6.3 years).

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

9. RELATED PARTY DISCLOSURE

[a] Transactions with related parties

Related parties include members of the board of directors (“the **Board**”) and officers of the Company, and enterprises controlled by these individuals. The following fees and expenses were incurred in the normal course of business:

	Year Ended December 31, 2016	Year Ended December 31, 2015
	\$	\$
Subcontract research and licensing fees ^[i]	518,707	331,924
Management fees ^{[ii] [iii] [iv]}	559,000	424,000
Consulting fees ^{[v] [vi] [vii] [viii]}	375,951	354,417
	1,453,658	1,110,341

[i] On August 1, 2013, the Company and Transdermal Pharma Research Laboratories LLC (“**TRPL**”), entered into a research service contract to cover formulation work in connection with the aripiprazole formulation and other pipeline programs as directed by the Company. TRPL is controlled by Dr. Fotios Plakogiannis and Dr. Rodoula Plakogiannis, two of the current directors of the Company. Pursuant to the terms of this research service contract which expired on November 30, 2016, the Company compensates TRPL for research work requested and pre-approved by the Company in exchange for the right to acquire an exclusive worldwide right to any intellectual property arising from or related to the research work. There is no fixed financial commitment under this research service contract. The Company incurred subcontract research fees of \$518,707, including a \$25,000 tech transfer bonus, and \$331,924 during the years ended December 31, 2016 and 2015, respectively.

As of December 31, 2016, the Company included in its accounts payable and accrued liabilities \$25,000 (2015 – \$Nil) due to TRPL.

[ii] Effective September 1, 2014, the Company entered into a management services agreement (the “**Northview Agreement**”) with Northview Lifesciences (formerly Northview Ventures and Associates General Partnership) (“**Northview**”), Doug Janzen, and Anne Stevens. Mr. Janzen is Chairman, President, and Chief Executive Officer of the Company and Ms. Stevens is the Corporate Secretary, Chief Operating Officer and a director of the Company. Pursuant to the Northview Agreement, Mr. Janzen, Ms. Stevens and other employees of Northview, directed and managed the affairs and the day-to-day operations of the Company at a monthly rate of \$27,000. Effective February 1, 2016, the monthly rate was increased to \$37,000. Northview was entitled to incentive bonuses upon the satisfaction of specified milestones. Management fees are allocated to research and development and general administration based on Mr. Janzen and Ms. Steven’s time involvement in the respective activities. The Northview Agreement expired on November 30, 2016. During the year ended December 31, 2016, Northview charged a total management fee of \$522,000 including bonuses of \$100,000 for completing financing milestones and \$25,000 for completing a tech transfer. During the preceding year ended December 31, 2015, Northview charged total management fees of \$424,000 including bonuses of \$40,000 and \$60,000 for completing a multi-product collaboration deal with Corium and listing on the TSX Venture Exchange, respectively.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

9. RELATED PARTY DISCLOSURE (CONTINUED)

[a] Transactions with related parties (continued)

As of December 31, 2016, the Company included in its accounts payable and accrued liabilities \$50,115 (2015 – \$77,622) due to Northview.

- [iii] Effective December 1, 2016, the Company entered into a consulting agreement with Northview Ventures Inc. (“NVI”) and Doug Janzen. Mr. Janzen is the Chairman, President, and Chief Executive Officer of the Company. Northview Ventures Inc. will be compensated at a monthly rate of \$25,000 from December 1, 2016 to March 31, 2017 then \$15,000 per month thereafter. During the year ended December 31, 2016, NVI received \$25,000 in compensation (2015 - \$Nil).

As of December 31, 2016, the Company included in its accounts payable and accrued liabilities \$26,250 (2015 – \$Nil) due to NVI.

