# CRH Medical Corporation

**522 – 999 Canada Place**
**Vancouver, BC**
**V6C 3E1**

# First Quarter Ended March 31, 2015
# Financial Report

**Trading Information:** Toronto Stock Exchange (Symbol "CRH")
**For Information Contact:** Richard Bear, Chief Financial Officer
**Email:** info@crhmedcorp.com
**Web:** www.crhmedcorp.com

For further information about CRH Medical Corporation, please visit the Company website at www.crhmedcorp.com or www.sedar.com or email us at info@crhmedcorp.com.

# CRH MEDICAL CORPORATION

## MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2015

The following discussion and analysis should be read in conjunction with CRH Medical Corporation's (the "Company" or "CRH") unaudited condensed consolidated interim financial statements for the three months ended March 31, 2015 and 2014 and the annual consolidated financial statements and the corresponding notes thereto for the year ended December 31, 2014. The unaudited condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Unless otherwise specified, all financial data is presented in United States dollars. This management discussion and analysis is as of April 28, 2015.

### CAUTION REGARDING FORWARD-LOOKING STATEMENTS

Information included or incorporated by reference in this report may contain forward-looking statements. This information may involve known and unknown risks, uncertainties, and other factors which may cause our actual results, performance, or achievements to be materially different from the future results, performance, or achievements expressed or implied by any forward-looking statements. Forward-looking statements, which involve assumptions and describe our future plans, strategies, and expectations, are generally identifiable by use of the words "may," "will," "should," "expect," "anticipate," "estimate," "believe," "plan," "intend" or "project" or the negative of these words or other variations on these words or comparable terminology. Readers are cautioned regarding statements discussing profitability; growth strategies; anticipated trends in our industry; our future financing plans; and our anticipated needs for working capital. Forward looking statements in this report include statements regarding additional acquisitions, increasing revenue and operating EBITDA, continued growth of our business and leveraging our capabilities. Actual events or results may differ materially from those discussed in forward-looking statements. There can be no assurance that the forward-looking statements currently contained in this report will in fact occur. The Company bases its forward-looking statements on information currently available to it, and assumes no obligation to update them. The Company disclaims any intent or obligations to update or revise publicly any forward-looking statements whether as a result of new information, estimates or options, future events or results or otherwise, unless required to do so by law.

Forward-looking information reflects current expectations of management regarding future events and operating performance as of the date of this document. Such information involves significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not such results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in forward-looking information, including, without limitation: our need for additional financing and our estimates regarding our capital requirements, future revenues and profitability; unfavourable economic conditions could have an adverse effect on our business; risks related to the Company's credit facilities; the policies of health insurance carriers may affect the amount of revenue the Company receives; our ability to successfully market and sell our products and services; our estimates of the size of the potential markets for our products and services; we may be subject to competition and technological risk which may impact the price and amount of product we can sell and nature of services we can provide; our ability to and the cost of compliance with extensive existing regulation and any changes or amendments thereto;

changes within the medical industry and third-party reimbursement policies and our estimates of associated timing and costs with the same; changes in key United States federal or state laws, rules, and regulations; our ability to establish, maintain and defend intellectual property rights; risks related to U.S. antitrust regulations; risks related to record keeping and confidentiality by our affiliated physicians; our ability to recruit and retain qualified physicians to provide our services; our ability to enforce non-competition covenants of any departed physicians; risks related to corporate practice of medicine and our ability to renew and maintain agreements with anesthesiologists and other contractors; risks related to our ability to renegotiate, renew or replace services agreements under which we provide anesthesia services; risks related to changes in regulations that would necessitate adapting or re-negotiating our existing operating agreements; our ability and forecasts of expansion and the Company's management of anticipated growth; our senior management has been key to our growth and we may be adversely affected if we are unable to retain, conflicts of interest develop with or we lose any key member of our senior management; risks associated with manufacture of our products and our economic dependence on suppliers; changes in the industry and the economy may affect the Company's business; risks related to the competitive nature of the medical industry; evolving regulation of corporate governance and public disclosure may result in additional corporate expenses; adverse events relating to our product or services could result risks relating to in product liability, medical malpractice, other legal claims, insurance, product recalls and other liabilities; risks associated with use of our products in unapproved circumstances; various risks associated with legal, regulatory or investigative proceedings; health and safety risks are intrinsic within our industry; our ability to successfully identify evaluation and complete future transactions; anti-takeover provisions create risks related to lost opportunities; we may not continue to attract gastroenterologists and other licensed providers to purchase and use the CRH O'Regan System or to provide our services; risks associated with the trading of our common shares on a public marketplace; risks related to adverse movements in foreign currency exchange rates; and risks related to maintaining our foreign private issuer status.

Although the GAA acquisition has diversified the Company's revenue sources, any adverse event directly or indirectly related to the CRH O'Regan System will have a material impact on the Company's financial performance. In addition, there is a risk that some or all of the expected benefits from the GAA acquisition will not be realized, and risks associated with the integration of the GAA business, as planned.

**OVERVIEW**

CRH Medical Corporation is a North American company focused on providing physicians with innovative products and services for the treatment of gastrointestinal diseases. The Company's product distribution strategy focuses on physician education, patient outcomes, and patient awareness. The Company's first product, the CRH O'Regan System, is a single use, disposable, hemorrhoid banding technology that is safe and highly effective in treating hemorrhoid grades I – IV. CRH distributes the CRH O'Regan System, treatment protocols, operational and marketing expertise as a complete, turnkey package directly to physicians, allowing CRH to create meaningful relationships with the physicians it serves. In 2014, CRH acquired a full service gastroenterology anesthesia company, Gastroenterology Anesthesia Associates, LLC ("GAA"), which provides anesthesia services for patients undergoing endoscopies and colonoscopies and has complemented this acquisition with further acquisitions of anesthesia transactions announced during the first quarter of 2015. Anesthesia assisted endoscopies makes these procedures more comfortable for patients and allows gastroenterologists to perform more procedures. CRH plans to leverage the capabilities it acquired through GAA to consolidate the highly fragmented gastroenterology anesthesia provider business. The Company's goal

is to establish CRH as the premier provider of innovative products and essential services to gastroenterologists throughout the United States.

The Company has financed its cash requirements primarily from revenues generated from the sale of its product directly to physicians, anesthesia sales, equity financings, debt financings and a prior line of credit. The Company's ability to maintain the carrying value of its assets is dependent on successfully marketing its products and services and maintaining future profitable operations, the outcome of which cannot be predicted at this time. The Company has also stated its intention to acquire or build additional anesthesia businesses. It may be necessary for the Company to raise additional funds for the continuing development of its business plan, including additional acquisitions.

For further information about CRH Medical Corporation, including the Company's Annual Information Form, please visit the Company website at www.crhmedcorp.com or www.sedar.com, or email us at info@crhmedcorp.com.

## RECENT EVENTS

*Bought Deal Equity Offering – March 25, 2015*

On March 25, 2015, the Company closed a bought deal equity offering and over-allotment option of 7,000,000 and 1,050,000 common shares, respectively, at a price of $2.72 (CAD$3.40) per common share for gross proceeds of $21,865,893 (CAD$27,370,000). In connection with the offering, the underwriters were paid a 6% commission totaling approximately $1,311,954 (CAD$1,642,200). The Company also issued 241,500 Broker Warrants with a total value of $249,149 to the underwriters and incurred additional share issuance costs of $269,539 (CAD$337,388) in relation to the offering.

The proceeds of the offering were used in part to reduce corporate indebtedness and the balance will be used to fund future acquisitions, as well as for working capital and general corporate purposes.

*Transactions – March 2, 2015*

On March 2, 2015, the Company closed two transactions to provide anesthesia services to four ambulatory surgery centers in Florida and North Carolina representing approximately 9,000 patient procedures per year. The first transaction, representing the acquisition of two anesthesia providers servicing three ambulatory surgery centers and approximately 5,000 annual procedures was effective March 1, 2015. The Company paid $600,000 at close for the transaction; the transaction was financed by cash on hand. The second transaction represents a new anesthesia services customer and will be effective in May 2015.

