ZENITH EPIGENETICS

Condensed Interim Consolidated Financial Statements

For the three and six months ended October 31, 2014 and 2013

Condensed Interim Consolidated Statements of Financial Position
(unaudited)

In thousands of US dollars	Notes	October 31, 2014	April 30, 2014
Assets			
Current assets:			
Cash		$ 395	$ 1,151
Clinical supplies		-	31
Prepaid expenses and deposits		101	89
Investment tax credit receivable		507	332
Other assets		74	323
Total current assets		1,077	1,926
Non-current assets:			
Property and equipment		1,470	1,591
Intangible assets		96	185
Clinical supplies		-	30
Total non-current assets		1,566	1,806
Total assets		$ 2,643	$ 3,732
Liabilities			
Current liabilities:			
Trade and other payables		$ 1,483	$ 2,285
Due to Resverlogix Corp.		1,060	167
Warrant liability	9 (e)	752	1,444
Financing rights	8	2,892	3,262
Total liabilities		6,187	7,158
Shareholders' deficit:			
Share capital	9 (a)	38,659	33,987
Contributed surplus		1,333	915
Deficit		(43,536)	(38,328)
Total shareholders' deficit		(3,544)	(3,426)
Total liabilities and shareholders' deficit		$ 2,643	$ 3,732

Commitments (note 11)

Signed on behalf of the Board:

Signed: "Donald McCaffrey" Director

Signed: "Kenneth Zuerblis" Director

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

Condensed Interim Consolidated Statements of Comprehensive Loss

For the three and six months ended October 31

(unaudited)

		Three months ended October 31,		Six months ended October 31,	
In thousands of US dollars	Notes	2014	2013	2014	2013
Expenses:					
Research and development	10	$ 3,137	$ 3,117	$ 6,957	$ 7,139
Investment tax credits		(81)	(57)	(188)	(122)
Net research and development		3,056	3,060	6,769	7,017
General and administrative	10	674	346	1,261	992
		3,730	3,406	8,030	8,009
Finance costs:					
Loss (gain) on change in fair value of warrant liability		(439)	61	(668)	(1,101)
Gain on change in fair value of financing rights		(1,791)	-	(2,212)	-
Interest income		-	(12)	-	(17)
Foreign exchange loss		30	72	33	65
Net finance costs (income)		(2,200)	121	(2,847)	(1,053)
Loss before income taxes		$ 1,530	$ 3,527	$ 5,183	$ 6,956
Income taxes		25	-	25	-
Net and total comprehensive loss		$ 1,555	$ 3,527	$ 5,208	$ 6,956
Net loss per share *(note 9(f))*					
Basic and diluted		$ 0.02	$ 0.05	$ 0.06	$ 0.11

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

Condensed Interim Consolidated Statements of Changes in Shareholders' Deficit

For the six months ended October 31

(unaudited)

In thousands of US dollars	Share Capital	Contributed Surplus	Deficit	Total Shareholders' Deficit
Balance, April 30, 2013	$ 982	$ -	$ (19,168)	$ (18,186)
Distribution of RVX Therapeutics to Zenith Epigenetics Corp.	27,145	-	-	27,145
Common shares issued in connection with warrant exercises	43	-	-	43
Common shares issued in connection with long term incentive plan	3	(3)	-	-
Shared-based payment transactions	-	830	-	830
Net and total comprehensive loss	-	-	(6,956)	(6,956)
Balance, October 31, 2013	$ 28,173	$ 827	$ (26,124)	$ 2,876
Balance, April 30, 2014	$ 33,987	$ 915	$ (38,328)	$ (3,426)
Common shares issued in connection with private placements, net of financing rights	4,426	-	-	4,426
Common shares issued in connection with warrant exercises	154	-	-	154
Common shares issued in connection with stock option plan and long term incentive plan	98	(69)	-	29
Share issue costs	(6)	-	-	(6)
Shared-based payment transactions	-	487	-	487
Net and total comprehensive loss	-	-	(5,208)	(5,208)
Balance, October 31, 2014	$ 38,659	$ 1,333	$ (43,536)	$ (3,544)

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

Condensed Interim Consolidated Statements of Cash Flows

For the six months ended October 31

(unaudited)

