Acerus Pharmaceuticals Corporation

Audited Consolidated Financial Statements

December 31, 2017

(expressed in thousands of U.S. dollars except per share amounts and unless otherwise stated)

March 20, 2018

Independent Auditor's Report

To the Shareholders of
Acerus Pharmaceuticals Corporation

We have audited the accompanying consolidated financial statements of Acerus Pharmaceuticals Corporation and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2017 and December 31, 2016 and the consolidated statements of (loss)/income and comprehensive (loss)/income, changes in shareholders' equity (deficiency) and cash flows for the years then ended, and the related notes, which comprise 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 as issued by the International Accounting Standards Board, 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 audit 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 Acerus Pharmaceuticals Corporation and its subsidiaries as at December 31, 2017 and December 31, 2016 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Emphasis of matter
Without qualifying our opinion, we draw attention to note 1 in the consolidated financial statements which describes matters and conditions that indicate the existence of a material uncertainty that may cast significant doubt about Acerus Pharmaceuticals Corporation and its subsidiaries' ability to continue as a going concern.

(Signed) "PricewaterhouseCoopers LLP"

Chartered Professional Accountants, Licensed Public Accountants

Oakville, Ontario

Acerus Pharmaceuticals Corporation
Consolidated Statement of Financial Position
As at December 31, 2017 and 2016
(expressed in thousands of U.S. dollars)

	Notes	December 31, 2017	December 31, 2016
ASSETS			
Current assets			
Cash		$ 3,156	$ 5,199
Trade and other receivables	6	1,542	1,059
Licensing fee receivable		300	4,150
Inventory	7	2,979	3,770
Prepaid and other assets	8	229	226
Total current assets		8,206	14,404
Property and equipment, net	9	1,487	1,710
Intangible assets, net	10	12,561	13,602
Total assets		$ 22,254	$ 29,716
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Accounts payable and accrued liabilities	11	$ 3,134	$ 3,322
Current portion of deferred lease inducement	12	50	47
Current portion of long-term debt	13	1,026	4,092
Current portion of deferred revenue		1,206	1,006
Total current liabilities		5,416	8,467
Accrued liabilities	11	178	-
Deferred lease inducement	12	327	352
Long-term debt	13	3,543	2,357
Deferred revenue		6,567	6,198
Derivative financial instruments	14	307	141
Total liabilities		16,338	17,515
Shareholders' equity			
Share capital	15	$ 151,766	$ 151,766
Warrants	15	-	37
Contributed surplus		11,066	10,440
Accumulated other comprehensive loss		(14,091)	(15,931)
Deficit		(142,825)	(134,111)
Total shareholders' equity		5,916	12,201
Total liabilities & shareholders' equity		$ 22,254	$ 29,716

The accompanying notes are an integral part of these consolidated financial statements
Going concern (note 1)
Commitments and contingencies (note 22)
These consolidated financial statements were authorized for issue by the Board of Directors on March 20, 2018.

Acerus Pharmaceuticals Corporation

Consolidated Statement of (Loss)/Income and Comprehensive (Loss)/Income
For the years ended December 31, 2017 and 2016
(expressed in thousands of U.S. dollars, except per share and share data)

	Notes	December 31, 2017	December 31, 2016
Revenue			
Product revenue		$ 5,348	$ 7,013
Licensing revenue		1,096	17,473
		6,444	24,486
Cost of goods sold	16	3,263	4,453
Gross margin		3,181	20,033
Expenses			
Research and development	16	2,166	1,596
Selling, general and administrative	16	7,967	5,478
Total operating expenses		10,133	7,074
Other expenses/(income)			
Interest on long-term debt and other financing costs	17	380	1,179
Interest income		(21)	(17)
Foreign exchange loss	21	1,521	341
Change in fair value of derivative financial instruments	14	156	37
Gain on extinguishment of payables		(321)	-
Total other expenses		1,715	1,540
(Loss)/Income before income taxes		(8,667)	11,419
Current income tax expense	18	47	-
Deferred income tax expense	18	-	300
Net (loss)/income for the year		$ (8,714)	$ 11,119
Other comprehensive (loss)/income, net of income tax			
Foreign currency translation adjustment		1,840	1,267
Total comprehensive (loss)/income for the year		$ (6,874)	$ 12,386
(Loss)/earnings per common share			
Basic and diluted net (loss)/earnings per common share	19	$ (0.04)	$ 0.05
Weighted average common shares outstanding			
Basic	19	213,118,645	209,193,404
Diluted	19	213,118,645	210,479,254

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

Acerus Pharmaceuticals Corporation

Consolidated Statement of Changes in Shareholders' Equity (Deficiency)
For the years ended December 31, 2017 and 2016
(expressed in thousands of U.S. dollars)

	Notes	Share capital	Warrants	Contributed surplus	Accumulated other comprehensive loss	Deficit	Total
Balance, January 1, 2016		$ 149,766	$ 37	$ 10,166	$ (17,198)	$ (145,230)	$ (2,459)
Net income for the year		-	-	-	-	11,119	11,119
Foreign currency translation adjustment		-	-	-	1,267	-	1,267
Total comprehensive income for the year		-	-	-	1,267	11,119	12,386
Common shares issued	15	2,000	-	-	-	-	2,000
Shared based compensation	20	-	-	274	-	-	274
Balance as at December 31, 2016		151,766	37	10,440	(15,931)	(134,111)	12,201
Net loss for the year		-	-	-	-	(8,714)	(8,714)
Foreign currency translation adjustment		-	-	-	1,840	-	1,840
Total comprehensive loss for the year		-	-	-	1,840	(8,714)	(6,874)
Expiry of warrants	15	-	(37)	37	-	-	-
Shared based compensation	20	-	-	589	-	-	589
Balance as at December 31, 2017		$ 151,766	$ -	$ 11,066	$ (14,091)	$ (142,825)	$ 5,916

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

Acerus Pharmaceuticals Corporation

Consolidated Statement of Cash Flows

For the years ended December 31, 2017 and 2016

(expressed in thousands of U.S. dollars)

	Notes	December 31, 2017	December 31, 2016
Operating activities:			
Net (loss)/income for the year		$ (8,714)	$ 11,119
Items not affecting cash:			
Adjustment for unrealized foreign exchange loss		1,437	103
Deferred licensing revenue		(1,096)	(17,473)
Amortization of intangible assets	10	1,781	1,811
Depreciation of property and equipment	9	264	397
Amortization of deferred leasehold inducement	12	(49)	(48)
Interest on long-term debt and other financing costs	17	380	1,179
Change in fair value of derivative financial instruments	14	156	37
Share based compensation	20	589	274
(Gain)/loss on disposal of property and equipment		(8)	4
Gain on extinguishment of payables		(321)	-
Deferred income tax expense		-	300
Net changes in non-cash working capital items related to operating activities:			
Trade and other receivables		(398)	950
Inventory		641	(191)
Prepaids and other assets		12	(43)
Accounts payable and accrued liabilities		447	1,341
Deferred revenue		828	4,000
Licensing fee receivable		4,150	-
Customer deposits		-	(549)
Net cash from operating activities		99	3,211
Financing activities			
Interest and financing fees paid	13	(687)	(686)
Proceeds from issuance of common shares, net of financing costs	15	-	2,000
Proceeds from debt issuance	13	2,352	-
Payment of long-term debt obligations	13	(4,098)	(5,786)
Net cash (used in) operating activities		(2,433)	(4,472)
Investing activities			
Acquisition of property and equipment, net of deposits		-	(71)
Proceeds from sale of property and equipment		10	-
Net cash (used in)/from investing activities		10	(71)
Net decrease in cash for the year		(2,324)	(1,332)
Exchange gain on cash		281	198
Cash, beginning of year		5,199	6,333
Cash, end of year		$ 3,156	$ 5,199

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

1. GOING CONCERN

These audited consolidated financial statements have been prepared using International Financial Reporting Standards applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they come due for the foreseeable future.

The ability of Acerus Pharmaceuticals Corporation ("Acerus") and its subsidiaries (together, the "Company") to realize its assets and meet its obligations as they come due is dependent on successfully commercializing its existing products, bringing new products and technologies to market and achieving future profitable operations, the outcome of which cannot be predicted at this time. Furthermore, the Company will require additional funding, either from commercial sales of its existing products, commercial transactions or investors, to continue the development and commercialization of additional products. These circumstances lend significant doubt as to the ability of the Company to meet its obligations as they come due and, accordingly, the ultimate appropriateness of the use of accounting principles applicable to a going concern.

Management has assessed the Company's ability to continue as a going concern and concluded that in order to complete its planned product development and commercialization programs, capital will be required. The Company's ability to accomplish its strategic plans is dependent upon earning sufficient revenues from existing products, bringing new products and technologies to market, achieving future profitable operations and possibly obtaining additional financing, executing other strategic initiatives that could provide cash flows, or alternatively curtail expenditures. There are no assurances that any of these initiatives will be successful. Factors within and outside the Company's control could have a significant bearing on its ability to obtain additional financing.

These consolidated financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial position classifications that would be necessary if the Company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

2. DESCRIPTION OF BUSINESS

These audited consolidated financial statements represent the consolidated accounts of Acerus (incorporated in Ontario, Canada) and its wholly-owned subsidiaries, Acerus Labs Inc. ("ALI") (incorporated in Ontario), Acerus Biopharma Inc. ("ABI") (formerly named Acerus Pharmaceuticals SRL ("SRL")) (incorporated in Ontario), and Acerus Pharmaceuticals (Barbados) Inc. ("APBI") (incorporated in Barbados). On November 6, 2017, ABI migrated jurisdiction of incorporation, corporate law residence, and tax residence from Barbados to Canada. APBI was officially dissolved on February 26, 2018. The head office, principal address and records office of the Company are located in Mississauga, Ontario, Canada. The Company's registered address is 2486 Dunwin Drive, Mississauga, Ontario, L5L 1J9.

