2018 Quarterly Report

January, February, March

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Message from the President and Chief Executive Officer

Dear Valued Shareholders

I am writing this letter while attending the 2018 International Association of Healthcare Central Service Materiel Management (IAHCSMM) annual conference and exposition. It has been some time since TSO_3 has attended such a conference as a participant and exhibitor, as marketing activities were the responsibility of our distributor.

Our distribution partner, Getinge Infection Control AB, is also here and is displaying the TSO_3 STERIZONE® VP4 sterilizer in its booth along with its entire line of washers and steam sterilizers.

So how did TSO_3 get here and where are we going commercially? In January 2018, TSO_3 elected to reset its commercial strategy moving from an exclusive worldwide arrangement with Getinge to a co-commercial strategy in North America. This new agreement was signed because TSO_3 believes customer uptake for the STERIZONE® VP4 Sterilizer should be faster.

As our relationship with Getinge evolved over the past two years, we believe that these recent modifications to our partnership will add speed and flexibility to our joint sales and marketing efforts, while addressing inventory levels.

So we are here at IAHCSMM, as we were at the AORN conference last month and will be at the SGNA and APIC conferences in the next two months. In accordance with the terms of our new agreement with Getinge, TSO_3 is now building a funnel of opportunities and quoting direct business, and we currently expect to begin shipping sterilizers to end customers in the second half of 2018. The terms of our new agreement will also allow us, in the coming quarters, to be more transparent about our pipeline, the number of quotes, backlog, and sales to end users. As for our relationship with Getinge, it remains intact as we negotiate terms under which a new agreement could be signed. We both know that elimination of the current inventory is required and plans to accomplish this are underway.

Lastly, we are here at this conference with the only Food and Drug Administration (FDA) cleared sterilizer with the ability to sterilize multi-channeled flexible endoscopes. While we continue to wait to hear from the FDA on the decision to add duodenoscopes to our labeling, we are not simply standing by, rather we are leading education forums and bringing sterilization and endoscopy equipment thought leaders to the targeted customer base.

Sincerely,

R.M. Rumble

Overview

General Description

TSO_3 Inc. ("TSO_3" or the "Company") was founded in June 1998 in Québec City, Canada and employs 73 people as at March 31, 2018. The Company's activities encompass the sale, production, maintenance, research, development and licensing of sterilization processes, related consumable supplies and accessories for medical devices that are sensitive to heat and moisture. The Company designs products for sterile processing areas in medical facilities that offer an advantageous replacement solution to other low temperature sterilization and high-level disinfection processes currently used. TSO_3 also offers services related to the maintenance of sterilization equipment and compatibility testing of medical devices with such processes.

TSO_3 Corporation, the Company's wholly-owned subsidiary incorporated in 2015, is located in the State of South Carolina, USA and was established to meet US customer requirements. The US represents approximately 40% of the worldwide market for low-temperature sterilization equipment. The US location is used for sales and marketing, administration, engineering, warehousing and distribution of parts and consumables, laboratory services, conducting light assembly, and providing service and education to US customers.

Technology

TSO_3's principal product is the STERIZONE® VP4 Sterilizer. The STERIZONE® VP4 Sterilizer is a dual sterilant, low temperature sterilization system that utilizes vaporized hydrogen peroxide (H_2O_2) and ozone (O_3) as its sterilants. It is a product which evolved from the Company's STERIZONE® 125L+ Sterilizer, which was originally licensed by Health Canada (Canadian equivalent of the United States FDA) in 2009, CE marked in 2010 and of which the Company subsequently sold a number of units in Canada. These initial units have been upgraded to STERIZONE® VP4 Sterilizers and have been in continuous operation for a number of years.

In December 2014, TSO_3 achieved a major milestone when its STERIZONE® VP4 Sterilizer received 510(k) clearance from the Food and Drug Administration (FDA). In October 2015, the STERIZONE® VP4 Sterilizer received clearance from Health Canada to sell the STERIZONE® VP4 Sterilizer with extended claims associated with multi-channel flexible endoscopes in the Canadian market and on July 4, 2016, TSO_3 announced that the FDA had also cleared TSO_3's expanded indications for use (IFU's) of its STERIZONE® VP4 Sterilizer relating to certain multi-channel flexible endoscopes of up to 3.5 meters in length and four or fewer channels.

Regulatory clearance of the additional claims represents an entirely new level of patient protection against ineffective device reprocessing resulting from the use of less robust disinfecting systems, particularly for flexible endoscopes. These extended claims further expand the Company's technology leadership – offering enhanced patient protection in applications where terminal sterilization was not previously possible. The extended IFU claims cleared by the FDA demonstrate the truly superior capabilities of the STERIZONE® Sterilization System.

The STERIZONE® Sterilization System has now achieved a number of industry-firsts:

- First and only dual-sterilant sterilizer cleared by the FDA for sale in the US;
- First single cycle, low-temperature sterilizer cleared in the US, Europe and Canada to process a 75-pound load of general instruments, single channel flexible endoscopes, and rigid and semi-rigid channeled devices;
- First low temperature sterilizer validated and cleared in the US, Europe and Canada to sterilize multi-channeled endoscopes (with four or fewer channels) up to 3.5 metres in length such as video colonoscopes and gastroscopes, along with duodenoscopes in Europe and Canada;

- First sterilizer validated and cleared to terminally sterilize duodenoscopes (Canada and Europe)
- First low-temperature sterilizer with a load-sensitive *Dynamic Sterilant Delivery System*™;
- First documented "wet" cycle with validated micro-condensation sterilant layer;
- First Biological Indicator Test Pack to survive past the first half-cycle.

As these technologies and claims are unique in the industry and significantly superior to incumbent technologies, the STERIZONE® Sterilization System can significantly improve efficiency, cost, risk mitigation and throughput in traditional central sterilization reprocessing departments in hospitals.

TSO_3's technologies also allow an industry first in terminal medical device sterilization: medical facilities now have an opportunity to terminally sterilize complex medical instruments such as colonoscopes, gastroscopes and other multi-channel flexible scopes, which previously could only be treated in a less effective process known as "high-level disinfection". Low temperature sterilization with the STERIZONE® VP4 Sterilizer offers a more robust solution than disinfection, since it involves a proprietary process that destroys all types of microbiological organisms, including bacterial spores.

The expanded claims now cleared for the STERIZONE® VP4 Sterilizer correspond to increasing scrutiny by regulatory authorities over medical device reprocessing, particularly for colonoscopes and other complex medical devices used during minimally invasive surgical (MIS) and endoscopic procedures. Much of this concern stems from patient-to-patient transfer of multidrug resistant bacteria that have been transmitted after cleaning by high-level disinfection. Published reports confirm the significant health risk of device-related transfer of antibiotic resistant microbes, including patient injury or death.

TSO_3 has established laboratory data validating the STERIZONE® VP4 Sterilizer, with its dual sterilants of hydrogen peroxide and ozone, can repeatedly sterilize duodenoscopes used in endoscopic retrograde cholangio-pancreatography (ERCP) procedures. This breakthrough comes at a critical time, with the growing use of duodenoscopes, along with the increasing number of adverse incidents related to ineffectual reprocessing. TSO_3 is currently cleared for duodenoscopes in the Canadian and European markets and on July 20, 2017, the Company filed a 510(k) submission for its STERIZONE® VP4 Sterilizer for the terminal sterilization of duodenoscopes in the United States, the claim for which has not yet been granted by US regulators.