In thousands of US dollars	Note	2014	2013
Cash used in:			
Cash flows used in operating activities:			
Net loss		$ (5,208)	$ (6,956)
Less: RVX Therapeutics Inc. pre-acquisition net loss	2 (a)	-	1,191
Items not involving cash:			
Equity-settled share-based payment transactions		488	830
Depreciation and amortization		123	13
Impairment of clinical supplies		382	-
Impairment of intangible assets		144	-
Change in fair value of warrant liability		(668)	(1,101)
Change in fair value of financing rights		(2,212)	-
Interest income		-	(17)
Income taxes		25	-
Changes in non-cash working capital:			
Prepaid expenses and deposits		(12)	(37)
Clinical supplies		(321)	-
Investment tax credit receivable		(175)	(118)
Other assets		248	-
Trade and other payables		(349)	282
Cash used in operating activities		(7,535)	(5,913)
Interest received		-	17
Income taxes paid		-	-
Net cash used in operating activities		(7,535)	(5,896)
Cash flows generated from financing activities:			
Proceeds from the issuance of common shares		6,268	-
Share issuance costs		(6)	-
Distribution from Resverlogix Corp.		-	9,700
Increase in due to Resverlogix Corp.		894	540
Proceeds from exercise of warrants		130	41
Proceeds from exercise of stock options		29	-
Deferred financing costs		-	(16)
Changes in non-cash financing working capital		(2)	1
Net cash generated from financing activities		7,313	10,266
Cash flows used in investing activities:			
Property and equipment (expenditures) recovery		8	(178)
Intangible asset (expenditures)		(66)	(44)
Changes in non-cash investing working capital		(466)	(12)
Net cash used in investing activities		(524)	(234)
Effect of foreign currency translation on cash		(10)	(70)
Increase in cash		(756)	4,066
Cash, beginning of period		1,151	97
Cash, end of period		$ 395	$ 4,163

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

Notes to the Condensed Interim Consolidated Financial Statements

For the three and six months ended October 31, 2014 and 2013

(unaudited)

(amounts in thousands of US dollars, except for number of shares)

1. General information

Zenith Epigenetics Corp. (formerly 1741273 Alberta Ltd.) (the “Company” or “Zenith”) is a company domiciled in Canada and was incorporated under the *Business Corporations Act* (Alberta) on April 10, 2013. On May 24, 2013, 1741273 Alberta Ltd. changed its name to Zenith Epigenetics Corp. The Company was a wholly owned subsidiary of Resverlogix Corp. (“Resverlogix”) until June 3, 2013. On June 3, 2013, Resverlogix, RVX Therapeutics Inc., and the Company completed a Plan of Arrangement ("the Arrangement") pursuant to the *Business Corporations Act* (Alberta). Under the terms of the Arrangement, every Resverlogix shareholder received one share in the Company for every share held in Resverlogix at the effective date. Upon the effective time of the Arrangement, the Company owns all of the shares of RVX Therapeutics Inc. and all outstanding Resverlogix royalty preferred shares.

The condensed interim consolidated financial statements comprise the Company and its wholly-owned subsidiaries RVX Therapeutics Inc. and Zenith Epigenetics Inc. (together referred to as the “Group”). The Company and RVX Therapeutics Inc. are incorporated under the laws of Alberta. Zenith Epigenetics Inc. is incorporated under the laws of Delaware. The Company’s head office is located at Suite 300, 4820 Richard Road S.W., Calgary, Alberta, T3E 6L1, and also has offices at Suite 4010, 44 Montgomery Street, San Francisco, 94104. The registered and records office is located at Suite 600, 815 - 8th Avenue S.W., Calgary, Alberta, T2P 3P2.

The Company is a biotechnology company focused on the discovery and development of novel therapeutics by applying its proprietary epigenetics platform. Zenith’s bromodomain (BET) inhibitors are being advanced in several oncology indications and have the potential to impact multiple additional diseases.

Wind up

On May 1, 2014, the Company wound-up RVX Therapeutics Inc. RVX Therapeutics Inc. transferred all of its assets to the Company and the Company assumed all of RVX Therapeutics Inc.’s liabilities.

2. Background and basis of preparation

(a) Background

Plan of Arrangement

As described in Note 1, on June 3, 2013, Resverlogix, Zenith and RVX Therapeutics Inc. completed the Arrangement. The Company was incorporated for the purposes of participating in the Arrangement. The Company was not a business as defined under IFRS 3 “Business Combinations” and no independent parties were involved in the Arrangement; therefore, the Company cannot be an acquiree and thus no business combination occurred. Accordingly, in the Group’s consolidated financial statements book value accounting has been used to account for the assets acquired and liabilities assumed upon completion of the Arrangement on the basis that there has been no business combination.

Upon the effective time of the Arrangement: every Resverlogix shareholder received one share in Zenith for every share held in Resverlogix at the effective date; Zenith owns all of the outstanding shares of RVX Therapeutics Inc.; and Zenith owns all of the outstanding royalty preferred shares of Resverlogix.

Every holder of a Resverlogix warrant, stock option and restricted stock unit at the effective date of the Arrangement received one warrant, stock option and restricted stock unit in the Company for every warrant, stock option and restricted stock unit, respectively, held in Resverlogix. The exercise prices of all outstanding warrants and stock options in Resverlogix were reduced by approximately 9.1%, and the exercise price of each warrant and stock option in the Company was calculated as approximately 9.1% of the exercise price of each corresponding warrant and stock option of Resverlogix at the effective time of the Arrangement, to reflect the fair market value of the Company.

