Alkalon A/S

Farverland 6, st., 2600 Glostrup

Company reg. no. 30 27 38 26

Annual report

1 January - 31 December 2017

The annual report have been submitted and approved by the general meeting on the 25 April 2018.

Ricki Boye
Chairman of the meeting

Notes to users of the English version of this document:

- To ensure the greatest possible applicability of this document, British English terminology has been used.
- Please note that decimal points remain unchanged from the Danish version of the document. This means that for instance DKK 146.940 is the same as the English amount of DKK 146,940, and that 23,5 % is the same as the English 23.5 %.

Contents

Management's report

The board of directors and the managing director have today presented the annual report of Alkalon A/S for the financial year 1 January to 31 December 2017.

The annual report has been presented in accordance with the Danish Financial Statements Act.

We consider the accounting policies used appropriate, and in our opinion the annual accounts provide a true and fair view of the company's assets and liabilities and its financial position as on 31 December 2017 and of the company's results of its activities in the financial year 1 January to 31 December 2017.

We are of the opinion that the management's review includes a fair description of the issues dealt with.

The annual report is recommended for approval by the general meeting.

Glostrup, 25 April 2018

Managing Director

Bjarne Carsten Pedersen

Board of directors

Robin James Scott Cridland Chairman of the Board	Thor Nels Andersen	Rasmus Forup Helmich
Nicholas Cecil Marks	Peter Sølbeck	

Independent auditor's report

To the shareholders of Alkalon A/S

Opinion

We have audited the annual accounts of Alkalon A/S for the financial year 1 January to 31 December 2017, which comprise accounting policies used, profit and loss account, balance sheet and notes. The annual accounts are prepared in accordance with the Danish Financial Statements Act.

In our opinion, the annual accounts give a true and fair view of the company's assets, liabilities and financial position at 31 December 2017 and of the results of the company's operations for the financial year 1 January to 31 December 2017 in accordance with the Danish Financial Statements Act.

Basis for opinion

We conducted our audit in accordance with international standards on auditing and the additional requirements applicable in Denmark. Our responsibilities under those standards and requirements are further described in the below section “Auditor’s responsibilities for the audit of the annual accounts”. We are independent of the company in accordance with international ethics standards for accountants (IESBA's Code of Ethics) and the additional requirements applicable in Denmark, and we have fulfilled our other ethical responsibilities in accordance with these standards and requirements. We believe that the audit evidence obtained is sufficient and appropriate to provide a basis for our opinion.

Material uncertainties concerning the enterprise's ability to continue as a going concern

Please see note 1 in the annual accounts in which the management describes the company's capital resources for the coming financial year.

Emphasis of matter

Without qualifying our opinion, we draw attention to note 2 in the annual accounts in which the management outlines its expectations to the significantly improved earnings that are a precondition for the value of the tax asset of DKK 1,672,000 recognised in the balance sheet.

The management's responsibilities for the annual accounts

The management is responsible for the preparation of annual accounts that give a true and fair view in accordance with the Danish Financial Statements Act. The management is also responsible for such internal control as the management determines is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the annual accounts, the management is responsible for evaluating the company’s ability to continue as a going concern, and, when relevant, disclosing matters related to going concern and using the going concern basis of accounting when preparing the annual accounts, unless the management either intends to liquidate the company or to cease operations, or if it has no realistic alternative but to do so.

Auditor’s responsibilities for the audit of the annual accounts

Our objectives are to obtain reasonable assurance about whether the annual accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report including an opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with international standards on auditing and the additional requirements applicable in Denmark will always detect a material misstatement when it exists. Misstatements may arise due to fraud or error and may be considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions made by users on the basis of the annual accounts.

As part of an audit conducted in accordance with international standards on auditing and the additional requirements applicable in Denmark, we exercise professional evaluations and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement in the annual accounts, whether due to fraud or error, design and perform audit procedures in response to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting a misstatement resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of the internal control relevant to the audit 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 company’s internal control.

