

# **Theralase Technologies Inc.**

## **Condensed Interim Consolidated Financial Statements - Unaudited**

As at March 31, 2017 and for the three-month period ended March 31, 2017, 2016 and 2015

### **NOTICE OF NO AUDITOR REVIEW OF INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the interim financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed interim consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these condensed interim consolidated financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

# THERALASE® TECHNOLOGIES INC.

Consolidated Balance Sheets

As at March 31, 2017 and December 31, 2016

Stated in Canadian Dollars

	Note	2017	2016
<b>Assets</b>			
Current assets			
Cash and cash equivalents		\$ 1,598,322	\$ 2,970,198
Trade and other receivables	5	1,218,655	1,200,082
Inventories	6	1,163,602	1,215,753
Prepaid expenses and other assets		260,112	231,092
<b>Total current assets</b>		<b>4,240,691</b>	<b>5,617,125</b>
Non-Current assets			
Property and equipment	7	529,858	569,679
Intangible assets	8	50,751	53,979
<b>Total non-current assets</b>		<b>580,609</b>	<b>623,658</b>
<b>Total Assets</b>		<b>\$ 4,821,300</b>	<b>\$ 6,240,783</b>
<b>Liabilities</b>			
Current liabilities			
Payables and accruals	9	518,032	\$ 549,742
<b>Total liabilities</b>		<b>518,032</b>	<b>549,742</b>
<b>Equity attributable to shareholders</b>			
Share capital	10, 13	22,568,232	22,568,232
Common share purchase warrants	10, 12	3,596,395	3,596,395
Contributed surplus	11	5,398,592	5,314,181
Deficit		(27,259,951)	(25,787,767)
<b>Total Equity</b>		<b>4,303,268</b>	<b>5,691,041</b>
<b>Total Shareholders' Equity and Liabilities</b>		<b>\$ 4,821,300</b>	<b>\$ 6,240,783</b>

Commitments (Note 21)

Approved on Behalf of the Board

[Roger Dumoulin-White]

Director

[Guy Anderson]

Director

# THERALASE® TECHNOLOGIES INC.

Consolidated Statements of Operations

For the 3-month period ended March 31

Stated in Canadian Dollars

	Note	2017	2016	2015
Sales		\$ 507,428	\$ 411,448	\$ 368,304
Cost of Sales		207,237	131,764	135,156
Gross Margin		300,191	279,684	233,148
<b>Operating Expenses</b>				
Selling expenses	15	\$ 410,979	\$ 316,254	\$ 184,488
Administrative expenses	16	700,924	623,314	456,123
Research and development expenses	17	668,723	477,588	545,645
(Gain) Loss on foreign exchange		(7,519)	16,879	(15,228)
Interest expense		32	127	67
Interest income		(766)	(8,740)	(4,303)
		\$ 1,772,374	\$ 1,425,423	\$ 1,166,791
Loss for the year	14	\$ (1,472,184)	\$ (1,145,739)	\$ (933,643)
Basic and diluted loss per common share	14	\$ (0.014)	\$ (0.012)	\$ (0.012)
Weighted average number of common shares outstanding (basic and diluted)		109,035,634	95,957,158	74,979,539

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

# THERALASE® TECHNOLOGIES INC.

Consolidated Statements of Cash Flows  
For the 3-month period ended March 31  
Stated in Canadian Dollars

	Note	2017	2016	2015
<b>Cash flows from operating activities</b>				
Net loss for the period		\$ (1,472,184)	\$ (1,145,739)	\$ (933,643)
Items not involving cash				
Amortization of property and equipment	7	46,922	33,512	25,940
Amortization of intangibles	8	3,228	4,510	4,510
Stock-based compensation expense	11	84,411	151,435	120,553
Gain(loss) on foreign exchange		7,519	(16,879)	15,228
loss on sale of property and equipment			-	-
Lease inducements		(700)	(700)	(700)
		(1,330,803)	(973,860)	(768,112)
Change in operating assets and liabilities other than cash				
Trade and other receivables		(26,092)	544,644	72,193
Finance receivables		-	19,367	2,906
Inventories		52,151	(160,105)	(61,785)
Prepaid expenses and other assets		(28,320)	(48,786)	295,920
Payables and accruals		(31,710)	(81,219)	(52,113)
		(1,364,774)	(699,959)	(510,991)
<b>Cash flows from investing activities</b>				
Purchase of property and equipment	7	(7,101)	(31,820)	(76,351)
		(7,101)	(31,820)	(76,351)
<b>Cash flows from financing activities</b>				
Proceeds from public offering (net of issue costs)	10	-	-	6,990,896
Proceeds from the exercising of share warrants		-	-	210,000
		-	-	7,200,896
Increase in cash during the year		\$ (1,371,875)	\$ (731,779)	\$ 6,613,553
Cash, beginning of period		\$ 2,970,198	\$ 4,340,856	\$ 1,922,454
Cash, end of period		\$ 1,598,322	\$ 3,609,077	\$ 8,536,007
<b>Supplementary Information</b>				
Interest Paid		\$ 32	\$ 127	\$ 67
Interest Received		\$ 766	\$ 8,740	\$ 4,303