Pursuant to the Arrangement, Resverlogix advanced a non-repayable amount of CAD$10 million to Zenith to provide working capital to the Group. The promissory notes and the aggregate advances due to Resverlogix from RVX Therapeutics Inc. immediately prior to the effective time of the Arrangement were transferred from Resverlogix to Zenith such that, subsequent to the effective time of the Arrangement, RVX Therapeutics Inc. was indebted to Zenith in respect of these liabilities.

Pursuant to the Arrangement, the Company was also issued royalty preferred shares in the capital of Resverlogix which will provide the Company with dividends receivable on a percentage of revenue, if any, received by Resverlogix for compounds that result in a therapeutic relevant elevation in the plasma levels of Apo A-I (see Note 7 “Royalty preferred shares”).

2. Background and basis of preparation (continued)

(a) Background (continued)

Pursuant to an assignment and services agreement between Resverlogix and the Company (the "Assignment and Services Agreement"), Resverlogix paid certain costs for the Group and performed certain activities on behalf of the Group. As a result, it was necessary to make allocations of certain costs reported in these condensed interim consolidated financial statements. The costs are primarily employee related or associated with research performed by external research organizations. Research fees and compensation related costs have been allocated to the Group using methodologies primarily based on proportionate time spent on the Group's and Resverlogix's respective activities. These cost allocations have been determined on a basis considered by the Group and Resverlogix to be a reasonable reflection of the utilization of services provided to the Group.

The Company has licensed or acquired intellectual property from Resverlogix (pursuant to the Assignment and Services Agreement) and has developed intellectual property, and conducts research related to epigenetics, autoimmune diseases and cancer. These financial statements include the Company's assets and liabilities and costs related to its programs.

For comparative purposes, operational results for RVX Therapeutics Inc. for the pre-Arrangement period of May 1, 2013 to June 2, 2013 have been included in the comparative consolidated statement of comprehensive loss and the comparative consolidated statement of cash flows to present complete information about the acquired entity. Also, the balances presented in the comparative statement of changes in shareholders' deficit as at April 30, 2013 reflect those of RVX Therapeutics Inc. prior to the completion of the Arrangement. RVX Therapeutics Inc.'s pre-Arrangement cash flows have not been included in the comparative consolidated statement of cash flows.

(b) Statement of compliance

These condensed interim consolidated financial statements have been prepared in accordance with IAS 34 – *Interim Financial Reporting.* These condensed interim consolidated financial statements were approved and authorized for issue by the Board of Directors on December 18, 2014.

Certain information, in particular the accompanying notes normally included in the annual financial statements prepared in accordance with IFRS, has been omitted or condensed. These condensed interim consolidated financial statements do not include all disclosures required under IFRS and, accordingly, should be read in conjunction with the annual financial statements for the year ended April 30, 2014 and the notes thereto prepared in accordance with International Financial Reporting Standards ("IFRS") as prescribed by the International Accounting Standards Board ("IASB").

(c) Basis of measurement

The condensed interim consolidated financial statements have been prepared on the historical cost basis except for the revaluation of the liability classified warrants and financing rights, which are measured at fair value each reporting period, and cash, which is carried at fair value. Historical cost is based on the fair value of the consideration given in exchange for assets recorded on the date of the transaction. The financial statements have been prepared on a going concern basis (refer to Note 3).

(d) Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the three and six months ended October 31, 2014.

(e) Functional and presentation currency

The functional currency of all entities within the Group is the US dollar, which is also the presentation currency. All financial information presented in dollars has been rounded to the nearest thousand except for per share amounts.

(f) Use of estimates and judgment

The preparation of the condensed interim consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the amounts reported in these condensed interim consolidated financial statements and notes. Accordingly, actual results may differ from estimated amounts as future confirming events occur. Significant estimates and judgment used in the preparation of the condensed interim consolidated financial statements remain unchanged from those described in the Group's consolidated financial statements for the year ended April 30, 2014.

3. Future operations

The success of the Company is dependent on the continuation of its research and development activities and its ability to finance its cash requirements. It is not possible to predict the outcome of future research and development programs, or the Company's ability to fund these programs in the future.

The accompanying condensed interim consolidated financial statements have been prepared pursuant to International Financing Reporting Standards applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they come due. The Company has incurred significant losses to date, and with no assumption of revenues, is dependent on its ability to raise additional financial capital by continuing to demonstrate the successful progression of its research and development activities if it is to remain as a going concern.

As at October 31, 2014, the Company had $0.4 million of cash and is committed to pay $1.5 million of trade and other payables, and $0.5 million for research and development commitments and $0.4 million of lease obligations over the next twelve months as described further in Note 11 "Commitments". Subsequent to October 31, 2014, the company closed a private placement for gross proceeds of $0.6 million as described in Note 12 "Subsequent events".