## NON-IFRS FINANCIAL MEASURES

In addition to results reported in accordance with IFRS, the Company uses certain non-IFRS financial measures as supplemental indicators of its financial and operating performance. These non-IFRS financial measures include Operating EBITDA and Operating expenses – adjusted. The Company believes these supplementary financial measures reflect the Company's ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in its business.

The Company defines Operating EBITDA as operating earnings before interest, taxes, depreciation, amortization, stock based compensation and acquisition related corporate expense. Operating EBITDA is presented on a basis consistent with the Company's internal management reports. The Company discloses Operating EBITDA to capture the profitability of its business before the impact of items not considered in management's evaluation of operating unit performance.

The Company defines Operating expenses – adjusted as operating expenses before expenses related to acquisitions, stock based compensation, depreciation and amortization. Operating expenses – adjusted is presented on a basis consistent with the Company's internal management reports. The Company discloses Operating expenses – adjusted to capture the non-recurring expenses of the business before the impact of items not considered in management's evaluation of operating expenses. The Company also discloses Operating expenses – adjusted by segment.

Operating EBITDA and Operating expenses – adjusted do not have any standardized meaning prescribed by IFRS and therefore may not be comparable to similar measures presented by other companies. The Company cautions readers to consider these non-IFRS financial measures in addition to, and not as an alternative for, measures calculated in accordance with IFRS.

**SELECTED QUARTERLY INFORMATION**

| | Q1 2015 | Q1 2014 |
|---|---|---|
| Product sales revenue | $ 2,162,519 | $ 1,991,224 |
| Anesthesia services revenue | 7,457,131 | - |
| **Total revenue** | **9,619,650** | **1,991,224** |
| | | |
| Operating expenses – adjusted[1] | | |
| Product sales | 904,185 | 866,915 |
| Anesthesia services | 2,984,159 | - |
| Corporate | 638,305 | 433,646 |
| **Total operating expenses - adjusted[1]** | **4,526,649** | **1,300,561** |
| | | |
| **Operating EBITDA[2]** | **5,093,001** | **690,663** |
| | | |
| Operating income | 3,319,658 | 562,324 |
| Net income and comprehensive income | $ 1,924,047 | $ 368,389 |
| | | |
| Earnings per share basic | $ 0.031 | $ 0.008 |
| Earnings per share diluted | $ 0.030 | $ 0.007 |
| | | |
| Total assets | $ 89,352,156 | $ 9,249,921 |
| Total non-current liabilities | 42,599,617 | - |
| Total liabilities | $ 47,443,614 | $ 461,371 |

[1] Operating expenses - adjusted: This is a non-IFRS measure defined as operating expenses before acquisition related corporate expenses, stock based compensation, depreciation and amortization. Refer to the end of this document for the reconciliation of reported financial results to non-IFRS measures.

[2] Operating EBITDA: This is a non-IFRS measure defined as operating income before interest, taxes, depreciation, amortization stock based compensation and acquisition related corporate expense. Refer to the end of this document for the reconciliation of reported financial results to non-IFRS measures.

## RESULTS OF OPERATIONS

### Revenue

Revenues for the three months ended March 31, 2015 were $9,619,650 compared to $1,991,224 for the three months ended March 31, 2014. The increase in revenues is mainly attributable to the Company's newly acquired anesthesia service providers, with total revenue contributions from these acquisitions of $7,457,131 in combination with an increase in product sales of $171,295.

Revenues from product sales for the quarter ended March 31, 2015 were $2,162,519 compared to $1,991,224 for the quarter ended March 31, 2014. The 9% increase in product sales is the result of the continuing successful execution of the Company's direct to physician program that provides physicians the ability to purchase our hemorrhoid banding technology, treatment protocols, marketing and operational experience. As of March 31, 2015 the Company has trained 1,983 physicians to use the O'Regan System, representing 730 clinical practices. This compares to 1,690 physicians trained, representing 609 clinical practices, as of March 31, 2014. Based on historical information, the first quarter of the year represents approximately 23% of total annual product revenue.

In the future, the Company expects revenue from product sales to continue to increase as we expand our physician network and increase physician use of our technology.

Revenues from anesthesia services for the quarter ended March 31, 2015 were $7,457,131. On March 1, 2015, the Company announced the acquisition of additional services providers. The first acquisition was effective on March 1, 2015 and, as such, the Company's results of operations contain one month of activity from this acquisition and three months of activity from its initial acquisition which completed in December 2014 (the other transaction will not be included in operations until May 2015). As a result, there is no comparison to the first quarter of 2014. The new transaction in 2015 contributed revenue of $163,031 during the quarter. Based on historical information, the first quarter of the year represents approximately 21% of total annual anesthesia revenues. During the quarter, the anesthesia services segment serviced 12,395 patient cases through 12 anesthesia service center agreements.

In the future, the Company expects anesthesia revenue to increase through organic growth and through additional acquisitions.

### Total operating expenses - adjusted

For the quarter ended March 31, 2015, total adjusted operating expenses were $4,526,649 compared to $1,300,561 for the first quarter of 2014. The $3,226,088 increase is primarily related to adjusted operating expenses for anesthesia services as the prior year comparable quarter does not contain any anesthesia activity.

Product sales adjusted operating expenses for the quarter were $904,185 compared to $866,915 for the comparable quarter in 2014. The increase in expenses compared to the first quarter of 2014 is a reflection of increased product cost and support resulting from increased sales. Product sales increased by 9% in the period, compared to an increase in expenses of 4%. Effective February 17, 2014, the Company began invoicing customers for the 2.3% medical device excise tax. Prior to February 17, 2014 the Company was expensing the cost of the medical device excise tax. This has contributed to product sales growth outpacing the growth in expenses during the quarter. Product sales expenses primarily include employee wages, product cost and support, marketing programs, office expenses, professional fees, and insurance. In the future, the Company expects adjusted operating expenses to increase as the Company continues to invest in activities designed to increase demand for training and use of the CRH O'Regan System.

Anesthesia services adjusted operating expenses for the quarter ended March 31, 2015 were $2,984,159. Anesthesia services expenses primarily include labor related cost for the medical director and certified registered nurse anesthetists, medical drugs and supplies, and billing and management related expenses. The anesthesia segment of the Company was acquired and introduced in the last quarter of 2014, hence the first quarter of 2014 is not comparable. Adjusted operating expense, as a percent of revenues, was 40% in the quarter.

Corporate adjusted operating expenses for the quarter ended March 31, 2015 were $638,305 compared to $433,646 for the first quarter of 2014. This reflects a growth in expenses in 2015 of $204,659. The growth in corporate expenses is primarily the result of an increase in employee related costs and professional fees and, in general, is reflective of the additional activities incurred in support of the Company's expanded service offering.

**Operating EBITDA**

Operating EBITDA for the quarter was $5,093,001, an increase of $4,402,338 from the first quarter of 2014. This is primarily a reflection of the Company's newly acquired anesthesia service providers offset by net increases in product and corporate operating expenses.

**Operating Income**

Operating income for the quarter ended March 31, 2015 was $3,319,658 compared to $562,324 for the quarter ended March 31, 2014, an increase of $2,757,334. Contributing to the improved operating income is the increase in total Operating EBITDA of $4,402,338, less costs related to the amortization of acquired professional service agreements of $1,402,585 and an increase in stock based compensation expense of $232,474.

The GAA acquisition in December 2014 was financed by cash on hand along with senior and subordinated credit facilities from Knight Therapeutics Inc. and affiliates of Crown Capital Partners Inc., in the amounts of $30,000,000 and CAD$22,500,000 (USD$19,863,000) respectively, as well as a loan from The Bloom Burton Healthcare Structured Lending Fund II and a private placement of the Company's common shares.

As a result of the debt acquired to fund the GAA acquisition in 2014, the Company has recorded net finance expense of $1,665,190 during the quarter. Net finance expense is comprised of both interest and other debt related expenses, as well as foreign exchange gains and losses on the Crown debt which is denominated in Canadian dollars. In the quarter ended March 31, 2015, the Company recorded an exchange gain of $1,402,078 in relation to the Crown note. Excluding the impact of the exchange gain, the finance expense for the period was $3,067,268. During the first quarter of 2015, the Company repaid $7,968,526 in principal on the Knight facility, thereby reducing finance costs relating to this facility in the future.