Acerus is a Canadian-based specialty pharmaceutical company focused on the development, manufacture, marketing and distribution of branded products with a primary focus in the field of men's and women's health. The Company commercializes its products via its own salesforce in Canada, and through a global network of licensed distributors in the U.S. and other territories.

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

2. DESCRIPTION OF BUSINESS (continued)

Natesto®

The Company entered into the following license, development and supply agreements with regards to Natesto®:

Date	Company	Territory	Terms
April 22, 2016	Aytu BioScience Inc. ("Aytu")	United States	• Upfront payments totaling $8,000 • Entitled to sales-based milestones that could potentially total $37,400 • Tiered supply price per unit
December 15, 2016	Hyundai Pharm Co., Ltd ("Hyundai")	South Korea	• Non-refundable upfront fee • Milestone payment on regulatory approval • Tiered supply price per unit
June 5, 2017	Therios Healthcare ("Therios")	Saudi Arabia, United Arab Emirates, and Egypt	• Fixed supply price per unit
June 14, 2017	medac Gesellschaft fϋr Klinische Spezialpräparate mbH ("medac")	15 European countries	• Non-refundable upfront fee • Milestone payment on regulatory approval and sales-based milestone payments • Tiered supply price per unit
October 17, 2017	Eu Hwa Pte LTD. ("EU")	Thailand, Malaysia/Brunei, Singapore, Vietnam, Philippines, Hong Kong/Macau and one other small South East Asian country	• Non-refundable upfront fee • Milestone payment on regulatory approval • Tiered supply price per unit
November 23, 2017	Apsen Farmacêutica ("Apsen")	Brazil	• Non-refundable upfront fee (received in 2018) • Milestone payment on regulatory approval • Tiered supply price per unit

Gynoflor™

The Company entered into a license and supply agreement with Medinova AG on April 6, 2016, a Swiss pharmaceutical company, granting it the exclusive rights to commercialize Gynoflor™ in Canada. On December 24, 2017, the Company received a Notice of Deficiency ("NOD"). In its notice, Health Canada requested additional technical information on Gynoflor™ in order to complete its assessment of the product, which we believe will cause a delay in the review process.

Elegant™ franchise

On December 20, 2017, Acerus entered into a license, development and supply agreement with Viramal Limited ("Viramal"), a London-based specialty pharmaceutical company, granting Acerus exclusive rights to commercialize the Elegant™ franchise in Canada. Under the terms of the license, development and supply agreement, Acerus will pay Viramal a regulatory milestone payment upon receiving marketing approval in Canada, as well as milestone payments based on achieving sales targets. Viramal will oversee the manufacturing of Elegant™ and will receive a supply price for the product.

3. SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Financial Reporting Interpretations Committee ("IFRIC") interpretations assessed by the International Accounting Standards Board. The consolidated financial statements have been prepared under the historical cost convention, except for certain financial instruments (warrants) that are measured at fair value, as explained in the accounting policies below. The accounting policies have been consistently applied to the years presented unless otherwise stated.

The preparation of the consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 4.

(b) Changes in accounting policy and disclosures

The following standards have been adopted on January 1, 2017:

IAS 7 *Statement of cash flows – Disclosures related to financing activities*

Amended to require disclosures about changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The amendment is effective for years beginning on or after January 1, 2017. Management has implemented the additional disclosures required in its annual consolidated financial statements for the year ending December 31, 2017 (see note 13).

IAS 12 *Income taxes – Deferred tax*

Amended the standard to clarify (i) the requirements for recognizing deferred tax assets on unrealized losses; (ii) deferred tax where an asset is measured at fair value below the asset's tax base, and (iii) certain other aspects of accounting for deferred tax assets. The adoption of this standard on January 1, 2017 did not have a material impact on the consolidated financial statements.

New and revised IFRSs issued but not yet effective

A number of new standards and amendments to standards and interpretations have not been applied in preparing these consolidated financial statements. None of these standards are expected to have a significant effect on the consolidated financial statements of the Company, except the following set out below:

IFRS 9 *Financial Instruments*

In July 2014, the IASB issued IFRS 9 Financial Instruments to replace IAS 39 "*Financial Instruments: Recognition and Measurement*". The new standard uses a principle-based approach for the classification and measurement of financial assets: amortized cost and fair value. Additional amendments include a single "expected loss" impairment method and a substantially reformed approach to hedge accounting. This standard is effective for annual periods beginning on or after January 1, 2018. The Company's financial assets primarily consist of trade receivables. The adoption of IFRS 9 will be applied on a retrospective basis on January 1, 2018 without restatement of comparatives and will not have a significant effect on the valuation of the Company's financial assets.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

b) Changes in accounting policy and disclosures (continued)

IFRS 15 *Revenue from Contracts with Customers*

IFRS 15 specifies how and when to recognize revenue as well as requiring the Company to provide users of financial statements with more informative, and relevant disclosures. The standard provides a single, principles-based five-step model to be applied to all contracts with customers. Extensive disclosures will be required, including: disaggregation of total revenue; information about performance obligations; changes in contract asset and liability account balances between periods; and key judgments and estimates. IFRS 15 applies to annual reporting periods beginning on or after January 1, 2018. In its review of out-licensing agreements, the Company expects that the license will be considered distinct from other goods and services in the contract. The license provides the partner with the right to use the Company's intellectual property. As such, management expects that revenue may be recognized when control transfers to the licensee and the license period begins. Management is continuing to evaluate the impact of the standard.

The Company will adopt this accounting standard on January 1, 2018, using full retrospective approach. The Company expects the adoption of the standard to result in a decrease in the amount recognized as deferred revenue by $7,204, a decrease in accumulated other comprehensive income of $129 and a corresponding increase in retained earnings of approximately $7,333, net of income taxes, as at January 1, 2017. Revenues for the year ended December 31, 2017 is expected to increase by $91 and the net loss and comprehensive loss is expected to decline by $91.

IFRS 16 *Leases*

The new standard brings most leases on-balance sheet, eliminating the distinction between operating and finance leases. Lessor accounting remains largely unchanged and the distinction between operating and finance leases is retained. The new standard is effective for annual reporting periods beginning on or after January 1, 2019. The Company has yet to assess IFRS 16's full impact and will not early adopt the standard.

(c) Consolidation

The wholly-owned subsidiaries of the Company are consolidated to produce the financial results for the consolidated Company. All intercompany transactions, balances, income and expenses on transactions between subsidiaries are fully eliminated. Profits and losses resulting from intercompany transactions that were recognized are also fully eliminated.

(d) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-makers. The chief operating decision-makers, who are responsible for allocating resources and assessing performance of the operating segments, have been identified as the interim Chief Executive Officer and the Chief Financial Officer.

(e) Foreign currency translation

Presentation currency

Items included in the financial statements of each of the Company's entities are measured using the currency of the primary economic environment in which each entity operates (the "functional currency"). The consolidated financial statements are presented in United States dollars, which in the opinion of management, is the most appropriate presentation currency as the United States dollar is used to significant effect in, or has a significant impact on, the operations of the Company and reflects the economic substance of a majority of the underlying events and circumstances relevant to the Company.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Foreign currency translation (continued)

Transactions and balances

Foreign currency transactions are translated into the functional currency of the relevant entity using the exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in finance costs in the consolidated statement of loss/income and comprehensive loss/income.

Financial Statements

Management has determined that the functional currency of ABI is the United States dollar, and the functional currency for the Canadian parent and the remaining subsidiaries is the Canadian dollar. The Canadian dollar is the appropriate functional currency for the parent as it the primary economic environment in which the parent operates. The results and financial statements of the parent are translated at the end of each reporting period as follows:

- Monetary assets and liabilities are translated at the period-end closing rate including trade receivables from its subsidiary company;
- Management has elected equity and shareholders' equity (deficiency), are measured in terms of the exchange rate at the date of the transaction; and
- Revenue and expenses at an average rate for the period where this rate approximates the exchange rates at the dates of the transactions.

All resulting currency translation gains or losses from translating the financial statements from the functional currency to the presentation currency are recorded in other comprehensive loss/income in the consolidated statement of loss /income and comprehensive loss/income.

(f) Trade receivables

Trade receivables are amounts due from customers for inventory sold in the ordinary course of business. If collection is expected in one year or less, they are classified as current assets. If not, they are presented as non-current assets.

Trade receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. As at December 31, 2017 and 2016, management determined that no provision for impairment was required.

(g) Inventory

Inventories consist of raw materials, work-in-process and finished goods. Inventories are stated at the lower of cost based on first-in-first-out ("FIFO") and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Property and equipment

Property and equipment are stated at cost less accumulated depreciation and impairment losses. Depreciation is recorded as follows:

Computers	- straight-line over 3 years;
Office furniture and fixtures	- straight-line over 5 years;
Laboratory equipment	- straight-line over 5 to 10 years;
Manufacturing equipment	- straight-line over 3 to 10 years;
Leasehold improvements	- straight-line over the expected term of the lease.

Expenditures that extend the useful life of the asset are capitalized and minor repair and maintenance costs are expensed as incurred to the consolidated statement of loss/income and comprehensive loss/income. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognized within the consolidated statement of loss/income and comprehensive loss/income.