Business Environment and the Market Drivers

Sterile reprocessing of medical devices is essential to ensure positive surgical outcomes. The use of non-sterile surgical instruments contributes to increased infection rates and, in turn, leads to increased patient hospital stays, higher cost of care and greater mortality rates.

The world population is aging, with the fastest growing segment age 65+ expected to nearly double by 2020 from 2010, according to the United Nations. This aging population is expected to result in increasing demand for diagnostic procedures and surgical operations involving scopes and MIS devices, and thereby increase demand for efficacious and high-throughput sterilization methods that can process such devices, such as low temperature terminal sterilization systems.

Today, it is not uncommon to find sterile reprocessing of instruments conducted in three areas of a hospital: the central sterile department (CS), the sub-sterile area of the operating room (OR), and the gastroenterology department (GI).

Why Low Temperature Sterile Reprocessing

While some medical instruments are designed for single use, the majority must be reprocessed between surgical cases and therefore need to be compatible with the sterilization process used. Traditionally, steam was used to sterilize surgical instruments.

Today's surgical suite is very different from operating rooms of the past. Currently, the trend continues towards the practice of MIS. Devices used in MIS are complex, expensive and delicate, and in most cases, do not tolerate the steam sterilization process. Instead, they require low-temperature sterilization. These high-demands, complex devices represent a major financial investment for hospitals as well as a challenge to sterilize.

Disinfection is significantly less effective than sterilization because it does not necessarily kill all harmful microorganisms, especially bacterial spores. Low temperature terminal sterilization offers an increased level of safety, since it involves a process that thoroughly destroys all types of microbiological organisms with a sterility assurance level of 10^{-6} (SAL^{-6}).

Competitive Landscape

The Company competes in an industry characterized by both multinational and regional companies that market sterilization technologies, such as Getinge AB, STERIS Corporation, Johnson & Johnson, 3M Company, Cantel Medical Inc., Olympus Corporation, Custom Ultrasonics Inc., and Belimed AG.

The low-temperature vapour sterilization methods most commonly used today are hydrogen peroxide (H_2O_2) sterilization systems. These methods offer "terminal sterilization", which indicates the instruments are packaged and remain sterile until opened at the surgical site. Current H_2O_2 sterilization methods are fast, however they are very expensive to operate, and have limits as to efficacy and loading capacity based on their design.

Another method that played a role in a sub-segment of low temperature reprocessing was that of liquid chemical sterilization processes. This type of process is used directly in the operating room as a just-in-time method to complement the central sterilization department's sterile production. The gastrointestinal department remains a heavy user of liquid chemical systems for the reprocessing of endoscopes. These systems are under increased scrutiny due to identified cases of patient to patient cross contamination of multidrug resistant bacteria.

Each of these sterilization methods offers benefits to the customers, but none is a complete solution matching the customer need for high and cost effective throughput of complex and expensive medical devices. Customers must purchase and support a combination of products to meet their daily requirements for sterile instruments. TSO_3 technology brings its customers closer to a complete solution, and the extended claims cleared by the FDA demonstrate the truly superior capabilities of the STERIZONE® Sterilization System.

First Quarter 2018 and Recent Activities

Board of Directors

In April 2018, Dr. Douglas Dieter joined TSO_3's board of directors. Dr. Dieter is currently a Managing Director at Ares Management, an asset manager headquartered in Los Angeles, CA, where he is responsible for investments across the healthcare spectrum, including inpatient and outpatient healthcare services, health insurers, medical device and pharmaceutical and biotech companies. Prior to joining Ares Management in 2016, Dr. Dieter was a Senior Analyst at Western Asset Management Company, an asset manager based in Pasadena, CA, where he was responsible for healthcare and technology high yield and loan investments. At Ares Management and Western Asset Management, his primary focus has been to provide capital solutions and financing for healthcare M&A and leveraged buyouts. He is a recognized authority on healthcare finance and has deep knowledge of the healthcare system, including Medicare and Medicaid payment systems.

Regulatory Status

In March 2016, the Company received FDA 510(k) clearance for a universal design of its STERIZONE® VP4 Sterilizer. The STERIZONE® VP4 Sterilizer was originally cleared for commercialization in the US in December 2014. The new clearance enables the Company to streamline assembly and shipping around a single sterilizer platform that meets global regulations for electromechanical design. The Company has now harmonized production around a single design, reducing inventory costs and complexity, while improving production rates and efficiency.

On July 4, 2016, TSO_3 announced that the FDA had also cleared TSO_3's expanded IFU's of its STERIZONE® VP4 Sterilizer relating to certain multi-channel flexible endoscopes of up to 3.5 meters in length and four or fewer channels. Regulatory clearance of the additional claims represents an entirely new level of patient protection against ineffective device reprocessing resulting from the use of less robust disinfecting systems, particularly for flexible endoscopes. These extended claims further expand the Company technology leadership – offering enhanced patient protection in applications where terminal sterilization was not previously possible.

The expanded claims now cleared for the STERIZONE® VP4 Sterilizer correspond to increasing scrutiny by regulatory authorities over medical device reprocessing, particularly for colonoscopes and other complex medical devices used during MIS procedures. Disinfection is less effective than sterilization because it does not necessarily kill all harmful microorganisms, especially bacterial spores. Low temperature terminal sterilization with the STERIZONE® VP4 Sterilizer offers a more effective solution, since it involves a proprietary process that thoroughly destroys all types of microbiological organisms with a sterility assurance level of 10^{-6} (SAL^{-6}). Further, the evidence TSO_3 has provided to the FDA confirms that the STERIZONE® VP4 Sterilizer can terminally sterilize multi-channeled flexible endoscopes (with a maximum of four channels) having internal lumens of ≥ 1.45 mm in inner diameter and ≤ 3,500 mm in overall length, and ≥ 1.2 mm in inner diameter and ≤ 1,955 mm in overall length, which are commonly found in video colonoscopes and gastroscopes - an industry first for any medical device sterilization process.

On July 20, 2017, the Company announced that it had filed a 510(k) submission with US regulators for its STERIZONE® VP4 Sterilizer for the terminal sterilization of duodenoscopes used in ERCP procedures. If awarded such claim, TSO_3's STERIZONE® VP4 Sterilizer would become the first and only validated sterilizer technology in the US with a cleared label claim for the terminal sterilization of duodenoscopes.

The Company's filing is supported by laboratory data that validates that the STERIZONE® VP4 Sterilizer, with its dual sterilants of hydrogen peroxide and ozone, can terminally sterilize multi-channel flexible endoscopes with a sealed distal end elevator mechanism (duodenovideoscopes). If achieved, the claim will match existing claims already made by the Company in Canada and Europe.

On September 7, 2017, the Company announced that the second largest hospital in Canada had completed the installation of multiple STERIZONE® VP4 Sterilizers and is now using these sterilizers to terminally process duodenoscopes used on patients undergoing ERCP procedures. TSO_3 also announced the successful completion of a routine Quality System compliance inspection by US regulators. The Company passed the inspection without any reportable findings – which is considerable given the recent expansion of the Company. The Company has and continues to follow a continuous improvement based regulatory compliance program which was commended by the regulators.

On September 27, 2017, the Company announced that it had received correspondence from US regulators pertaining to its submission for extended claims for the STERIZONE® VP4 Sterilizer in relation to the terminal sterilization of duodenoscopes. In their correspondence, US regulators requested clarification on certain aspects of the Company's proposed labeling consistent with the reprocessing of specific duodenoscopes using the STERIZONE® VP4 Sterilizer. In addition, acknowledging recent challenges that have impacted ERCP scopes, regulators have also asked for specific testing to be documented pertaining to what they describe as "challenge features" of the

identified devices. This includes testing the integrity of the adhesive seal found at and under the distal endcap of the duodenoscope after sterilization processing.

