Cipher Pharmaceuticals Inc.

Interim Condensed Consolidated Financial Statements

For the Three and Nine Months Ended September 30, 2017

(Unaudited)

Cipher Pharmaceuticals Inc.
Interim Consolidated Statements of Financial Position

As at September 30, 2017 and December 31, 2016
(in thousands of United States dollars - unaudited)

	Note	2017	2016
		$	$
ASSETS			
Current assets			
Cash	3, 4	**24,342**	34,486
Accounts receivable		**17,400**	14,644
Inventory		**700**	1,272
Prepaid expenses and other assets	3	**1,818**	1,767
		44,260	52,169
Property and equipment, net	3	**297**	790
Intangible assets, net	3, 5	**5,601**	17,582
Other receivable	3	**1,700**	-
Deferred tax assets	9	**4,644**	6,864
Total assets		**56,502**	77,405
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities	3	**13,910**	16,003
Provisions	3	**2,100**	4,769
Current portion of deferred revenue		**177**	176
		16,187	20,948
Deferred revenue		**357**	487
Senior secured notes	4	**19,724**	36,377
Derivative financial instrument	4	**495**	583
Other long term liabilities	3	**697**	996
Total liabilities		**37,460**	59,391
SHAREHOLDERS' EQUITY			
Share capital	6	**17,929**	16,192
Contributed surplus		**4,731**	6,024
Accumulated other comprehensive loss		**(9,514)**	(9,514)
Retained earnings		**5,896**	5,312
Total shareholders' equity		**19,042**	18,014
Total liabilities and shareholders' equity		**56,502**	77,405

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

Cipher Pharmaceuticals Inc.

Interim Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)

Three and nine month periods ended September 30, 2017 and 2016
(in thousands of United States dollars, except per share data - unaudited)

	Note	Three months ended September 30 2017	Three months ended September 30 2016	Nine months ended September 30 2017	Nine months ended September 30 2016
		$	$	**$**	$
Revenues					
Licensing revenue	11	**8,851**	6,811	**24,369**	20,203
Product revenue		**1,239**	1,000	**3,779**	3,039
Net revenues		**10,090**	7,811	**28,148**	23,242
Operating expenses					
Cost of products sold		**395**	360	**1,210**	1,027
Research and development		**117**	74	**286**	460
Selling, general and administrative	7	**3,326**	4,069	**9,329**	12,189
Total operating expenses		**3,838**	4,503	**10,825**	13,676
Other expenses (income)					
Interest on senior secured notes	4	**631**	1,858	**2,707**	6,334
Change in fair value of derivative financial instrument	4	**(82)**	(1,122)	**(88)**	(996)
Interest income		**-**	(4)	**(5)**	(52)
Loss on debt extinguishment	4	**-**	-	**5,223**	-
Impairment of intangible assets	5	**561**	-	**561**	-
Foreign exchange gain (loss)		**(34)**	27	**(93)**	(907)
Total other expenses		**1,076**	759	**8,305**	4,379
Income before income taxes from continuing operations		**5,176**	2,549	**9,018**	5,187
Income taxes	9	**1,253**	327	**2,220**	949
Income and comprehensive income from continuing operations		**3,923**	2,222	**6,798**	4,238
Loss and comprehensive loss from discontinued operations	3	**(1,184)**	(24,010)	**(6,214)**	(32,091)
Income (loss) and comprehensive income (loss) for the period		**2,739**	(21,788)	**584**	(27,853)
Income from continuing operations per common share	10				
Basic		**0.15**	0.08	**0.26**	0.16
Diluted		**0.15**	0.08	**0.25**	0.16
Loss from discontinued operations per common share	10				
Basic		**(0.05)**	(0.89)	**(0.23)**	(1.22)
Diluted		**(0.05)**	(0.89)	**(0.23)**	(1.22)
Income (loss) and comprehensive income (loss) per common share	10				
Basic		**0.10**	(0.81)	**0.03**	(1.06)
Diluted		**0.10**	(0.81)	**0.02**	(1.06)

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

Cipher Pharmaceuticals Inc.
Interim Consolidated Statements of Changes in Shareholders' Equity