- Evaluate the appropriateness of accounting policies used by the management and the reasonableness of accounting estimates and related disclosures made by the management.

- Conclude on the appropriateness of the management’s preparation of the annual accounts being based on the going concern principle and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may raise significant doubt about the company’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the annual accounts or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the company to cease to continue as a going concern.

- Evaluate the overall presentation, structure and contents of the annual accounts, including the disclosures in the notes, and whether the annual accounts reflect the underlying transactions and events in a manner that gives a true and fair view.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in the internal control that we identify during our audit.

Independent auditor's report

Statement on the management's review

The management is responsible for the management's review.

Our opinion on the annual accounts does not cover the management’s review, and we do not express any kind of assurance opinion on the management's review.

In connection with our audit of the annual accounts, our responsibility is to read the management’s review and in that connection consider whether the management’s review is materially inconsistent with the annual accounts or our knowledge obtained during the audit, or whether it otherwise appears to contain material misstatement.

Furthermore, it is our responsibility to consider whether the management's review provides the information required under the Danish Financial Statements Act.

Based on the work we have performed, we believe that the management's review is in accordance with the annual accounts and that it has been prepared in accordance with the requirements of the Danish Financial Statement Acts. We did not find any material misstatement in the management's review.

Copenhagen, 25 April 2018

BUUS JENSEN
State Authorised Public Accountants
Company reg. no. 16 11 90 40

Ulrik Nørskov
State Authorised Public Accountant
MNE-nr. 29456

Company data

The company	Alkalon A/S Farverland 6, st. 2600 Glostrup	
	Company reg. no.	30 27 38 26
	Domicile:	Glostrup
	Financial year:	1 January - 31 December
Board of directors	Robin James Scott Cridland, Chairman of the Board Thor Nels Andersen Rasmus Forup Helmich Nicholas Cecil Marks Peter Sølbeck	
Managing Director	Bjarne Carsten Pedersen	
Auditors	BUUS JENSEN, Statsautoriserede revisorer	

The principal activities of the company

Alkalon's activities are to develop, register and commercialize new generic NRT products to the pharmaceutical industry and retailers around the world.

Uncertainties as to recognition or measurement

A deferred tax asset of DKK 4,582,900 has been reduced to 1.672.000 by end 2017 and incorporated into the annual accounts which, in all material respects, concerns unutilized tax losses. The deferred tax asset has been measured based on then material respects, concerns unutilized tax losses. The deferred tax asset has been measured based on the management's expectations to the company’s short time future earnings. Based on the above, the management is of management's expectations to the company’s short time future earnings. Based on the above, the management is of the opinion that the measurement is reasonable and justifiable

Development in activities and financial matters

The gross loss The gross profit for the year is DKK 1.889.561 against DKK 5.880.920 last year. The results from ordinary activities after tax are DKK –10.940.634 against against DKK -1.975.991 last year. During 2017 Alkalon product sales declined by high single digit percentage compared with 2015 sales as a consequence of delayed launch of new main customer and ongoing changes of the 3rd party Manufacturing supplier. The delayed approval of the new supplier had a very negative impact on product sales in 2017. The final result for 2017 was further negative impacted onadditional cost for transfer Manufacturing site and obsolete stock. All impacted negative to the 2017 result. The merger with Revolymer back in November 2016 did not give the expected positive impact in 2017. Based on above major activities to secure future strong growth plans both the management and board of directors see the 2017 result unacceptable but still believe the fundamental for a strong future growth plan has been established despite the positive results were delayed into the coming years.

Capital resources:

As a consequence of the operating loss realized for the year, the company's liquidity is tight. The management expects positive results and deriving cash flow from operations for the coming financial year. On this basis, the management expects that the enterprise is able to maintain sufficient cash resources to carry out the operating activities planned for the coming financial year, but at the same time, it acknowledges the necessity of the earnings expectations being realized.

In order to strengthen the company's capital resources, a proposal for a capital increase of DKK 750,000 is proposed at the Annual General Meeting. The proposal is expected to be adopted.