(i) Leases

All leases are treated as operating leases. Payments on operating lease agreements are recognized as an expense on a straight-line basis over the lease term. Associated costs, such as maintenance and insurance, are expensed as incurred.

(j) Deferred lease inducements

Lease inducements, representing reduced rental periods and non-repayable leasehold improvement allowances received from the landlord are amortized on a straight-line basis as a reduction of rent expense over the term of the lease.

(k) Intangible assets

Intangible assets acquired separately

Intangible assets with determinable lives are stated at cost less accumulated amortization and impairment losses. Such intangible assets are amortized over their estimated useful lives using the straight-line method. Intangible assets held by the Company currently hold estimated useful lives between eight to twenty years.

Derecognition of intangible assets

An intangible asset is derecognized on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset, are recognized in the consolidated statement of loss/income and comprehensive loss/income when the asset is derecognized.

(l) Impairment of non-financial assets

The Company reviews assets such as property and equipment and intangible assets with finite useful lives for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units or "CGUs"). Recoverable amount is the higher of an asset's fair value less the cost of disposal and value in use (being the present value of the expected future cash flows of the relevant asset or CGU) as determined by management.

Any impairment losses are recognized immediately in the consolidated statement of loss/income and comprehensive loss/income. Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(m) Income taxes

Income taxes are accounted for using the liability method. Deferred tax assets and liabilities are recognized for the differences between the tax basis and carrying amounts of assets and liabilities, for operating losses and for tax credit carry-forwards. Deferred tax assets are recognized to the extent that it is probable that future taxable profit will be available against which temporary differences can be utilized. Deferred tax assets and liabilities are measured using enacted or substantially enacted tax rates and laws.

(n) Financial instruments

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instruments.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs related to other liabilities and loans and receivables are added to the carrying value of the asset or netted against the carrying value of the liability and are then recognized over the expected life of the instrument using the effective interest method.

Financial assets

Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss' (FVTPL), and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Financial assets at FVTPL

Financial assets are classified as FVTPL when the financial asset is held for trading.

A financial asset is classified as held for trading if it has been acquired principally for the purpose of selling in the near future, if it is part of an identified portfolio of financial instruments that the Company manages and has an actual pattern of short-term profit-taking, or if it is a derivative that is not designated and effective as a hedging instrument. Financial assets and derivative financial instruments classified as FVTPL are initially measured at fair value with any subsequent gain or loss arising from changes in fair value recognized in the consolidated statement of loss/income and comprehensive loss/income.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured initially at fair value and subsequently at amortized cost using the effective interest method, less any impairment.

Financial liabilities

Financial liabilities are classified as either financial liabilities classified as 'FVTPL' or 'other financial liabilities'.

Financial liabilities at FVTPL

Financial liabilities classified as FVTPL are financial liabilities held for trading or derivative financial instruments. A financial liability is classified as FVTPL if the instrument is acquired or incurred principally for the purpose of selling or repurchasing in the short-term or where the Company does not have the unconditional right to avoid delivering cash or another financial asset to the holders in certain circumstances. Financial liabilities at FVTPL are classified as current liabilities if expected or potentially required to be settled within 12 months from the end of a given reporting period; otherwise, the liabilities are classified as non-current.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(n) Financial instruments (continued)

Financial liabilities at amortized cost

Other financial liabilities are subsequently measured at amortized cost using the effective interest method.

Impairment of financial assets

Assets carried at amortized cost

The Company assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognized in the consolidated statement of loss/income and comprehensive loss/income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Company may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the reversal of the previously recognized impairment loss is recognized in the consolidated statement of loss/income and comprehensive loss/income.

Financial liabilities and equity instruments

Classification as debt or equity

Instruments issued by the Company are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recognized at the proceeds received, net of direct issue costs. Proceeds received on issuance of units, consisting of common shares and warrants, are allocated to those two instruments based on their relative fair values. Transaction costs are also allocated to the common shares and warrants in proportion to the allocation of proceeds.

Repurchase of the Company's own equity instruments is recognized and deducted directly in equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Compound financial instruments

Compound financial instruments contain both a liability and an embedded derivative in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability component is estimated using the interest rate applied by the market for similar debt instruments. The liability is subsequently measured on an amortized cost basis using the effective interest method over the expected life. The embedded derivative is initially recorded at fair value using pricing model techniques. It is recognized and presented together with the liability in the consolidated statement of financial position and is subsequently re-measured at fair value through profit and loss.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(o) Derivative financial instruments

Acerus has issued warrants with a cashless exercise option, some with an exercise price in a currency other than the functional currency (CDN). These are treated as a derivative liability and therefore measured at fair value. Gains and losses on re-measurement are presented separately in the consolidated statement of loss/income and comprehensive loss/income. These instruments are classified as non-current based on their expected life. Transaction costs that are directly attributable to the long-term debt and the joint issuance of these warrants have been allocated to long term debt and to the warrants based on their relative fair value.

In addition to the above, the Company also has an embedded derivative of nominal value related to long-term debt (interest floor and prepayment option) and an embedded derivative related to the license, development and supply agreement for the sale of Natesto® (fixed price contract denominated in a currency other than the entity's functional currency).

Derivatives embedded in non-derivative host contracts are separated from the host contract when their economic risk and characteristics are not closely related to those of the host contract and the compound instrument is not measured at FVTPL.

(p) Revenue

Revenue is measured at the fair value of consideration received or receivable. Revenue is reduced for estimated customer returns, rebates and other similar allowances based on historical information of the Company and consideration of the type of customer, type of transaction and the specifics of each arrangement.

Product Revenue:

Revenue from the sale of goods is recognized when title has passed and when all the following conditions are satisfied:

- The Company has transferred to the buyer the significant risks and rewards of ownership of the goods.
- The Company retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold.
- The amount of revenue can be measured reliably.
- It is probable that the economic benefits associated with the transaction will flow to the Company.
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

License and other fees:

License and supply agreements may contain multiple elements. The individual elements of each agreement are divided into separate units of accounting if certain criteria are met. The applicable revenue recognition approach is then applied to each unit. Otherwise, the applicable revenue recognition criteria are applied to combined elements as a single unit of accounting.

Milestone payments are recorded as deferred revenue when received and amortized on a straight-line basis over the term of the agreement.

(q) Deferred revenue

Deferred revenue consists of amounts received from customers in advance of revenue recognition. Amounts expected to be recognized within one year or less are classified as current liabilities with the balance being classified as non-current liabilities.

(r) Cost of sales

Costs of sales comprise the cost of inventory sold during the year, royalty expenses, depreciation, amortization charges and distribution costs.

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(s) Share-based compensation

The Company has a stock option plan as described in note 20 that allows for the issuance of stock options to employees, directors, officers, consultants and others as determined by the Board of Directors. Under IFRS, each option installment is treated as a separate option grant with graded-vesting features, forfeitures are estimated at the time of grant and revised if actual forfeitures are likely to differ from previous estimates, and options granted to parties other than employees are measured at their fair value on the date goods or services are received. The fair value of the goods and services received are determined indirectly by reference to the fair value of the instrument granted, unless the fair value of the goods and services received is readily apparent.

Over the vesting period of the option grants, the fair value is recognized as compensation expense and a related credit is recorded as contributed surplus. The contributed surplus is reduced as options are exercised through a credit to share capital. The consideration paid by option holders is credited to share capital when the options are exercised.

(t) Investment tax credits

Investment tax credits, which are earned as a result of incurring qualifying research and development expenditures, are treated either as a reduction of the relevant asset account or research and development expenses in the period that the credits become available and there is reasonable assurance that they will be realized.

(u) Loss/income per share

Basic loss/income per share is calculated by dividing the net loss/income by the weighted average number of common shares outstanding during the year. Diluted loss/income per share is calculated by dividing the applicable net loss/income by the sum of the weighted average number of shares outstanding during the year and all additional common shares that would have been outstanding if potentially dilutive common shares had been issued during the year.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

When preparing the consolidated financial statements, management undertakes a number of judgments, estimates and assumptions regarding recognition and measurement of assets, liabilities, income and expenses. Information about the judgments, estimates and assumptions that have the most significant effect on the recognition and measurement of assets, liabilities, income and expenses are discussed below.

Critical accounting estimates and judgments

Revenue recognition

Product revenue is recorded at the invoiced amount less estimated accruals for product returns, discounts, chargebacks and other price adjustments. These provisions with respect to Estrace® and Natesto® are presently based on historical levels and are recognized as a reduction of revenue. While such experience has allowed for reasonable estimates in the past, history may not always be an accurate indicator of future events. Management will monitor these provisions and make adjustments when it believes actual results may differ from established reserves.

Fair value of derivative financial instruments

The fair values of derivative financial instruments that are not traded in an active market are determined using valuation techniques. The Company uses its judgment to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period. Additional information is disclosed in note 14.

4. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

Clinical trial expenses

Clinical trial expenses are accrued based on estimates of the services received and efforts expended pursuant to contracts with clinical research organizations (CROs), consultants and other vendors. In the normal course of business, the Company contracts third parties to perform various clinical trial activities in the ongoing development of potential products. The financial terms of these agreements vary from contract to contract, are subject to negotiation and may result in uneven payment flows. Payments under the contracts depend on factors such as the achievement of certain events, the successful enrolment of patients or the completion of portions of the clinical trial or similar conditions. The Company accrues and expenses clinical trial activities based upon estimates of the proportion of work completed over the life of the individual clinical trial and patient enrolment rates in accordance with agreements established with CROs and clinical trial sites. The Company determines the estimates by reviewing contracts, vendor agreements and purchase orders, and through discussions with internal personnel and external service providers as to the progress or stage of completion of trials or services and the agreed-upon fee to be paid for such services. However, actual costs and timing of clinical trials are highly uncertain, subject to risks and may change depending upon a number of factors, including the Company's clinical development plan.