Nine month periods ended September 30, 2017 and 2016
(in thousands of United States dollars - unaudited)

	Note	Share Capital		Contributed Surplus	Accumulated Other Comprehensive Loss	Retained Earnings	Total Shareholders' Equity
		000's	$	$	$	$	$
Balance, January 1, 2017		26,313	16,192	6,024	(9,514)	5,312	18,014
Income for the period		-	-	-	-	584	584
Exercise of stock options	6	278	1,264	(724)	-	-	540
Shares issued under the share purchase plan	6	25	96	-	-	-	96
Shares issued under the RSU plan	6	73	377	(377)	-	-	-
Share-based compensation expense	6	-	-	(192)	-	-	(192)
Balance, September 30, 2017		**26,689**	**17,929**	**4,731**	**(9,514)**	**5,896**	**19,042**
Balance, January 1, 2016		26,058	14,947	4,363	(9,514)	44,461	54,257
Loss for the period		-	-	-	-	(27,853)	(27,853)
Exercise of stock options	6	116	521	(253)	-	-	268
Shares issued under the share purchase plan	6	83	395	-	-	-	395
Shares issued under the RSU plan	6	36	266	(266)	-	-	-
Share-based compensation expense	6	-	-	2,326	-	-	2,326
Balance, September 30, 2016		26,293	16,129	6,170	(9,514)	16,608	29,393

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Cipher Pharmaceuticals Inc.
Interim Consolidated Statements of Cash Flows

Nine months period ended September 30, 2017 and 2016
(in thousands of United States dollars - unaudited)

	Note	2017	2016
		$	$
Operating activities			
Income for the period from continuing operations		**6,798**	4,238
Items not affecting cash:			
Depreciation of property and equipment		**97**	80
Amortization of intangible assets		**631**	799
Impairment of intangible assets	5	**561**	-
Share-based compensation		**321**	1,580
Foreign exchange (gain) loss on cash		**70**	(55)
Change in fair value of derivative		**(88)**	(996)
Loss on debt extinguishment	4	**5,223**	-
Interest on senior secured notes	4	**2,707**	6,334
Deferred income taxes		**2,220**	949
Changes in non-cash operating items:			
Accounts receivable		**(5,198)**	(503)
Inventory		**75**	(524)
Prepaid expenses and other assets		**(35)**	315
Accounts payable and accrued liabilities		**(446)**	832
Deferred revenue		**(129)**	(356)
Net cash provided by operating activities		**12,807**	12,693
Investing activities			
Purchase of property and equipment		**(39)**	(29)
Acquisition of intangible assets		**-**	(74)
Milestone payments related to intangible assets		**(148)**	-
Net cash received from disposal of assets	3	**7,619**	-
Net cash provided by (used in) investing activities		**7,432**	(103)
Financing activities			
Interest payments		**(2,083)**	(3,121)
Repayment of senior secured notes	4	**(20,000)**	-
Financing costs	4	**(2,500)**	-
Payment of finance lease liability		**(35)**	(20)
Proceeds from shares issued under the share purchase plan		**81**	336
Proceeds from exercise of stock options		**540**	268
Net cash used in financing activities		**(23,997)**	(2,537)
Cash used in discontinued operations	3	**(6,316)**	(6,690)
(Decrease) increase in cash		**(10,074)**	3,363
Impact of foreign exchange on cash		**(70)**	55
Cash, beginning of period		**34,486**	27,182
Cash, end of period		**24,342**	30,600

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

1. NATURE OF OPERATIONS

Cipher Pharmaceuticals Inc. ("Cipher") and its subsidiaries (together the "Company") is a specialty pharmaceutical company with a diversified portfolio of commercial and early to late stage products. The Company acquires products that fulfill unmet medical needs, manages the required clinical development and regulatory approval process, and markets those products either directly in Canada and the United States ("U.S.") or indirectly through partners in the U.S., Canada and South America. The Company is building its business through product licensing and acquisitions. Cipher was incorporated under the Business Corporations Act of Ontario on January 9, 2004 and is located at 2345 Argentia Road, Mississauga, Ontario.