**Income tax recovery**

For the quarter ended March 31, 2015, the Company recorded an income tax recovery of $269,578 compared to an income tax expense of $193,935 for the quarter ended March 31, 2014. The recovery experienced in the quarter is a reflection of the utilization of previously unrecognized brought forward losses in the US as a result of the income generated by the Company's anesthesia services segment. The Company estimates that it will fully utilize its brought forward tax losses in 2015.

### Net and comprehensive income

For the quarter ended March 31, 2015, the Company recorded net income of $1,924,046 ($0.031 basic and $0.030 diluted income per share) compared to a net income of $368,389 ($0.008 basic and $0.007 diluted income per share) for the first quarter of 2014. The increase in net income year over year is largely a reflection of anesthesia services' contribution to earnings during the quarter.

### SUMMARY OF QUARTERLY RESULTS (Unaudited)

The following table sets forth certain unaudited consolidated statements of operations data expressed in thousands of United States dollars, except for per share figures, for each of the eight most recent quarters that, in management's opinion, have been prepared on a basis consistent with the audited consolidated financial statements for the year ended December 31, 2014

| (in 000's of US$, except EPS) | Q1 '15 | Q4 '14 | Q3 '14 | Q2 '14 | Q1 '14 | Q4 '13 | Q3 '13 | Q2 '13 |
|---|---|---|---|---|---|---|---|---|
| Product sales revenue | 2,163 | 2,360 | 2,200 | 2,046 | 1,991 | 2,047 | 1,851 | 1,950 |
| Anesthesia services revenue | 7,457 | 3,386 | - | - | - | - | - | - |
| **Total revenue** | **9,620** | **5,746** | **2,200** | **2,046** | **1,991** | **2,047** | **1,851** | **1,950** |
| Operating expenses – adjusted[1] | | | | | | | | |
| Product sales[1] | 904 | 978 | 1,034 | 990 | 867 | 1,006 | 926 | 976 |
| Anesthesia services[1] | 2,984 | 1,255 | - | - | - | - | - | - |
| Corporate[1] | 639 | 843 | 445 | 442 | 434 | 402 | 398 | 394 |
| **Total operating expenses – adjusted[1]** | **4,527** | **3,076** | **1,479** | **1,432** | **1,301** | **1,408** | **1,324** | **1,370** |
| **Operating EBITDA[2]** | **5,093** | **2,670** | **721** | **614** | **691** | **639** | **527** | **580** |
| Operating income | 3,320 | 1,285 | 630 | 501 | 562 | 571 | 454 | 502 |
| Net finance expense | 1,665 | 1,623 | - | - | - | - | - | - |
| Income tax expense (recovery) | (269) | (721) | 210 | 174 | 194 | (693) | - | - |
| **Net and comprehensive income** | **1,924** | **383** | **420** | **327** | **368** | **1,264** | **454** | **502** |
| Earnings per share – basic | 0.031 | 0.008 | 0.009 | 0.007 | 0.008 | 0.027 | 0.009 | 0.010 |
| Earnings per share - diluted | 0.030 | 0.007 | 0.009 | 0.007 | 0.007 | 0.027 | 0.009 | 0.010 |

[1] Operating expenses - adjusted: This is a non-IFRS measure defined as operating expenses before acquisition related corporate expenses, stock based compensation, depreciation and amortization. Refer to the end of this document for the reconciliation of reported financial results to non-IFRS measures.

[2] Operating EBITDA: This is a non-IFRS measure defined as operating earnings before interest, taxes, depreciation, amortization, stock based compensation and acquisition related corporate expense. Refer to the end of this document for the reconciliation of reporting financial results to non-IFRS measures.

## LIQUIDITY AND CAPITAL RESOURCES

As at March 31, 2015, the Company had $16,313,885 in cash and cash equivalents compared to $4,133,663 at the end of 2014. The increase in cash and equivalents is primarily a reflection of the bought deal equity offering that the Company completed on March 25, 2015. Net proceeds from the offering were $20,284,399.

Working capital was $16,505,106 compared to negative working capital of $2,577,963 at December 31, 2014. The Company expects to meet its short-term obligations, including short-term obligations in respect of its notes payable through cash earned through operating activities and from the proceeds of its bought deal equity offering completed on March 25, 2015.

The Company has financed its operations primarily from revenues generated from product and anesthesia sales and through equity and debt financings. As of March 31, 2015, the Company has raised approximately $46 million from the sale and issuance of equity securities. The Company has also obtained debt financing of $52 million via senior and subordinated credit facilities with Crown, Bloom Burton and Knight in 2014. There have been no changes in the Crown and Bloom Burton facilities since December 31, 2014; however, in conjunction with the Company's bought deal equity offering, the Company repaid principal of $7,968,526 on its Knight facility. As at March 31, 2015, the Company is in compliance with all debt covenants relating to these facilities.

Although the Company recorded net earnings for the year ending December 31, 2014 and in the current quarter, the Company has incurred historical losses, and as at March 31, 2015 had an accumulated deficit of $10,983,223. The Company expects that going forward cash from operating activities will be positive and will be sufficient to fund the current business.

Cash provided by operating activities for the quarter ended March 31, 2015 was $2,059,756 compared to $731,587 for the first quarter of 2014. The acquisition completed during the quarter was financed by cash on hand.

The Company's near-term cash requirements relate primarily to interest payments, operations, working capital and general corporate purposes, including acquisitions. Based on the current business plan, the Company believes cash and cash equivalents will be sufficient to fund the Company's operating, debt repayment and capital requirements for at least the next 12 months. The Company updates its forecasts on a regular basis and will consider additional financing sources as appropriate.

There were no significant changes, except as previously disclosed in relation to the early repayment of principal under the Knight facility, in the Company's contractual commitments compared with those set forth in the Company's 2014 Management Discussion and Analysis, available on SEDAR at www.sedar.com

## OUTSTANDING SHARE CAPITAL

As at March 31, 2015, there were 69,060,697 common shares issued and outstanding for a total of $46,554,104 in share capital.

As at March 31, 2015, there were 3,635,000 options outstanding at a weighted-average exercise price of $0.54 per share, of which 2,143,149 were exercisable into common shares at a weighted-average exercise price of $0.57 per share. As at March 31, 2015, there were 2,276,000 share units issued and outstanding.

As at April 28, 2015 there were 69,060,697 common shares issued and outstanding for a total of $46,554,104 in share capital. There are 3,635,000 options outstanding at a weighted-average exercise price of $0.57 per share, of which 2,215,014 were exercisable into common shares at a weighted average price of $0.60 per share.

**OFF BALANCE SHEET ARRANGEMENTS**

The Company has no material undisclosed off-balance sheet arrangements that have or are reasonably likely to have, a current or future effect on our results of operations or financial condition.

**PROPOSED TRANSACTIONS**

As at March 31, 2015, the Board of Directors had not committed to proceed with any proposed asset or business acquisitions or dispositions that are not disclosed herein.

**TRANSACTIONS WITH RELATED PARTIES**

Balances and transactions between the Company and its wholly owned subsidiaries and entities over which the Company has control have been eliminated on consolidation. There have been no changes to the Company's identification of related parties, as defined under IAS 24, Related Party Disclosures.

For the period ended March 31, 2015, the Company had related party transactions with key management personnel pertaining to the ordinary course of their employment or directorship arrangements. In addition, the Company made product sales to companies owned or controlled by two of the Company's Directors.

**DISCLOSURE CONTROLS AND PROCEDURES (DCP) AND INTERNAL CONTROLS OVER FINANCIAL REPORTING (ICFR)**

The Company's disclosure controls and procedures are designed to provide reasonable assurance that material information required to be disclosed in the prescribed filings and reports filed with the Canadian securities regulatory authorities is recorded, processed, summarized and reported on a timely basis. The Company's controls are also designed to provide reasonable assurance that information required to be disclosed is assimilated and communicated to senior management in a timely manner so that appropriate decisions can be made regarding public disclosure.

Management has also designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements in accordance with International Financial Reporting Standards. Management, including the Company's Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate ICFR, which has been developed based on the framework established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO (1992)).