Share based payments

The compensation expense related to share-based payments is determined using the Black-Scholes option pricing model. The significant variables and estimates used in the model are the volatility, dividend yield, expected option life, and risk-free interest rate. In addition, management also applies an estimated forfeiture rate. Additional information is disclosed in note 20.

Income taxes

The Company is subject to income taxes in different jurisdictions and therefore uses judgment to determine the provision for income taxes. Management makes estimates and takes tax filing positions and it is uncertain whether certain estimates and tax filing positions will be sustained upon examination by applicable tax authorities. Provisions for uncertain tax positions are recorded based on management's estimate of the most likely outcome. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made.

5. PRODUCT RIGHTS AND ASSET ACQUISITIONS

(a) Bio-adhesive gel technology

In May 2009 (and in accordance with certain subsequent contractual amendments), ABI acquired certain rights from M&P Patent AG (since renamed Mattern Pharma) to use certain technology to develop, apply for and obtain regulatory approval, and to manufacture and sell four product candidates pursuant to an Intellectual Property Rights and Product Development Agreement ("IP Agreement") in exchange for milestones, royalties based on the Company's gross margin, and other payments depending on the achievement of specified goals for Natesto® and Tefina™. There are potential future milestone payments totaling $4,500 for Tefina™. Pursuant to an amendment to the IP Agreement in December 2013, the Company forfeited all rights to the third product candidate (dopamine). There are no milestones associated with the fourth product candidate (an anxiety product to be named later). Starting in fiscal 2018, there is a minimum annual royalty obligation of $5,000 if the gross annual sales of Natesto™ exceed $75,000 in a calendar year or $2,500 if the gross annual sales of the Natesto® product are below $75,000 in the applicable calendar year. For the year ended December 31, 2017, the Company expensed $201 in royalty expense due to royalty payments related to the $1,128 upfront fee from the Natesto® license, supply and development agreements.

The Company must pay minimum royalties of $5,000 per year in each full calendar year following the first commercial sale of Tefina™.

5. PRODUCT RIGHTS AND ASSET ACQUISITIONS (continued)

(a) Bio-adhesive gel technology (continued)

The minimum royalty amounts may be subject to a potential reduction mechanism in the IP Agreement after the total amount of royalties paid to M&P under the IP Agreement exceeds $80,000. There is an expiry of the royalty obligations at the earliest of (a) cumulative royalty payments of $250,000 or (b) May 22, 2024.

(b) Pulmonary and nasal dry powder delivery technology

On November 30, 2009, ABI entered into an asset purchase agreement with Keldmann Healthcare A/S ("Keldmann"), a privately-held Denmark-based technology company.

Pursuant to the terms of the asset purchase agreement, ABI paid $4,500 to Keldmann to acquire the Direct Haler technology platform (TriVair) for pulmonary and nasal delivery of pharmaceutical medications. This acquisition was accounted for as a purchase of identifiable intangible and tangible assets.

As part of this transaction with Keldmann, and pursuant to an Amended Product Development Agreement dated December 30, 2009, ABI may collaborate with Keldmann on the development of certain product candidates in exchange for consulting fees and will make milestone, royalty and other payments depending on achievement of specified development and other goals.

There is a milestone payment of $2,000 due upon Food and Drug Administration ("FDA") approval for each product to a maximum of $8,000. As well, there is a cap on royalty payments of $25,000 per product.

(c) Gynoflor™

The Company entered into a license and supply agreement with Medinova AG, a Swiss pharmaceutical company, granting the Company the exclusive rights to commercialize Gynoflor™ in Canada. On December 24, 2017 the Company received a Notice of Deficiency ("NOD"). In its notice, Health Canada requested additional technical information on Gynoflor™ in order to complete its assessment of the product, which the Company believes will cause a delay in the review process.

(d) Elegant™ franchise

On December 20, 2017, the Company entered into a license, development and supply agreement with Viramal Limited ("Viramal"), a London-based specialty pharmaceutical company, granting the Company exclusive rights to commercialize the Elegant™ franchise in Canada. Under the terms of the license, development and supply agreement, the Company will pay Viramal a regulatory milestone payment upon the Company receiving marketing approval in Canada, as well as milestone payments based on achieving sales targets. Viramal will oversee the manufacturing of Elegant™ and will receive a supply price for the product.

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

6. TRADE AND OTHER RECEIVABLES

	December 31, 2017	December 31, 2016
Trade receivables	$ 1,311	$ 947
Other receivables	231	112
Total trade and other receivables	$ 1,542	$ 1,059

Allowance for doubtful accounts are recognized based on estimated irrecoverable amounts determined by reference historical default experience of the counterparty and an analysis of the counterparty's current financial position. As at December 31, 2017 the Company has recognized $nil in allowance for doubtful accounts ($nil as at December 31, 2017).

Trade and other receivables disclosed above include amounts that are past due at the end of the reporting period for which the Company has not recognized an allowance for doubtful accounts as there has not been a significant change in credit quality and the amounts are still considered recoverable.

Age of receivables that are past due but not impaired:

	December 31, 2017	December 31, 2016
60 - 90 days	$ 413	$ 30
Greater than 90 days	149	45
	$ 562	$ 75

The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivables mentioned above. The Company does not hold any collateral as security. Of the amount past due at year end, $516 was collected subsequent to year end.

7. INVENTORY

	December 31, 2017	December 31, 2016
Raw materials	$ 2,532	$ 2,917
Finished goods	447	853
Total inventory	$ 2,979	$ 3,770

The cost of finished goods recognized as an expense and included in cost of sales amounted to $960 for the year ended December 31, 2017 ($1,103 for the year ended December 31, 2016).

8. PREPAIDS AND OTHER ASSETS

	December 31, 2017	December 31, 2016
Deposits with vendors	$ 155	$ 161
Other	74	65
Total prepaid and other assets	$ 229	$ 226

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

9. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	Computers	Office, furniture and fixtures	Manufacturing and laboratory equipment	Leasehold improvements	Total
Cost					
Balance, January 1, 2017	$ 47	$ 193	$ 2,989	$ 713	$ 3,942
Disposals	(45)	(72)	-	-	(117)
Effect of foreign currency exchange difference	-	5	105	51	161
Balance, December 31, 2017	$ 2	$ 126	$ 3,094	$ 764	$ 3,986
Accumulated depreciation					
Balance, January 1, 2017	$ 45	$ 106	$ 1,975	$ 106	$ 2,232
Depreciation	-	25	163	76	264
Disposals	(45)	(70)	-	-	(115)
Effect of foreign currency exchange difference	1	4	104	9	118
Balance, December 31, 2017	$ 1	$ 65	$ 2,242	$ 191	$ 2,499
Net book value					
December 31, 2017	$ 1	$ 61	$ 852	$ 573	$ 1,487

	Computers	Office, furniture and fixtures	Manufacturing and laboratory equipment	Leasehold improvements	Total
Cost					
Balance, January 1, 2016	$ 47	$ 185	$ 2,945	$ 671	$ 3,862
Additions	-	4	-	7	11
Transfer to completed asset	-	-	-	14	-
Effect of foreign currency exchange difference	-	4	44	21	69
Balance, December 31, 2016	$ 47	$ 193	$ 2,989	$ 713	$ 3,942
Accumulated depreciation					
Balance, January 1, 2016	$ 43	$ 81	$ 1,641	$ 31	$ 1,796
Depreciation	2	25	296	74	397
Effect of foreign currency exchange difference	-	-	38	1	39
Balance, December 31, 2016	$ 45	$ 106	$ 1,975	$ 106	$ 2,232
Net book value					
December 31, 2016	$ 2	$ 87	$ 1,014	$ 607	$ 1,710

At December 31, 2017, manufacturing equipment with a net book value of $846 was held off-site with a third party ($998 at December 31, 2016).

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

10. INTANGIBLE ASSETS

	Technology and patents	Product rights	Total
Cost			
Balance, January 1, 2017	$ 4,400	$ 29,416	$ 33,816
Effect of foreign currency exchange difference	-	2,068	2,068
Balance, December 31, 2017	$ 4,400	$ 31,484	$ 35,884
Accumulated depreciation			
Balance, January 1, 2017	$ 2,071	$ 18,143	$ 20,214
Amortization	234	1,547	1,781
Effect of foreign currency exchange difference	-	1,328	1,328
Balance, December 31, 2017	$ 2,305	$ 21,018	$ 23,323
Net book value			
December 31, 2017	$ 2,095	$ 10,466	$ 12,561

	Technology and patents	Product rights	Total
Cost			
Balance, January 1, 2016	$ 4,400	$ 28,538	$ 32,938
Effect of foreign currency exchange difference	-	878	878
Balance, December 31, 2016	$ 4,400	$ 29,416	$ 33,816
Accumulated depreciation			
Balance, January 1, 2016	$ 1,775	$ 16,152	$ 17,927
Amortization	296	1,515	1,811
Effect of foreign currency exchange difference	-	476	476
Balance, December 31, 2016	$ 2,071	$ 18,143	$ 20,214
Net book value			
December 31, 2016	$ 2,329	$ 11,273	$ 13,602

Amortization expense related to the technology and patents is computed based on the life of the existing patents and is included in the research and development expense on the consolidated statement of loss/income and comprehensive loss/income. The remaining life of the Direct Haler patents and patent applications (if issued) is 19 years and 1 month. Amortization of $234 has been recorded for the year ending December 31, 2017 ($296 for the year ending December 31, 2016).