On May 1, 2017, the Company sold its U.S. assets related to Innocutis Holdings LLC and no longer directly markets in the U.S.

2. BASIS OF PREPARATION

These interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. These interim condensed consolidated financial statements should be read in conjunction with the Company's annual consolidated financial statements for the year ended December 31, 2016, which were prepared in accordance with IFRS as issued by the IASB and are available on SEDAR at www.sedar.com. The Board of Directors approved these interim condensed consolidated financial statements on November 2, 2017.

Reclassification of comparative period presentation

Certain prior year amounts have been reclassified for consistency with the current period presentation. These reclassifications had no effect on the reported results of operations, only classifications of certain operating expenses. Specifically, selling and marketing have been combined with general and administrative (G&A), which is now reflected in selling, general and administrative (“SG&A”). In addition, foreign exchange gains have been reclassified from SG&A (formerly G&A) expenses to other expenses (income) and amortization of intangible assets has been reclassified to SG&A in order to better present the consolidated statements of income (loss) and comprehensive income (loss) by function.

Discontinued operations

The Company reports financial results for discontinued operations separately from continuing operations to distinguish the financial impact of disposal transactions from ongoing operations. Discontinued operations reporting occurs when the disposal of a component or a group of components of the Company represents a strategic shift that will have major impact on the Company’s operations and financial results, and where the operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the Company.

The results of discontinued operations are excluded from both continuing operations and business segment information in the interim condensed consolidated financial statements and the notes to the interim condensed consolidated financial statements, unless otherwise noted, and are presented net of tax in the statement of income (loss) and comprehensive income (loss) for the current and comparative periods. Refer to Note 3 Discontinued Operations.

Fair value of financial instruments

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.

As at September 30, 2017, the Company’s financial instruments consisted of cash, accounts receivable, accounts payable and accrued liabilities, the Senior Secured Notes (the “Notes”) and the derivative financial instrument. The derivative financial instrument is measured at fair value with any changes recognized through the consolidated statements of income (loss) and comprehensive income (loss) and is classified as Level 2 (as defined under IFRS). Cash, accounts receivable, accounts payable and accrued liabilities are measured at amortized cost and their fair values approximate carrying values.

The Notes are measured at amortized cost. At September 30, 2017, the fair value of the remaining Notes approximates its carrying value. The fair value is based on cash flows discounted using a rate based on the borrowing rate.

Accounting standards issued but not yet adopted

IFRS 15, Revenue from Contracts with Customers: This standard replaces International Accounting Standards ("IAS") 11 *Construction Contracts*, IAS 18, *Revenue* and IFRIC 13, *Customer Loyalty Programmes* and was issued in May 2014. This standard outlines a single comprehensive model for entities to account for revenue arising from contracts with customers. The latest date of mandatory implementation of IFRS 15 is for annual reporting periods beginning on or after January 1, 2018. The Company has determined the impact of adopting this standard on its licensing revenue as certain milestone payments which were previously deferred and amortized over a relevant period, will be recognized at the point-in-time of transfer of control to the customer. The Company in the process of quantifying the impact to the consolidated financial statements. Additionally, the Company is still assessing whether it will continue to be considered an agent in its relationship with Galephar under IFRS 15. A change in this determination, if required will result in the Company reporting its revenue on a gross basis rather than net. The Company will adopt this accounting standard on January 1, 2018, using the full retrospective approach. The adoption of IFRS 15 has no material impact on the Company's product revenue.

IFRS 9, Financial Instruments: The final version of IFRS 9, *Financial Instruments*, was issued by the IASB in July 2014 and will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 introduces a model for classification and measurement, a single, forward-looking 'expected loss' impairment model and a substantially reformed approach to hedge accounting. The new single, principle based approach for determining the classification of financial assets is driven by cash flow characteristics and the business model in which an asset is held. The new model also results in a single impairment model being applied to all financial instruments, which will require more timely recognition of expected credit losses. It also includes changes in respect of own credit risk in measuring liabilities elected to be measured at fair value, so that gains caused by the deterioration of an entity's own credit risk on such liabilities are no longer recognized in profit or loss. IFRS 9 is effective for annual reporting periods beginning on or after January 1, 2018, however is available for early adoption. The Company is in the process of evaluating the impact on the consolidated financial statements.