The Company's cash is not sufficient to fund the Company's contractual commitments over the next year and is not sufficient to fund all of the Company's planned business operations over the next year. The Company will have to raise additional capital. The Company intends to raise additional capital by way of debt and/or equity private placements. The Company announced on October 14, 2014 that it was suspending its clinical development efforts with ZEN-3365, its first lead compound, and is pursuing additional compounds and progressing its preclinical development programs. This may adversely affect its ability to raise capital. If the Company is not able to raise capital, the Company would have to reduce its cash requirements by eliminating or deferring spending on research, development and corporate activities. These conditions result in a material uncertainty which may cast significant doubt on the Company's ability to continue as a going concern.

In addition, the Company will require additional capital to fund its planned research, development and corporate activities beyond the next year. The Company will continue to explore alternatives to generate positive cash flow including raising additional equity and product licensing; however, there is no assurance that these initiatives will be successful. The Company intends to raise capital from equity and/or debt offering and partnering in the future.

These financial statements do not include any adjustments to the amounts and classifications of assets and liabilities, and the reported revenues and expenses that might be necessary should the Company be unable to continue as a going concern.

4. Significant accounting policies

The condensed interim consolidated financial statements should be read in conjunction with the Company's annual consolidated financial statements for the year ended April 30, 2014 prepared in accordance with IFRS applicable to those annual consolidated financial statements. Except as disclosed below, the same accounting policies, presentation and methods of computation have been followed in these condensed interim consolidated financial statements as were applied in the Company's consolidated financial statements for the year ended April 30, 2014.

New standards and interpretations adopted

The Company has adopted the following amendment to standards, with a date of initial application of May 1, 2014:

Offsetting Financial Assets and Liabilities

An amendment to IAS 32 - *Offsetting Financial Assets and Liabilities,* (a) clarifies requirements for the right to set-off for rights that are contingent, and enforceability in default, insolvency or bankruptcy of all parties to a liability and (b) clarifies provisions on net settlement. The amendments to IAS 32 did not have a material impact on the condensed interim consolidated financial statements.

5. License

Amended and Restated License Agreement

On June 3, 2013, RVX Therapeutics Inc. and Resverlogix entered into an Amended and Restated License Agreement (the “License Amendment”), effective January 31, 2013, which amended a License Agreement dated August 1, 2005. Pursuant to the License Amendment, Resverlogix granted an irrevocable, worldwide license to RVX Therapeutics Inc. under certain licensed patents and licensed know-how to develop, commercialize and sell licensed products in any field other than the Apolipoprotein A-I (“ApoA-I”) therapeutic field (the prevention, treatment or mitigation of any disease via the administration of a pharmaceutical agent that results in a specified therapeutic elevation in the plasma levels of ApoA-I).

As ongoing consideration for the grant of the License, RVX Therapeutics Inc. shall pay Resverlogix a royalty from 1% to 5% of gross amounts received by RVX Therapeutics Inc. from the sale of any product in any field other than the ApoA-I therapeutic field which is encompassed within a patent licensed from Resverlogix.

Waiver Agreement

On March 17, 2014, RVX Therapeutics Inc. and Resverlogix entered into a Waiver Agreement whereby Resverlogix waived its right under the Amended and Restated License Agreement dated June 3, 2013 (the “License Agreement”) to license any method or pharmaceutical agent within the scope of certain Licensee Patents owned or controlled by RVX Therapeutics Inc. that may be determined to come within the ApoA-I Therapeutic Field (as defined in the License Agreement), and RVX Therapeutics Inc. agreed not to develop any patents for any indication within the ApoA-I Therapeutic Field for a period of five years and granted to Resverlogix a right of first refusal for a period of three years thereafter in respect of the license or sale of such patents and or compounds that are determined to come within the ApoA-I Therapeutic Field. In consideration for this waiver, RVX Therapeutics Inc. paid Resverlogix $2.5 million in cash. This $2.5 million acquisition of rights is separately disclosed in the statement of comprehensive loss for the year ended April 30, 2014. The payment does not meet the recognition criteria for intangible assets.

6. Asset impairment

The Company announced on October 14, 2014 that it was suspending its clinical development efforts with ZEN-3365, its first lead compound, the related patents and clinical supplies were written off. During the three months ended October 31, 2014 the Company recognized a $0.1 million impairment loss on intellectual property. A $0.4 million impairment loss on clinical supplies was also recognized during the three months ended October 31, 2014. Both were included in research and development on the statement of comprehensive loss. The Company is pursuing additional compounds and progressing its preclinical development programs.

7. Royalty preferred shares

Pursuant to the Plan of Arrangement described in Note 2(a), on June 3, 2013 Resverlogix issued 75,202,620 royalty preferred shares to the Company.