During the first quarter of 2015, there were no significant changes in the Company's internal controls over financial reporting that have materially affected or are reasonably likely to affect the Company's internal controls over financial reporting. The Company's management has evaluated the effectiveness of the design of the Company's DCP and ICFR. Based upon the results of that evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as at March 31, 2015, the design of the Company's DCP and ICFR is appropriate.

As permitted by National Instrument 52-109, the evaluation of the design of disclosure controls and procedures and internal controls over financial reporting does not include controls, policies and procedures covering GAA. Prior to its acquisition by the Company, GAA was a privately held company. GAA had revenues of $7,294,100 and expenses of $4,549,499 million which were included in our consolidated financial statements for the quarter ended March 31, 2015.

## CRITICAL ACCOUNTING ESTIMATES

There were no significant changes to the Company's critical accounting estimates during the quarter ended March 31, 2015, except as noted below:

- The Company granted share units during the period. The Company uses a fair value based method of accounting for share-based compensation. As these instruments differ from the options granted in previous years, the Company has applied a binomial pricing model to value these instruments. Similar to the Black-Scholes model which was used to value previously granted options, the application of the binomial pricing model requires management to estimate several variables, including the period for which the instrument is expected to be outstanding, price volatility of the Company's stock over the relevant timeframe, the determination of a relevant risk free interest rate, assumption regarding the Company's future dividend rate policy and estimate of the number of awards that will vest. Changes in one or more assumptions could materially impact the value derived for these equity instruments.
- Historically, the cost of the Company's intangibles assets have been amortized over the estimated useful life ranging from 12 to 20 years. As a result of the acquisition completed on March 1, 2015, the timeframe over which intangibles assets are amortized has been has been revised to a range of 0.7 to 20 years.

CRH's critical accounting estimates are described in its MD&A for the year ended December 31, 2014, filed under the Company's profile on www.sedar.com.

## FUTURE CHANGES IN ACCOUNTING POLICIES

All accounting standards effective for periods beginning on or after January 1, 2015 have been adopted by the Company. New accounting pronouncements issued but not yet effective are described in note 3 to the annual consolidated financial statements for the year ended December 31, 2014. There are no new standards issued subsequent to December 31, 2014 which are considered to have an impact on the Company.

## FINANCIAL INSTRUMENTS

The Company's financial instruments consist of cash and cash equivalents, trade and other receivables, trade and other payables, employee benefit obligations, short term advances, notes payable, and the Company's earn-out obligation. The fair values of these financial instruments, except the notes payable balances and the earn-out obligation, approximate carrying value because of their short-term nature. The Knight debt and the earn-out obligation arising from the Company's acquisition of GAA are classified as financial liabilities recorded at fair value through earnings. For all other debt balances, the fair value of these financial instruments approximates carrying value as the debt was acquired on December 1, 2014 and there have been no events or circumstances subsequent to this date that would suggest a change in fair value.

The Company's financial instruments are exposed to certain financial risks, including credit risk, liquidity risk and market risk. There have been no significant changes to those risks impacting the Company since December 31, 2014, nor has there been a significant change in the composition of its financial instruments since December 31, 2014, except for the following.

- As a result of the close of the Company's bought deal equity offering on March 25, 2015, there has been a significant increase in the Company's cash and cash equivalents. At March 31, 2015, cash and cash equivalents totaled $16,313,885 (December 31, 2014 - $4,133,663). The Company continues to limit its exposure to credit risk on its cash and cash equivalents by placing these financial instruments with high-credit quality financial institutions and only investing in liquid, investment grade securities.
- On March 25, 2015, in conjunction with the close of the Company's bought deal equity offering, the Company repaid $7,968,526 of the principal balance owing, with related interest of $251,063. The Company has used a probability weighted valuation technique in calculating the fair value of the Knight note. Due to the timing of the principal repayment, the Company has revised certain inputs and probabilities relating to estimated cash flows. This resulted in an upward adjustment of $654,249 to the fair value of the Knight note with the impact of the adjustment recorded through finance expense in the period.

## NON-IFRS MEASUREMENTS

The following are non-IFRS measures and investors are cautioned not to place undue reliance on them and are urged to read all IFRS accounting disclosures present in the condensed consolidated interim financial statements and accompanying notes for the three months ended March 31, 2015 and consolidated financial statements and accompanying notes for the year ended December 31, 2014.

The Company uses certain non-IFRS financial measures as supplemental indicators of its financial and operating performance. These non-IFRS financial measures include Operating EBITDA and Operating expenses - adjusted. The Company believes these supplementary financial measure reflects the Company's ongoing business in a manner that allows for meaningful period-to-period comparisons and analysis of trends in its business. These non-IFRS measures do not have any standardized meaning prescribed under IFRS and are therefore unlikely to be comparable to similar measures presented by other companies.

The Company defines Operating EBITDA as operating earnings before interest, taxes, depreciation, amortization, stock based compensation and acquisition related corporate expense. Operating EBITDA is presented on a basis consistent with the Company's internal management reports. The Company discloses Operating EBITDA to capture the profitability of its business before the impact of items not considered in management's evaluation of operating unit performance.

The Company defines Operating expenses - adjusted as operating expenses before acquisition related corporate expense, stock based compensation, depreciation, and amortization. Operating expenses - adjusted is presented on a basis consistent with the Company's internal management reports.

The non-IFRS measures are reconciled to reported IFRS figures in the tables below:

### Operating EBITDA

| **For the three months ended** | **2015** | **2014** | | | | **2013** | | | |
|---|---|---|---|---|---|---|---|---|---|
| *(USD in thousands)* | Mar | Dec | Sep | Jun | Mar | Dec | Sep | Jun | Mar |
| **Total Operating EBITDA** | **5,093** | **2,670** | **721** | **614** | **691** | **639** | **527** | **580** | **371** |
| Amortization expense | (1,402) | (458) | - | - | - | - | - | - | - |
| Depreciation expense | (12) | (13) | (10) | (12) | (18) | (28) | (19) | (18) | (18) |
| Stock based compensation | (343) | (69) | (82) | (101) | (110) | (40) | (54) | (61) | (80) |
| Acquisition expenses | (16) | (845) | - | - | - | - | - | - | - |
| **Operating income** | **3,320** | **1,285** | **629** | **501** | **563** | **571** | **454** | **501** | **273** |

## Operating expenses - adjusted

| For the three months ended | 2015 | 2014 | | | | 2013 | | | |
|---|---|---|---|---|---|---|---|---|---|
| *(USD in thousands)* | Mar | Dec | Sep | Jun | Mar | Dec | Sep | Jun | Mar |
| **Product sales operating expense – adjusted** | **904** | **978** | **1,034** | **990** | **867** | **1,005** | **926** | **976** | **1,105** |
| Amortization expense | - | - | - | - | - | - | - | - | - |
| Depreciation expense | 1 | 1 | - | 1 | 7 | 1 | 9 | 8 | 8 |
| Stock based compensation | 136 | 22 | 19 | 21 | 31 | 20 | 30 | 33 | 45 |
| **Product sales expense** | **1,041** | **1,001** | **1,053** | **1,012** | **905** | **1,026** | **965** | **1,017** | **1,158** |
| **Anesthesia services operating expense – adjusted** | **2,984** | **1,255** | **-** | **-** | **-** | **-** | **-** | **-** | **-** |
| Amortization expense | 1,403 | 458 | - | - | - | - | - | - | - |
| Depreciation expense | - | - | - | - | - | - | - | - | - |
| Stock based compensation | 2 | - | - | - | - | - | - | - | - |
| **Anesthesia services expense** | **4,389** | **1,713** | **-** | **-** | **-** | **-** | **-** | **-** | **-** |
| **Corporate operating expenses – adjusted** | **638** | **843** | **445** | **442** | **434** | **402** | **398** | **394** | **360** |
| Amortization expense | - | - | - | - | - | - | - | - | - |
| Depreciation expense | 11 | 12 | 10 | 11 | 11 | 27 | 10 | 9 | 9 |
| Stock based compensation | 205 | 47 | 63 | 80 | 79 | 21 | 24 | 28 | 34 |
| Acquisition expenses | 16 | 845 | - | - | - | - | - | - | - |
| **Corporate expense** | **870** | **1,747** | **518** | **533** | **524** | **450** | **432** | **431** | **403** |
| **Total operating expense – adjusted** | **4,527** | **3,076** | **1,479** | **1,432** | **1,301** | **1,407** | **1,324** | **1,370** | **1,465** |
| **Total operating expense** | **6,300** | **4,461** | **1,571** | **1,545** | **1,429** | **1,476** | **1,397** | **1,448** | **1,561** |

Condensed Consolidated Interim Financial Statements
(Expressed in United States dollars)

# CRH MEDICAL CORPORATION

(unaudited)

Three months ended March 31, 2015 and 2014

## Notice of no auditor review of Interim 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 financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim 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 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.