The Company responded on November 16, 2017 and the response included a summary of results from tests evaluating the effect of TSO_3's sterilization process on specific features incorporated in the design of identified scopes, as well as additional labeling targeted at a selected duodenoscope. Lastly, in its response, the Company defined recommended device inspection and use intervals to assist end-users in their instrument surveillance when performing terminal sterilization of duodenoscopes within the STERIZONE® Sterilization System.

On December 19, 2017, the Company announced that it has had further dialogue with US regulators and had determined that the information the Company provided to the regulators addressed the majority of items listed within the initial additional information request. Regulators at the time recommended including additional data that specifically related to statements associated with compatibility and the Company began accumulating this data at that time. On March 19, 2018, the company provided its final response to US regulators. In the response, the Company included data on modified leak test experiments, testing to confirm lack of fluid ingress occurring under the distal end cap of the devices, as well as real-world data from market research commissioned by TSO_3 reflecting the actual use-life of duodenoscopes.

On March 14, 2018, the Company announced that it has received 510(k) clearance from US regulators for a significant improvement to its STERIZONE® VP4 Sterilizer. The cleared change can improve the customer installation process and reduce start-up costs by significantly reducing the oxygen supply requirements for the system.

Commercial Activities

On November 25, 2015, TSO_3 and Getinge Infection Control AB ("Getinge"), a global leader in infection control solutions, entered into an agreement (the "Getinge Agreement") which granted Getinge exclusive worldwide global distributor rights to TSO_3's STERIZONE® VP4 Sterilizer in exchange for $7.5 million plus performance minimums. In association with the Getinge Agreement, TSO_3 received purchase orders from Getinge in December of 2015 and 2016. The Company shipped 110 and 170 STERIZONE® VP4 Sterilizers in 2016 and 2017 respectively in full fulfillment of those purchase orders. These shipments supplied Getinge with sterilizers for sale to end users, and allowed the Company to establish higher volume production, production capacities, purchasing methodologies, cost improvements and supply chain structures. In November 2017, the Company indicated that over 50 STERIZONE®VP4 Sterilizers had been delivered to end users in Canada and in the United States.

Sales under the Getinge Agreement are made in US dollars to Getinge. The Company recognizes revenue when it sells its sterilizers to Getinge. Getinge is also receiving ongoing technical support from TSO_3 as part of the Getinge Agreement.

The performance requirements in the Getinge Agreement involve minimum annual unit purchase commitments from Getinge and fulfillment obligations by TSO_3. Getinge must provide a purchase order to be obligated to buy units under its minimum annual commitments, and as January 1st, 2018, Getinge did not yet provided such a purchase order for sterilizers in 2018. As a result, the Company did not ship any sterilizers in the first quarter of 2018.

On January 25, 2018, the Company entered into a co-commercialization agreement (the "co-commercialization Agreement") with Getinge in a joint effort to increase sales to end users and optimize the customer experience. The Co-commercialization Agreement allows the Company to sell its STERIZONE® VP4 Sterilizers and associated products and services directly into the United States and Canada and repurchase not less than 100 STERIZONE® VP4 Sterilizers for $3.3 million. Getinge will continue to sell STERIZONE® VP4 Sterilizers in North America and the rest of the world and the parties have agreed to a customer selection mechanism to prevent the likelihood of channel conflict.

The parties are in negotiations regarding modifications to the distribution relationship, either through a new agreement or a modification of the Getinge Agreement, with the objective of further increasing the speed, flexibility and effectiveness of the relationship. The Co-commercialization Agreement and the Getinge Agreement will terminate on August 1, 2018 unless extended by mutual agreement. If agreement between the parties is not reached, TSO_3 has agreed, by July 1, 2019, to repurchase Getinge's remaining STERIZONE® VP4 Sterilizers at the same unit price in the Co-commercialization Agreement. In the event the Getinge Agreement terminates, Getinge would lose licensing and other rights made available by the agreement, and the Company's only other recourse against Getinge would be to retain in full the US$7.5 million license fee payment made by Getinge when the Getinge Agreement was entered into and require Getinge to accept delivery and pay for units under any then outstanding purchase orders.

The Getinge Agreement also contains termination provisions in favour of Getinge, should TSO_3 ever be in a material breach which is not cured within 90 days of a notice from Getinge or in certain circumstances in the event of a change of control of the Company. Under such a termination by Getinge, the Company shall pay a termination fee to Getinge equal to the greater of: (i) US$5 million or two times Getinge's prior twelve months revenues with the products for a termination within the first or second year of the agreement, (ii) US$7.5 million or one and a half times Getinge's prior twelve months revenues with the products for a termination within the third year of the agreement, or (iii) US$10 million or one time Getinge's prior twelve months revenues with the products for a termination within the fourth or fifth year of the agreement.

Supply Chain Financing

In December 2016, TSO_3 secured access to an automated receivable factoring program through a joint effort with Getinge and a Getinge global banking partner. This program provides a simple and inexpensive instrument for Getinge and TSO_3 to finance working capital. Under this program, TSO_3 may at any time factor (sell to the bank) up to 100% of the outstanding receivables that Getinge posts to the program in exchange for a small discount.

Getinge currently represents substantially all of TSO_3's revenue and trade accounts receivable. Payment terms for invoices Getinge posts to this program are 90 days from invoice date, rather than standard 45 day terms. There are no bank setup fees associated with this program and TSO_3 has full independent discretion as to whether it shall or shall not factor any or all posted receivables.

TSO_3 used the program during the first quarter of 2018.

European Expansion

Getinge continued to launch the STERIZONE® VP4 Sterilizer in Europe in 2017. Key sales and marketing staff have been hired by Getinge and training sessions have occurred. Getinge has sold and installed several STERIZONE® VP4 Sterilizers in Europe to date, and more are planned in 2018.

In 2016, in support of a planned European product launch in the first quarter of 2017, TSO_3 completed development of a double door or "pass-through" option for the STERIZONE® VP4 Sterilizer. Pass-through systems are highly desirable in certain sterilization department designs where a wall separates dirty from clean and clean from sterile inventory – an approach favoured by many European hospitals. While the double door option is less popular in the US, the Company plans to pursue clearance to sell the device in the US in the ordinary course.

On April 26, 2018, the Company announced that an independent laboratory has completed studies demonstrating the efficacy of the STERIZONE® VP4 Sterilizer for inactivation of prions. Prions are abnormal, pathogenic agents believed to cause transmissible spongiform encephalopathies (TSEs), such as Variant Creutzfeldt-Jakob Disease. TSEs are rapidly progressive, uniformly fatal neurodegenerative diseases that can infect humans and animals. Prions generated great public concern after an outbreak of bovine spongiform encephalopathy occurred in many European countries and scientific evidence indicated its transmission to humans. Prions are unique in demonstrating a high level of resistance to conventional device reprocessing methods and have been linked to patient-

to-patient transmission via contaminated medical devices. This data enables the Company to pursue approval from regulators in Europe to be listed as a device that inactivates these challenging infectious agents.