IFRS 16, Leases: In January 2016, the IASB published a new standard, IFRS 16. The new standard will eliminate the distinction between operating and finance leases and will bring most leases on the balance sheet for lessees. This standard is effective for annual reporting periods beginning on or after January 1, 2019. The Company has determined that all its leases except for its low value leases will be recorded on the consolidated statements of financial position upon adoption.

IFRS 2, Share-based Payment: In June 2016, the IASB issued final amendments to IFRS 2, clarifying how to account for certain types of share- based payment transactions. The amendments, which were developed through the IFRS Interpretations Committee, provide requirements on the accounting for: (i) the effect of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; (ii) share-based payment transactions with a net settlement feature for withholding tax obligations; and (iii) a modification to the terms and conditions of a share-based payment that changes the classifications of the transaction from cash-settled to equity-settled. The amendments are effective for annual reporting periods beginning on or after January 1, 2018. The Company does not expect these amendments to have a material impact on the consolidated financial statements upon adoption.

Other accounting standards or amendments to existing accounting standards that have been issued, but have future effective dates, are either not applicable or are not expected to have a significant impact on the Company's consolidated financial statements.

3. DISCONTINUED OPERATIONS

On May 1, 2017, the Company entered into an Asset Purchase Agreement (the "U.S. APA") and completed the sale of substantially all of the assets comprising the U.S. segment. In accordance with the terms of the U.S. APA, the purchase price of $13,600 is subject to customary working capital adjustments and other transferred liabilities as defined in the U.S. APA**.** The Company retained responsibility for certain liabilities and commitments. On closing, the Company received $7,619 in cash.

The terms of the U.S. APA, include a hold back of $1,700, which will be settled 18 months from the date of closing and an additional regulatory milestone of $750 if certain predefined conditions are achieved. The hold back of $1,700 is classified as a non-current asset in the interim consolidated statements of financial position. As at September 30, 2017, the predefined conditions which would trigger the recognition of the regulatory milestone of $750 were not achieved.

During the quarter, the working capital adjustments were finalized. The following table summarizes the assets and liabilities disposed of and the calculation of the gain on sale after these adjustments:

(in thousands of United States dollars, except per share amounts)

	$
Purchase price	13,600
Less: contractual working capital adjustment	(2,801)
Cash consideration	10,799
Working capital, net	1,019
Property and equipment, net	(100)
Intangible assets, net	(10,385)
Transaction costs	(1,000)
Gain on disposal	**333**

The following table summarizes the balances retained by the Company as at September 30, 2017, which are included in the interim consolidated statements of financial position:

	$
Accounts payable and accrued liabilities	1,561
Provisions	2,100
Other long term liabilities	616
Total	4,277

Accounts payable and accrued liabilities and other long term liabilities includes provisions for onerous contracts, and amounts due to former customers and vendors. Provisions reflects product returns that were retained by the Company. Prepaids and other assets includes a working capital adjustment of $1,047 to reflect a reduction in liabilities assumed on day of closing, which is outstanding from the buyer as at September 30, 2017. During the quarter, the Company received $433, which was attributable to the working capital adjustment.

A reconciliation of the major classes of line items constituting income from discontinued operations, net of tax, as presented in the consolidated statements of income (loss) and comprehensive income (loss) is as follows:

	Three months ended Sept 30, 2017	Three months ended Sept 30, 2016	**Nine months ended Sept 30, 2017**	Nine months ended Sept 30, 2016
	$	$	**$**	$
Net revenues	**(584)**	1,455	**2,347**	6,816
Operating expenses	**568**	25,465	**8,894**	38,907
Loss before gain on disposal	**1,152**	24,010	**6,547**	32,091
Loss (gain) on disposal	**32**	-	**(333)**	-
Loss before income taxes	**1,184**	24,010	**6,214**	32,091
Income taxes	**-**	-	**-**	-
Loss and comprehensive loss from discontinued operations	**1,184**	24,010	**6,214**	32,091

Included in the three and nine months ending September 30, 2016 are impairment charges relating to goodwill and intangible assets in the amount of $2,277 and $17,285, respectively.