The expected development

Management is very positive about the future sales and profit as we have very strong plans and initiatives in place to grow our business significantly in the coming years. We expect the growth in product sales will increase significantly in 2018 with high double digit growth after the Canadian business is fully integrated and new customers have been included from January 2018. Within the coming 5-7 years the company aim to reach 10% market-share in the global gum segment for nicotine replacement products with an improved margin. In parallel the management is focusing on a tight control of all investments in a prioritized fashion to ensure a strong profitable growth scenario.

Furthermore ,the management is working on other strategic initiatives that can ensure a stronger cash resource to secure the strong growth rates.

The management expects a small positive operating result in 2018. Operating result is expected to improve further during the next 2-3 years, which expectedly will result in a full utilization of the deferred tax asset which has been reduces by end 2017.

Accounting policies used

The annual report for Alkalon A/S is presented in accordance with those regulations of the Danish Financial Statements Act concerning companies identified as class B enterprises. Furthermore, the company has chosen to comply with some of the rules applying for class C enterprises.

The accounting policies used are unchanged compared to last year, and the annual accounts are presented in Danish kroner (DKK).

Recognition and measurement in general

Income is recognised in the profit and loss account concurrently with its realisation, including the recognition of value adjustments of financial assets and liabilities. Likewise, all costs, these including depreciation, amortisation, writedown, provisions, and reversals which are due to changes in estimated amounts previously recognised in the profit and loss account are recognised in the profit and loss account.

Assets are recognised in the balance sheet when the company is liable to achieve future, financial benefits and the value of the asset can be measured reliably.

Liabilities are recognised in the balance sheet when the company is liable to lose future, financial benefits and the value of the liability can be measured reliably.

At the first recognition, assets and liabilities are measured at cost. Later, assets and liabilities are measured as described below for each individual accounting item.

Certain fixed asset investments and liabilities are measured at amortised cost, by which method a fixed, effective interest is recognised during the useful life of the asset or the liability. Amortised cost is recognised as the original cost with deduction of any payments and additions/deductions of the accrued amortisation of the difference between cost and nominal amount. In this way capital losses and capital profits are spread over the useful life.

At recognition and measurement, such predictable losses and risks are taken into consideration, which may appear before the annual report is presented, and which concerns matters existing on the balance sheet date.

Translation of foreign currency

Transactions in foreign currency are translated by using the exchange rate prevailing at the date of the transaction. Differences in the rate of exchange arising between the rate at the date of transaction and the rate at the date of payment are recognised in the profit and loss account as an item under net financials.

Debtors, creditors, and other monetary items in foreign currency are translated by using the closing rate. The difference between the closing rate and the rate at the time of the occurrence or the recognition in the latest annual accounts of the amount owed or the liability is recognised in the profit and loss account under financial income and expenses.

Fixed assets and other non-monetary assets acquired in foreign currency and which are not considered to be investment assets purchased in foreign currencies are measured at the exchange rate on the transaction date.

The profit and loss account

Gross loss

The gross loss comprises the net turnover, changes in inventories of finished goods and work in progress, work performed for own purposes and capitalised, other operating income, and external costs.

The net turnover is recognised in the profit and loss account if delivery and risk transfer to the buyer have taken place before the end of the year, and if the income can be determined reliably and is expected to be received. The net turnover is recognised exclusive of VAT and taxes and with the deduction of any discounts granted in connection with the sale.

Costs of sales includes costs for the purchase of raw materials and consumables less discounts and changes in inventories.

Other external costs comprise costs for distribution, sales, advertisement, administration, premises, loss on debtors, and operational leasing costs.

Staff costs

Staff costs include salaries and wages including holiday allowances, pensions and other costs for social security etc. for staff members. Staff costs are less public reimbursements.

Depreciation, amortisation and writedown

Depreciation, amortisation and writedown comprise depreciation on, amortisation of and writedown relating to intangible and tangible fixed assets respectively.