Intellectual Property

Considering the time and investment required to develop new products and obtain marketing authorization, the Company places considerable importance on protecting its research findings, trade secrets and technologies. As of March 31, 2018, TSO_3 had 185 patents or patent applications pending, with 91 relating specifically to the Company's STERIZONE® VP4 Sterilizer and related technology. TSO_3 relies on a combination of patents, laws, trade secrets, non-disclosure agreements and various contractual arrangements to protect its exclusive technology. There is no guarantee that TSO_3's protective measures are enforceable or sufficient to prevent illicit appropriation of its technology or development of the same or similar technology by a third party.

On September 29, 2010, TSO_3 filed patent applications for its innovations related to hydrogen peroxide alone and hydrogen peroxide and ozone sterilization systems and methods to be protected in the United States, Europe and various other countries including Japan.

During the first quarter of 2013, and in 2015, TSO_3 filed a number of divisional patent applications in all of the countries mentioned above to protect most of individual innovative concepts disclosed in the original application. Several patents on technology embedded in the STERIZONE® Sterilization System have now been granted while the other applications are still pending.

In September 2014, TSO_3 filed a new International patent application on its innovative methods to further improve compatibility under differing load conditions for surgical instruments and accessories.

In 2015, the US Patent Office and the Canadian Patent Office each granted to the Company a first patent on a core aspect of the technology embedded in the TSO_3 STERIZONE® Sterilization System. Also in 2015, six additional Japanese patents have been granted (seven granted patents) while the European Patent Office notified its decision to grant two additional patents (seven granted patents in force in up to 13 European countries).

At the end of 2015, TSO_3 also filed new US and international patent applications related to biological indicators (BI) used to monitor effectiveness of a sterilization process.

In 2016, the US Patent Office granted to the Company six additional patents covering important aspects of TSO_3's technology and mostly embedded in the STERIZONE® VP4 Sterilizer.

Also in 2016:

- TSO_3 filed new divisional patent applications covering additional critical aspects of TSO_3's technology in US and Europe to still strengthen patent protection of the STERIZONE® Sterilization System;
- A first patent covering the technology embedded in the STERIZONE® VP4 Sterilizer has been granted in Mexico to further expand the geographical patent protection coverage of the Company;
- An International Patent Application previously filed on innovative methods to further improve compatibility under differing load conditions has now entered the national phase in several countries, including the United States.

In 2017, the US Patent Office and the Japanese patent Office each granted to the Company an additional patent covering a critical aspect of TSO_3's technology to further strengthen patent protection of the STERIZONE® Sterilization System.

The Canadian Patent Office also granted to the Company five additional patents on distinct important aspects of TSO_3's technology mostly embedded in the STERIZONE® Sterilization System.

Five additional patents have been granted in Mexico while seven patents have been granted in South Korea to further expand the geographical patent protection coverage of the STERIZONE® Sterilization System.

Also in 2017, the Australian Patent Office and the Patent Office of South Africa each granted to the Company a patent on its innovative methods to further improve compatibility under differing load conditions for surgical instruments and accessories.

Still in 2017, an International Patent Application previously filed on biological indicators (BI) used to monitor effectiveness of a sterilization process entered the national phase in several countries.

During the first quarter of 2018, the Patent Office of South Korea notified the Company of his intent to grant an additional patent covering a critical aspect of TSO_3's technology embedded in the STERIZONE® Sterilization System.

Other patent applications are still pending in the United States as well as elsewhere in the world. TSO_3's unique *Dynamic Sterilant Delivery System*™ is core to the differentiation of its products and its protection enhances the Company's value.

Trademarks are important assets of the Company. STERIZONE® is a registered trademark of TSO_3 in the United States, Canada and Europe while STERIZONE TECHNOLOGY® is registered in the name of TSO_3 in not less than 43 countries.

2018 Focus

On January 25, 2018, the Company entered into the Co-commercialization Agreement with Getinge. The Company and Getinge have agreed to share the US and Canadian market and co-commercialize the Company's STERIZONE® VP4 Sterilizer, while Getinge retains the rights and responsibility for commercializing in the rest of the world. The Co-commercialization Agreement and the Getinge Agreement will terminate on August 1, 2018 unless extended by mutual agreement, and parties are in negotiations regarding modifications to the distribution relationship, either through a new agreement or a modification of the Getinge Agreement. While negotiations are in place, both Getinge and TSO_3 are working toward selling Getinge's existing inventory, including the Company's direct sales of inventory repurchased from Getinge. The parties agreed to a customer selection mechanism to prevent the likelihood of channel conflict in North America and are currently in negotiations regarding modifications to the distribution relationship, either through a new agreement or a modification of the Getinge Agreement.

As a result of the Co-commercialization Agreement, the Company plans to sell its STERIZONE® VP4 Sterilizers and associated products and services directly into the US and Canada and repurchase not less than 100 sterilizers (for US$3.3 million) back from Getinge as a source of Company product inventory for future sales.

As 2018 progresses, the Company plans to redirect more of its originally planned expenditures toward sales and marketing initiatives. To date, the Company's research and development and general and administrative expenses have declined relative to the fourth quarter of 2017, which the Company has invested in its team of sales, clinical and field service professionals, as well as sales and marketing activities. The Company's sales and marketing team is tasked with selling and providing support directly to end users in the central sterilization (CSSD) department of acute care hospitals, as well as to develop additional opportunities in the gastrointestinal reprocessing market segment. TSO_3 will also continue to support Getinge in the sale, support, installation and servicing of existing and future customers.

The capital equipment sales process in the medical device industry remains slow relative to other industries, but the Company is making progress. The Company made progress on a direct sales basis in the first quarter of 2018, and, based on customer feedback the Company has received, TSO_3 is able to provide sales and customer support at industry leading levels. It has successfully segmented and classified its target customer base, has contacted 531 of these customers, and directly issued quotations to US medical facilities for over 30 STERIZONE® VP4 Sterilizers, plus associated accessories and consumables. Each quotation is now being managed through the Company's funnel management process. Additionally, the Company has devised new and innovative sales incentives and structures to match customer feedback. The Company is involved in direct communication, industry events, and other customer outreach activities. Additionally, we believe that Getinge sold and installed fewer than 10 STERIZONE® VP4 Sterilizers in the first quarter of 2018, which was below Getinge's and TSO_3's expectations. TSO_3 is working with Getinge to improve this rate of sales toward a goal of exceeding installation rates of the previous year. Due to inventory levels at Getinge, the Company currently does not anticipate selling more STERIZONE® VP4 Sterilizers to Getinge throughout the remainder of 2018.

The Company plans to conduct additional training and sales meetings and further invest in marketing and sales collateral in support of the deployment of the STERIZONE® VP4 Sterilizers in the US and Europe and will continue to work collaboratively with Getinge with respect to launching into additional targeted international markets.

Additionally, the Company will continue to use its laboratories in support of its traditional device compatibility testing, endoscope compatibility testing and our new product development initiatives. Such efforts will help the Company to demonstrate to manufacturers, Getinge and hospitals the impact its technologies can have on medical devices, reprocessing efficiency, effectiveness, throughput and simplicity, as well as endoscope terminal sterilization.

The Company will continue to pursue its 510(k) submission with US regulators for the terminal sterilization of duodenoscopes used in ERCP procedures. If awarded such claim, TSO_3's STERIZONE® VP4 Sterilizer would become the first and only validated sterilizer technology in the US with a cleared label claim for the terminal sterilization of duodenoscopes.