(in thousands of United States dollars, except per share amounts)

Disclosures with respect to the consolidated statements of cash flows are as follows:

	Nine months ended Sept 30, 2017	Nine months ended Sept 30, 2016
	$	$
Net cash flows attributable to:		
Operating activities	**(6,308)**	(6,170)
Investing activities	**(8)**	(520)
Cash used in discontinued operations	**(6,316)**	(6,690)

4. SENIOR SECURED NOTES

In the first quarter, the Company entered into its sixth amendment to the Securities Purchase Agreement (the "Amendment") with its lenders to amend the terms of the Notes under the original Securities Purchase Agreement (the "Original SPA"), dated April 13, 2015. In connection with the Amendment, the Company prepaid $20,000 of the outstanding Notes balance on April 5, 2017. The Amendment was accounted for as an extinguishment, as the terms of the amended agreement were substantially different. Therefore, the unamortized costs related to the Notes were accelerated and recognized as part of the loss on extinguishment. In addition, on April 5, 2017, the Company paid the 5% borrowing fee of $1,000, the 5% prepayment penalty of $1,000 and an amendment fee of $500. In consideration for the prepayment, the lender modified the financial covenants and removed its security interest in the U.S. segment assets.

The Notes bear interest at a fixed rate of 10.25% per annum, payable quarterly in arrears on the last day of each quarter, and will mature on April 13, 2020, unless repaid earlier. Upon repayment of the principal in part or in full, a 5% borrowing fee is assessed and payable. In addition, voluntary prepayment of the notes, in part or in full prior to certain anniversary dates, will be subject to a prepayment penalty. The Notes are secured by all present and future assets of the Company, except for the U.S. segment and have certain restrictive covenants, including quarterly consolidated net revenue, minimum cash balance and consolidated leverage ratio. The minimum cash balance that must be maintained is $6,000. The Company is in compliance with these covenants as at September 30, 2017.

The following is the continuity of the Notes from January 1, 2016 to September 30, 2017:

	$
Balance, January 1, 2016	34,578
Interest expense	4,168
Interest paid	(4,168)
Accretion expense	1,799
Balance, December 31, 2016	36,377
Interest expense	1,024
Interest paid	(1,024)
Accretion expense	400
Carrying value of Notes before extinguishment	36,777
Loss on extinguishment	5,223
Balance, March 31, 2017	42,000
Prepayment of senior secured notes	(22,500)
Interest expense	541
Interest paid	(541)
Accretion expense	111
Balance, June 30, 2017	19,611
Interest expense	518
Interest paid	(518)
Accretion expense	113
Balance, September 30, 2017	**19,724**

(in thousands of United States dollars, except per share amounts)

Derivative financial instrument

Under the terms of the Original SPA, the Company issued 600,000 common share purchase warrants to the lender with an option for a cashless exercise in which the settlement price caused the conversion ratio to be variable. Accordingly, the warrants are classified as a financial liability. Gains and losses on re-measurement are presented separately in the consolidated statements of income (loss) and comprehensive income (loss). The exercise price of the warrants is $9.22 (equal to the five day volume-weighted average price on the Toronto Stock Exchange prior to closing, converted to U.S. dollars), which expire seven years from the date of issuance. A pricing model with observable market-based inputs was used to estimate the fair value of the warrants issued. The estimated fair value of the warrants as at December 31, 2016 and September 30, 2017 were $583 and $495, respectively.

The variables used to compute the fair value are as follows:

	Dec 31, 2016	Sept 30, 2017
Share price	$3.65	$3.81
Expected life	5.2 years	4.5 years
Volatility	56.00%	54.00%

5. IMPAIRMENT OF INTANGIBLE ASSETS

During the third quarter of 2017, the Company completed its assessment of the Melanovus oncology assets acquired in 2014 and decided not to continue with this program. The Company provided notice of termination to the seller. Accordingly, the Company recorded an impairment charge of $561 in other expenses in the interim consolidated statements of income (loss) and comprehensive income (loss).

6. SHARE CAPITAL

Authorized share capital

The authorized share capital consists of an unlimited number of preference shares, issuable in series, and an unlimited number of voting common shares, with no par value.