The holder of the royalty preferred shares is entitled to dividends in the amount of 6-12% of net Apo Revenue, if any. Net Apo revenue is defined as the aggregate of the following amounts: (i) amounts received by Resverlogix or its affiliates (as defined in the Arrangement) from any person who is not Resverlogix or its affiliate (a “third party”) in consideration for granting a license or other rights to the third party which entitle the third party to research, develop, make, manufacture, modify, administer, offer to sell, sell or distribute one or more of the Apo products and/or Apo intellectual property rights or amounts received under the terms of such license or other right that are granted to the third party; (ii) the gross consideration received from a third party by Resverlogix, any licensee or their respective affiliates from the sale of any Apo product (other than consideration received by Resverlogix, any licensee or their respective affiliates from a licensee of such Apo product or its affiliate); less (A) credits or allowances, if any, actually granted; (B) discounts actually allowed; (C) freight, postage, and insurance charges and additional special packaging charges; and (D) customs duties, and excise sales taxes, duties or other taxes imposed upon and paid with respect to such sales (excluding what is commonly known as income taxes); and (iii) amounts received from a third party by Resverlogix or its affiliates in consideration for the sale of any Apo intellectual property right.

Notes to the Condensed Interim Consolidated Financial Statements

For the three and six months ended October 31, 2014 and 2013

(unaudited)

(amounts in thousands of US dollars, except for number of shares)

7. Royalty preferred shares (continued)

The holder of the preferred shares does not have the right to participate in any additional dividends declared, if any, to common shareholders nor do they carry the right to vote. The holder of the preferred shares does not have any claim on Resverlogix's residual net assets other than an amount equal to the greater of (i) $1.00 divided by the number of outstanding royalty preferred shares; and (ii) the amount of any accrued, but unpaid royalty dividend payment and additional royalty dividend payment.

The royalty preferred shares have not been recognized because book value accounting has been applied to the assets that have been acquired through the distribution in connection with the Arrangement and they were not previously recognized in Resverlogix's financial statements. The Company will recognize a royalty receivable when royalties are reasonably determinable and the economic benefits are probable to flow to the Company.

8. Financing rights

Pursuant to the terms of the private placements that the Company closed on March 14, 2014, July 23, 2014, and October 7, 2014, described in Note 9 "Shareholders' deficit", in the event that the Company completes an equity financing within 18 months and the price per share is lower than US$1.00, the price per share paid by the initial subscribers will be adjusted to the lower price per share and they will, accordingly, receive additional common shares for no additional consideration. Furthermore, in the event that the Company completes an equity financing within 18 months and the Company issues or grants additional securities, contractual rights or entitlements to any of the subsequent subscribers, then the Company shall issue or grant the same additional securities, contractual rights or entitlements to the initial subscribers.

Additionally, pursuant to the terms of the private placements that the Company closed on March 14, 2014, and October 7, 2014, in the event that the Company receives gross proceeds from equity financings of less than US$25 million and grants a license to a third party, sells intellectual property rights to a third party, or greater than 66 2/3% of the Company's common shares are sold to a third party, the initial subscribers shall receive, for no additional consideration, additional common shares equal to the number originally subscribed for by each party as described above.

The Company determined the fair value of the 8.0 million common shares issued in March 2014 to be $4.8 million which is net of $2.3 million of anti-dilution rights and $0.9 million of transaction rights. The Company determined the fair value of the 4.3 million common shares issued in July 2014 to be $3.2 million which is net of $1.1 million of anti-dilution rights. The Company determined the fair value of the 2.0 million common shares issued in October 2014 to be $1.3 million which is net of $0.5 million of anti-dilution rights and $0.2 million of transaction rights. The determination of the fair value of the anti-dilution rights required management to use judgment, including management's estimates of: (1) various probabilities of future equity offerings at various prices below $1 per share, and (2) the fair value of the Company's common shares. The determination of the fair value of the transaction rights required management to use judgment, including management's estimates of: (1) the probability of a transaction occurring prior to the Company raising an additional $25 million in equity, and (2) the fair value of the Company. The Company recorded the anti-dilution and transaction rights as liabilities with off-setting reductions to the carrying amount of the common shares. Management's estimate of the fair value of the Company's common shares was $0.41 per share as at April 30, 2014 and $0.27 per share as at October 31, 2014. Management's estimates of the fair value of the anti-dilution and transaction rights as at October 31, 2014 were otherwise unchanged.

(amounts in thousands of US dollars, except for number of shares)

9. Shareholders' deficit

(a) Common shares

(i) Authorized:

Unlimited number of common shares
Unlimited number of preferred shares issuable in series with rights as determined by the Board of Directors at the time of issue.