# THERALASE® TECHNOLOGIES INC.

Consolidated Statements of Changes in Equity

As at March 31, 2017, 2016 and 2015

Stated in Canadian Dollars

		Number of Shares	Share Capital	Contributed Surplus	Common Share Purchase Warrants	Deficit	Total Shareholders' Equity
	Note	#	\$	\$	\$	\$	\$
<b>Balance, December 31, 2014</b>		85,321,293	14,436,356	4,312,729	214,624	(15,658,375)	3,305,334
Stock-based compensation expense	11	-	-	120,553	-	-	120,553
Exercised share purchase warrants	12	1,050,000	260,109	-	(50,109)	-	210,000
Issued pursuant to public offering	10	18,181,817	5,357,144	-	2,642,588	-	7,999,732
Transaction cost on public offering		-	(717,566)	-	(291,270)	-	(1,008,836)
Loss for the year		-	-	-	-	(933,643)	(933,643)
<b>Balance, March 30, 2015</b>		104,553,110	19,336,043	4,433,282	2,515,833	(16,592,018)	9,693,140
<b>Balance, December 31, 2015</b>		107,047,360	19,967,937	4,822,699	2,392,342	(20,866,519)	6,316,459
Stock-based compensation expense	11	-	-	151,435	-	-	151,435
Loss for the period		-	-	-	-	(1,145,739)	(1,145,739)
<b>Balance, March 31, 2016</b>		107,047,360	19,967,937	4,974,134	2,392,342	(22,012,258)	5,322,154
<b>Balance, December 31, 2016</b>		121,284,026	22,568,232	5,314,181	3,596,395	(25,787,767)	5,691,041
Stock-based compensation expense	11	-	-	84,411	-	-	84,411
Loss for the year		-	-	-	-	(1,472,184)	(1,472,184)
<b>Balance, March 31, 2017</b>		121,284,026	22,568,232	5,398,592	3,596,395	(27,259,951)	4,303,268

# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

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### 1. Nature of Operations

Theralase Technologies Inc. (the “Company” or “Theralase”) has two main divisions.

The Therapeutic Laser Technology (“TLT”) division designs, develops, manufactures and markets patented and proprietary super-pulsed laser technology indicated and cleared by Health Canada and the Food and Drug Administration (“FDA”) for the healing of chronic knee pain. The technology has been used off-label for healing numerous nerve, muscle and joint conditions, including arthritis, osteoarthritis and wounds. The Photo Dynamic Therapy (“PDT”) division develops patented and patent pending drugs, called Photo Dynamic Compounds (“PDCs”) and activates them with proprietary and patent pending laser technology to destroy specifically targeted cancers and bacteria.

The Company develops products both internally and using the assistance of specialist external resources. Successful financing enables the commercialization of the Company’s current and future product offerings, which is further supported through the Company’s established network of direct sales and indirect distribution networks.

Theralase was incorporated by articles of incorporation in the province of Ontario in September, 2004. The Company’s common shares trade on the Toronto Stock Exchange Venture Exchange under the symbol TLT. The registered office is 1945 Queen Street East, Toronto, Ontario, M4L 1H7, Canada.

#### Statement of Compliance

The condensed interim consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and interpretations of the IFRS Interpretations Committee.

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34 “Interim Financial Reporting”. The interim consolidated financial statements do not include all the information and disclosures required in the Company’s annual financial statements and should be read in conjunction with the Company’s annual consolidated financial statements for the year ended December 31, 2016.

The condensed interim consolidated financial statements for the three-month period ended March 31, 2017 (including comparatives) were approved and authorized for issue by the board of directors on May 30, 2017.

### 2. Capital Disclosures

The Company’s objective is to maintain a sufficient capital base to support future research, development and strategic business initiatives allowing the Company to invest in its future and maintain investor, creditor and market confidence. The Company makes every attempt to manage its liquidity to minimize shareholder dilution when possible.

The Company’s capital is composed of total shareholders’ equity. For the three-month period ended March 31, 2017, the Company reported a loss of \$1,472,184, and an accumulated deficit of \$27,259,951 as at that date. Sales of the TLC-1000 and TLC-2000, the Company’s existing product lines have not met expectations and have not been sufficient in and of themselves to enable the Company to fund all its continuing development and commercialization efforts and, accordingly, management is pursuing alternate financing

# THERALASE<sup>®</sup> TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

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sources to fund the Company's development and commercialization efforts. The Company has successfully raised capital through equity offerings in 2015 and 2016 (note 10). Nevertheless, while there is no assurance that these initiatives will be successful, management believes that the Company has sufficient cash on hand to meet its operating and working capital needs for the next twelve months (see note 18i)

The Company is not subject to any externally imposed capital requirements and the company does not use financial ratios to manage capital. There were no changes in the Company's approach to capital management during the years presented.