The Company has three stock-based compensation plans: The Stock Option Plan ("SOP"), the Employee and Director Share Purchase Plan (“ESPP”) and the Restricted Share Units and Performance Share Units ("PR Plan"). Full descriptions of the three stock-based compensation plans are included in Note 13 “Share Capital” to the Company’s annual consolidated financial statements for the year ended December 31, 2016.

Share purchase plan

The Company's ESPP allows employees and directors to share in the growth of the Company through share ownership. Through the ESPP, employees and directors may contribute amounts to purchase shares of the Company at a 15% discount from the prevailing trading price. Plan members must hold their shares for a period of at least six months before they can be sold. During the three months ended September 30, 2017, 7,340 shares were issued under the ESPP (three months ended September 30, 2016 - 24,456). Included in share-based compensation expense is $5 (three months ended September 30, 2016 - $17), which is the discount on the shares issued during the period. During the nine months ended September 30, 2017, 25,580 shares were issued under the ESPP (nine months ended September 30, 2016 - 82,157). Included in share-based compensation expense is $15 (nine months ended September 30, 2016 - $59).

Stock option plan

The following is a summary of the changes in the stock options outstanding from January 1, 2016 to September 30, 2017:

	Number of options (in thousands)	Weighted average exercise price $
Balance, January 1, 2016	1,414	6.39
Granted during the year	688	4.94
Exercised during the year	(116)	2.49
Forfeited during the year	(429)	5.70
Balance, December 31, 2016	1,557	6.39
Granted during the period	536	5.09
Exercised during the period	(366)	3.05
Forfeited/expired during the period	(816)	8.03
Balance, September 30, 2017	**911**	**6.84**

As at September 30, 2017, 406,415 options were fully vested and exercisable (September 30, 2016 - 763,287).

During the quarter, the Company granted 99,372 stock options under the stock option plan. The options vest over a four year period from the grant date, at a rate of 25% per year and expire seven years from the day of grant. The expected volatility is based on the Company's historical volatility over a comparable period based on expected life. Forfeitures are accounted for as necessary. There is no expected dividend. The exercise price and Black Scholes assumptions are as follows:

Grant date	Number granted	Exercise price	Black Scholes value	Risk-free interest rate	Expected life	Expected volatility
May 15, 2017	436,811	CDN$5.06	CDN$2.17	1.18%	4.9 years	49.6%
August 15, 2017	85,898	CDN$5.24	CDN$2.28	1.50%	4.9 years	49.5%
August 28, 2017	13,474	CDN$5.00	CDN$2.14	1.50%	4.9 years	48.6%

Total compensation cost for these stock options is estimated to be $179 which will be recognized on a graded basis over the vesting period of the stock options. The total expense for stock options for the three months ended September 30, 2017 was $37 (three months ended September 30, 2016 - $554). The total expense for stock options for the nine month ended September 30, 2017 was a recovery of $80 (nine months ended September 30, 2016 - $1,609).

The following information relates to stock options that were outstanding as at September 30, 2017:

Range of exercise prices	Number of options (in thousands)	Weighted average remaining contractual life (years)	Weighted average exercise price
CDN$			CDN$
1.05 - 4.60	39	4.1	1.82
4.61 - 6.20	495	7.2	5.26
6.21 - 13.88	377	7.3	9.43
	911	7.1	6.84

During the quarter, 64,000 stock options were exercised in exchange for 64,000 common shares (three months ended September 30, 2016 - 68,966 stock options in exchange for 68,966 common shares). During the nine months ended September 30, 2017, 365,627 stock options were exercised for 278,499 common shares (nine months ended September 30, 2016 - 115,966 stock options exchanged for 115,966 common shares). The Company's stock option plan provides that an option holder may elect to receive a number of shares equivalent to the growth value of vested options, which is the difference between the market price and the exercise price of the options. The total cash consideration received by the Company for stock option exercises during the three months ended September 30, 2017 was $103 (three months ended September 30, 2016 - $153). The total cash consideration received by the Company for stock option exercised for the nine months ended September 30, 2017 was $540 (nine months ended September 30, 2016 - $268).