(ii) Issued and outstanding:

Common shares	Number of shares	Amount
Balance, April 30, 2013	1	0.001
Cancelled in connection with Plan of Arrangement	(1)	(0.001)
Issued in connection with Plan of Arrangement	75,202,620	28,127
Issued in connection with private placements	8,100,000	4,838
Issued in connection with warrant exercises	2,452,686	929
Issued in connection with stock option plan	293,332	99
Issued in connection with long term incentive plan	14,367	4
Share issue costs	-	(10)
Balance, April 30, 2014	86,063,005	$ 33,987
Issued in connection with private placement	6,267,800	4,426
Issued in connection with warrant exercises	397,267	154
Issued in connection with stock option plan	182,900	64
Issued in connection with long term incentive plan	107,510	34
Share issue costs	-	(6)
Balance, October 31, 2014	93,018,482	$ 38,659

Issuance of Common Shares

On April 10, 2013, the Company issued 1 common share at CAD$1.00 per common share to Resverlogix. This common share was cancelled on June 3, 2013 in connection with the Arrangement.

As described in Note 2a, on June 3, 2013, upon the effective time of the Arrangement, every Resverlogix shareholder received one share in Zenith for every share held in Resverlogix at the effective date.

Private Placements

On March 14, 2014 the Company issued 8,000,000 common shares at a price of $1.00 per share for gross proceeds of $8.0 million to Eastern Capital Limited and NGN BioMed Opportunity II, L.P., and on April 1, 2014 the Company issued 100,000 common shares at a price of $1.00 per share for gross proceeds of $100 thousand. As described in Note 8 "Financing rights", under certain conditions, the subscribers are entitled to receive additional shares.

On July 22, 2014 the Company issued 4,272,500 common shares at a price of $1.00 per share for gross proceeds of $4.3 million to NGN BioMed Opportunity II, L.P. and other subscribers. As described in Note 8 "Financing rights", under certain conditions, the subscribers are entitled to receive additional shares.

On October 7, 2014 the Company issued 1,995,300 common shares at a price of $1.00 per share for gross proceeds of $2.0 million to NGN BioMed Opportunity II, L.P. and other subscribers. As described in Note 8 "Financing rights", under certain conditions, the subscribers are entitled to receive additional shares.

(amounts in thousands of US dollars, except for number of shares)

9. Shareholders' deficit (continued)

(a) Common shares (continued)

Subsequent to October 31, 2014 the Company closed a private placement for gross proceeds of $0.6 million as described in Note 12.

(b) Stock options

The Company's stock option plan has been approved as a rolling 10% plan that allows for reservation of a number of common shares under the plan equal to 10% of the Company's issued and outstanding common shares on an undiluted basis. Additionally, the plan is a reloading plan, which allows for the number of common shares reserved for issuance related to the options under the plan to automatically become eligible to be reallocated pursuant to stock option based grants upon option expiry, cancellation or exercise. The Company may grant options to its directors, officers, employees and consultants. The stock options vest over zero to three years including certain stock options that vested in part or entirely upon issuance pursuant to the Arrangement. There were stock options granted in the three months ended October 31, 2014 with performance conditions which are required to be met in order for the options to vest. The stock options have between a one and ten year term. The options are settled by way of the issuance of equity instruments of the Company ("equity-settled").

	Number of options	Weighted average exercise price (CAD)
Outstanding, April 30, 2013	-	$ -
Granted	5,198,070	0.24
Exercised	(293,332)	0.26
Expired	(1,218,550)	0.27
Forfeited	(64,550)	0.22
Outstanding, April 30, 2014	3,621,638	$ 0.23
Granted	2,632,100	0.44
Exercised	(182,900)	0.18
Expired	(63,469)	0.33
Forfeited	(71,431)	0.39
Outstanding, October 31, 2014	5,935,938	$ 0.33

The following table summarizes information about the options outstanding and exercisable at October 31, 2014.

Range of Exercise Prices (CAD)	Number Outstanding	Weighted Average Remaining Life (years)	Weighted Average Exercise Price (CAD)	Number Exercisable
$0.11 - $0.13	1,900,404	1.92	$ 0.15	1,836,772
$0.21 - $0.30	490,400	1.28	0.25	427,066
$0.32 - $0.40	638,400	3.01	0.34	337,039
$0.45 - $0.51	2,906,734	6.27	0.46	746,062
	5,935,938	4.12	$ 0.33	3,346,939

The number of options exercisable at October 31, 2014 was 3,346,939 (2013 – 3,000,523) with a weighted average exercise strike price of CAD$0.25 (2013 – CAD$0.24).

Notes to the Condensed Interim Consolidated Financial Statements

For the three and six months ended October 31, 2014 and 2013

(unaudited)

(amounts in thousands of US dollars, except for number of shares)

9. Shareholders' deficit (continued)

(b) Stock options (continued)

On June 3, 2013, pursuant to the Plan of Arrangement (described in Note 2a), every Resverlogix stock option holder at the effective date of the Arrangement received one stock option in the Company for every stock option held in Resverlogix (with identical vesting and terms as the corresponding Resverlogix stock options).