# CRH MEDICAL CORPORATION

Condensed Consolidated Balance Sheets
(Unaudited)
(Expressed in United States dollars)

As at March 31, 2015 and December 31, 2014

| | Notes | March 31, 2015 | December 31, 2014 |
|---|---|---|---|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | | $ 16,313,885 | $ 4,133,663 |
| Trade and other receivables | | 4,192,423 | 5,718,651 |
| Current tax receivable | | 53,629 | - |
| Prepaid expenses and deposits | | 314,989 | 181,923 |
| Inventories | | 474,177 | 614,337 |
| | | 21,349,103 | 10,648,574 |
| Non-current assets: | | | |
| Property and equipment | | 149,167 | 129,864 |
| Intangible assets | | 64,793,551 | 65,604,729 |
| Other asset | | 1,348,645 | 1,550,940 |
| Deferred tax assets | | 1,711,690 | 1,030,183 |
| | | 68,003,053 | 68,315,716 |
| Total assets | | $ 89,352,156 | $ 78,964,290 |
| Liabilities | | | |
| Current liabilities: | | | |
| Trade and other payables | | $ 1,687,588 | $ 6,051,213 |
| Employee benefits | | 120,687 | 105,930 |
| Current tax liabilities | | - | 193,612 |
| Notes payable | 8 | 2,773,240 | 6,613,300 |
| Short term advances | | 262,482 | 262,482 |
| | | 4,843,997 | 13,226,537 |
| Non-current liabilities: | | | |
| Notes payable | 8 | 34,844,301 | 39,509,431 |
| Earn-out obligation | | 7,755,316 | 7,440,960 |
| | | 42,599,617 | 46,950,391 |
| Shareholders' equity | | | |
| Share capital | 9 | 46,554,104 | 25,913,839 |
| Contributed surplus | | 6,404,433 | 5,847,564 |
| Accumulated other comprehensive income | | (66,772) | (66,772) |
| Deficit | | (10,983,223) | (12,907,269) |
| Total shareholders' equity | | 41,908,542 | 18,787,362 |
| Total liabilities and shareholders' equity | | $ 89,352,156 | $ 78,964,290 |

See accompanying notes to condensed consolidated interim financial statements.

Approved on behalf of the Board:

"Edward Wright" Director
Edward Wright

"Anthony Holler" Director
Anthony Holler

# CRH MEDICAL CORPORATION

Condensed Consolidated Interim Statements of Operations and Comprehensive Income
(Unaudited)
(Expressed in United States dollars)

Three month periods ended March 31, 2015 and 2014

| | Notes | | Three months ended March 31, 2015 | | Three months ended March 31, 2014 |
|---|---|---|---|---|---|
| Revenue: | | | | | |
| Product sales | 12 | $ | 2,162,519 | $ | 1,991,224 |
| Anesthesia services | 12 | | 7,457,131 | | - |
| | | | 9,619,650 | | 1,991,224 |
| Expenses: | | | | | |
| Product sales expense | 5 | | 1,040,336 | | 904,903 |
| Anesthesia services expense | 6 | | 4,389,083 | | - |
| Corporate expense | 7 | | 870,573 | | 523,997 |
| | | | 6,299,992 | | 1,428,900 |
| Operating income | | | 3,319,658 | | 562,324 |
| Net finance income | 10 | | (1,402,078) | | - |
| Net finance expense | 10 | | 3,067,268 | | - |
| Income and comprehensive income before tax | | | 1,654,468 | | 562,324 |
| Income tax (recovery) | | | (269,578) | | 193,935 |
| Net and comprehensive income | | $ | 1,924,046 | $ | 368,389 |
| Earnings per share - basic | 9(c) | $ | 0.031 | $ | 0.008 |
| - diluted | 9(c) | $ | 0.030 | $ | 0.007 |
| Weighted average shares outstanding: - basic | | | 61,466,638 | | 48,779,026 |
| - diluted | | | 64,456,374 | | 49,221,007 |

See accompanying notes to condensed consolidated interim financial statements.

# CRH MEDICAL CORPORATION

Condensed Consolidated Interim Statements of Changes in Equity
(Unaudited)
(Expressed in United States dollars)

Three month periods ended March 31, 2015 and 2014

| | Number of shares | Share capital | Contributed surplus | Accumulated other comprehensive income | Deficit | Total |
|---|---|---|---|---|---|---|
| Balance as at January 1, 2014 | 48,746,914 | $ 17,181,474 | $ 5,570,839 | $ (66,772) | $ (14,405,422) | $ 8,280,119 |
| Total net and comprehensive income for the period | - | - | - | - | 368,389 | 368,389 |
| Transactions with owners, recorded directly in equity: | | | | | | |
| Stock based compensation for stock option plan | - | - | 110,218 | - | - | 110,218 |
| Common shares purchased on exercise of options | 50,000 | 46,315 | (16,490) | - | - | 29,825 |
| Balance as at March 31, 2014 | 48,796,914 | 17,227,789 | 5,664,567 | (66,772) | (14,037,033) | 8,788,551 |
| Balance as at January 1, 2015 | 60,881,947 | 25,913,839 | 5,847,564 | (66,772) | (12,907,269) | 18,787,362 |
| Total net and comprehensive income for the period | - | - | - | - | 1,924,046 | 1,924,046 |
| Transactions with owners, recorded directly in equity: | | | | | | |
| Stock based compensation for stock option and share unit plans | - | - | 342,693 | - | - | 342,693 |
| Common shares purchased on exercise of options | 128,750 | 152,846 | (34,973) | - | - | 117,873 |
| Shares issued through share offering, net of fees (note 9) | 8,050,000 | 20,284,399 | - | - | - | 20,284,399 |
| Deferred tax recovery on share issuance costs (note 9) | - | 452,169 | - | - | - | 452,169 |
| Broker warrants issued in connection with share offering (note 9) | - | (249,149) | 249,149 | - | - | - |
| Balance as at March 31, 2015 | 69,060,697 | $ 46,554,104 | $ 6,404,433 | $ (66,772) | $ (10,983,223) | $ 41,908,542 |

See accompanying notes to condensed consolidated interim financial statements.

# CRH MEDICAL CORPORATION

Condensed Consolidated Interim Statements of Cash Flows
(Unaudited)
(Expressed in United States dollars)

Three month periods ended March 31, 2015 and 2014

| | | Three months ended | |
|---|---|---|---|
| | | March 31, 2015 | March 31, 2014 |
| Cash provided by (used in): | | | |
| Operating activities: | | | |
| Net income | | $ 1,924,046 | $ 368,389 |
| Adjustments for: | | | |
| Depreciation of property, equipment and intangibles | | 1,414,568 | 18,121 |
| Stock based compensation | | 342,693 | 110,218 |
| Unrealized foreign exchange (gain) | | (1,396,695) | - |
| Net finance expense | | 3,067,268 | - |
| Income tax expense (recovery) | | (269,578) | 193,935 |
| Operating activity before changes in operating assets and liabilities | | 5,082,302 | 690,663 |
| Taxes paid | | (207,000) | - |
| Change in trade and other receivables | | 1,526,228 | 36,116 |
| Change in prepaid expenses and deposits | | (133,066) | (52,647) |
| Change in inventories | | 140,160 | (50,661) |
| Change in trade and other payables | | (4,363,625) | 21,596 |
| Change in employee benefits | | 14,757 | 86,520 |
| Cash provided by operating activities | | 2,059,756 | 731,587 |
| Financing activities | | | |
| Net proceeds on the issuance of shares | | 20,284,399 | - |
| Repayment of notes payable, principal and interest | | (9,653,658) | - |
| Proceeds from the issuance of shares relating to stock based compensation | | 117,873 | 29,825 |
| Cash provided by financing activities | | 10,748,614 | 29,825 |
| Investing activities: | | | |
| Acquisition of property and equipment | | (22,693) | (1,115) |
| Acquisition of anesthesia services provider | 4 | (600,000) | - |
| Cash used in investing activities | | (622,693) | (1,115) |
| Effects of foreign exchange on cash and cash equivalents | | (5,455) | - |
| Increase in cash and cash equivalents | | 12,180,222 | 760,297 |
| Cash and cash equivalents, beginning of period | | 4,133,663 | 6,602,798 |
| Cash and cash equivalents, end of period | | $ 16,313,885 | $ 7,363,095 |

See accompanying notes to condensed consolidated interim financial statements.