(in thousands of United States dollars, except per share amounts)

Restricted Share Unit (RSU) and Performance Share Unit (PSU) Plan

On May 13, 2015, the Company adopted a RSU and PSU plan. RSU's and PSU's are notional share units exchangeable for common shares of the Company. RSU's are granted to all employees and directors of the Company and PSU's are granted to certain executives. RSU's granted to employees vest annually over a three year and RSU's granted to directors' vest over a one year period. PSU's vest based upon the achievement of financial performance goals for the Company for the three years ended December 31, 2018. If certain targets are achieved, up to four times the PSU's granted will be exchanged for an equal number of common shares.

On September 19, 2017, 63,282 PSUs were granted to key management personnel that vest October 2020 upon the achievement of certain market based performance goals, however if not achieved the performance date extends to October 2021. If certain targets are achieved, up to 5 times the number of PSUs granted will be awarded. Each PSU can be exchanged for an equal number of common shares. The determination of the number of shares that will ultimately vest was based on weighted average probabilities.

A summary of the RSU's and PSU's granted and outstanding as at September 30, 2017 is as follows:

	RSU's Number of units	**PSU's Number of units**
	000's	000's
Balance, January 1, 2017	202	78
Granted during the period	130	63
Vested during the period	(73)	-
Forfeited/cancelled during the period	(152)	(62)
Balance, September 30, 2017	**107**	**79**

The total expense for RSU's and PSU's for the three months ended September 30, 2017 was $42 (three months ended September 30, 2016 - $271). The total expense for the nine months ended September 30, 2017 was a recovery of $112 (nine months ended September 30, 2016 - $717).

7. EXPENSES BY NATURE

The consolidated statements of income (loss) and comprehensive income (loss) include the following expenses by nature:

Employee salaries and benefits expenses

	Three months ended Sept 30, 2017	Three months ended Sept 30, 2016	**Nine months ended Sept 30, 2017**	Nine months ended Sept 30, 2016
	$	$	**$**	$
Salaries, bonuses and benefits	**1,136**	1,058	**2,814**	3,208
Share-based compensation	**84**	581	**321**	1,580
Termination benefits	**241**	-	**801**	93
Total employee costs	**1,461**	1,639	**3,936**	4,881

For the three and nine months ended September 30, 2017 and 2016, all employee salaries and benefits are recorded in selling, general and administrative on the interim consolidated statements of income (loss) and comprehensive income (loss).

(in thousands of United States dollars, except per share amounts)

8. COMPENSATION OF KEY MANAGEMENT

Key management includes directors and executives of the Company. The compensation paid or payable to key management for services is shown below:

	Three months ended Sept 30, 2017	Three months ended Sept 30, 2016	**Nine months ended Sept 30, 2017**	Nine months ended Sept 30, 2016
	$	$	**$**	$
Salaries, bonuses and benefits	**374**	325	**709**	940
Share-based compensation	**159**	421	**260**	1,144
Directors fees	**57**	152	**187**	298
Termination benefits	**24**	-	**289**	-
	614	898	**1,445**	2,382

9. INCOME TAXES

Management uses estimates when determining current and deferred income taxes. These estimates are used to determine the recoverability of tax loss carry forward amounts, research and development expenditures and investment tax credits. Significant judgment is required regarding future probability of the Company to be able to realize deferred taxes. Changes in market conditions, changes in tax legislation, patent challenges and other factors, including the approval or launch of generic versions of any of the Company's products, could adversely affect the ongoing value of deferred taxes. The carrying amount of deferred income tax assets is reassessed at each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to utilize all or part of the deferred income tax assets. Unrecognized deferred income tax assets are reassessed at each reporting period and are recognized to the extent that it is probable that there will be sufficient taxable profits to allow all or part of the asset to be recovered.