Net financials

Net financials comprise interest, realised and unrealised capital gains and losses concerning financial assets and liabilities, amortisation of financial assets and liabilities, additions and reimbursements under the Danish tax prepayment scheme, etc. Financial income and expenses are recognised in the profit and loss account with the amounts that concerns the financial year.

Tax of the results for the year

The tax for the year comprises the current tax for the year and the changes in deferred tax, and it is recognised in the profit and loss account with the share referring to the results for the year and directly in the equity with the share referring to entries directly on the equity.

The balance sheet

Intangible fixed assets

Development projects, patents, and licences

Development costs comprise e.g. salaries, wages, and amortisation which directly refer to the development activities.

Clearly defined and identifiable development projects are recognised as intangible fixed assets provided that the technical feasibility, sufficient resources, and a potential market or a development opportunity can be demonstrated, and provided that it is the intention to produce, market or utilise the project. It is, however, a condition that the cost can be calculated reliably and that a sufficiently high degree of certainty indicates that future earnings will cover the costs for production, sales, and administration. Other development costs are recognised in the profit and loss account concurrently with their realisation.

Development costs recognised in the balance sheet are measured at cost with deduction of accrued depreciation and writedown.

After completion of the development work, capitalised development costs are amortised on a straight line basis over the estimated financial useful life. Usually, the amortisation period is 5 years.

Gain and loss from the sale of development projects, patents, and licenses are measured as the difference between the sales price with deduction of sales costs and the book value at the time of the sale. Gain or loss are recognised in the profit and loss account as other operating income or other operating expenses respectively.

Goodwill

Goodwill is amortised over its estimated useful life, which is determined on the basis of the management's experience with the individual business areas. Goodwill is amortised on a straight-line basis over the amortisation period, which is 5 years. The amortisation period is determined on the basis of an expected payback period, being the longer for strategical acquirees with a strong market position and an expected long-term earnings profile.

Tangible fixed assets

Tangible fixed assets are measured at cost with deduction of accrued depreciation and writedown.

The basis of depreciation is cost with deduction of any expected residual value after the end of the useful life of the asset. The amortisation period and the residual value are determined at the acquisition date and reassessed annually. If the residual value exceeds the book value, the amortisation discontinues.

The cost comprises the acquisition cost and costs directly attached to the acquisition until the time when the asset is ready for use.

Depreciation takes place on a straight line basis and based on an evaluation of the expected useful life:

	Useful life
Other plants, operating assets, fixtures and furniture	*3-5 years*

Minor assets with an expected useful life of less than 1 year are recognised as costs in the profit and loss account in the year of acquisition.

Profit or loss deriving from the sales of tangible fixed assets is measured as the difference between the sales price reduced by the selling costs and the book value at the time of the sale. Profit or losses are recognised in the profit and loss account as other operating income or other operating expenses.

Inventories

Inventories are measured at cost on basis of the FIFO method. In case the net realisable value of the inventories is lower than the cost, writedown takes place to this lower value.

The cost for trade goods, raw materials, and consumables comprises the acquisition cost with the addition of the delivery costs.

The net realisable value for inventories is recognised as the market price with deduction of completion costs and selling costs. The net realisable value is determined taking into consideration the negotiability, obsolescence, and development of the expected market price.

Debtors

Debtors are measured at amortised cost which usually corresponds to face value. In order to meet expected losses, writedown takes place at the net realisable value.

Accrued income and deferred expenses

Accrued income and deferred expenses recognised under assets comprise incurred costs concerning the next financial year.

Available funds

Available funds comprise cash at bank and in hand.

Corporate tax and deferred tax

Current tax receivable and tax liabilities are recognised in the balance sheet at the amount calculated on the basis of the expected taxable income for the year adjusted for tax on previous years' taxable income and prepaid taxes. Tax receivable and tax liabilities are set off to the extent that legal right of set-off exists and if the items are expected to be settled net or simultaneously.