- [iv] Effective December 1, 2016, the Company entered into a consulting agreement with Crecera Consulting Inc. (“Crecera”) and Anne Stevens. Ms. Stevens is the Corporate Secretary, Chief Operating Officer and a director of the Company. Crecera will be compensated at a monthly rate of \$12,000 from December 1, 2016 to March 31, 2017 then \$12,500 per month thereafter. During the year ended December 31, 2016, Crecera received \$12,000 (2015 - \$Nil) in compensation.

As of December 31, 2016, the Company included in its accounts payable and accrued liabilities \$12,600 (2015 – \$Nil) due to Crecera.

- [v] On December 1, 2014, the Company entered into a consulting services agreement with KeenVision Consulting Inc. (“KeenVision”) and Christina Yip (the “KeenVision Agreement”). Ms. Yip served as the Acting Chief Financial Officer of the Company. KeenVision was compensated at a monthly rate of \$8,000 and entitled to incentive bonuses upon the satisfaction of specified milestones. During the year ended December 31, 2016, KeenVision received total consulting fees of \$72,000 including two bonuses of \$10,000 each for completing a financing milestone. During the preceding year ended December 31, 2015, KeenVision received total consulting fees of \$123,500 including bonuses of \$12,500 and \$15,000 for listing on the TSX Venture Exchange and filing a shelf prospectus, respectively. The KeenVision Agreement was terminated on July 17, 2016 in connection with Christina Yip’s resignation as the Company’s Chief Financial Officer.

As of December 31, 2016, the Company has included in its accounts payable and accrued liabilities \$10,500 (2015 -\$25,200) due to KeenVision.

- [vi] The Company entered into a consulting service agreement with Mr. Ian Ball who serves as the Chief Commercial Officer of the Company, effective July 28, 2015. Pursuant to this consulting agreement with a term to July 31, 2019, Mr. Ball is compensated at a monthly rate of \$12,000. During the year ended December 31, 2016, Mr. Ball charged total consulting fees of \$144,000 (2015 - \$67,304).

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

9. RELATED PARTY DISCLOSURE (CONTINUED)

[a] Transactions with related parties (continued)

As of December 31, 2016, the Company has included in its accounts payable and accrued liabilities \$16,864 (2015 - \$15,041) due to Mr. Ball.

- [vii] The Company entered into a consulting service agreement with Dr. Don McAfee who serves as the Acting Chief Scientific Officer of the Company. Pursuant to the Consulting Agreement with a term expiring on December 31, 2017, Dr. McAfee was compensated at a daily rate of US\$1,000. During the year ended December 31, 2016, Dr. McAfee charged total consulting fees of \$99,838 (2015 - \$163,613.)

As of December 31, 2016, the Company has included in its accounts payable and accrued liabilities \$6,307 (2015 - \$7,620) due to Dr. McAfee.

- [viii] The Company entered into a consulting service agreement with Ann Fehr and Fehr & Associates on July 22, 2016. Mrs. Fehr is the Chief Financial Officer of the Company. Pursuant to this consulting agreement, Mrs. Fehr is compensated at a rate of \$1,000 per month plus \$100 per hour. Fehr & Associates also provides a part time controller and book-keeping services to the Company. During the year ended December 31, 2016, Fehr & Associates charged total consulting fees of \$60,113 for CFO and accounting services.

As of December 31, 2016, the Company has included in its accounts payable and accrued liabilities \$5,481 due to Fehr & Associates.

[b] Key management compensation

Key management includes members of the Board of Directors and executive officers of the Company. Compensation awarded to key management is listed below:

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Management fees, General & administration	425,500	254,400
Management fees, Research & development	133,500	169,600
Consulting fees, General & administration	182,513	123,500
Consulting fees, Research & development	99,838	163,613
Consulting fees, Sales & marketing	93,600	67,304
Share-based payments, General & administration	225,069	500,998
Share-based payments, Research & development	19,064	28,439
Share-based payments, Sales & marketing	137,049	112,838
	1,316,133	1,420,692

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

10. COMMITMENTS AND CONTINGENCIES

[a] Operating lease

On April 9, 2015, the Company entered into a sublease agreement for its Vancouver head office premise expiring on November 30, 2018 and paid a security deposit of \$62,192. Pursuant to this agreement, the Company is obligated to pay basic rent of \$8,893 and operating costs, currently estimated at \$6,655, on a monthly basis starting June 1, 2015. The Company has entered into sublease agreements of the space providing monthly rental revenue of \$3,650 to offset rent expense.