**1. Reporting entity:**

CRH Medical Corporation ("CRH" or "the Company") was incorporated on April 21, 2001 and is incorporated under the Business Corporations Act and specializes in the treatment of hemorrhoids utilizing its treatment protocol and patented proprietary technology. The Company also provides anesthesiology services to gastroenterologists in the southeastern United States through its subsidiaries. Refer to note 4.

CRH principally operates in the United States and is headquartered from its registered offices located at Unit 522, 999 Canada Place, Vancouver, British Columbia, Canada.

**2. Basis of preparation:**

(a) Statement of compliance:

These unaudited condensed consolidated interim financial statement of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Accordingly, these condensed consolidated interim financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including International Accounting Standard 34, Interim Financial Reporting ("IAS 34"). These condensed consolidated interim financial statements do not include all the information and note disclosures required by IFRS for annual financial statements and therefore should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto for the year ended December 31, 2014. In management's opinion, all adjustments considered necessary for fair presentation have been included in these financial statements. Interim results are not necessarily indicative of the results expected for the fiscal year. Certain comparative figures have been reclassified to conform to the current period's presentation.

The condensed consolidated interim financial statements were authorized for issue by the Board of Directors on April 28, 2015.

(b) Basis of measurement:

The Company's condensed consolidated interim financial statements have been prepared on a going concern and historical cost basis except for certain financial instruments which are recorded at fair value.

(c) Functional and presentation currency:

These condensed consolidated interim financial statements are presented in United States dollars, which is the Company's functional currency.

**2. Basis of preparation (continued):**

(d) Use of estimates, assumptions and judgments:

The preparation of the Company's condensed consolidated interim financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies, the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Significant areas requiring the use of management estimates relate to the assessment for impairment and useful lives of intangible assets, determining the fair value of share units, estimates of accruals, estimation of useful lives of property, plant and equipment, estimates supporting reported revenues, the recoverability of trade receivables, the valuation of certain long term liabilities and other assets, including liabilities relating to contingent consideration, the valuation of acquired intangibles and the valuation of deferred tax assets

Significant judgments made by management in the process of applying accounting policies and that have the most significant effect on the amounts recognized in the consolidated financial statements includes the determination of functional currency and the accounting classification of financial instruments. In conjunction with the Company's business acquisition, these judgments also include the Company's determination of control for the purposes of consolidation, the Company's definition of a business, as well as the allocation of purchase consideration to the fair value of assets acquired and liabilities assumed.

Reported amounts and note disclosures reflect the overall economic conditions that are most likely to occur and anticipated measures management intends to take. Actual results could differ from those estimates.

**3. Significant accounting policies:**

These condensed consolidated interim financial statements have been prepared using the significant accounting policies and methods of computation consistent with those applied in the Company's December 31, 2014 annual consolidated financial statements.

The Company has not early adopted any amendment, standard or interpretation that has been issued by the IASB but is not yet effective. Amendments, standards and interpretations that are issued but not yet effective are described in the Company's annual financial statements for the period ended December 31, 2014.

The Company's interim results are not necessarily indicative of its results for a full year.

## 4. Business combinations:

On March 1, 2015, a subsidiary of the Company entered into an asset purchase agreement to purchase certain assets of two anesthesia services providers in the Southeastern United States. The total purchase price under the asset purchase agreement was $600,000.

The following table summarizes the fair value of the consideration transferred and the preliminary estimated fair values of the assets and liabilities acquired at the acquisition date. Certain of the estimates of fair value, most notably the professional services agreements, may be subject to further adjustments.

| | | |
|---|---|---|
| Cash | $ | 600,000 |
| Purchase consideration | $ | 600,000 |
| Assets and liabilities acquired: | | |
| Exclusive professional services agreements | $ | 600,000 |
| Fair value of net identifiable assets acquired | $ | 600,000 |

The value of the acquired intangible assets, being exclusive professional services agreements, has been determined on a provisional basis and relates to the acquisition of exclusive professional services agreements to provide professional anesthesia services. As at the acquisition date, the exclusive professional services agreements had estimated remaining contractual terms varying from 0.7 to 2.8 years. The Company will amortize these contractual assets the length of the remaining contractual terms. Should the amount allocated to intangible assets materially change in the final purchase price allocation, amortization will be adjusted.

The Company incurred acquisition related costs of $16,082 relating to legal fees which have been expensed as incurred.

In the period March 1, 2015 to March 31, 2015, this acquisition contributed revenue of $163,031 and net earnings before tax of $11,430. The following unaudited supplemental pro forma financial information presents consolidated information as if the acquisition had been completed on January 1, 2015. The pro forma financial information presented below (unaudited) is for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of fiscal 2015. The pro forma financial information (unaudited) presented includes amortization charges for acquired intangible assets based on the values assigned in the purchase price allocation. Amortization charges in the period were $28,376.

| | | 2015 |
|---|---|---|
| **Pro Forma Information (unaudited)** | | |
| Revenue | $ | 489,093 |
| Net income before tax | $ | 34,290 |

**4. Business combinations (continued):**

*Gastroenterology Anesthesia Associates LLC ("GAA")*

On December 1, 2014, a subsidiary of the Company entered into an acquisition agreement to purchase the business, assets and interests of Gastroenterology Anesthesia Associates LLC (the "LLC") and the business interest contained in a management services agreement held by another private entity ("GAAM"), together the combined business hereinafter referred to as "GAA". The total purchase price under the agreement was $58,623,000 paid at closing and up to an additional $14,655,000 payable within 4.5 years based on the achievement of certain financial performance targets of GAA (the "Earn-out obligation"). As at March 31, 2015, the Company has estimated that potential payments in respect of the earn-out obligation will range from $11,981,135 to $14,655,000. The maximum total purchase price assuming achievement of all performance measures is $73,278,000. The earn-out obligation has been recorded at the net present value of its fair value as at the date of the acquisition, discounted at 18%, and changes in the fair value are recorded through earnings.

Included in these condensed consolidated interim financial statements for the three month period ended March 31, 2015 for GAA are sales of $7,294,100 and net earnings before tax of $2,744,602.

CRH has obtained control over GAA through its contractual ability to direct its relevant activities and its right to variable returns.

The following table summarizes the fair value of the consideration transferred and the estimated fair values of the assets and liabilities acquired at the acquisition date. Certain of the estimates of fair value, most notably, professional services agreements and the contingent earn-out obligation are preliminary and may be subject to further adjustments.

| | | |
|---|---|---|
| Cash | $ | 58,623,000 |
| Contingent consideration ("Earn-out obligation") | | 7,339,032 |
| Purchase consideration | | 65,962,032 |
| Assets and liabilities acquired | | |
| Exclusive professional services agreements | | 65,962,032 |
| Cash | | 2,011,548 |
| Pre-close trade receivables | | 4,849,289 |
| Pre-close trade payables | | (6,860,837) |
| **Fair value of net identifiable assets acquired** | $ | 65,962,032 |

The value of the acquired intangible assets, being the exclusive professional services agreements, has been determined on a provisional basis and relates to the acquisition of exclusive professional services agreements to provide professional anesthesia services. As at the acquisition date, the exclusive professional services agreements had a remaining contractual term of 6 years and 11 months and can be renewed by agreement of both parties. The Company amortizes these contractual assets over a term of 12 years.