Over the past years the Company has continued to invest in developing product enhancements. TSO_3 and Getinge have discussed these feature improvements, which are expected to make installations faster and easier. In the interim, TSO_3 is planning to adjust, for a charge, inventory currently held by Getinge, as these product enhancements have been deliberately designed to be fully "upgradable" with current versions of the sterilizer. These adjustments are described in the Co-commercialization Agreement and to date, Getinge has provided a purchase order to TSO_3 for over 40 such upgrades. The work associated with these upgrades began in April of 2018.

Management Discussion and Analysis

This management discussion and analysis (MD&A) is intended to help readers assess the consolidated financial position and consolidated financial performance of TSO_3 Inc. ("TSO_3", or the "Company") for the three-month period ended March 31, 2018 and to compare them with the three-month period ended March 31, 2017. This information is dated May 8, 2018 and should be read in conjunction with the Interim Condensed Consolidated Unaudited Financial Statements and the accompanying notes. Unless specified otherwise, all amounts are stated in US dollars.

The financial information contained in this MD&A and in the Interim Condensed Consolidated Unaudited Financial Statements has been prepared in accordance with the International Financial Reporting Standards ("IFRS"). The Company occasionally refers to non-IFRS financial measures in the MD&A. See the Non-IFRS financial measures section for more information.

The Interim Condensed Consolidated Unaudited Financial Statements, accompanying notes and MD&A have been reviewed by the Audit and Risk Management Committee of TSO_3 and approved by the Board of Directors.

This MD&A contains forward-looking information. A statement about the forward-looking information is made in the next section. Also, the reader should review the section on Risk Factors discussing some of the risks and uncertainties that may have a material adverse effect on the Company's business, results of operations, or financial condition as well as on an investment in the Company's securities.

Additional information regarding TSO_3 can be found in its Annual Information Form, and under TSO_3's issuer profile on SEDAR at (www.sedar.com) and TSO_3's website at www.tso3.com.

Forward Looking Statements

Certain statements contained in this report and the MD&A constitute forward-looking statements. These statements relate to future events or the Company's future performance, business prospects or opportunities and product development. All statements other than statements of historical facts may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect, "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements.

The Company believes that the expectations reflected in these forward-looking statements are reasonable, but no assurance can be given that these expectations will prove to be correct. These statements speak only as of the date of this report. Such statements are based on a number of assumptions which may prove to be incorrect, including, but not limited to, assumptions about:

- The success of the relationship with Getinge and suppliers;
- The ability for the Company and Getinge to deploy TSO_3's products to end customers;
- The ability for the Company to market and sell its products;
- Business and economic conditions;
- The ability to obtain sufficient quantities of supplies and materials when needed;
- The ability to obtain regulatory authorizations that are required to market its product;
- The ability to attract and retain skilled staff;
- Regulatory Approvals;
- Competition;
- Tax benefits and tax rates;
- The ability to complete research and development work;
- Foreign currency exchange rates;

- The ability for the Company to attract capital and other financial risks;
- The compatibility of medical instruments with the Company's technology.

These forward-looking statements involve risks and uncertainties relating to, among other things, commercial operations, compatibility, biocompatibility, research and development projects, dependency on key personnel, limited history of commercialization, management of business growth, intellectual property and counterfeiting, competition, product liability issues, litigation, regulatory approvals and financial instruments. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements. Factors that could cause actual results to differ materially include, but are not limited to, the risk factors described under the section "Risk factors" in the Annual MD&A of the Company for the year ended December 31, 2017, which reflect to the Company's knowledge, the material risks and uncertainties it faced as at May 8, 2018, the date of filing for the first fiscal quarter of 2018. Disclosure contained in this document is current to that date, unless otherwise stated.

Investors should not place undue reliance on forward-looking statements as the plans, intentions or expectations upon which they are based might not occur. The Company cautions that the foregoing list of risk factors is not exhaustive. Investors and others who base themselves on the Company's forward-looking statements should carefully consider the above factors as well as the uncertainties they represent and the risk they entail. The reader must not unduly rely upon the Company's prospective statements.

Further, the Company does not intend, and does not assume any obligation, to update these forward looking statements, except as may be required by applicable laws.

Summary of Results

Periods ended March 31, 2018 and 2017 (Unaudited, IFRS Basis, in thousands of US dollars, except per share amounts)

	First Quarter	
	2018	2017
	$	$
Revenues	**255**	4,211
Cost of sales	**526**	2,641
	(271)	1,570
Expenses		
Research and development	**1,704**	1,353
Selling, general and administrative	**2,551**	2,209
Financial income	**(14)**	(39)
Total Expenses	**4,241**	3,523
Net loss before income taxes	**(4,512)**	(1,953)
Income taxes	**-**	27
Net loss and comprehensive loss	**(4,512)**	(1,980)
Weighted average number of outstanding shares (in thousands)	**92,877**	91,995
Basic and diluted net loss per share	**(0.05)**	(0.02)
Basic and diluted net comprehensive loss per share	**(0.05)**	(0.02)

Results Analysis

Below, the Company discusses the variations of certain accounts for the three-month periods ending March 31, 2018 and 2017.

All dollar amounts are in **US Dollars** unless otherwise noted.

REVENUES

For the first quarter of 2018, revenues equalled $0.3 million, as compared to $4.2 million in the first quarter of 2017. TSO_3 revenues in the first quarter of 2018 are related to consumables and service parts. Consumables and parts revenue in the first quarter of 2018 were lower than anticipated principally due to inventory adjustments at Getinge. The Company did not ship STERIZONE® VP4 Sterilizers to Getinge, nor did it receive a purchase order for such sterilizers, in the first quarter of 2018 as compared to 36 units shipped in 2017. Sales of the Company's proprietary consumables in the first quarter of 2018 grew relative to 2017 as a result of increased orders from Getinge relating to increased installations of the Company's STERIZONE® VP4 Sterilizer.

The Company did not record license fee revenue in the first quarter of 2018, as compared to $0.2 million recorded in the first quarter of 2017. In the first quarter of 2018, the Company did not recognize a portion of the $6.0 million balance in deferred license fee associated with the Getinge Agreement as negotiations with Getinge are ongoing. The Company expects to recognize this license revenue in the future in a manner which reflects the outcome of the negotiations with Getinge.

NET LOSS

In the first quarter of 2018, net loss and comprehensive loss totaled $4.5 million or ($0.05) per share, as compared to $2.0 million or ($0.02) per share of net loss and comprehensive loss in the first quarter of 2017.

In the first quarter of 2018, gross profit decreased by $1.8 million, as compared to the same period last year, mainly related to the decrease of sterilizer sales to Getinge and the lack of deferred license fee revenue recognition. The Company increased the investments made in research and development activities by $0.4 million and by $0.3 million in sales, general and administrative activities to support the business.

For the first quarter of 2018, the Company incurred no material events which would have impacted its comprehensive loss.

Supplemental Non-IFRS Financial Measures

This MD&A was prepared using results and financial information determined under IFRS. In addition to IFRS financial measures, management uses non-IFRS financial measures to assess the Company's operational performance. It is likely that the non-IFRS financial measures used by the Company will not be comparable to similar measures reported by other issuers or those used by financial analysts as their measures may have different definitions. The measures used by the Company are intended to provide additional information and should not be considered in isolation or as a substitute for IFRS financial performance measures.

Generally, a non-IFRS financial measure is a numerical measure of an entity's historical or future financial performance, financial position or cash flows that is neither calculated nor recognized under IFRS. Management believes that such non-IFRS financial measures are important as they provide users of the financial statements with a better understanding of the results of the Company's recurring operations and their related trends, while increasing transparency and clarity into its operating results. Management also believes these measures can be useful in assessing the Company's capacity to discharge its financial obligations.