[b] Development agreement

On May 23, 2014, the Company entered into a development agreement with Corium International Inc. (“**Corium**”) which requires the Company to fund research and development work. Pursuant to this development agreement, the Company has a minimum financial commitment of \$289,815 (US\$261,000) and an option to contract additional research studies at \$464,040 (US\$400,000). The Company fulfilled its minimum financial commitment of \$289,815 (US\$261,000) during the fiscal year ended December 31, 2014. During the fiscal year ended December 31, 2016, the Company had renegotiated with Corium for work conducted in the preceding year and recovered subcontract development costs of \$67,719 (US\$50,000) and paid \$30,994 (US\$23,177) in subcontract development costs for aggregate recovered amount of \$36,725 (\$26,823 USD) from Corium (2015 – paid \$1,072,784 or US\$840,324).

[c] Licensing agreement

Pursuant to the terms of the Supernus Agreement [Note 6[b]], and in addition to the upfront payment of \$478,940 (US\$350,000), the Company is further obligated to pay US\$2.15 million following a successful pre-submission meeting with Health Canada, US\$2.5 million upon regulatory approval of Topiramate XR, and US\$500,000 upon regulatory approval of Oxcarbazepine XR. The Company is also required to pay royalty payments based on net sales at a rate of 15%, as well as a milestone payment of US\$1.5 million linked to achievement of a combined sales of US\$25 million of Topiramate XR and Oxcarbazepine XR. The Company is responsible for the regulatory submission and commercial activities for both products in Canada. The term of the Supernus Agreement will continue as long as the Topiramate XR and Oxcarbazepine XR products are sold in Canada.

[d] Contingencies

The Company has entered into agreements with third parties that include indemnification provisions that are customary in the industry. These guarantees generally require the Company to compensate the other party for certain damages and costs incurred as a result of third party claims or damages arising from these transactions. In some cases, the maximum potential amount of future payments that could be required under these indemnification provisions is unlimited. These indemnification provisions may survive termination of the underlying agreement. The nature of the indemnification obligations prevents the Company from making a reasonable estimate of the maximum potential amount it could be required to pay.

As of December 31, 2016 and 2015, the Company had not made any indemnification payments under such agreements and no amount had been accrued in the Financial Statements with respect to these indemnification obligations.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

11. OPERATING SEGMENT

The Company has a single operating segment, the sales and marketing of pharmaceutical drugs developed by the Company or by its collaborative partners. Substantially all of the Company's operations, assets, and employees are in Canada.

12. OPERATING EXPENSES

[a] Research and development expenses

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Consulting and management fees <i>[note 9[a]]</i>	361,147	380,970
Office and other	218	—
Patent and intellectual property protection	147,226	104,629
Salaries and wages	12,721	—
Share-based payments	45,882	54,705
Subcontract research costs and development costs <i>[note9]</i>	558,101	1,559,967
Travel and accommodation	2,485	44,217
	1,127,780	2,144,488

[b] Sales and marketing expenses

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Advertising and promotion	152,302	35,806
Consulting and management fees <i>[note 9]</i>	394,317	152,870
Depreciation and amortization	169,589	84,794
Printing and other expenses	51,765	20,039
Salaries and wages	87,615	—
Subcontract salesforce	523,292	103,804
Share-based payments	190,178	139,796
Travel and accommodation	198,306	18,068
	1,767,364	555,177