### 3. Summary of Significant Accounting Policies

#### Basis of presentation

These condensed interim financial statements have been prepared on a historical basis. In addition, these financial statements have been prepared using the accrual basis of accounting.

#### Basis of consolidation

The condensed interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries; Theralase Inc. and Theralase Biotech Inc., over which the Company exercises control. Inter-company balances and transactions are eliminated in preparing the consolidated financial statements.

### 4. Accounting Standards Issued But Not Yet Applied

The IASB has issued the following standards which have not yet been adopted by the Company. The Company has not yet begun the process of assessing the impact that the new standards will have on its financial statements.

The following is a description of the new standards:

***IFRS 9, Financial Instruments*** ("*IFRS 9*") was issued in final form in July 2014 by the IASB and will replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 also includes requirements relating to a new hedge accounting model, which represents a substantial overhaul of hedge accounting which will allow entities to better reflect their risk management activities in the financial statements. The most significant improvements apply to those that hedge non-financial risk, and so these improvements are expected to be of particular interest to non-financial institutions. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted.

***IFRS 15, Revenue from contract with customers*** ("*IFRS 15*") was issued in May 2014 and specifies how and when revenue is recognised as well as provides users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers.

# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

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The core principle of IFRS 15 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to receive in exchange for those goods and services. IFRS 15 will require enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (particularly, service revenue and contract modifications) and improve guidance for multiple –element arrangements.

IFRS 15 is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted. The company has not yet assessed the impacts of adopting this standard on its consolidated financial statements.

**IFRS 16, Leases** (“IFRS 16”) was issued in January 2016 and specifies how to recognize, measure, present and disclose leases. The standard provides a single lease accounting model, requiring the recognition of assets and liabilities for all leases, unless the lease term is 12 months or less or the underlying asset has a low value. Lessor accounting however remains largely unchanged from IAS 17 and the distinction between operating and finance leases is retained. IFRS 16 is effective for annual periods beginning on or after January 1, 2019.

### 5. Trade and Other Receivables

	As at March 31, 2017	As at December 31, 2016
Trade Accounts Receivable (net amount)	\$ 558,587	\$ 567,725
Government Tax Credits Receivable	660,068	632,357
<b>Total</b>	<b>\$ 1,218,655</b>	<b>\$ 1,200,082</b>

Write offs of trade receivables for the three-month period ended March 31, 2017 amounted to \$nil which was previously provided for (2016 - \$nil). In addition, a direct write-off of \$nil was made during the year (2016 - \$nil). Refer to note 18 (i) for the continuity schedule of allowance for trade receivables.

Government tax credits receivable comprise research and development investment tax credits receivable from the federal government which relate to qualifiable research and development expenditures under the applicable tax laws.

The Company’s exposure to credit and currency risks related to trade and other receivables is presented in note 18.

### 6. Inventories

	As at March 31, 2017	As at December 31, 2016
Raw materials	\$ 706,913	\$ 694,862
Work-in-process	6,519	54,481
Finished goods	450,170	466,410
<b>Total</b>	<b>\$ 1,163,602</b>	<b>\$ 1,215,753</b>



# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

### 7. Property and Equipment

#### Cost

	Tools and Dies	Finance Lease Equipment	Computer Equipment	Furniture and Fixtures	Rental units (1)	Equipment	Leasehold Improvements	Total
Balance at January 1, 2015	\$ 39,653	\$ 2,595	\$ 118,745	\$ 97,107	\$ 25,248	\$ 143,023	\$ 217,767	\$ 644,138
Additions	148,168	-	32,629	15,959	2,900	48,840	-	248,496
Balance at December 31, 2015	\$ 187,821	\$ 2,595	\$ 151,374	\$ 113,066	\$ 28,148	\$ 191,863	\$ 217,767	\$ 892,634
Balance at January 1, 2016	\$ 187,821	\$ 2,595	\$ 151,374	\$ 113,066	\$ 28,148	\$ 191,863	\$ 217,767	\$ 892,634
Additions	10,850	-	151,304	29,281	89,467	5,140	10,170	296,212
Disposals	-	-	-	(6,357)	-	-	-	(6,357)
Balance at December 31, 2016	\$ 198,671	\$ 2,595	\$ 302,678	\$ 135,990	\$ 117,615	\$ 197,003	\$ 227,937	\$ 1,182,489
Balance at January 1, 2017	\$ 198,671	\$ 2,595	\$ 302,678	\$ 135,990	\$ 117,615	\$ 197,003	\$ 227,937	\$ 1,182,489
Additions	-	-	5,826	1,275	-	-	-	7,101
Balance at March 31, 2017	\$ 198,671	\$ 2,595	\$ 308,504	\$ 137,265	\$ 117,615	\$ 197,003	\$ 227,937	\$ 1,189,590