Management is assessing its operational performance using supplemental non-IFRS measures which removes significant unusual items that do not reflect the recurring and ongoing operational results and trends.

IFRS TO NON-IFRS ADJUSTED EBITDA RECONCILIATION

$000's	**2018 Q1**	Q4	Q3	Q2	2017 Q1
Net loss	**(4,512)**	(1,449)	(1,771)	(2,254)	(1,980)
Financial expenses (income)	**(14)**	74	48	49	(39)
Amortization and depreciation	**315**	246	331	221	168
Share-based compensation expense	**371**	301	632	592	609
Income taxes	**-**	(59)	33	29	27
Adjusted Ebitda	**(3,840)**	(887)	(727)	(1,363)	(1,215)

(1) Refer to the Non-IFRS financial measures.

Adjusted EBITDA, is adjusted Earnings before Interest, Taxes, Depreciation, and Amortization (Adjusted EBITDA). Adjusted EBITDA adjusts net income for (1) significant realized and unrealized foreign exchange gains or losses, (2) financial expenses (income), (3) amortization and depreciation expenses (4) share-based compensation expense, (5) write-downs of certain tangible and intangible assets, (6) one-time write-off of inventory, (7) income taxes, and (8) other significant unusual items.

EXPENSES

Foreign Exchange Impact

The Company is reporting currency in US dollars as the significant majority of its current and future revenues are and are expected to be denominated in US dollars.

A significant portion of the Company's expenses are denominated in Canadian dollars. Fluctuations in the value of Canadian dollars (CAD) relative to US dollars (USD) will have an impact on the Company's operating results to the extent expenses in Canadian dollars are not offset by revenues in the same currency. The Company currently does not otherwise hedge against foreign exchange rate fluctuations.

In the first quarter of 2018, total expenses denominated in Canadian dollars were CAD$2.3 million, as compared to CAD$4.1 million in the first quarter of 2017. The average USD/CAD foreign exchange rate in the first quarter of 2018 was 0.7910 as compared to 0.7559 in 2017, which is reflected in an increase in expenses of 5% year over year upon conversion to USD.

From a quarterly sequential perspective, the USD/CAD foreign exchange rate in the first quarter of 2018 was 0.7910 as compared to 0.7867 in the fourth quarter of 2017, which is reflected in an increase in expenses of 1% quarter over quarter upon conversion to USD.

In the first quarter of 2018, total cost of sales related expenses denominated in Canadian dollars were CAD$0.7 million, as compared to CAD$2.4 million in the first quarter of 2017. Total research and development expenses denominated in Canadian dollars were CAD$0.8 million in the first quarter of 2018, which is consistent with to the first quarter of 2017. In the first quarter of 2018, total SG&A expenses denominated in Canadian dollars were CAD$0.8 million, as compared to CAD$0.9 million in the first quarter of 2017.

Cost of sales

Cost of sales include all expenses incurred in connection with production costs, related quality control and assurance expenses, cost of services sold to end-users, shipping expenses, supply chain activities as well as layout improvements.

For the three-month period ended March 31, 2018, cost of sales amounted to $0.5 million, as compared to $2.6 million for the same period in 2017. In the first quarter of 2018, TSO_3 did not ship STERIZONE® VP4 Sterilizers as compared to 36 sterilizers in the first quarter of 2017.

Gross profit was negative by $0.3 million in the first quarter of 2018, as compared to positive $1.6 million in the first quarter of 2017. Gross profit in the first quarter of 2018 declined as the Company did not ship STERIZONE® VP4 Sterilizers to Getinge and did not recognize licencing fee revenue. First quarter 2018 gross profit contributed from the sales of consumables and service parts were less than fixed overhead and other costs associated with goods sold in the quarter.

Research and development

For the quarter ended March 31, 2018, research and development expenses were $1.7 million, as compared to $1.4 million for the same period in 2017. During the first quarter of 2018, the Company incurred $0.2 million of additional expenses related to material purchases, equipment maintenance, depreciation and building expenses to run the laboratory in Myrtle Beach. Also, these expenses were for extended endoscope regulatory claims, other endoscope and medical device compatibility studies for its STERIZONE® VP4 Sterilizer. To support product development and the laboratory, the Company also increased salary, share-based compensation, travelling expenses and professional fees by $0.1 million in the first quarter of 2018 as compared to the same period in 2017.

Selling, General and Administrative (SG&A)

Selling, general and administrative (SG&A) include marketing, sales and service and administrative expenses. SG&A expenses were $2.6 million for the quarter ended March 31, 2018, as compared to $2.2 million for the same period in 2017.

During the first quarter of 2018, as compared to the same period in 2017, the Company incurred an additional $0.3 million in salary, share-based compensation, travelling and recruiting fees as a result of the creation of its commercialization team, and $0.2 million in professional fees associated with commercialization, marketing and administration. General and administrative expenses declined on a year over year basis by $0.3 million.

Share-based compensation expense

For the quarter ended March 31, 2018, non-cash share-based compensation amortization amounted to $0.4 million, as compared to $0.6 million for the same period in 2017. Share-based compensation amortization decreased as a result of employee departures during the first quarter of 2018.

As March 31, 2018, the Company had 7.7 million stock options oustanding, as compared to 7.3 million at the same date in 2017.

These expenses are presented in the Interim Condensed Consolidated Statements of Loss and Comprehensive Loss in the expense line items which correspond to the functions of the equity incentive holders.

Financial income

For the quarter ended March 31, 2018, financial income is not significant and comparable.

Financial Position Analysis

(Unaudited, IFRS Basis, in thousands of US dollars)

	March 31, 2018 $	December 31, 2017 $
Cash, cash equivalents and investments	**9,951**	14,808
Accounts receivable	**582**	651
Inventories	**2,456**	2,040
Property, plant and equipment	**2,984**	3,184
Intangibles assets	**1,879**	1,886
Accounts payable, accrued liabilities, current and deferred income tax liabilities	**2,110**	2,515
Warranty provision	**1,182**	1,263
Deferred revenues (short and long term)	**6,044**	6,050
Equity	**8,775**	12,891

Liquid Assets

As at March 31, 2018, cash, cash equivalents and investments amounted to $10.0 million, as compared to $14.8 million as at December 31, 2017.

In the first quarter of 2018, the Company used approximately $3.9 million in cash for operations, excluding non-cash working capital, and $0.9 million consumed from changes in non-cash working capital. This compares to $0.6 million of cash generated from operations in the first quarter of 2017, which included use of $1.3 million in operations, excluding non-cash working capital, and the generation of $1.8 million from changes in non-cash working capital, particularly from the early receipt of accounts receivables. Cash used from operations increased predominantly in the first quarter of 2018 relative to the comparable period due to the decrease in sales of sterilizers to Getinge.

Accounts Receivable

As at March 31, 2018, accounts receivable amounted to $0.6 million, as compared to $0.7 million as at December 31, 2017. As at March 31, 2018, receivables were related to R&D and sales tax credits and a unsecured receivable outstanding from an executive in relation to an ordinary course income tax refund, while receivables as at March 31, 2017 were mainly related to R&D and sales tax credits. In the first quarters of 2018 and 2017, the Company used the automated receivable factoring program for almost all accounts receivable from Getinge.

Inventories

As at March 31, 2018, inventories amounted to $2.5 million, as compared to $2.0 million as at December 31, 2017.

