Alkalon A/S

Naverland 1, 14., 2600 Glostrup

Company reg. no. 30 27 38 26

Annual report

1 January - 31 December 2015

The annual report has been submitted and approved by the general meeting on the 8 June 2016.

Ricki Boye
Chairman of the meeting

Notes:
- To ensure the greatest possible applicability of this document, British English terminology has been used.
- Please note that decimal points have not been used in the usual English way. This means that for instance DKK 146.940 means the amount of DKK 146,940, and that 23,5 % means 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 2015.

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 2015 and of the company's results of its activities in the financial year 1 January to 31 December 2015.

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, 6 June 2016

Managing Director

Bjarne Carsten Pedersen

Board of directors

Thomas Bjerregaard Thomsen (Chairman)	Bo Tandrup	Ulf Lennart Rosen

Anne Christine Beck

The independent auditor's reports

To the shareholders of Alkalon A/S

Report on the annual accounts

We have audited the annual accounts of Alkalon A/S for the financial year 1 January to 31 December 2015, 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.

The management's responsibility 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. Furthermore, the management is responsible for such internal control as it determines necessary in order to prepare annual accounts that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the annual accounts based on our audit. We conducted our audit in accordance with international standards on auditing and additional requirements under Danish audit regulation. This requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatements in the annual accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation of annual accounts that give a true and fair view 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management, as well as the overall presentation of the annual accounts.

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

The audit has not resulted in any qualification.

The independent auditor's reports

Opinion

In our opinion, the annual accounts give a true and fair view of the company's assets, liabilities and financial position at 31 December 2015 and of the results of the company's operations for the financial year 1 January to 31 December 2015 in accordance with the Danish Financial Statements Act.

Emphasis of matter paragraph on matters in the accounts

Without qualifying our opinion, we draw attention to note 3 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 4,582,900 recognised in the balance sheet.

Statement on the management's review

Pursuant to the Danish Financial Statements Act, we have read the management's review. We have not performed any further procedures in addition to the audit of the annual accounts. On this basis, it is our opinion that the information provided in the management's review is consistent with the annual accounts.

Copenhagen, 6 June 2016

BUUS JENSEN
State Authorised Public Accountants
CVR-nr. 16 11 90 40

Ulrik Nørskov
State Authorised Public Accountant

Company data

The company	Alkalon A/S Naverland 1, 14. 2600 Glostrup	
	Company reg. no.:	30 27 38 26
	Domicile:	Glostrup
	Financial year:	1 January - 31 December
Board of directors	Thomas Bjerregaard Thomsen (Chairman) Bo Tandrup Ulf Lennart Rosen Anne Christine Beck	
Managing Director	Bjarne Carsten Pedersen	
Auditors	BUUS JENSEN, Statsautoriserede revisorer	

The significant activities of the enterprise

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 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 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 profit for the year is DKK 4.000.763 against DKK -1.865.272 last year. The results from ordinary activities after tax are DKK -1.402.480 against DKK -7.626.071 last year.

During 2015 Alkalon managed to get product sales back on track to meet expectation. The management and board of directors consider the results satisfactory.

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 continue in 2016 with double digit growth after 3 new customers launched the Alkalon products in late 2015 and this will continue in the following years. Long term the company expects to reach a substantial market share within the global gum segment for nicotine replacement products, and 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 positive operating result in 2016. Operating result is expected to improve further during the next 2-3 years, which expectedly will result in a utilization of the deferred tax asset.

Events subsequent to the financial year

As a consequence of the operating loss realized for the year, the company's liquidity is tight. The management has in 2016 extended the current credit facility with the bank to 2017 as well as some of the current shareholders has made a capital injection of DKK 1.5 million. Furthermore, 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.

The financial report is prepared as going concern since liquidity has been improved after year-end 2015 following an extension of the current credit facility with the bank to 2017 as well as a capital injection in form of equity. Management therefore expects to have sufficient cash resources to fund operations for 2016.

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.

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, which are not settled at the date of the balance sheet, are translated by using the closing rate. The difference between the closing rate and the rate at the time of establishment of the receivable or the payable is recognised in the profit and loss account under financial income and financial costs.

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 profit

The gross profit 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.

Cost of sales include 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 include interest income, interest expenses, and realised and unrealised capital gains and losses on financial assets and liabilities. Net financials are recognised in the profit and loss account with the amounts concerning the financial year.

Results from equity investments in group enterprises

After full elimination of intercompany profit or loss and deduction of amortisation of consolidated goodwill, the equity investment in the individual group enterprises are recognised in the profit and loss account at a proportional share of the group enterprises' results after tax.

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

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 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:

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. In the period 2014 to 2016, the corporate tax rate will be reduced gradually from 25 % to 22 %, which will affect the deferred tax liabilities and deferred tax assets. Unless a recognition with a different tax rate than 22 % will result in a significant material deviation in the estimated deferred tax liability or tax asset, deferred tax liabilities and assets are recognised by 22 %.