Product rights includes rights for Estrace®. Amortization of $1,547 has been recorded in cost of goods sold for the fiscal year ending December 31, 2017 ($1,515 for the year ending December 31, 2016).

11. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	December 31, 2017	December 31, 2016
Accounts payable	$ 1,213	$ 1,604
Employee salaries, severance and benefits payable	1,104	281
Royalty payable	54	747
Interest and financing fees payable	99	256
Accrued liabilities	464	310
Other	200	124
Total current accounts payable and accrued liabilities	$ 3,134	$ 3,322
Employee severance, long-term liability	178	-
Total accounts payable and accrued liabilities	$ 3,312	$ 3,322

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

12. DEFERRED LEASEHOLD INDUCEMENT

	December 31, 2017	December 31, 2016
Balance, January 1	$ 399	$ 436
Amortized to rent expense	(49)	(48)
Effect of foreign currency exchange differences	27	11
Total balance of leasehold inducements	$ 377	$ 399
Current portion	50	47
Non-current portion	$ 327	$ 352

The deferred leasehold inducement is being amortized on a straight-line basis over the term of the lease which ends June 30, 2025.

13. LONG-TERM DEBT

Long-term debt balance	Senior Financing	Promissory Note	Quantius Debt	Total
Balance, January 1, 2016	$ 8,031	$ -	$ -	$ 8,031
Conversion of customer deposit to loan	-	3,800	-	3,800
Amortization of deferred financing costs	424	-	-	424
Repayment of principal	(5,286)	(500)	-	(5,786)
Effect of foreign currency exchange difference	(20)	-	-	(20)
Balance, December 31, 2016	$ 3,149	$ 3,300	$ -	$ 6,449
Current portion at December 31, 2016	3,149	943	-	4,092
Long-term portion at December 31, 2016	$ -	$ 2,357	$ -	$ 2,357
Balance, January 1, 2017	$ 3,149	$ 3,300	$ -	$ 6,449
Debt issued	-	-	2,352	2,352
Transaction costs	-	-	(191)	(191)
Accrued royalty payable	-	-	6	6
Amortization of deferred financing costs	5	-	5	10
Repayment of principal	(3,155)	(943)	-	(4,098)
Effect of foreign currency exchange difference	1	-	40	41
Balance, December 31, 2017	$ -	$ 2,357	$ 2,212	$ 4,569
Current portion at December 31, 2017	-	943	83	1,026
Long-term portion at December 31, 2017	$ -	$ 1,414	$ 2,129	$ 3,543

MidCap V, LLC senior financing

On July 16, 2014, the Company entered into a senior financing with MidCap V, LLC (“MidCap”) for facilities of up to $25,000. On December 11, 2015, the Company entered into an agreement to amend the senior financing with MidCap. Pursuant to the terms and conditions of the amendment, the Company immediately repaid $17,000 of its existing $25,000 principal amount outstanding. The remainder of the outstanding principal amount matured on January 9, 2017. The senior financing bore interest at a rate of LIBOR + 9.5% per annum with a LIBOR floor rate of 1% and was secured by all of the assets of the Company and included a covenant to maintain a minimum cash balance as set out in the amended agreement.

An amendment to the senior financing was entered into on April 22, 2016 pursuant to which certain adjustments were made to the Company’s minimum cash covenants. The Company used $3,000 of the cash proceeds received from the Aytu transactions to retire a portion of the outstanding principal amount owed to MidCap in connection with the senior financing. The debt was extinguished on January 6, 2017.

In accordance with the credit and security agreement with MidCap, the Company had granted security over the assets of the Company and its subsidiaries. In connection with the transaction, the lenders were issued warrants exercisable for an aggregate of 3,034,814 common shares of the Company. The warrants are exercisable for a period of seven years (expires July 2021) at an exercise price of CDN$0.7095, which was calculated using the volume weighted average trading price of the Company’s common shares on the Toronto Stock Exchange for the period of five days ending immediately prior to the closing date of the senior financing. The fair value of the warrants on the date of issuance was $1,324.

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

13. LONG-TERM DEBT (continued)

Endo International plc promissory note

Pursuant to the transition agreement between Acerus and an affiliate of Endo International plc ("Endo"), both parties have also entered into an agreement related to the unused customer deposit (pre-paid inventory) owed to Endo following the termination of the Natesto® agreement. A $500 cash payment was paid to Endo in July 2016 and $3,800 of the remaining principal amount is subject to a promissory note, of which $500 was paid in December 2016 and the remaining amounts are payable in equal quarterly installments of $236 with the final payment and maturity date of June 30, 2020. The promissory note is unsecured and bears interest at a rate of LIBOR + 9.5% per annum with a LIBOR floor rate of 1%. On March 15, 2018, the promissory note was amended such that principal repayments under the promissory note would now be made annually on the last business day of the month of December of each year instead of quarterly. Payments of interest will continue to be made quarterly.

Quantius Inc. credit facility

On December 6, 2017, Acerus entered into a senior secured term credit facility with Quantius Inc. ("Quantius") for up to CDN$5.0 million. Of which CDN$3.0 million was available at closing, with the remaining CDN$2.0 million becoming available upon satisfaction of certain future conditions, including 1) Aytu achieving a pre-determined number of prescriptions per month for Natesto® in the U.S., and 2) maintaining Estrace® sales at a pre-determined minimum level. The credit facility bears interest at a rate equivalent to the Bank of Canada prime plus 11.05% and matures on December 1, 2019. The credit facility is repayable in monthly instalments of 1/48 of the balance owing commencing December 1, 2018 with the remaining balance due at maturity. As part of the transaction, Quantius received an underwriting fee representing low single digit percentage of the maximum facility amount and will receive a royalty fee representing low single digit percentage on our revenues over the term of the facility, capped at a high single digit percentage of the borrowed amount. Under terms of the agreement, we will have the option to prepay the credit facility with the payment of low single digit prepayment penalties. The prepayment penalties will be fully offset against the royalty fee payable at the time of termination. The terms of the agreement also contain customary financial covenants. The Company was in compliance with the covenants as of December 31, 2017.

Interest and financing costs

Interest expense on long-term debt was $370 for the year ended December 31, 2017 ($700 for December 31, 2016).

Accrued interest & financing costs		
Balance, January 1, 2016	$	160
Interest and financing fees		1,179
Amortization of deferred financing costs		(424)
Interest paid		(686)
Effect of foreign currency exchange difference		27
Balance, December 31, 2016	$	256
Balance, January 1, 2017	$	256
Interest expense		380
Transaction costs		191
Amortization of deferred financing costs		(10)
Interest paid		(687)
Effect of foreign currency exchange difference		(31)
Balance, December 31, 2017	$	99

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

13. LONG-TERM DEBT (continued)

Future principal and interest payments

The Company has the following future payments of principal and interest concerning the debt:

		December 31, 2017
No later than 1 year	$	1,511
Later than 1 year and no later than 5 years		4,043
		5,554
Interest expense and other financing costs		806
Total principal portion of debt	$	4,748

14. DERIVATIVE FINANCIAL INSTRUMENT

The change in the Company's derivative financial instrument can be summarized as follows:

		December 31, 2017		December 31, 2016
Balance of warrants, January 1,		141		106
Change in fair value of the derivative financial instruments		156		37
Effect of foreign currency exchange difference		10		(2)
Balance of warrants	$	307	$	141

General Electric Capital Corporation warrants

In connection with a previous debt agreement, the lender was issued warrants exercisable for an aggregate of 154,916 common shares. The warrants were exercisable for a period of five years (until July 2017) at an exercise price of $1.4524. The warrant holder may also choose a cashless exercise, in which case the settlement price will then be calculated using the volume weighted average trading price of the Company's common shares on the Toronto Stock Exchange for the period of three days ending immediately prior to the date of exercise. On August 22, 2016, the holder irrevocably abandoned its warrants and accordingly the value of the warrants was expensed.

MidCap Financial V, LLC warrants

In accordance with the senior financing with MidCap entered into on July 16, 2014, the lenders have been issued warrants exercisable for an aggregate of 3,034,814 common shares of the Company. The warrants are exercisable for a period of seven years at an exercise price of CDN$0.7095, which was calculated using the volume weighted average trading price of the Company's common shares on the Toronto Stock Exchange for the period of five days ending immediately prior to the closing date of the senior financing. The warrant holder may also choose a cashless exercise, in which case the settlement price will then be calculated using the volume weighted average trading price of the Company's common shares on the Toronto Stock Exchange for the period of five days ending immediately prior to the date of exercise.

A pricing model with observable market-based inputs was used to estimate the fair value of the warrants issued. The variables used to compute the values as at December 31, 2017 were as follows: a share price of CDN$0.29; an expected life of 3.5 years; a risk-free rate of 1.63%; a volatility of 91%; and an exercise price of CDN$0.7095 (a share price of CDN$0.135; an expected life of 4.5 years; a risk-free rate of 0.60%; a volatility of 102%; an exercise price of CDN$0.7095 was used to compute the values at December 31, 2016). At December 31, 2017, the warrants had an average fair value of CDN$0.13 per warrant (CDN$0.06 per warrant at December 31, 2016).