#### Depreciation

Balance at January 1, 2015	\$ 39,385	\$ 2,404	\$ 83,921	\$ 80,089	\$ 21,022	\$ 57,862	\$ 88,698	\$ 373,381
Depreciation for the year	18,905	125	13,898	3,979	1,282	28,264	47,577	114,030
Balance at December 31, 2015	\$ 58,290	\$ 2,529	\$ 97,819	\$ 84,068	\$ 22,304	\$ 86,126	\$ 136,275	\$ 487,411
Balance at January 1, 2016	\$ 58,290	\$ 2,529	\$ 97,819	\$ 84,068	\$ 22,304	\$ 86,126	\$ 136,275	\$ 487,411
Depreciation for the year	34,121	66	30,573	7,734	5,337	27,619	24,527	129,977
Disposals for the year	-	-	-	(4,578)	-	-	-	(4,578)
Balance at December 31, 2016	\$ 92,411	\$ 2,595	\$ 128,392	\$ 87,224	\$ 27,641	\$ 113,745	\$ 160,802	\$ 612,810
Balance at January 1, 2017	\$ 92,411	\$ 2,595	\$ 128,392	\$ 87,224	\$ 27,641	\$ 113,745	\$ 160,802	\$ 612,810
Depreciation for the year	6,550	-	13,001	2,426	4,846	5,133	14,966	46,922
Balance at March 31, 2017	\$ 98,961	\$ 2,595	\$ 141,393	\$ 89,650	\$ 32,487	\$ 118,878	\$ 175,768	\$ 659,732

#### Carrying Amounts

At December 31, 2015	\$129,531	\$66	\$53,555	\$28,998	\$5,843	\$105,737	\$81,492	\$405,223
At December 31, 2016	\$106,260	\$0	\$174,286	\$48,766	\$89,973	\$83,258	\$67,135	\$569,679
At December 31, 2016	\$99,710	\$0	\$167,111	\$47,615	\$85,127	\$78,125	\$52,169	\$529,858

(1) Rental units consist of TLC-1000 systems used in customer rentals, demonstrations and service loaners

# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

### 8. Intangible Assets

#### Cost

	Patents	Trademarks	Development Costs	FDA Clinical Study Costs(1)	Total
Balance at December 31, 2015	\$ 199,622	\$ 58,346	\$ 344,093	\$ 509,649	\$ 1,111,710
Balance at December 31, 2016	\$ 199,622	\$ 58,346	\$ 344,093	\$ 509,649	\$ 1,111,710
Balance at March 31, 2017	\$ 199,622	\$ 58,346	\$ 344,093	\$ 509,649	\$ 1,111,710

#### Amortization

Balance at January 1, 2015	\$ 119,327	\$ 44,376	\$ 344,093	\$ 509,649	\$ 1,017,445
Amortization for the year	17,533	3,434	-	-	20,967
Balance at December 31, 2015	\$ 136,860	\$ 47,809	\$ 344,093	\$ 509,649	\$ 1,038,411
Balance at January 1, 2016	\$ 136,860	\$ 47,809	\$ 344,093	\$ 509,649	\$ 1,038,411
Amortization for the year	15,889	3,431	-	-	19,320
Balance at December 31, 2016	\$ 152,749	\$ 51,240	\$ 344,093	\$ 509,649	\$ 1,057,731
Balance at January 1, 2016	\$ 152,749	\$ 51,240	\$ 344,093	\$ 509,649	\$ 1,057,731
Amortization for the year	2,370	858	-	-	3,228
Balance at December 31, 2016	\$ 155,119	\$ 52,098	\$ 344,093	\$ 509,649	\$ 1,060,959

#### Carrying Amounts

At December 31, 2015	\$ 80,295	\$ 13,970	\$ -	\$ -	\$ 94,265
At December 31, 2016	\$ 46,873	\$ 7,106	\$ -	\$ -	\$ 53,979
At March 31, 2017	\$ 62,762	\$ 10,537	\$ -	\$ -	\$ 50,751

(1) FDA clinical study costs consist of expenses incurred in conducting the clinical trial Laser Therapy Applications for Chronic Joint Pain used to obtain the FDA clearance in July 2005, which allows for the marketing and sale of the TLC-1000 product line into the US market.

### 9. Payables and Accruals

	As at March 31, 2017	As at December 31, 2016
Trade payables	\$ 230,745	\$ 311,905
Salaries, employment taxes, and benefits	65,994	65,994
Current portion of warranty liability	1,100	1,100
Audit fees and contract payments	220,193	170,743
<b>Total</b>	<b>\$ 518,032</b>	<b>\$ 549,742</b>

### 10. Public Offering

On March 3, 2015, the Company completed a financing by way of a public offering, where 18,181,817 units were issued at a price of \$0.44 per unit for gross proceeds of \$8,000,000. Each unit consisted of 1 common share and 1 non-transferable common share purchase warrant. Each whole warrant entitles the holder thereof to acquire 1 common share at a price of \$0.54, expiring on March 3, 2020. In connection with the offering, the Company incurred financing costs of \$1,053,871, of which \$997,852 was paid in cash and \$56,019 was paid through issuance of 890,123 broker warrants. Each broker warrant is exercisable into one common share at an exercise price of \$0.54 per share for a period of 60 months after the closing of the offering.