Income tax expense is recognized based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

Income tax expense as reported differs from the amount that would be computed by applying the combined Canadian federal and provincial statutory income tax rates to income before income taxes. The reasons for the differences are as follows:

	Three months ended Sept 30, 2017	Three months ended Sept 30, 2016	**Nine months ended Sept 30, 2017**	Nine months ended Sept 30, 2016
	$	$	**$**	$
Income before income taxes from continuing operations	**5,176**	2,549	**9,018**	5,187
Tax provision at the statutory income tax rate of 26.5%	**1,372**	675	**2,390**	1,375
Permanent differences	**134**	(398)	**521**	(15)
Effect of currency translation adjustment	**(253)**	50	**(691)**	(411)
Income tax expense	**1,253**	327	**2,220**	949

The movement in the deferred income tax asset for the nine months ended September 30, 2017 and 2016 is as follows:

	Nine months ended Sept 30, 2017	Nine months ended Sept 30, 2016
	$	$
As at January 1	**6,864**	8,356
Change in deferred tax as asset	**(2,220)**	(949)
As at September 30	**4,644**	7,407

10. EARNINGS (LOSS) PER SHARE

Earnings (loss) per share is calculated using the weighted average number of shares outstanding. The weighted average number of shares outstanding for the three months ended September 30, 2017 was 26,656,840 (three months ended September 30, 2016 - 26,799,312). The weighted average number of shares outstanding for the nine months ended September 30, 2017 was 26,527,383 (for the nine months ended September 30, 2016 - 26,160,849).

Diluted earnings (loss) per share is calculated using the weighted average number of shares outstanding taking into consideration the weighted average impact of dilutive securities. The dilutive weighted average for the three months ended September 30, 2017 was 26,826,260 (three months ended September 30, 2016 - 26,495,705). The diluted weighted average number of shares outstanding for the nine months ended September 30, 2017 was 26,896,636 (for the nine months ended September 30, 2016 - 26,682,408).

11. COMMITMENTS AND CONTINGENCIES

In the normal course of business, the Company may be the subject of litigation or other potential claims. While management assesses the merits of each lawsuit and defends itself accordingly, the Company may be required to incur significant expenses or devote significant resources to defending itself against litigation.

Licensing Agreements with Galephar

In 2002, the Company entered into a Master Licensing and Clinical Supply Agreement ("the Agreement") with Galephar, a Puerto Rico based pharmaceutical research and manufacturing company. Under the Agreement, the Company acquired the rights to package, test, obtain regulatory approvals and market CIP-FENOFIBRATE, CIP-ISOTRETINOIN and CIP-TRAMADOL ER ("the CIP Products") in various countries. In accordance with the Agreement, the Company retains 50% of all revenue from licensing and distribution arrangements entered into with respect to the CIP Products, with the other 50% due to Galephar. Where the Company has opted to market and sell a CIP Product directly in a territory, the Company pays a royalty to Galephar. Galephar retains the right to manufacture and supply the CIP Products. With respect to licensing and distribution arrangements, the Company manages the product supply arrangements with their respective marketing partners and Galephar; product is shipped directly from Galephar to the respective marketing partners. Where the Company has opted to market and sell the CIP Product directly, the Company purchases the finished goods from Galephar directly.

With respect to CIP-ISOTRETINOIN, the Company has entered into licensing and distribution arrangements for the U.S. and Brazil, while opting to market and sell the product directly in Canada. The Company also has in place various licensing and distribution arrangements with respect to CIP-FENOFIBRATE and CIP-TRAMADOL ER in Canada, the U.S. and Central and South America.

In 2016, Galephar entered into a contract with another party (the “Assignee”) to assign certain rights relating to CIP-ISOTRETINOIN under the Agreement. The Company is a party to this contract, agreeing to remit revenue on the same terms as the Agreement, from licensing and distribution within the U.S. for CIP-ISOTRETOIN directly to the Assignee.

During the three and nine months ended September 30, 2017, the Company paid royalties of $1,383 (three months ended September 30, 2016 - $5,644) and $3,765 (nine months ended September 30, 2016 - $13,883), respectively to Galephar. As at September 30, 2017, the amount in accounts payable and accrued liabilities owed to Galephar were $2,683 (December 31, 2016 - $5,972). Amounts payable to Galephar are remitted quarterly, after the Company collects from its licensing partners. Accordingly, the Company’s accounts receivable has a corresponding balance representing amounts owed by its licensing partners.