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

14. DERIVATIVE FINANCIAL INSTRUMENT (continued)

Pre-payment option

As per note 13, under terms of the Credit Facility, the Company will have the option to prepay the Credit Facility. The prepayment penalties vary depending on the time frame and will be fully offset against the royalty fee payable at the time of termination. The prepayment option is considered to be an embedded derivative with a fair value of nil at the date of issuance and at December 31, 2017.

15. SHARE CAPITAL AND WARRANTS

Shares Issued and Outstanding

	Number		Value ($)		
	Commong shares	Warrants	Common shares	Warrants	Total
Balance as at January 1, 2016	200,873,234	51,639	$ 149,766	$ 37	$ 149,803
Private placement, April 27, 2016	12,245,411	-	2,000	-	2,000
Balance as at December 31, 2016	213,118,645	51,639	$ 151,766	$ 37	$ 151,803
Balance as at January 1, 2017	213,118,645	51,639	$ 151,766	$ 37	$ 151,803
Expiry of warrants, July 18, 2017	-	(51,639)	-	(37)	(37)
	213,118,645	-	$ 151,766	$ -	$ 151,766

The Company is authorized to issue an unlimited number of common shares.

In addition to the warrants in the table above, there are 3,034,814 (December 31, 2016 – 3,034,814) warrants issued that have been classified as a derivative financial instrument (note 14).

Acerus entered into a subscription agreement with Aytu pursuant to which Aytu acquired 12,245,411 common shares for gross cash proceeds of $2,000. This private placement was completed on April 27, 2016.

On July 18, 2017, a total of 51,639 warrants with a cumulative value of $37 and an exercise price of $1.4524 expired. A total of $37, which represents the cumulative value of the warrants, was transferred to contributed surplus.

16. NATURE OF EXPENSES

	For the year ended December 31, 2017			
	Cost of sales	R&D	SG&A	Total
Cost of finished goods	$ 960	$ -	$ -	$ 960
Royalty expense	201	-	-	201
Salaries and benefits	-	918	1,757	2,675
Severance	-	-	1,061	1,061
Amortization of intangible assets	1,547	234	-	1,781
Depreciation of property and equipment	135	32	97	264
Share-based compensation	-	72	517	589
Research and development	-	910	-	910
Selling and marketing	-	-	2,096	2,096
General and administrative	-	-	2,439	2,439
Other	420	-	-	420
	$ 3,263	$ 2,166	$ 7,967	$ 13,396

(All amounts expressed in thousands of U.S. dollars except per share amounts and unless otherwise stated)

16. NATURE OF EXPENSES (continued)

	For the year ended December 31, 2016			
	Cost of sales	R&D	SG&A	Total
Cost of finished goods	$ 1,103	$ -	$ -	$ 1,103
Royalty expense	1,451	-	-	1,451
Salaries and benefits	6	699	1,361	2,066
Severance	-	-	98	98
Amortization of intangible assets	1,515	296	-	1,811
Depreciation of property and equipment	135	167	95	397
Share-based compensation	-	58	216	274
Research and development	-	376	-	376
Selling and marketing	-	-	1,217	1,217
General and administrative	-	-	2,491	2,491
Other	243	-	-	243
	$ 4,453	$ 1,596	$ 5,478	$ 11,527

17. INTEREST AND OTHER FINANCING COSTS

	December 31, 2017	December 31, 2016
Interest expense on long-term debt	$ 370	$ 755
Amortization of deferred financing costs	10	424
	$ 380	$ 1,179

18. INCOME TAXES

In Barbados, the Acerus subsidiary is classified as an International Business Corporations ("IBC") where there is a sliding scale corporate tax rate with a ceiling rate of 2.5% on income up to BBD$10 million and a minimum floor rate of 0.25% when income exceeds BBD$30 million. The rate declines by 0.5% for each incremental BBD$10 million until the floor rate is achieved.

On November 6, 2017, ABI migrated jurisdiction of incorporation, corporate law residence, and tax residence from Barbados to Canada. APBI was officially dissolved on February 26, 2018.

The difference between the amount of the provision for income taxes and the amount computed by multiplying loss/income before taxes by the statutory Canadian and Barbados rates are reconciled as follows:

	For the year ended December 31,	
	2017	2016
Loss before income taxes	$ (8,667)	$ 11,419
Tax recovery at the Canadian corporate tax rate of 26.5% (2016 - 26.5%)	(2,297)	3,026
Benefit of previously unrecognized deferred tax asset		(145)
Tax effect of permanent differences (Canada)	2,672	83
Barbados losses for which no benefit is recognized	(52)	2
Corporate tax rate differential on Barbados losses	(5,437)	(4,256)
Unrecognized deferred tax benefits	5,190	1,590
Other tax credits	(29)	-
Tax expense recognized for the year	$ 47	$ 300

18. INCOME TAXES (continued)

At each balance sheet date, the Company assesses whether the realization of future tax benefits is sufficiently probable to recognize a deferred tax asset. This assessment requires the exercise of judgment, which includes a review of projected taxable income. The Company has not recognized the deferred tax assets, arising from accumulated losses carried forward from previous years, and the corresponding deferred tax recovery on the statements of loss/income and comprehensive loss/income.

In Canada, the Company also has a net operating loss carry forwards of $11,137 that will expire by 2037 ($3,591 in 2036 and $7,546 in 2037). The Company also has a capital loss of $21,221 that can be carried forward indefinitely.

In addition, the Company has the following deferred tax assets that are not recognized:

	As at December 31,	
	2017	2016
Property and equipment	19	13
Intangible assets	7,251	2,391
Financing costs	133	373
Licensing payments	2,146	889
R&D pools	538	295
Investment tax credits	448	27
Accruals	172	82
Unrealized foreign exchange	(12)	51
Capital loss carryforwards	2,812	278
Loss carry forwards	3,008	1,986
Total	16,515	6,385

19. EARNINGS/LOSS PER SHARE

The following table sets forth the computing of basic and diluted earnings/(loss) per share (share and per share amounts below are not in thousands):

	December 31, 2017	December 31, 2016
Numerator for basic and diluted (loss)/earnings per share available to common shareholders	$ (8,714)	$ 11,119
Denominator for basic (loss)/earnings per share	213,118,645	209,193,404
Denominator for diluted (loss)/earnings per share	213,118,645	210,479,254
Basic and diluted (loss)/earnings per share	$ (0.04)	$ 0.05

Weighted Average Common Shares Outstanding

		Weighted Average Shares	
	Total issued	Basic	Diluted
Balance, January 1, 2016	200,873,234	200,873,234	200,873,234
Incremental shares from assumed exercise	-	-	1,285,850
Private placement, April 27, 2016	12,245,411	8,320,170	8,320,170
Balance, December 31, 2016	213,118,645	209,193,404	210,479,254
Balance, December 31, 2017	213,118,645	213,118,645	213,118,645

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

20. SHARE BASED COMPENSATION

The Company has an incentive stock option plan that permits it to, from time to time, grant options to acquire common shares to its directors, officers, employees, consultants, and others, up to the maximum number of a "rolling" amount equal to 10% of the total shares issued and outstanding (21,311,864 options available as at December 31, 2017). The option exercise price must be equal to or greater than the market price of the Company's common shares at the date of grant.

The stock option plan also provides that:

- upon the surrender, termination, expiry or exercise of any options granted under the stock option plan, common shares subject to such options shall become available to satisfy future grants of options under the stock option plan; and

- a holder of an option may, rather than exercise such option, elect a cashless exercise of such option payable in common shares equaling the amount by which the value of an underlying share at that time exceeds the exercise price of such option or warrant to acquire such common share.

The Company uses the Black-Scholes option pricing model to price its options, which requires certain assumptions including the stock price volatility for a publicly held corporation.

						Black-scholes model variables			
Grant date	Number granted	Granted to	Exercise price (CDN$)	Life (Years)	Vesting periods (Years)	Risk free rate	Expected volatility	Expected dividend rate	Fair value per options (CDN$)
Mar 04, 2016	5,700,000	Employees & directors	$0.10	5	1-3	1.0%	86.0%	nil	$0.07
Aug 11, 2016	400,000	Employees & directors	$0.09	5	1-3	0.9%	96.0%	nil	$0.06
Aug 23, 2016	325,000	Employee	$0.13	5	3	0.9%	101.0%	nil	$0.14
Nov 04, 2016	500,000	Employee	$0.18	5	3	0.6%	99.0%	nil	$0.12
Mar 10, 2017	4,810,000	Employees & directors	$0.12	5	1-3	1.1%	98.2%	nil	$0.08
May 18, 2017	900,000	Employee	$0.13	5	3	1.8%	103.3%	nil	$0.09
Jun 01, 2017	500,000	Employee	$0.11	5	3	1.8%	95.7%	nil	$0.08
Jun 12, 2017	50,000	Employee	$0.11	5	1-3	1.8%	97.6%	nil	$0.08
Sep 18, 2017	425,000	Employees & directors	$0.11	5	1-3	1.8%	96.2%	nil	$0.08
Nov 09, 2017	3,235,000	Employees & directors	$0.12	3-5	0-3	1.6% 1.8%	93.4% 94.1%	nil	$0.08 $0.10
Nov 22, 2017	20,000	Employees	$0.17	5	3	1.8%	98.8%	nil	$0.15
Dec 06, 2017	200,000	Director	$0.36	5	1	1.8%	104.4%	nil	$0.28
Dec 11, 2017	35,000	Employee	$0.35	5	3	1.8%	107.8%	nil	$0.26

A forfeiture rate of 3% was used to estimate option expenses during the year. The Company recognized total share-based compensation expense of $589 for the year ended December 31, 2017 ($274 for the year ended December 31, 2016).