The purchase price of \$0.44 per unit was allocated between the common shares (\$0.30 per share) and common share purchase warrants (\$0.14 per warrant), based on their relative fair values. Management determined that the allocation of the net proceeds of \$6,946,129 was \$4,650,562 for the common shares issued and \$2,295,567 for the common share purchase warrants issued.

# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

The fair value of each common share purchase warrant granted was estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

	March 3, 2015
Expected volatility (based on historical share prices)	68.27%
Risk-free interest rate	0.81%
Expected life	5 Years
Expected dividends	\$nil
Strike price	\$0.54
Share price	\$0.395

### 11. Stock Options

The Company has a rolling stock option plan reserving for issue under this plan 10% (12,128,402 common shares) of the outstanding common shares at a purchase price not less than the fair market value of the

Company's stock at the grant date. Under the Company's stock option plan, the board of directors may grant, at its discretion, stock options to purchase common shares to certain employees, officers, directors and consultants of the Company. Terms and conditions of the stock option and vesting provisions are at the discretion of the board of directors.

A summary of stock options issued under the stock option plan for three-month period ended March 31, 2017 and years ended December 31, 2016 and 2015 is provided below.

	Common shares under option	Weighted average exercised price \$
Outstanding, December 31, 2014	5,095,000	0.50
Granted (1)	5,340,000	0.50
Forfeited (2)	(330,000)	0.50
Outstanding, December 31, 2015	10,105,000	0.50
Granted (3)	380,000	0.50
Forfeited (4)	(1,310,000)	0.50
Expired (5)	(1,765,000)	0.50
Outstanding, December 31, 2016	7,410,000	0.50
Forfeited (6)	(30,000)	0.50
<b>Outstanding, March 31, 2017</b>	<b>7,380,000</b>	<b>0.50</b>

1) On May 28, July 27, October 13 and November 2, 2016 options were granted to certain employees, board members, medical scientific and advisory board members and consultants of the Company totaling 5,340,000 for \$0.50 vesting in three tranches with tranches vesting in one year, two years and three years respectively and expiring five years from date of issue.

2) During 2016 a board member resigned from the employment of the Company and forfeited all non-vested options totaling 330,000.

3) On January 1, April 4, April 18, May 16 and November 2, 2016 options were granted to certain employees and consultants of the Company totaling 380,000 for \$0.50 vesting in three tranches with tranches vesting in one year, two years and three years respectively and expiring five years from date of issue.

4) During 2016, certain employees and consultants were terminated and/or resigned from the employment of the Company and forfeited all non-vested options totaling 1,310,000.

5) On October 25, 2016, certain stock options previously issued to employees and consultants expired.

6) During 2017 certain employees and consultants were terminated and/or resigned from the employment of the Company and forfeited all non-vested options totaling 1,310,000.

# THERALASE® TECHNOLOGIES INC.

## Notes to Consolidated Financial Statements

Three-month period ended March 31, 2017, 2016 & 2015

Stated in Canadian Dollars

The following table summarizes information on the stock options outstanding as at March 31, 2017:

Stock Options Outstanding			Stock Options Exercisable		
Stock Options Outstanding	Weighted Average Remaining Life (years)	Weighted Average Exercise Price \$	Stock Options Exercisable	Weighted Average Exercise Price \$	
2,420,000	2.3	\$ 0.50	1,613,333	0.50	
80,000	2.6	\$ 0.50	53,333	0.50	
4,460,000	3.2	\$ 0.50	1,486,667	0.50	
110,000	3.3	\$ 0.50	-	-	
50,000	3.5	\$ 0.50	-	-	
20,000	4.0	\$ 0.50	-	-	
10,000	4.1	\$ 0.50	-	-	
230,000	4.6	\$ 0.50	-	-	
<b>7,380,000</b>		<b>\$ 0.50</b>	<b>3,153,334</b>	<b>\$ 0.50</b>	

Under the stock option plan, the stock options vest over a three year period, commencing one year after the grant. As at March 31, 2017, 3,153,334 of the stock options were vested. All outstanding stock options as at March 31, 2017 will be fully vested by November 2, 2019.