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

12. OPERATING EXPENSES (CONTINUED)

[c] General administration expenses

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Consulting and management fees <i>[note 9]</i>	1,274,099	616,813
Legal and professional fees	329,787	259,900
Other general administration expenses	341,235	561,829
Regulatory and transfer agent fees	62,571	70,473
Salaries and benefits	57,619	113,589
Share-based payments	438,981	626,417
Travel and accommodation	165,780	106,464
	2,670,072	2,355,485

13. CAPITAL DISCLOSURES

The Company's objectives when managing capital are to ensure its ability to continue as a going concern in order to pursue the development of its product candidates for ultimate sale or out-licensing. The Company attempts to maximize return to shareholders by minimizing shareholder dilution and, when possible, utilizing non-dilutive funding arrangements, such as collaborative partnership arrangements.

The Company defines its capital as share capital and contributed surplus. The Company has financed its capital requirements primarily through share and warrant issuances since inception.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and risk characteristics of the underlying assets. The Company may issue new securities. The Company is not subject to any externally imposed capital requirements. There were no changes to the Company's approach to capital management during the year ended December 31, 2016.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Fair value

The fair value of the Company's financial instruments is approximated by their carrying value due to their short-term nature.

IFRS 13 establishes a fair value hierarchy for financial instruments measured at fair value that reflects the significance of inputs used in making fair value measurements as follows:

Level 1 – quoted prices in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liabilities, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and

Level 3 – inputs for the asset or liability that are not based upon observable market data.

The fair value of cash and cash equivalents is based on Level 1 inputs.

[a] Credit risk

Credit risk is the risk of a financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises for the Company from its cash and cash equivalents and amounts receivable. The Company has adopted practices to mitigate against the deterioration of principal, to enhance the Company's ability to meet its liquidity needs, and to optimize yields within those parameters. These investment practices limit the investing of excess funds to liquid term deposits or cashable guaranteed investments ("GIC") invested only in Canadian Chartered Banks, and government guaranteed securities with maturities of one year or less. The Company did not have cashable GIC at December 31, 2016 (2015 - \$350,497). Amounts receivable consist of goods and services tax due from the Government of Canada and service fees owed from a collaborative partner.

[b] Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its obligations as they come due. The Company's exposure to liquidity risk is dependent on its purchasing commitments and obligations and its ability to raise funds to meet commitments and sustain operations. The Company manages liquidity risk by continuously monitoring its actual and forecasted working capital requirements, and actively managing its financing activities. As of December 31, 2016, the Company had working capital of \$59,142 (December 31, 2015 - \$239,863).

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

[c] Market risk

[i] Interest rate risk

Interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in the market interest rates. During the year ended December 31, 2016 and 2015, fluctuations in the market interest rates had no significant impact on its interest income.

[ii] Currency risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchanges rates. The Company has a portion of its operating expenses in U.S. dollars. The Company has not entered into foreign exchange derivative contracts. A significant change in the currency exchange rate between the Canadian dollar relative to the U.S. dollar could have an effect on the Company's results of operations, financial position or cash flows.

As at December 31, 2016 and 2015, the Company had the following assets and liabilities denominated in U.S. dollars:

	December 31, 2016 US\$	December 31, 2015 US\$
Cash and cash equivalents	2,145	384,841
Accounts payable and accrued liabilities	(52,844)	(375,748)
Total	(50,699)	9,093

Based on the above net exposure as at December 31, 2016, assuming that all other variables remain constant, a 5% appreciation or deterioration of the Canadian dollar against the U.S. dollar would result in a change of \$2,535 (2015 - \$629) in the Company's net loss and comprehensive loss. Furthermore, the company incurred \$872,925 USD expenditures during the year ended December 31, 2016. A 5% appreciation or deterioration of the Canadian dollar against the U.S. dollar would result in a change of \$43,646.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

15. INCOME TAXES

At December 31, 2016, the Company has non-capital loss carryforwards available to offset future taxable income in Canada, which expires as follows:

Expiry Date	Non-Capital Losses \$
December 31, 2032	615,012
December 31, 2033	1,853,110
December 31, 2034	613,893
December 31, 2035	2,705,562
December 31, 2036	3,935,792
	9,723,370

The Company also has a tax pool of approximately \$1,464,000 related to scientific research and experimental development expenditures in Canada available to carry forward indefinitely to reduce taxable income of future years.