Deferred tax is measured on the basis of all temporary differences in assets and liabilities with a balance sheet focus.

Deferred tax is measured based on the tax rules and tax rates applying under the legislation on the balance sheet date and prevailing when the deferred tax is expected to be released as current tax.

Liabilities

Financial liabilities related to borrowings are recognised at the received proceeds with the deduction of transaction costs incurred. In following periods, the financial liabilities are recognised at amortised cost, corresponding to the capitalised value by use of the effective interest. The difference between the proceeds and the nominal value is recognised in the profit and loss account during the term of the loan.

Other liabilities are measured at amortised cost which usually corresponds to the nominal value.

Profit and loss account 1 January - 31 December

All amounts in DKK.

Note		2017	2016
	Gross loss	**-988.038**	**3.296.880**
3	Staff costs	-4.260.288	-4.619.547
	Depreciation, amortisation and writedown relating to tangible and intangible fixed assets	-2.227.788	-141.489
	Operating profit	**-7.476.114**	**-1.464.156**
	Other financial income	0	6.744
4	Other financial costs	-553.620	-518.579
	Results before tax	**-8.029.734**	**-1.975.991**
5	Tax on ordinary results	-2.910.900	0
	Results from ordinary activities after tax	**-10.940.634**	**-1.975.991**
	Results for the year	**-10.940.634**	**-1.975.991**
	Proposed distribution of the results:		
	Allocated from results brought forward	-10.940.634	-1.975.991
	Distribution in total	**-10.940.634**	**-1.975.991**

Balance sheet 31 December

All amounts in DKK.

Note	Assets	2017	2016
	Fixed assets		
6	Goodwill	985.000	3.053.128
7	Development projects in progress and prepayments for intangible fixed assets	3.086.472	1.767.109
	Intangible fixed assets in total	4.071.472	4.820.237
8	Other plants, operating assets, and fixtures and furniture	364.138	522.672
	Tangible fixed assets in total	364.138	522.672
9	Other debtors	1.488.557	0
	Financial fixed assets in total	1.488.557	0
	Fixed assets in total	**5.924.167**	**5.342.909**
	Current assets		
	Raw materials and consumables	568.760	414.362
	Work in progress	0	1.990.593
	Manufactured goods and trade goods	8.805.679	3.701.098
	Inventories in total	9.374.439	6.106.053
	Trade debtors	3.838.037	10.369.057
	Deferred tax assets	1.672.000	4.582.900
	Other debtors	420.980	652.416
	Debtors in total	5.931.017	15.604.373
	Available funds	160.503	12.017
	Current assets in total	**15.465.959**	**21.722.443**
	Assets in total	**21.390.126**	**27.065.352**

Balance sheet 31 December

All amounts in DKK.

Note	Equity and liabilities	2017	2016
	Equity		
10	Contributed capital	6.633.650	2.949.318
12	Reserve for development expenditure	3.086.472	0
13	Results brought forward	-5.684.233	8.527.205
	Equity in total	**4.035.889**	**11.476.523**
	Liabilities		
	Bank debts	7.428.044	5.609.140
	Trade creditors	5.454.992	9.233.693
	Other debts	4.471.201	745.996
	Short-term liabilities in total	17.354.237	15.588.829
	Liabilities in total	**17.354.237**	**15.588.829**
	Equity and liabilities in total	**21.390.126**	**27.065.352**

1 Uncertainties concerning the enterprise's ability to continue as a going concern

2 Uncertainties concerning recognition and measurement

14 Mortgage and securities

15 Contingencies

Notes

All amounts in DKK.

	2017	2016

1. Uncertainties concerning the enterprise's ability to continue as a going concern

As a consequence of the operating loss realized for the year, the company's liquidity is tight. The management expects positive results and deriving cash flow from operations for the coming financial year. On this basis, the management expects that the enterprise is able to maintain sufficient cash resources to carry out the operating activities planned for the coming financial year, but at the same time,it acknowledges the necessity of the earnings expectations being realized.