Options to employees are measured at the fair value of the equity instruments granted on the grant date were measured using the following weighted average assumptions:

	2017	2016	2015
Risk-free interest rate	0.68%	0.68%	0.94%
Expected volatility*	63.28%	63.28%	78.88%
Expected life	5 years	5 years	5 years
Expected dividends	Nil	Nil	Nil
Weighted average grant date fair value	\$0.20	\$0.20	\$0.20
Weighted average exercise price	\$0.50	\$0.50	\$0.50
Forfeiture rate	28%	28%	28%

Options to non-employees are measured at the fair value of the equity instruments granted, as the fair market value of the services received cannot be reliably measured. The fair value of non-employee stock options was recalculated using the following assumptions:

	2017	2016	2015
Risk-free interest rate	0.87%	0.84%	0.81%
Expected volatility*	61.36%	71.07%	78.47%
Expected life	5 years	5 years	5 years
Expected dividends	Nil	Nil	Nil
Weighted average grant date fair value	\$0.24	\$0.24	\$0.20
Weighted average exercise price	\$0.50	\$0.50	\$0.50
Forfeiture rate	18%	18%	18%

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For the three- month period ended March 31, 2017, the Company recognized stock-based compensation expense of \$84,411 (2016 - \$151,435, 2015 - \$120,553) for stock options issued to directors, employees, medical scientific and advisory board, marketing and media relation consultants and business development consultants, of which \$78,220 is included in administrative expenses, \$(81) in selling expenses and \$6,272 is included in research and development expenses.

\*Based on historical volatility

### 12. Common Share Purchase Warrants

As at March 31, common share purchase warrants consisted of the following:

	Number outstanding	Weighted average exercised price \$	Fair value at date of grant \$
Outstanding, January 1, 2015	5,034,250	0.25	214,624
Issued with shares	19,071,940	0.54	2,351,587
Exercised (1)	(3,544,250)	0.20	(172,171)
Expired	(35,000)	0.20	(1,697)
Outstanding December 31, 2015	20,526,940	0.53	2,392,342
Issued with shares	14,763,599	0.38	1,204,053
Outstanding December 31, 2016	35,290,539	0.46	3,596,395
<b>Outstanding March 31, 2017</b>	<b>35,290,539</b>	<b>0.46</b>	<b>3,596,395</b>

1) During 2015, 3,544,250 warrants were exercised. The share price at the exercise date was \$0.20

The following table summarizes information on the common share purchase warrants outstanding for the three-month period ended March 31, 2017

Exercise Price	Outstanding Beginning of the Period	Expired During the Period	Exercised During the Period	Granted During the Period	Outstanding End of Period	Weighted Average Remaining Contractual Life (years)
\$0.38	1,455,000	-	-	-	1,455,000	0.04
\$0.54	19,071,940	-	-	-	19,071,940	3.16
\$0.38	14,763,599	-	-	-	14,763,599	4.61
	<b>35,290,539</b>	-	-	-	<b>35,290,539</b>	-

### 13. Share Capital

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

### 14. Loss Per Common Share

Basic loss per common share has been calculated based on the weighted average number of common shares outstanding during each of the years presented in the consolidated financial statements.

Stock options to purchase 7,380,000 (2016 – 10,035,000, 2015 – 5,095,000) common shares and common share purchase warrants totaling 35,290,539 (2016 – 20,526,940, 2015 – 23,029,523) were not included in the computation of diluted loss and comprehensive loss per common share due to their anti-dilutive nature.

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### 15. Selling Expenses

The following are expenses classified as selling expenses on the consolidated financial statements:

	2017	2016	2015
Sales salaries	\$ 273,308	\$ 198,153	\$ 102,785
Advertising	69,114	33,239	12,781
Commission	22,523	19,055	22,596
Travel	22,803	46,464	35,670
Stock based compensation	(81)	6,861	1,244
Amortization and depreciation allocation	23,312	12,482	9,412
<b>Total selling expenses</b>	<b>\$410,979</b>	<b>\$316,254</b>	<b>\$184,488</b>

### 16. Administrative Expenses

The following are expenses classified as administrative expenses on the consolidated financial statements:

	2017	2016	2015
Insurance	\$ 25,002	\$ 19,708	\$ 15,338
Professional fees	71,748	73,303	77,385
Rent	20,300	20,300	20,300
General and administrative expenses	221,139	134,532	115,462
Administrative salaries	254,430	220,400	139,437
Director and advisory fees	17,993	24,613	23,387
Stock based compensation	78,220	120,769	57,582
Amortization and depreciation allocation	12,092	9,688	7,232
<b>Total administrative expenses</b>	<b>\$700,924</b>	<b>\$623,314</b>	<b>\$456,123</b>

### 17. Research and Development Expenses

The following are expenses classified as research and development expenses on the consolidated financial statements:

	2017	2016	2015
Research and development (net of investment tax credit)	\$ 647,705	\$ 437,932	\$ 470,113
Stock based compensation	6,272	23,803	61,726
Amortization and depreciation allocation	14,746	15,853	13,806
<b>Total research and development expenses</b>	<b>\$668,723</b>	<b>\$477,588</b>	<b>\$545,645</b>

### 18. Financial Instruments – Fair Value and Risks

IFRS 7 - Financial Instruments: Disclosures establishes a fair value hierarchy that reflects the significance of inputs used in making fair value measurements as follows:

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

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

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

The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximate fair value due to the short-term maturities of these instruments

Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. As at March 31, 2017 and December 31, 2016, the Company's cash is categorized as Level 1. There were no financial instruments categorised as Level 2 or 3.