Significant components of the Company's deferred income tax assets and liabilities are shown below:

	December 31, 2016 \$	December 31, 2015 \$
Deferred income tax assets (liabilities):		
Property and equipment	2,071	1,340
Share issuance costs	193,958	151,900
Scientific research and experimental development expenditures	380,593	313,812
Non-capital loss carryforwards	2,528,076	1,504,770
Total deferred income tax assets	3,104,698	1,981,939
Deferred income tax assets not recognized	(3,104,698)	(1,981,939)
Net deferred income tax assets	—	—

The potential income tax benefits relating to the net deferred income tax assets have not been recognized in the financial statements as their realization did not meet the requirements of "probable" under the liability method of tax allocation. Accordingly, no net deferred income tax assets have been recognized as at December 31, 2016 and 2015. The reconciliation of income tax attributable to operations computed at the statutory tax rates to income tax expenses using a 26% statutory tax rate is:

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Expected income tax recovery at statutory rates	(1,251,134)	(1,302,966)
Items not deductible for tax purposes	227,267	243,764
Benefits not recognized	1,023,867	1,059,202
Income tax expense	—	—

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

16. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

	Year Ended December 31, 2016 \$	Year Ended December 31, 2015 \$
Cash and cash equivalents consist of:		
Cash	473,242	813,315
Demand Deposits	—	350,497
	<u>473,242</u>	<u>1,163,812</u>

Non-cash transactions:

Deferred financing cost included in accounts payable and accrued liabilities	—	(51,563)
Common shares issued to acquire intangible assets and services	—	(1,002,120)
Fair value of options exercised	—	37,524
Fair value of securities issued as financing compensation	—	(34,439)
Fair value of securities issued for services	(51,279)	—
Addition to property and equipment included in accounts payable and accrued liabilities	(42,235)	—

17. SUBSEQUENT EVENTS

- [a] On February 1, 2017, the Company was granted funding up to a maximum of \$90,220 from the National Research Council of Canada and Industrial Research Assistance Program (“NRC-IRAP”) to support the ongoing Proof of Concept clinical study of its lead product candidate, AQS 1301, a once-weekly transdermal aripiprazole patch.
- [b] On March 13, 2017 the Company closed an agreement with Canaccord Genuity Corp. (“Canaccord”) to which they agreed to purchase, on a bought deal basis, 17,250,000 units at a price of \$0.30 per unit, for aggregate gross proceeds to the Company of \$5,175,000. The 17,250,000 Units issued include 2,250,000 units issued and sold pursuant to the over-allotment option granted by the Company to Canaccord. Each unit is comprised of one common share of the company and one-half of one common share purchase warrant. Each whole warrant is exercisable to acquire one common share for a period of two years at an exercise price of \$0.45 per share, subject to adjustment in certain events.

In the event the volume weighted average trading price of the Company’s common shares on the TSX Venture Exchange is greater than \$0.80 per common share for a period of 15 consecutive trading days, the Company may accelerate the expiry date of the warrants by giving notice to the holders thereof by way of press release and in such case the warrants will expire on the 30th day after such notice is given.

In addition, the Company issued 862,500 broker warrants in connection with the offering. Each broker warrant entitles the holder to acquire a unit at an exercise price of \$0.30 per unit for a period of two years following the closing of the offering.

Aequus Pharmaceuticals Inc.
Notes to Consolidated Financial Statements
For the years ended December 31, 2016 and 2015
(Expressed in Canadian dollars)

17. SUBSEQUENT EVENTS (CONTINUED)

- [c] Pursuant to the terms of the TeOra acquisition and the terms of the escrow agreement [*note 8[b]*], the Company cancelled 336,000 common shares relating to an unachieved performance milestone.