## 5. Product sales expense:

For the three month periods ended March 31:

| | | 2015 | | 2014 |
|---|---|---|---|---|
| Employee related | $ | 331,471 | $ | 348,834 |
| Product cost and support | | 463,046 | | 419,831 |
| Professional fees | | 38,853 | | 47,556 |
| Office related | | 50,662 | | 38,868 |
| Stock based compensation | | 135,502 | | 30,769 |
| Insurance | | 14,275 | | 11,826 |
| Depreciation and amortization | | 649 | | 7,219 |
| Foreign exchange | | 5,878 | | - |
| | $ | 1,040,336 | $ | 904,903 |

## 6. Anesthesia services expense:

For the three month periods ended March 31:

| | | 2015 | | 2014 |
|---|---|---|---|---|
| Employee related | $ | 1,707,300 | $ | - |
| Amortization | | 1,402,585 | | - |
| Bad debt expense | | 383,706 | | - |
| Office related | | 730,711 | | - |
| Medical supplies | | 162,042 | | - |
| Stock based compensation | | 2,339 | | - |
| Professional fees | | 400 | | - |
| | $ | 4,389,083 | $ | - |

## 7. Corporate expense:

For the three month periods ended March 31:

| | | 2015 | | 2014 |
|---|---|---|---|---|
| Employee related | $ | 246,009 | $ | 216,798 |
| Professional expenses | | 162,978 | | 75,952 |
| Corporate | | 93,341 | | 74,040 |
| Stock based compensation | | 204,852 | | 79,449 |
| Travel and entertainment | | 62,244 | | 36,441 |
| Office related | | 33,902 | | 16,916 |
| Insurance | | 41,440 | | 13,499 |
| Acquisition expenses | | 16,082 | | - |
| Depreciation and amortization | | 11,334 | | 10,902 |
| Foreign exchange | | (1,609) | | - |
| | $ | 870,573 | $ | 523,997 |

## 8. Notes payable:

| March 31, 2015 | Crown Note | Knight Note | Knight Annual Fee | Bloom Burton Facility | Total |
|---|---|---|---|---|---|
| Current portion | $ - | 1,988,758 | 784,482 | - | $ 2,773,240 |
| Non-current portion | 15,014,552 | 17,819,193 | - | 2,010,556 | 34,844,301 |
| Total loans and borrowings | $ 15,014,552 | 19,807,951 | 784,482 | 2,010,556 | $ 37,617,541 |

| December 31, 2014 | Crown Note | Knight Note | Knight Annual Fee | Bloom Burton Facility | Total |
|---|---|---|---|---|---|
| Current portion | $ 193,950 | 5,666,667 | 752,683 | - | $ 6,613,300 |
| Non-current portion | 16,224,216 | 21,338,826 | - | 1,946,389 | 39,509,431 |
| Total loans and borrowings | $ 16,418,166 | 27,005,493 | 752,683 | 1,946,389 | $ 46,122,731 |

*Norrep Credit Opportunities Fund II, LP ("Crown Note")*

On December 1, 2014, the Company entered into an agreement to borrow funds in the form of a subordinated note payable from Norrep Credit Opportunities Fund II, LP. At inception, the original amount of the note payable was CAD$22,500,000 (USD$19,863,000). The note bears interest at 12% per annum with a decrease to 10% upon repayment and performance in full of the Company's obligations under its senior credit agreement (see Knight Note). Interest on the note is payable on a quarterly basis beginning March 31, 2015, with the payment of the principal scheduled for June 1, 2018. In compensation for its services, the Company paid Crown a combination of cash CAD$1,350,000 (USD$1,191,780) and shares (2,000,000 common shares) in addition to reimbursement of legal costs in relation to issuance of the note. The Crown note is subordinate to the Knight note. The note is classified as an other financial liability and recorded at amortized cost.

*Knight Therapeutics Inc. ("Knight Note")*

On December 1, 2014, the Company entered into an agreement to borrow funds in the form of a secured note payable from Knight Therapeutics Inc. At inception, the original amount of the note payable was $30,000,000. The note bears interest at a maximum of 12% per annum. Interest on the note is payable on a quarterly basis beginning March 31, 2015. The earliest maturity date of the loan is December 1, 2016, but may be extended to December 1, 2017 if certain conditions are met. The agreement contains contractual clauses that may require early repayment of a portion of the principal balance should the Company complete an equity financing. In compensation for its services, the Company paid Knight a combination of cash ($1,200,000) and shares (3,000,000 common shares) in addition to reimbursement of legal costs in relation to issuance of the note. The note is classified as an other financial liability and recorded at fair value through earnings.

**8. Notes payable (continued):**

*Knight Therapeutics Inc. ("Knight Note") - continued*

On March 25, 2015, in conjunction with the close of the Company's bought deal equity offering, the Company repaid $7,968,526 of the principal balance owing, with related interest of $251,063. The Company has used a probability weighted valuation technique in calculating the fair value of the Knight note. Due to the timing of the principal repayment, the Company has revised certain inputs and probabilities relating to estimated cash flows. This resulted in an upward adjustment of $654,249 to the fair value of the Knight note with the impact of the adjustment recorded through finance expense in the period. The principal repayment satisfies the Company's contractual requirement to repay a portion of the outstanding principal balance should the Company complete an equity financing.

*Knight Therapeutics Inc. – Annual Fee ("Knight Annual Fee")*

In accordance with the Knight note agreement, the Company is obligated to pay an annual fee relating to a comfort letter provided by Knight in respect of the Company's earn-out obligation (note 4). This fee has been recognized as a separate financial liability, and recorded at fair value based on the Company's best estimate of the amount to be paid, and subsequently measured at amortized cost.

*Bloom Burton Healthcare Structured Lending Fund II ("Bloom Burton Facility")*

On December 1, 2014, the Company entered into an unsecured facility agreement with Bloom Burton Healthcare Structured Lending Fund II ("Bloom Burton") with a maximum borrowing limit of $2,000,000. The facility bears interest at 12% per annum. Accrued interest is payable on the maturity date or the date of any voluntary prepayment of the loan. Full payment is required within 54 months after the first advance under the facility or at date mutually agreed between the Company and Bloom Burton. As at March 31, 2015, the Company had drawn $2,000,000 under the facility. The facility is subordinate to the Knight note. The facility is classified as an other financial liability and recorded at amortized cost.

The consolidated minimum loan payments (principal and interest) for all loan agreements in the future are as follows:

| | Minimum Principal and Interest |
|---|---|
| At March 31, 2015 | |
| Not later than one year | $ 5,210,797 |
| Between one and five years | $ 49,225,556 |
| | $ 54,436,353 |

**9. Share capital:**

(a) Issued and outstanding – common shares:

On March 25, 2015, the Company closed a bought deal equity offering and over-allotment option of 7,000,000 and 1,050,000 common shares, respectively, at a price of $2.72 (CAD$3.40) per common share for gross proceeds of $21,865,893 (CAD$27,370,000). In connection with the offering, the underwriters were paid a 6% commission totaling approximately $1,311,954 (CAD$1,642,200) and received 241,500 broker warrants with a fair value of $249,149 (CAD$311,535). Additional share issuance costs of $269,539 (CAD$337,388) were incurred in relation to the offering. The Company has recorded a deferred tax asset of $452,169 in relation to those share issuance costs incurred in relation to the offering. The deferred tax asset has been offset against share capital.

(b) Share unit plan:

In June 2014, the shareholders of the Company approved a Share Unit Plan. Employees, directors and eligible consultants of the Company and its designated subsidiaries are eligible to participate in the Share Unit Plan. In accordance with the terms of the plan, the Company will approve those employees, directors and eligible consultants who are entitled to receive share units and the number of share units to be awarded to each participant. Each share unit awarded conditionally entitles the participant to receive one common share of the Company upon attainment of the share unit vesting criteria. The vesting of share units is conditional upon the expiry of time-based vesting conditions, performance-based vesting conditions or a combination of the two. Once the share units vest, the participant is entitled to receive the equivalent number of underlying common shares.