### i Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Company's accounts receivable. The amounts reported in the consolidated balance sheets are net of allowances for bad debts, estimated by the Company's management based on prior experience and its assessment of the current economic environment. The Company reviews its trade receivable accounts regularly and reduces amounts to their expected realizable values by adjusting the allowance for doubtful accounts when management determines that the account may not be fully collectible. The Company has adopted credit policies in an effort to minimize those risks. The carrying value of trade and other receivables represent the Company's maximum exposure to credit risk.

The following table reflects the balance and age of trade receivables as at March 31, 2017 and December 31, 2016:

	<u>March 31, 2017</u>	<u>December 31, 2016</u>
Trade and other receivables	\$ 558,587	\$ 567,725
Percentage outstanding more than 30 days	11%	16%
Percentage outstanding more than 120 days	12%	10%

The following table reflects the changes in the allowance for trade receivables the three month period ended March 31, 2017 and December 31, 2016:

	<u>March 31, 2017</u>	<u>December 31, 2016</u>
Allowance for trade receivables - beginning of period	\$ 139,627	\$ 139,627
Allowance recorded against current period sales	-	-
Adjustment based on collection experience	-	10,479
Amounts written off	-	(10,478)
<b>Allowance for trade receivables - end of period</b>	<b>\$ 139,627</b>	<b>\$ 139,627</b>

### ii Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company manages its liquidity risk by continuously monitoring forecasted and actual cash flows,

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as well as anticipated investing and financing activities. The Company does not have material long-term financial liabilities.

The table below reflects the contractual obligations of the Company's undiscounted cash flows for its financial liabilities:

Contractual Obligations	Payments Due by Period		
	Total	2017	2018
Payables and accruals	\$ 518,032	\$ 518,032	\$ -
Commitments	\$ 155,724	\$ 115,183	\$ 19,541
Total contractual obligations	\$ 673,756	\$ 633,215	\$ 19,541

The Company also has contractual obligations (note 21) in the form of lease obligations related to the Company's premises and research and development commitments.

### iii Interest rate risk

Interest rate risk is the risk that changes in interest rates will affect the Company's income or the value of the financial instruments held.

The Company is subject to interest rate risk on its cash; however, it does not expect a movement in interest rates to have a significant impact on the Company's financial position.

### iv Foreign currency exchange risk

The Company is exposed to foreign currency exchange risk. This risk arises from the Company's holdings of US dollar denominated cash, trade and other receivables and payables and accrued liabilities. Changes arising from this risk could impact the Company's reported foreign currency exchange gains or losses.

Accounts exposed to foreign currency exchange risk as at March 31 2017 and December 31, 2016 are as follows:

	March 31, 2017	December 31, 2016
Cash	\$ 26,940	\$ 50,977
Trade and other receivables	159,727	131,159
Payables and accruals	(63,821)	(112,979)
<b>Total</b>	<b>\$ 122,846</b>	<b>\$ 69,157</b>

The above US dollar balances are shown in Canadian dollar equivalents.

### v Foreign currency exchange risk sensitivity analysis

The following table details the Company's sensitivity analysis to a 10% strengthening in the US dollar on foreign currency denominated monetary items and adjusts its translation at the consolidated balance sheet dates for a 10% change in foreign currency exchange rates. For a 10% weakening of the US dollar



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against the Canadian dollar, there would be an equal and opposite impact on loss and comprehensive loss for the year.

	March 31, 2017	December 31, 2016
Cash	\$ 2,694	\$ 5,098
Trade and other receivables	15,973	13,116
Payables and accruals	(6,382)	(11,298)
<b>Total</b>	<b>\$ 12,285</b>	<b>\$ 6,916</b>

### 19. Related Party Disclosure

The compensation of the directors and other key management of the Company are included in the summary table below. Key management includes those persons having authority and responsibility for planning, directing and controlling the activities, directly or indirectly, of the Company.

	2017	2016	2015
Short-term compensation	\$175,000	\$125,000	\$87,500
Stock-based compensation	59,732	106,469	60,792
<b>Total</b>	<b>\$234,732</b>	<b>\$231,469</b>	<b>\$148,292</b>

Key management personnel were not paid post-employment benefits, termination benefits or other long term benefits during the three-month period ended March 31, 2017, 2016 and 2015. Fees paid to directors have been disclosed in note 16.

Stock-based compensation made to directors and officers are the fair value of options that vested to key management personnel during the year.

### 20. Segmented Information

For management purposes, the Company is organized into two separate reportable operating divisions; (1) Therapeutic Laser Technology (TLT) division and (2) Photo Dynamic Therapy (PDT) division. The TLT division is responsible for all aspects of the Company's therapeutic laser business, which manufactures products used by healthcare practitioners predominantly for the healing of pain. The PDT division is responsible for the research and development of Photo Dynamic Compounds (PDCs) for the destruction of primarily cancer.