	March 31, 2018 $	December 31, 2017 $
Raw Materials	**1,546**	1,137
Work in Progress	**258**	242
Finished Goods	**652**	661
	2,456	2,040

In the first quarter of 2018, the Company grew its raw material inventories to build supply of parts for upgrades to STERIZONE® VP4 Sterilizers held in Getinge's inventory.

Property, Plant and Equipment

Property, plant and equipment, net of depreciation, amounted to $3.0 million as at March 31, 2018 which is $0.2 million lower compared to December 31, 2017. During the quarter, TSO_3 acquired a total of $0.1 million in property, plant and equipment. Depreciation increased to $0.3 million during the first quarter of 2018.

Intangible Assets

Intangible assets, net of amortization, amounted to $1.9 million as at March 31, 2018 (unchanged relative to March 31, 2017). The Company invested $0.04 million in patents and amortization increased by $0.04 million during the first quarter of 2018.

Accounts Payable, Accrued Liabilities, Current and Deferred Income Tax Liabilities

As at March 31, 2018, accounts payable, accrued liabilities, current and deferred income tax liabilities amounted to $2.1 million, which is $0.4 million lower compared to December 31, 2017. The decrease is due to a decline in raw materials and other purchasing relative to the prior year. As at March 31, 2018 the Company had $0.1 million as current and deferred income tax liabilities (same level as at December 31, 2017).

Deferred Revenues

At the end of the first quarter of 2018, deferred revenues represented almost exclusively the unamortized part of the deferred license revenue received under the Getinge Agreement.

The Company did not record license fee revenue in the first quarter of 2018, as compared to $0.2 million recorded in the first quarter of 2017. In the first quarter of 2018, the Company did not recognize a portion of the $6.0 million balance in deferred license fee associated with the Getinge Agreement as negotiations with Getinge are ongoing. The Company expects to recognize this license revenue in the future in a manner which reflects the outcome of the negotiations with Getinge.

Shareholders' Equity

As at March 31, 2018, Shareholders' Equity amounted to $8.8 million, as compared to $12.9 million as at December 31, 2017. The variation is mainly the result of the absorption of the operating deficit incurred during the three-month period ended March 31, 2018, partially offset by $0.4 million in share-based compensation recognized during the same period.

As at March 31, 2018, the number of outstanding shares was 92,891,304 (92,854,304 as at December 31, 2017). As of May 8, 2018, the date of filing for the first fiscal quarter of 2018, the number of outstanding shares was 92,891,304.

Cash Flows Analysis

(Unaudited, IFRS Basis, in thousands of US dollars)

	First Quarter	
	2018	2017
	$	$
Operating Activities	**(4,766)**	555
Investing Activities	**2,218**	(1,770)
Financing Activities	**25**	63

Operating Activities

In the first quarter of 2018, the Company used approximately $3.9 million in cash for operations, excluding non-cash working capital, and $0.9 million consumed from changes in non-cash working capital. This compares to $0.6 million of cash generated from operations in the first quarter of 2017, which included use of $1.3 million in operations, excluding non-cash working capital, and the generation of $1.8 million from changes in non-cash working capital, particularly from the early receipt of accounts receivables. Cash used from operations increased predominantly in the first quarter of 2018 relative to the comparable period due to the decrease in sales of sterilizers to Getinge.

Investing Activities

For the three-month period ended March 31, 2018, investing activities generated $2.2 million, as compared to $1.8 million generated during the same period in 2017. In the first quarter of 2018, the Company generated $2.3 million from the net disposal of short term investments and used $0.1 million to purchase property plant and equipment and intangible assets in 2018, as compared to $2.1 million generated for net disposal in investments and $0.3 million used in purchase of property plant and equipment and intangible assets in the same period in 2017.

Financing Activities

For the three-month period ended March 31, 2018, financing activities generated $0.02 million as compared to $0.06 million for the same period in 2017. The total amount generated in the first quarter of 2018 and 2017 was from options exercised.

Summary of Quarterly Results

(Unaudited, IFRS Basis, in thousands of US dollars, except per share amounts)

This table shows the quarterly evolution of sales, net loss and net loss per share.

	2018				2017			2016
	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2
Revenues	**255**	5 780	5 105	4 630	4 211	3 746	3 507	2 977
Net loss	**(4,512)**	(1 449)	(1 771)	(2 254)	(1 980)	(2 068)	(1 473)	(1 487)
Net loss per Share (basic, in $)	**(0.05)**	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)

Segmented Information

The Company has one operating segment.

		First quarter
Revenues	**2018**	2017
Canada and Worldwide	**50**	110
United States	**205**	4,101
	255	4,211

	March 31, 2018			December 31, 2017		
	Inventories	**Property, Plant and Equipment**	**Intangible Assets**	Inventories	Property, Plant and Equipment	Intangible Assets
Canada and Worldwide	**1,967**	**1,246**	**1,865**	1,616	1,306	1,870
United States	**489**	**1,738**	**14**	424	1,878	16
	2,456	**2,984**	**1,879**	2,040	3,184	1,886

For the first quarter of 2018, revenue from Getinge represented 93% of the Company's total revenues in conjunction with the Getinge Agreement (99% for the same period in 2017).

Off-Balance Sheet Arrangement

The Company made no off-balance sheet arrangement during the first quarter of 2018 other than purchase orders issued in the normal course of business.

Additional Disclosure – Unrecorded Tax Assets

The Company has accumulated a substantial amount of losses, unclaimed expenses and tax credits that could be claimed in the future to reduce income taxes. The related deferred income tax assets will be recorded on the Condensed Consolidated Financial Statements only when the Company concludes that these tax assets will probably be materialized by shielding profits from taxes, or otherwise. If the Company had reached this conclusion on March 31, 2018, $24.6 million in tax assets would have been recorded based on an effective rate of 15% for federal taxes and 11.5% for provincial taxes ($23.7 million as at December 31, 2017 and same effective tax rate).

Financial Instruments

The reader is refered to note 6 of the Company's Annual Audited Consolidated Financial Statement for the year ended December 31, 2017 and note 6 of the Interim Unaudited Consolidated Financial Statements for the quarter ended March 31, 2018 for a detailed presentation of financial instruments.

Capital Resources

The Company needs capital primarily to finance its production, its research and development, its selling, general and administrative expenses, its working capital and its capital expenditures. The Company's capital is comprised of share capital and reserve for share-based compensation.

In the past, the Company has financed its activities through public and private equity financings and, to a small extent, through government grants and tax credits. In evaluating less dilutive options and depending on the quality of the credit structure of a prospective debt transaction and prevailing market conditions, the Company could finance a portion of its cash needs through debt issues.

The Company invests its funds in highly liquid short-term investments as required by its Investment Policy (see section on Risk Factors presented in the Annual Management Discussion and Analysis of the Company for the year ended December 31, 2017). These securities are chosen on the basis of foreseen cash requirements and safety.

Accounting Policies

The reader is refered to notes 2 and 3 of the Company's Annual Audited Consolidated Financial Statements for the year ended December 31, 2017 and Interim Consolidated Financial Statements for the quarter ended March 31, 2018 for a detailed presentation of accounting policies, critical accounting judgments, key source of estimation uncertainty and future accounting changes.

Risk Factors

The Company operates in industry segments that have a variety of risk factors and uncertainties. TSO_3 hereby incorporates by reference the risks and uncertainties described in our Annual Management Discussion and Analysis of the Company for the year ended December 31, 2017 which reflect, to its knowledge, the material risks and uncertainties the Company faced as at March 31, 2018.