20. SHARE BASED COMPENSATION (continued)

The following table summarizes the activity under the Company's stock option plan (amounts in chart below are not in thousands):

	2017						
	Canadian Dollar Options			US Dollar Options			
	Number		Weighted average exercise price (CDN)		Number		Weighted average exercise price (USD)
Balance at January 1,	9,743,240	$	0.71		1,717,500	$	6.25
Granted	10,175,000		0.13		-		-
Expired	(1,725,040)		2.38		(1,717,500)		6.25
Forfeited	(877,000)		0.16		-		-
Balance at December 31, 2017	17,316,200	$	0.23		-		-
Options exercisable at December 31, 2017	4,830,529	$	0.46	$	-	$	-

	2016					
	Canadian Dollar Options			US Dollar Options		
	Number		Weighted average exercise price (CDN)	Number		Weighted average exercise price (USD)
Balance at January 1,	5,922,790	$	1.29	2,081,225	$	5.68
Granted	6,925,000		0.11	-		-
Expired	(400,000)		1.49	(343,475)		2.93
Forfeited	(2,704,550)		0.32	(20,250)		3.40
Balance at December 31, 2016	9,743,240	$	0.71	1,717,500	$	6.25

	Canadian Dollar Options outstanding as at December 31, 2017		
Exercise prices	Number outstanding	Weighted average remaining life in years	Number excercisable
\$0.09 to \$0.11	5,045,000	3.3	1,906,663
\$0.12 to \$0.18	9,290,000	3.9	474,333
\$0.35 to \$0.75	1,375,000	2.2	843,333
\$0.82 to \$0.91	1,606,200	0.7	1,606,200
	17,316,200	3.3	4,830,529

21. RELATED PARTY TRANSACTIONS

Details of the transactions between the Company, key management and other related parties are disclosed below:

Key management includes the Company's directors and executive officers. The remuneration of directors and key members of management and professional fees paid or payable to firms affiliated with the current directors and interim CEO for the year ended December 31, 2017 and 2016 were as follows:

	For the year ended			
		December 31, 2017		December 31, 2016
Short-term compensation of key management and directors	$	1,432	$	1,319
Termination benefits		1,061		98
Share-based compensation		550		261
Professional fees paid or payable to firms affiliated with directors & officers		116		12
	$	3,159	$	1,690

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

21. RELATED PARTY TRANSACTIONS (continued)

These transactions are in the normal course of operations.

Executive employment agreements allow for total additional payments of approximately $447 if a change in control occurs, $914 if all are terminated without cause, and $nil if all are terminated with cause.

As at December 31, 2017, Acerus held a $7,188 payable ($32,716 receivable and $4,000 payable as at December 31, 2016) to its wholly owned subsidiary ABI. During the year, APC forgave $18,268 of its receivable outstanding and the remaining balance was converted to equity of ABI. The payable is non-interest bearing, due on demand and eliminates upon consolidation except for the foreign exchange loss of $1,677 for the year ended December 31, 2017 (loss of $690 for the year ended December 31, 2016) that has been recorded in the consolidated statement of income loss.

22. COMMITMENTS AND CONTINGENCIES

(a) Operating lease commitments

The Company has operating leases for the right to use office and manufacturing and laboratory facilities in Canada. The Company also has operating leases for some office equipment. There are no other off-balance sheet arrangements.

The Company's Canadian entity entered into a lease agreement for a 10,000 sq. ft. facility that expires in June 2025.

		December 31, 2017
No later than 1 year	$	179
Later than 1 year and no later than 5 years		749
Later than 5 years		488
Total	$	1,416

(b) Milestone payments

Under certain research and development agreements, the Company may be required to make payments contingent upon the achievement of specific development, regulatory or commercial milestones on or before specific dates.

The Company may be required to make remaining milestone payments in the aggregate amount of $4,500 for Tefina™ and $8,000 for TriVair™ products. The Tefina™ milestone payments are due in two tranches: the first $2,000 upon the acceptance for filing by the FDA or by the European Medicines Agency of the first application for regulatory approval of the product; another $2,500 is due upon the first commercial sale of the product in the USA or in at least two major markets (whichever is earlier). With regards to the TriVair™ products, there is a milestone payment of $2,000 upon FDA approval for each product to a maximum of $8,000. As well, there is a cap on royalty payments of $25,000 per product.

The Company may be required to make minimum royalty payments as disclosed in notes 5(a) and 5(b).

22. COMMITMENTS AND CONTINGENCIES (continued)

(c) Guarantees

All directors and/or officers of the Company, and each of its various subsidiary entities, are indemnified by the Company for various items including, but not limited to, all costs to settle lawsuits or actions due to their association with the Company, subject to certain restrictions. The Company has purchased directors' and officers' liability insurance to mitigate the cost of any potential future lawsuits or actions to the directors and officers. The term of the indemnification is not explicitly defined but is limited to events for the period during which the indemnified party served as a director or officer of the applicable Acerus entity. The maximum amount of any potential future payment required to be made by the Company cannot be reasonably estimated but could have a material adverse effect on the Company.

In the normal course of business, the Company has entered into agreements that include indemnities in favour of third parties, such as purchase and sale agreements, confidentiality agreements, engagement letters with advisors and consultants, leasing contracts, license agreements, information technology agreements and various product and service agreements. These indemnification arrangements may require the applicable Acerus entity to compensate counterparties for losses incurred by the counterparties as a result of breaches in representations, covenants and warranties provided by the particular Acerus entity or as a result of litigation or other third-party claims or statutory sanctions that may be suffered by the counterparties as a consequence of the relevant transaction. In some instances, the terms of these indemnities are not explicitly defined. The applicable Acerus entity, whenever possible, tries to limit this potential liability within the particular agreement or contract, but due to the unpredictability of future events the maximum amount of any potential reimbursement required to be made by the Company or its subsidiary entities cannot be reasonably estimated, but could have a material adverse effect on the Company.

(d) Litigation

Shenk Litigation

Valeant Pharmaceuticals International, Inc. and Valeant International Bermuda ("Valeant") are defendants in Ontario Superior Court of Justice Action No. CV-11-438382, which claims a declaration that Valeant is contractually obligated to compensate the Plaintiff, Reiner Schenk ("Schenk") pursuant to the terms of a contract between Schenk and Biovail Corporation. The main action was commenced by Notice of Action issued on October 31, 2011 and a Statement of Claim was issued on December 14, 2011. Acerus Pharmaceuticals Corporation was named as one of the defendants in the main action, but the action was discontinued as against Acerus on December 14, 2011. On October 29, 2013, Valeant commenced a third-party claim against Acerus (among others) claiming contribution, indemnity and other relief over to the full extent that Valeant may be held liable to Schenk, and damages for breach of fiduciary duty, breach of contract and intentional interference with economic relations in any amount for which Valeant is found liable to Schenk. Acerus has defended the third-party claim, denying any liability to Valeant. The parties have almost concluded examinations for discovery. It is expected that a date for trial will be set in the next few weeks.

Melnyk Litigation

In April 2016, the Company was served with a statement of claim filed in the Ontario Superior Court of Justice by Mr. Eugene Melnyk against the Company, as well as its Chairman and President & Chief Executive Officer. The Company, together with the other named co-defendants, brought a motion to strike the action as disclosing no reasonable cause of action, which was scheduled to be heard on July 27, 2016. In response to this motion the plaintiff advised of his intention to bring a motion to convert the proceeding into a derivative action and to pursue a new action in his personal capacity seeking, among other things, damages in the amount of CDN$100 million for negligent and/or reckless and/or fraudulent misrepresentation (the "Personal Action"). As a result, the hearing date was vacated, and the Court scheduled Mr. Melnyk's motion to convert the action into a derivative action, seeking,

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

22. COMMITMENTS AND CONTINGENCIES (continued)

(d) Litigation (continued)

among other things, CDN$150 million in damages, for December 21, 2016. No further steps have occurred or have been scheduled with respect to the Personal Action. On December 21, 2016, the Honourable Mr. Justice Wilton-Siegel of the Ontario Superior Court of Justice heard the motion brought by Mr. Eugene Melnyk for leave to commence a derivative action in the name of the Company and Justice Wilton-Siegel dismissed the motion with written reasons to follow. On February 22, 2017, Justice Wilton-Siegel issued his written reasons dismissing Mr. Melnyk's claim with costs. On April 6, 2017, Mr. Eugene Melnyk served a Notice of Appeal to appeal the decision of Justice Wilton-Siegel to the Divisional Court of the Ontario Superior Court of Justice. The appeal was heard by the Divisional Court on February 26, 2018 and was dismissed in a decision released on March 1, 2018. On March 14, 2018, Mr. Melnyk delivered a notice of motion for leave to appeal the dismissal of the motion to convert the action to a derivative action to the Court of Appeal for Ontario.