The fair value of each option granted is estimated as of the grant date using the Black-Scholes option pricing model. The following weighted average assumptions were used in arriving at the weighted average fair values of $0.31 per option and $0.15 per option associated with stock options granted during the six months ended October 31, 2014 and 2013, respectively:

	2014	2013
Risk-free interest rate	1.7%	1.1%
Expected life	6.2 years	2.1 years
Expected volatility	95%	73%
Share price at grant date	CAD$0.44	CAD$0.38
Expected dividends	Nil	Nil

(c) Restricted stock units

The Company's long term incentive plan allows for the reservation of a number of common shares not to exceed 10% of the Company's issued and outstanding common shares on an undiluted basis less the number of common shares reserved under the Company's stock option plan. The Company may grant restricted stock units ("RSUs") to directors, officers, employees, and consultants. The majority of restricted stock units fully vest over zero, two or three years.

During the six months ended October 31, 2014, the Company granted 809,200 (2013 – 753,000) RSUs to employees. The RSUs granted during the six months ended October 31, 2013 were issued in connection with the Plan of Arrangement. Every Resverlogix restricted stock unit holder at the effective date of the Arrangement received one RSU in the Company for every RSU held in Resverlogix (with identical vesting and terms as the corresponding Resverlogix RSUs). The RSUs vest over a period of two or three years from the original date of grant. Therefore, certain RSUs vested in part or entirely upon issuance pursuant to the Arrangement. The weighted average fair value of the RSUs granted in the six months ended October 31, 2014 was $0.41 per RSU (2013 - $0.30 per RSU). The Company estimates the fair value of RSUs based on the market price of the underlying stock (net of an estimated illiquidity discount) on the date of grant.

During the three months ended October 31, 2014, the Company allowed the exercise of RSUs on a "net of tax" basis, whereby the number of shares issued was equal to the number determined net of the respective taxes attributable to the exercise; 8,967 RSUs were exercised on a net of tax basis, resulting in the issuance of 5,694 common shares.

(amounts in thousands of US dollars, except for number of shares)

9. Shareholders' deficit (continued)

(c) Restricted stock units (continued)

	Number of restricted stock units	Weighted average grant date fair value (USD)
Outstanding, April 30, 2013	-	$ -
Granted	753,000	0.30
Exercised	(14,367)	0.30
Forfeited	(42,033)	0.30
Outstanding, April 30, 2014	696,600	$ 0.30
Granted	809,200	0.41
Exercised	(110,783)	0.31
Forfeited	(88,032)	0.40
Outstanding, October 31, 2014	1,306,985	$ 0.36

(d) Shares granted upon a change in control

The Company's CEO is entitled to 500,000 shares if a change in control transaction occurs where the value of the transaction exceeds $500 million. A change in control for the purposes of this agreement is defined as either per the US Securities Act of 1933, by the Company's board of directors being substantially replaced, through a merger, amalgamation or re-organization with another corporation, or if substantially all the assets or undertakings of the Company are sold.

The fair value of this instrument was estimated at $0.39 per share as at the grant date based on Management's estimate of the fair value of the Company's common shares. However, no expense has been recognized during the period.

(e) Warrant liability

The following table summarizes the changes in common share purchase warrants outstanding.

	Number of warrants	Weighted average exercise price (CAD)	Liability amount
Outstanding, April 30, 2013	-	$ -	$ -
Issued	11,647,282	0.24	1,667
Exercised	(2,452,686)	0.25	(361)
Expired	(1,393,466)	0.25	-
Revaluation of warrant liability	-	-	138
Outstanding, April 30, 2014	7,801,130	$ 0.24	$ 1,444
Exercised	(397,267)	0.35	(24)
Expired	(1,924,423)	0.36	-
Revaluation of warrant liability	-	-	(668)
Outstanding, October 31, 2014	5,479,440	$ 0.19	$ 752

(amounts in thousands of US dollars, except for number of shares)

9. Shareholders' deficit (continued)

(e) Warrant liability (continued)

The following table summarizes information about the warrants outstanding and exercisable at October 31, 2014.

Exercise Price (CAD)	Number Outstanding	Weighted Average Remaining Life (years)	Weighted Average Exercise Price (CAD)
$0.14	1,320,000	2.82	$ 0.14
$0.20	3,430,800	1.62	0.20
$0.22	728,640	3.35	0.22
	5,479,440	2.14	$ 0.19

On June 3, 2013, pursuant to the Plan of Arrangement (described in Note 2a), every Resverlogix warrant holder at the effective date of the Arrangement received one warrant in the Company for every warrant held in Resverlogix (with identical vesting and terms as the corresponding Resverlogix warrants).