The following table displays revenue and direct expenses from the TLT and PDT division for the three-month period ended March 31:

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	2017			2016			2015		
	TLT	PDT	Total	TLT	PDT	Total	TLT	PDT	Total
Sales	\$ 507,428	\$ -	\$ 507,428	\$ 411,448	\$ -	\$ 411,448	\$ 368,304	\$ -	\$ 368,304
Cost of Sales	207,237	-	207,237	131,764	-	131,764	135,156	-	135,156
Gross Margin	300,191	-	300,191	279,684	-	279,684	233,148	-	233,148
<b>Operating Expenses</b>									
Selling expenses	410,979	-	410,979	316,254	-	316,254	184,488	-	184,488
Administrative expenses	469,420	231,504	700,924	268,958	354,356	623,314	250,105	206,018	456,123
Research and development expenses	199,276	469,447	668,723	-	477,588	477,588	200,117	345,528	545,645
(Gain) loss on foreign exchange	(3,760)	(3,760)	(7,519)	8,440	8,440	16,880	(15,228)	-	(15,228)
Interest expense	16	16	32	64	64	127	34	34	68
Interest income	(766)	-	(766)	(8,740)	-	(8,740)	(4,303)	-	(4,303)
	1,075,166	697,207	1,772,374	584,974	840,448	1,425,422	615,212	551,581	1,166,792
Loss for the period	\$ (774,975)	\$ (697,207)	\$ (1,472,184)	\$ (305,291)	\$ (840,448)	\$ (1,145,739)	\$ (382,064)	\$ (551,581)	\$ (933,644)
Total Assets	\$ 4,532,537	\$ 288,763	\$ 4,821,300	\$ 5,599,229	\$ 356,914	\$ 5,956,142	\$ 9,382,999	\$ 334,306	\$ 10,167,305
Total Liabilities	389,683	128,349	518,032	342,614	361,831	704,445	283,551	176,086	459,637

The following table displays revenue and direct expenses from TLT division product sales by geographic area for the three-month periods ended March 31:

	2017			2016			2015		
	Canada	USA	International	Canada	USA	International	Canada	USA	International
Sales	\$ 322,186	\$ 141,714	\$ 43,528	\$ 180,069	\$ 152,375	\$ 79,004	\$ 344,351	\$ 8,369	\$ 15,584
Cost of Sales	131,583	57,877	17,777	51,290	45,713	34,762	126,342	3,071	5,743
Selling Expenses	323,619	87,360	-	177,700	128,022	10,532	183,051	502	935
	\$ (133,016)	\$ (3,523)	\$ 25,751	\$ (48,921)	\$ (21,360)	\$ 33,710	\$ 34,958	\$ 4,796	\$ 8,906

As at December 31, 2016, 2015 and 2014, the Company's long-lived assets used in operations are all located in Canada.

## 21. Commitments

The Company's commitments consist of the following:

	Total	2017	2018
Lease obligations (a)	\$ 49,000	\$ 28,000	
Lease obligations (b)	2,004	1,503	501
Research Agreement (c)	104,720	85,680	19,040
<b>Total</b>	<b>\$ 155,724</b>	<b>\$ 115,183</b>	<b>\$ 19,541</b>

- Lease obligations under a lease agreement related to the Company's premises, commenced on August 1, 2012 and expires on July 31, 2017. Under the terms of this lease, the Company is required to pay a proportionate share of operating costs, realty taxes and utilities, in addition to the minimum rental payments. The future minimum lease payments are shown in the table above.
- Lease obligations under a lease agreement related to the Company's office equipment, commenced on April 1, 2014 and expires on May 1, 2018. Under the terms of this lease, the Company is required to minimum rental payments of \$167 per month. The future minimum lease payments are shown in the table above.
- Research Commitments under a research collaboration agreement with University Health Network

# THERALASE<sup>®</sup> TECHNOLOGIES INC.

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for the TLC-3000 cancer therapy project. Under the terms of this agreement, the Company is required to pay \$156,240 for the period from March 1, 2017 through to February 28, 2018. The Company has paid \$51,520 relating to this commitment, in which \$104,720 is the remaining commitment.

The Company indemnifies its directors and officers against any and all costs, charges and expenses, including settlements of claims in respect of any civil, criminal or administrative action incurred in the performance of their service to the company to the extent permitted by law. The Company maintains liability insurance for its officers and directors.

## 22. Subsequent Events

On April 13, 2017, the Company received cash proceeds of \$369,550 from the exercise of 972,501 warrants to purchase common shares.

On April 18, 2017, the Company granted an aggregate of 2,800,000 options to purchase common stock to directors, officers and employees with an exercise price of \$0.50, a vesting period of 3 years and a term of 5 years.

On April 26, 2017, the Company received cash proceeds of \$168,750 from the exercise of 450,000 warrants to purchase common shares.

On May 15, 2017, the Company received cash proceeds of \$562,500 from the exercise of 1,500,000 warrants to purchase common shares.