The Company issued 2,276,000 share units during the period ended March 31, 2015. Of these units, 276,000 units vest over a 4 year term, with 50% vesting on the second anniversary and 25% vesting on each of the third and fourth anniversaries. The fair value per unit was $2.97 (CAD$3.72) based on the market value of the underlying shares at the date of issuance. The remaining 2,000,000 share units vest upon the Company meeting certain market based performance targets. The weighted average fair value of these units at the date of grant was $1.67 (CAD$2.09) per unit. The fair value of these share units was calculated as of the grant date using a binomial pricing model with the following weighted average assumptions:

| | 2015 |
|---|---|
| Risk-free interest rate | 0.61% |
| Expected volatility | 60.5% |
| Pre-vest forfeiture rate | 0% |
| Weighted average share price | CAD$2.45 |

For the three months ended March 31, 2015, the Company recognized $195,084 (2014 - $nil), in compensation expense in relation to the granting and vesting of share units. The Company also recognized $147,609 of compensation expense (2014 - $110,218) in relation to share options previously granted.

## 9. Share capital (continued):

(c) Earnings per share:

The calculation of basic earnings per share for the three months ended March 31, 2015 and 2014 is as follows:

| | 2015 | | | 2014 | | |
|---|---|---|---|---|---|---|
| | Net income | Weighted average number of common shares outstanding | Per share amount | Net income | Weighted average number of common shares outstanding | Per share amount |
| **Net earnings:** | | | | | | |
| Earnings per common share: | | | | | | |
| Basic | $ 1,924,046 | 61,466,638 | $ 0.031 | $ 368,389 | 48,779,026 | $ 0.008 |
| Share options | | 2,713,736 | | | 441,981 | |
| Share units | | 276,000 | | | - | |
| Diluted | $ 1,924,046 | 64,456,374 | $ 0.030 | $ 368,389 | 49,221,007 | $ 0.007 |

As at March 31, 2015, 921,264 options (2014 – 4,028,019) and 2,000,000 share units (2014 – nil) were excluded from the diluted weighted average number of common shares calculation.

The average market value of the Company's shares for purposes of calculating the dilutive effect of share options was based on quoted market prices for the period during which the options were outstanding.

## 10. Net finance expense

Recognized in earnings in the three month periods ended March 31:

| | 2015 | 2014 |
|---|---|---|
| Finance income: | | |
| Foreign exchange (gain) | $(1,402,078) | $ - |
| Total finance income | $(1,402,078) | $ - |
| Finance expense: | | |
| Interest and accretion expense on borrowings | $ 1,896,367 | - |
| Accretion expense on earn-out obligation | 314,356 | - |
| Amortization of deferred financing fees | 202,296 | - |
| Net change in fair value of financial liabilities at fair value through earnings | 654,249 | - |
| Total finance expense | $ 3,067,268 | $ - |
| Net finance expense | $ 1,665,190 | $ - |

## 11. Financial instruments:

The Company's financial instruments consist of cash and cash equivalents, trade and other receivables, trade and other payables, employee benefit obligations, short term advances, notes payable, and the Company's earn-out obligation. The fair values of these financial instruments, except the notes payable balances and the earn-out obligation, approximate carrying value because of their short-term nature. The Knight debt (note 8) and the earn-out obligation are classified as financial liabilities recorded at fair value through earnings. For all other debt balances, the fair value of these financial instruments approximates carrying value as the debt was acquired on December 1, 2014 and there have been no events or circumstances subsequent to this date that would suggest a change in fair value.

An established fair value hierarchy requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is available and significant to the fair value measurement. There are three levels of inputs that may be used to measure fair value:

- Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 - inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 - inputs for the asset or liability that are not based on observable market data (unobservable inputs).

**11. Financial instruments (continued):**

The following financial assets and liabilities are measured at fair value on a recurring basis using quoted prices in active markets for identifiable assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

| **March 31, 2015** | | Fair Value | | |
|---|---|---|---|---|
| | Carrying Value | Level 1 | Level 2 | Level 3 |
| **Financial liabilities** | | | | |
| Notes payable | $19,807,951 | - | - | $19,807,951 |
| Earn-out obligation | $ 7,755,316 | - | - | $ 7,755,316 |

| **December 31, 2014** | | Fair Value | | |
|---|---|---|---|---|
| | Carrying Value | Level 1 | Level 2 | Level 3 |
| **Financial liabilities** | | | | |
| Notes payable | $27,005,493 | - | - | $27,005,493 |
| Earn-out obligation | $ 7,440,960 | - | - | $ 7,440,960 |

The Company has used a probability weighted valuation technique in calculating the fair value of the Knight note payable and the earn-out obligation. This valuation technique included inputs relating to estimated cash outflows under each arrangement and the use of a discount rate appropriate to the Company (18%). The fair value measurements are sensitive to the discount rate used in calculating the fair values. A 1% increase in the discount rate would reduce the fair value of the Knight note and earn-out obligation, in combination, by $512,858. During the quarter ended March 31, 2015, the Company recorded accretion expense of $1,412,512 in relation to these liabilities, reflecting the change in fair value of the liabilities that is attributable to credit risk.

**Reconciliation of level 3 fair values:**

| | **Notes Payable** | **Earn-out Obligation** | **Total** |
|---|---|---|---|
| Balance as at January 1, 2015 | $27,005,493 | $7,440,960 | $34,446,453 |
| Repayment of principal and interest | (8,949,947) | - | (8,949,947) |
| Recorded in finance expense: | | | |
| Accretion expense | 1,098,156 | 314,356 | 1,412,512 |
| Fair value adjustment | 654,249 | - | 654,249 |
| Balance as at March 31, 2015 | $19,807,951 | $7,755,316 | $27,563,267 |

## 12. Segmented information:

The Company operates in two industry segments: the sale of medical products and the provision of anesthesia services. The revenues relating to geographic segments based on customer location, in United States dollars, for the three months ended March 31, 2015 and 2014 are as follows:

| **Revenue:** | **2015** | **2014** |
|---|---|---|
| Canada | $ 41,111 | $ 38,361 |
| United States | 9,578,539 | 1,952,863 |
| Total | $ 9,619,650 | $ 1,991,224 |

The Company's property and equipment, intangibles and other assets are located in the following geographic regions as at March 31, 2015 and December 31, 2014:

| | **2015** | **2014** |
|---|---|---|
| Property and equipment: | | |
| Canada | $ 147,082 | $ 129,864 |
| United States | 2,085 | - |
| Total | $ 149,167 | $ 129,864 |
| Intangible assets: | | |
| Canada | $ 92,174 | $ 100,767 |
| United States | $ 64,701,377 | 65,503,962 |
| Total | $ 64,793,551 | $ 65,604,729 |
| Other assets: | | |
| Canada | $ 1,348,645 | $ 1,550,940 |
| United States | - | - |
| Total | $ 1,348,645 | $ 1,550,940 |

**12. Segmented information (continued):**

The Company operates in two industry segments, being the sale of medical products and the provision of anesthesia services. Substantially all of the Company's operations, assets and employees are located in Canada and the United States. The financial measures reviewed by the Company's Chief Operating Decision Maker are presented below for the three month periods ended March 31, 2015 and 2014. The Company does not allocate expenses related to corporate activities. These expenses are presented within "Other" to allow for reconciliation to reported measures.

| | 2015 | | | |
|---|---|---|---|---|
| | Product sales | Anesthesia services | Other | Total |
| Revenue | $ 2,162,519 | $ 7,457,131 | $ - | $ 9,619,650 |
| Operating costs | 1,040,336 | 4,389,083 | 870,573 | 6,299,992 |
| Operating income | $ 1,122,183 | $ 3,068,048 | $ (870,573) | $ 3,319,658 |

| | 2014 | | | |
|---|---|---|---|---|
| | Product sales | Anesthesia services | Other | Total |
| Revenue | $ 1,991,224 | $ - | $ - | $ 1,991,224 |
| Operating costs | 904,903 | - | 523,997 | 1,428,900 |
| Operating income | $ 1,086,321 | $ - | $ (523,997) | $ 562,324 |