Under IFRS, the prescribed accounting treatment for warrants issued with an exercise price denominated in a foreign currency is to treat these warrants as a liability measured at fair value with subsequent changes in fair value accounted for through profit or loss. The fair value of these warrants is determined using the Black Scholes option pricing model. All of the Company's warrants meet this liability classification requirement and thus the value of these warrants are presented as a current liability on the condensed interim consolidated statement of financial position. As these warrants are exercised, the fair value of the recorded warrant liability on date of exercise is included in share capital along with the proceeds from the exercise. If these warrants expire, the related decrease in warrant liability is recognized in profit or loss, as part of the change in fair value of warrant liability. There is no cash flow impact as a result of this accounting treatment.

During the six months ended October 31, 2014 no warrants were issued. The grant date weighted average fair value of the warrants granted during the six months ended October 31, 2013 was $0.14 per warrant, using the Black-Scholes option pricing model with the following weighted average assumptions:

	2014	2013
Risk-free interest rate	-	1.1%
Expected life	-	2.1 years
Fair value per common share	-	CAD $0.38
Expected volatility	-	70%

(f) Per share amounts

The loss per share has been calculated using net loss for the period and the basic and diluted weighted average shares outstanding during the three and six months ended October 31, 2014 of 91,527,678 and 89,217,960 respectively (2013 – 75,376,904 and 61,811,173, respectively). The effect of any potential exercise of stock options, restricted stock units and warrants outstanding during the period has been excluded from the calculation of diluted loss per share, as it would be anti-dilutive.

Notes to the Condensed Interim Consolidated Financial Statements

For the three and six months ended October 31, 2014 and 2013

(unaudited)

(amounts in thousands of US dollars, except for number of shares)

10. Expenses by nature

Presentation of expenses is based on the function of each expense. The following details highlight certain components of the research and development and general and administrative expenses classified by nature. Remaining research and development and general and administrative expenses include personnel costs and expenses paid to third parties, including the service fees paid to Resverlogix.

	Three months ended October 31,		Six months ended October 31,	
	2014	2013	2014	2013
Included in research and development expenses:				
Share-based payment transaction costs	$ 37	$ 4	$ 165	$ 386
Amortization and depreciation	60	8	120	15
Included in general and administrative expenses:				
Share-based payment transaction costs	$ 174	$ 23	$ 323	$ 444
Amortization and depreciation	-	-	3	-

The Company has engaged Resverlogix under the Assignment and Services Agreement to supply research and administrative services.

11. Commitments

As at October 31, 2014, the Company is committed under various research and development contracts as follows:

	2014	2013
Less than 1 year	$ 547	$ 1,326
Between 1 and 5 years	-	-
More than 5 years	-	-
	$ 547	$ 1,326

As at October 31, 2014, Resverlogix was committed to operating lease payments for office and laboratory premises, for which the Company is allocated, as follows:

	2014	2013
Less than 1 year	$ 448	$ 78
Between 1 and 5 years	1,081	-
More than 5 years	1,085	-
	$ 2,614	$ 78

The Company agreed to pay Resverlogix for its proportionate share of operating lease payments and operating costs for office and laboratory premises of an estimated $0.2 million and $0.2 million, respectively, for the next twelve months.

12. Subsequent Events

Private Placement

On December 2, 2014, the Company issued 600,000 common shares at a price of $1.00 per share for gross proceeds of $0.6 million. NGN BioMed Opportunity II, L.P. ("NGN") subscribed for 500,000 of the 600,000 common shares.

Pursuant to the terms of the private placement, in the event that the Company completes an equity financing within 36 months and the price per share is lower than US$1.00, the price per share paid by the subscribers (the "Subscribers") will be adjusted to the lower price per share and they will, accordingly, receive additional common shares for no additional consideration. Furthermore, in the event that the Company completes an equity financing within 36 months and the Company issues or grants additional securities, contractual rights, or entitlements to any of those subsequent subscribers, then the Company shall issue or grant the same additional securities, contractual rights, or entitlements to the Subscribers.

The adjustment provisions of the subscription agreements dated March 14, 2014, July 22, 2014 and October 7, 2014, whereby the Subscribers subscribed for an aggregate of 4,500,000 common shares (including 4,000,000 common shares by NGN) and which entitled the Subscribers to additional common shares, securities, contractual rights or entitlements if the events described above occurred, were amended to apply for a period ending 36 months following December 2, 2014.

Additionally, pursuant to the terms of the private placement, in the event that the Company receives gross proceeds from equity financings of less than US$25 million and grants a license to a third party, sells intellectual property rights to a third party, or greater than 66 2/3% of the Company's common shares are sold to a third party, the Subscribers shall receive, for no additional consideration, additional common shares equal to the number originally subscribed for by each party as described above.

Restructuring

Subsequent to October 31, 2014, after we suspended clinical development of ZEN-3365, we restructured our operations and reduced staffing levels, total severance costs incurred were $0.2 million.