In order to strengthen the company's capital resources, a proposal for a capital increase of DKK 750,000 is proposed at the Annual General Meeting. The proposal is expected to be adopted.

2. Uncertainties concerning recognition and measurement

A deferred tax asset of DKK 1,672,000 has been incorporated into the annual accounts which, in all material respects, concerns unutilized tax losses. The deferred tax asset has been measured based on then management's expectations to the company's short time future earnings. Based on the above, the management is of the opinion that the measurement is reasonable and justifiable.

3. Staff costs

	2017	2016
Salaries and wages	3.800.079	4.008.140
Pension costs	278.790	313.160
Other costs for social security	33.076	38.471
Other staff costs	148.343	259.776
	4.260.288	**4.619.547**
Average number of employees	5	6

4. Other financial costs

	2017	2016
Other financial costs	553.620	518.579
	553.620	**518.579**

5. Tax on ordinary results

	2017	2016
Adjustment for the year of deferred tax	2.910.900	0
	2.910.900	**0**

All amounts in DKK.

		2017	2016
6.	**Goodwill**		
	Cost 1 January 2017	3.158.408	0
	Additions during the year	0	3.158.408
	Cost 31 December 2017	**3.158.408**	**3.158.408**
	Amortisation and writedown 1 January 2017	-105.280	0
	Amortisation and writedown for the year	-2.068.128	-105.280
	Amortisation and writedown 31 December 2017	**-2.173.408**	**-105.280**
	Book value 31 December 2017	**985.000**	**3.053.128**
7.	**Development projects in progress and prepayments for intangible fixed assets**		
	Cost 1 January 2017	1.767.109	0
	Additions during the year	1.319.363	1.767.109
	Cost 31 December 2017	**3.086.472**	**1.767.109**
	Book value 31 December 2017	**3.086.472**	**1.767.109**
8.	**Other plants, operating assets, and fixtures and furniture**		
	Cost 1 January 2017	1.316.442	776.128
	Additions during the year	26.589	540.314
	Disposals during the year	-27.778	0
	Cost 31 December 2017	**1.315.253**	**1.316.442**
	Depreciation and writedown 1 January 2017	-793.770	-757.561
	Depreciation and writedown for the year	-159.660	-36.209
	Depreciation and writedown, assets disposed of	2.315	0
	Depreciation and writedown 31 December 2017	**-951.115**	**-793.770**
	Book value 31 December 2017	**364.138**	**522.672**

Notes

All amounts in DKK.

		31/12 2017	31/12 2016
9.	**Other debtors**		
	Additions during the year	1.488.557	0
	Cost 31 December 2017	**1.488.557**	**0**
	Book value 31 December 2017	**1.488.557**	**0**
10.	**Contributed capital**		
	Contributed capital 1 January 2017	2.949.318	2.078.479
	Cash capital increase	3.500.000	870.839
	Transferred from distributed reserves	184.332	0
		6.633.650	**2.949.318**
11.	**Share premium account**		
	Share premium account for the year	0	10.147.677
	Transfer to results brought forward	0	-10.147.677
		0	**0**
12.	**Reserve for development expenditure**		
	Transferred from results brought forward	3.086.472	0
		3.086.472	**0**
13.	**Results brought forward**		
	Results brought forward 1 January 2017	8.527.205	355.519
	Profit or loss for the year brought forward	-10.940.634	-1.975.991
	Premium regarding to capital increase	0	10.147.677
	Transfer to development expenditure	-3.086.472	0
	Transfer to contributed capital	-184.332	0
		-5.684.233	**8.527.205**

Notes

All amounts in DKK.

14. Mortgage and securities

For bank debts, DKK 7,428,000, the company has provided security in company assets representing a nominal value of DKK 9,500,000.

15. Contingencies

Contingent liabilities

Leasing liabilities

The company has entered into lease agreement for premise with an annual rent of approx. DKK 250,000. If the lease is terminated the rent obligation is approx. DKK 790,000.