23. FINANCIAL INSTRUMENTS

(a) Classification of financial instruments

Financial assets (liabilities) as at December 31, 2017 and 2016 are presented below:

December 31, 2017	Loans and receivables	Assets/ (liabilities) at FVTPL	Other financial liabilities	Total
Cash	$ 3,156	$ -	$ -	$ 3,156
Trade and other receivables	1,542	-	-	1,542
Licensing fee receivable	300	-	-	300
Accounts payable and accrued liabilities	-	-	(3,312)	(3,312)
Long-term debt payable	-	-	(4,569)	(4,569)
Derivative financial instrument	-	(307)	-	(307)
	$ 4,998	$ (307)	$ (7,881)	$ (3,190)

December 31, 2016	Loans and receivables	Assets/ (liabilities) at FVTPL	Other financial liabilities	Total
Cash	$ 5,199	$ -	$ -	$ 5,199
Trade and other receivables	1,059	-	-	1,059
Licensing fee receivable	4,150	-	-	4,150
Accounts payable and accrued liabilities	-	-	(3,322)	(3,322)
Long-term debt payable	-	-	(6,449)	(6,449)
Derivative financial instrument	-	(141)	-	(141)
	$ 10,408	$ (141)	$ (9,771)	$ 496

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

23. FINANCIAL INSTRUMENTS (continued)

(b) Fair value of financial instruments (continued)

Fair value is defined as the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is quoted bid or ask prices in an active market. Quoted prices are not always available for over-the-counter transactions, as well as transactions in inactive or illiquid markets. In these instances, pricing models, normally with observable market-based inputs, are used to estimate fair value. Financial instruments traded in a less active market have been valued using indicative market prices, present value or other valuation techniques. Where financial instruments trade in inactive markets or when using models where observable parameters do not exist, greater management judgement is required for valuation purposes. In addition, the calculation of estimated fair value is based on market conditions at a specific point in time and therefore may not be reflective of future fair values.

At December 31, 2017, the Company's financial instruments consisted of cash, trade and other receivables, licensing fee receivable, accounts payable and accrued liabilities, long-term debt, and derivative financial instruments. Cash, trade and other receivables, licensing fee receivable and accounts payable and accrued liabilities are measured at amortized cost and their fair values approximate carrying values due to their short-term nature. The derivative financial instruments are measured at fair value with any changes recognized through the consolidated statement of income/(loss) and comprehensive income/(loss) and are classified as Level 2. The fair value of the derivative financial instrument is estimated using a Black-Scholes pricing model. Assumptions used in the model are disclosed in note 14.

The long-term debt is measured at amortized cost. At December 31, 2017, the fair value of the long-term debt approximates its face value of $4,748. The fair values are based on cash flows discounted using a rate based on the borrowing rate and are within Level 3 of the fair value hierarchy.

(c) Financial risk management

The Company's financial instruments are exposed to certain financial risks, including currency risk, interest rate risk, credit risk and liquidity risk.

(i) Currency risk

The Company is exposed to currency risk related to the fluctuation of foreign exchange rates. The Company operates primarily in U.S. and Canadian dollars. The Company, however, is exposed to currency risk though its net financial assets denominated in US dollars and Euros of the parent.

	December 31, 2017		
	USD	EUR	GBP
Cash	$ 939	$ -	$ -
Trade and other receivables	415	-	-
Accounts payable and accrued liabilities*	(7,039)	(183)	(30)
Long-term debt	(2,357)	-	-
	$ (8,042)	$ (183)	$ (30)

*includes intercompany payable of $7,030

Based on the above net exposure at December 31, 2017, and assuming that all other variables remain constant, a 5% appreciation or depreciation of the US dollar against the other currencies would have resulted in the following impact on net income:

Net income effect:	U.S. Dollar			
	US	EUR	GBP	Total
Appreciate 5%	$ 383	$ (9)	$ (10)	$ 364
Depreciate 5%	(423)	9	10	(404)

23. FINANCIAL INSTRUMENTS (continued)

(c) Financial risk management (continued)

(ii) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has an interest rate of LIBOR + 9.5% per annum with a LIBOR floor rate of 1.0% for the promissory note and Bank of Canada prime rate plus 11.05% for the Quantius debt.

Due to the LIBOR floor, a 0.5% appreciation or depreciation in the present LIBOR rate would have a nil effect on interest expense. However, in the event that LIBOR exceeds 1.0% in the future, any appreciation or depreciation of LIBOR could impact the Company's interest expense.

A 0.5% increase or decrease in the Bank of Canada prime rate would have an immaterial impact on the Company's remaining interest expense.

(iii) Credit risk

Credit risk is the risk of a financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligation. Financial instruments that potentially expose the Company to significant concentrations of credit risk consist of cash, trade and other receivables and licensing fee receivable. The Company's investment policies are designed to mitigate the possibility of deterioration of principal, enhance the Company's ability to meet its liquidity needs and provide high returns within those parameters. Cash is on deposit with a Canadian chartered bank located in Canada and Barbados.

Management monitors the collectability of trade and other receivable and estimates an allowance for doubtful accounts. The Company has concentration risk, as approximately 38% of its trade receivables are due from three pharmaceutical wholesalers in Canada and 27% from an out-licensing partner. The Company received the full amount of the licensing fee receivable ($300) in February 2018.

As at December 31, 2017, the allowance for doubtful accounts was $nil. Management has not recognized an allowance for doubtful accounts because there has not been a significant change in credit quality and all amounts are considered recoverable.

(iv) Market risk

The change in fair value of the Company's derivative liability, which is measured at FVTPL, results from the periodic "mark-to-market" revaluation. The valuation is impacted, among other inputs, by the market price of the Company's common shares. As a result, the change in fair value of the derivative liability, which is reported through the consolidated statement of loss/income and comprehensive loss/income, has been and may continue in future periods to be materially affected most notably by changes in the Company's common share price.

Assuming that all other variables remain constant, a 5% appreciation or depreciation of the Company's share price would have resulted in an $28 decrease and $28 increase in net loss respectively ($13 increase and $13 decrease in net income at December 31, 2016).

(All amounts expressed in thousands of U.S. dollars except per share amounts
and unless otherwise stated)

23. FINANCIAL INSTRUMENTS (continued)

(c) Financial risk management (continued)

(v) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulties in meeting its financial liability obligations as they become due. The Company has a planning and budgeting process in place to help determine the funds required to support normal operating requirements on an ongoing basis. Since inception, the Company has financed its cash requirements primarily through issuances of securities, short-term borrowings, issuances of long-term debt (including convertible debt) and interest income and upfront licensing fees.

The Company controls liquidity risk through management of working capital, cash flows and the availability and sourcing of financing.

The following table summarizes the Company's significant contractual undiscounted cash flows as at December 31, 2017 and 2016:

	Less than 3 months	3-6 months	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Accounts payable and accrued liabilities	$ 2,423	$ 178	$ 356	$ 178	$ -	$ 3,134
Derivative financial instruments	-	-	-	-	307	307
Long-term debt (principal and interest)	365	360	786	3,553	490	5,554
As at December 31, 2017	$ 2,788	$ 538	$ 1,142	$ 3,731	$ 797	$ 8,995

	Less than 3 months	3-6 months	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Accounts payable and accrued liabilities	$ 3,322	$ -	$ -	$ -	$ -	$ 3,322
Derivative financial instruments	-	-	-	-	141	141
Long-term debt (principal and interest)	3,484	317	617	1,156	1,546	7,120
As at December 31, 2016	$ 6,806	$ 317	$ 617	$ 1,156	$ 1,687	$ 10,583

24. CAPITAL MANAGEMENT

The Company’s capital management objectives are to safeguard its ability to continue as a going concern and to provide returns for shareholders and benefits for other stakeholders. The Company does this by ensuring it has sufficient cash resources to fund its research and development activities, to pursue its eventual commercialization efforts and to maintain its ongoing operations. The Company includes the long-term debt and shareholders’ equity in the definition of capital.

A summary of the Company’s capital structure is as follows:

	December 31, 2017	December 31, 2016
Long-term debt	$ 4,569	$ 6,449
Shareholders' equity	5,916	12,201
	$ 10,485	$ 18,650

The Company continually evaluates alternatives to raise additional capital. These alternatives include seeking additional capital from existing shareholders and new shareholders, from the issuance of debt and by way of monetizing its technologies or development programs through commercial or partnering arrangements.

25. SEGMENT REPORTING

The Interim Chief Executive Officer and Chief Financial Officer are the Company's chief operating decision-makers (CODM). Management has determined that there is one operating segment based on the information reviewed by the CODM for the purposes of allocating resources and assessing performance.

At December 31, 2017, the Company has total long-term assets in Canada and Germany in the amounts of $13,202 and $846 respectively ($11,982, $998 and $2,332 respectively in Canada, Germany and Barbados at December 31, 2016).

For the year ended December 31, 2016 the Company had product revenues from customers located in Canada of $4,860 and licensing and product revenues from U.S., Bermuda, Korea, Germany, Brazil and Singapore of $1,455, $68, $12, $43, $5 and $6 respectively ($6,899 from customers located in Canada and $17,082, $506 and $1 in licensing and product revenues from Bermuda, U.S. and Korea for the year ended December 31, 2016).

26. SUBSEQUENT EVENTS

UriVarx®

On January 8, 2018 the Company entered into an exclusive distributor and license agreement with Innovus Pharmaceuticals, Inc. ("Innovus"), granting Acerus the exclusive rights to commercialize UriVarx® in Canada. Under the terms of the exclusive distributor and license agreement, the Company paid an upfront payment at signing and will pay milestone payments based on the Company achieving certain sales targets. Innovus will oversee the manufacturing of UriVarx® and will receive a supply price for the product.

Amendment to Endo Promissory Note

On March 15, 2018, the promissory note was amended such that principal repayments under the promissory note would now be made annually on the last business day of the month of December of each year instead of quarterly. Payments of interest will continue to be made quarterly.