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		2015	2014
	Gross profit	**4.000.763**	**-1.865.271**
2	Staff costs	-4.634.434	-5.329.246
	Depreciation and writedown relating to tangible fixed assets	-16.023	-14.357
	Operating profit	**-649.694**	**-7.208.874**
	Income from equity investments in group enterprises	-6.054	-55.905
	Other financial income	3.902	8
4	Other financial costs	-750.634	-361.300
	Results before tax	**-1.402.480**	**-7.626.071**
	Results for the year	**-1.402.480**	**-7.626.071**
	Proposed distribution of the results:		
	Allocated from results brought forward	-1.402.480	-7.626.071
	Distribution in total	**-1.402.480**	**-7.626.071**

Balance sheet 31 December

All amounts in DKK.

Note	Assets	2015	2014
	Fixed assets		
5	Other plants, operating assets, and fixtures and furniture	18.567	34.590
	Tangible fixed assets in total	18.567	34.590
6	Equity investments in group enterprises	0	0
	Financial fixed assets in total	0	0
	Fixed assets in total	**18.567**	**34.590**
	Current assets		
	Raw materials and consumables	0	218.074
	Work in progress	66.320	0
	Manufactured goods and trade goods	278.767	285.847
	Inventories in total	345.087	503.921
	Trade debtors	6.660.693	3.433.284
	Deferred tax assets	4.582.900	4.582.900
	Other receivables	139.052	870.425
	Accrued income and deferred expenses	311.450	51.900
	Debtors in total	11.694.095	8.938.509
	Cash and cash equivalents	6.650	95.845
	Current assets in total	**12.045.832**	**9.538.275**
	Assets in total	**12.064.399**	**9.572.865**

Balance sheet 31 December

All amounts in DKK.

Note	Equity and liabilities	2015	2014
	Equity		
7	Share capital	2.078.479	2.078.479
8	Results brought forward	355.519	1.757.999
	Equity in total	**2.433.998**	**3.836.478**
	Liabilities		
	Bank debts	5.142.724	440.850
	Prepayments received from customers	116.909	122.824
	Trade creditors	2.147.220	3.254.980
	Debt to associated enterprises	1.310.198	1.218.790
	Other debts	913.350	698.943
	Short-term liabilities in total	9.630.401	5.736.387
	Liabilities in total	**9.630.401**	**5.736.387**
	Equity and liabilities in total	**12.064.399**	**9.572.865**

9 Mortgage and securities

10 Contingent liabilities

Notes

All amounts in DKK.

1. Subsequent events

As a consequence of the operating loss realized for the year, the company's liquidity is tight. The management has in 2016 extended the current credit facility with the bank to 2017 as well as some of the current shareholders has made a capital injection of DKK 1.5 million. Furthermore, 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.

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	2015	2014
2. Staff costs		
Salaries and wages	4.107.811	4.422.285
Pension costs	287.549	531.866
Other costs for social security	37.853	45.012
Other staff costs	201.221	330.083
	4.634.434	**5.329.246**
Average number of employees	6	7

	2015	2014
3. Tax on ordinary results		
Tax of the results for the year	0	0
	0	**0**

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

	2015	2014
4. Other financial costs		
Other financial costs	750.634	361.300
	750.634	**361.300**

Notes

All amounts in DKK.

		2015	2014
5.	**Other plants, operating assets, and fixtures and furniture**		
	Cost 1 January 2015	776.128	761.128
	Additions during the year	0	15.000
	Cost 31 December 2015	**776.128**	**776.128**
	Depreciation and writedown 1 January 2015	-741.538	-727.181
	Depreciation and writedown for the year	-16.023	-14.357
	Depreciation and writedown 31 December 2015	**-757.561**	**-741.538**
	Book value 31 December 2015	**18.567**	**34.590**
6.	**Equity investments in group enterprises**		
	Acquisition sum, opening balance 1 January 2015	80.260	80.260
	Disposals during the year	-80.260	0
	Cost 31 December 2015	**0**	**80.260**
	Revaluations, opening balance 1 January 2015	-72.932	-72.932
	Reversals for the year concerning disposals	72.932	0
	Revaluation 31 December 2015	**0**	**-72.932**
	Amortisation of goodwill, opening balance 1 January 2015	-7.328	-7.328
	Reversal of amortisation of goodwill concerning disposals	7.328	0
	Depreciation on goodwill 31 December 2015	**0**	**-7.328**
	Book value 31 December 2015	**0**	**0**
7.	**Share capital**		
	Share capital 1 January 2015	2.078.479	1.677.115
	Cash capital increase	0	401.364
		2.078.479	**2.078.479**

The share capital consists of the following: A - shares of DKK 375.000, B – shares of DKK 170.670, C - shares of DKK 622.191, D - shares of DKK 910.618. The management of the company has obtained the right to subscribe for shares Alkalon A/S for a nominal capital value of DKK 172.500 representing 9,33% of Capital.

Notes

All amounts in DKK.

		31/12 2015	31/12 2014
8.	**Results brought forward**		
	Results brought forward 1 January 2015	1.757.999	5.370.429
	Profit or loss for the year brought forward	-1.402.480	-7.626.071
	Premium relating to capital increase	0	4.013.641
		355.519	**1.757.999**

9. Mortgage and securities

For bank debts, t.kr. 5.143, the company has provided security in company assets representing a nominal value of t.kr. 9.500.

10. Contingent liabilities

The Company has entered into lease agreements for premises with an annual rent of approx. t.kr. 243. If the lease is terminated the rent obligation is t.kr. 61.