Disclosure Controls and Procedures and Internal Controls over Financial Reporting

In accordance with National Instrument 52-109 of the Canadian Securities Administrators, the Company has filed certificates signed by the President and Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") that, among other things, report on the design of disclosure controls and procedures (DC&P) and the design of internal control over financial reporting (ICFR).

The CEO and the CFO have designed DC&P, or caused them to be designed under their supervision, to provide reasonable assurance that (1) material information relating to the Company has been made known to them and that (2) information required to be disclosed in the Company's filings is recorded, processed, summarized and reported within the prescribed time periods under securities legislation as of March 31, 2018.

Also, the CEO and the CFO have designed ICFR, or have caused it to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Interim Financial Statements for financial reporting purposes in accordance with IFRS as of March 31, 2018.

Changes in internal controls over financial reporting

No changes were made to the Company's internal controls over financial reporting during the quarter ended March 31, 2018 that have materially affected, or are reasonably likely to materially affect, the internal controls over financial reporting.

INTERIM CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS

For the three-month periods ended March 31, 2018 and 2017

Interim Condensed Consolidated Statements of Loss and Comprehensive Loss

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, except per share amounts)

	Notes	First Quarter 2018 $	2017 $
Revenues		**255**	4,211
Cost of sales	**5**	**526**	2,641
		(271)	1,570
Expenses			
Research and development		**1,704**	1,353
Selling, general and administrative		**2,551**	2,209
Financial income	**4**	**(14)**	(39)
Total Expenses		**4,241**	3,523
Net loss before income taxes		**(4,512)**	(1,953)
Income taxes		**-**	27
Net loss and total comprehensive loss		**(4,512)**	(1,980)
Weighted average number of outstanding shares (in thousands)		**92,877**	91,995
Basic and diluted net loss per share	**15**	**(0.05)**	(0.02)
Basic and diluted net comprehensive loss per share	**15**	**(0.05)**	(0.02)

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

Interim Condensed Consolidated Statements of Changes in Equity

(Unaudited, in thousands of US dollars)

	Notes	Share Capital $	Reserve-Share-Based Compen-sation $	Deficit $	Other comprehen-sive income $	Total $
Balance at January 1, 2017		110,406	4,709	(95,732)	(1,712)	17,671
Options exercised	11	109	(46)	-	-	63
Share-based compensation	12	-	609	-	-	609
Net loss for the period		-	-	(1,980)	-	(1,980)
Balance at March 31, 2017		110,515	5,272	(97,712)	(1,712)	16,363
Balance at April 1, 2017		110,515	5,272	(97,712)	(1,712)	16,363
Options exercised	11	700	(223)	-	-	477
Share-based compensation	12	-	1,525	-	-	1,525
Net loss for the period		-	-	(5,474)	-	(5,474)
Balance at December 31, 2017		111,215	6,574	(103,186)	(1,712)	12,891
Balance at January 1, 2018		111,215	6,574	(103,186)	(1,712)	12,891
Options exercised	11	39	(14)	-	-	25
Share-based compensation	12	-	371	-	-	371
Net loss for the period		-	-	(4,512)	-	(4,512)
Balance at March 31, 2018		111,254	6,931	(107,698)	(1,712)	8,775

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

Interim Condensed Consolidated Statements of Financial Position

(Unaudited, in thousands of US dollars)

	Notes	March 31, 2018 $	December 31, 2017 $
Current Assets			
Cash and Cash Equivalents	6	**5,521**	8,044
Short-term Investments	6	**4,430**	6,764
Accounts Receivable	7	**582**	651
Inventories		**2,456**	2,040
Prepaid Expenses		**261**	150
		13,250	17,649
Non-current Assets			
Property, Plant and Equipment	8	**2,984**	3,184
Intangible Assets	9	**1,879**	1,886
		4,863	5,070
		18,113	22,719
Current Liabilities			
Accounts Payable and Accrued Liabilities	6	**2,025**	2,430
Warranty Provision		**1,182**	1,263
Current Tax Liabilities		**68**	68
Deferred Revenues	10	**2**	6
		3,277	3,767
Non-current Liabilities			
Defered Tax Liabilities		**17**	17
Deferred Revenues	10	**6,044**	6,044
		9,338	9,828
Equity			
Share Capital	11	**111,254**	111,215
Reserve – Share-based Compensation	12	**6,931**	6,574
Deficit		**(107,698)**	(103,186)
Accumulated Other Comprehensive Loss		**(1,712)**	(1,712)
		8,775	12,891
		18,113	22,719

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

Interim Condensed Consolidated Statements of Cash Flows

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars)

	Notes	Three months 2018 $	2017 $
Cash flows from operating activities			
Net loss		**(4,512)**	(1,980)
Adjustments for:			
Depreciation and amortization		**315**	168
Deferred income tax liabilities		**-**	27
Share-based compensation	12	**371**	609
Investment income	4	**(27)**	(75)
		(3,853)	(1,251)
Changes in non-cash operating working capital items	13	**(948)**	1,765
Interest received		**35**	41
Cash flows (used in) generated by operating activities		**(4,766)**	555
Cash flows from investing activities			
Acquisition of investments		**-**	(1,412)
Disposal of investments		**2,326**	3,504
Acquisition of property, plant and equipment	8	**(67)**	(193)
Acquisition of intangible assets	9	**(41)**	(129)
Cash flows generated by investing activities		**2,218**	1,770
Cash flows from financing activities			
Options exercised	11	**25**	63
Cash flows generated by financing activities		**25**	63
(Decrease) increase in cash and cash equivalents		**(2,523)**	2,388
Cash and cash equivalents at the beginning		**8,044**	2,698
Cash and cash equivalents at the end		**5,521**	5,086

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

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

1. Description of Business

TSO_3 ("TSO_3" or the "Company") exists under the Business Corporations Act (Québec). The Company's activities encompass the sale, production, maintenance, research, development and licensing of sterilization processes, related consumable supplies and accessories for medical devices that are sensitive to heat and moisture. The Company designs products for sterile processing areas in medical facilities that offer an advantageous replacement solution to other low temperature sterilization and high-level disinfection processes currently used. TSO_3 also offers services related to the maintenance of sterilization equipment and compatibility testing of medical devices with such processes. The head office of the Company is located at 2505, avenue Dalton, Québec (Québec), Canada and its subsidiary office is located at 1636 American Way, Myrtle Beach, SC, United States.

2. Accounting Policies

Statement of Compliance

The Interim condensed consolidated unaudited financial statements ("financial statements") are prepared in compliance with International Accounting Standard 34 – Interim Financial Reporting ("IAS 34"). Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards (IFRS) and applicable as at March 31, 2018 have been omitted or condensed. As such, these financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2017. The financial statements were prepared using the same basis of presentation, accounting policies and methods of computation as outlined in Note 2, *accounting policies* in our consolidated financial statements for the year ended December 31, 2017, except for the adoption of new and amended standards as set out below. The financial statements do not include all of the notes required in annual financial statements.

Going Concern

The Company started its US commercial operations at the end of 2015, when it announced a worldwide exclusive distribution agreement (the"Getinge agreement") with Getinge for the STERIZONE® VP4 Sterilizer. The Company has been highly dependent on Getinge's commitment and success at marketing and distributing the STERIZONE® VP4 Sterilizer.

Getinge's sales to end users did not occur at the same pace as Getinge's purchases from TSO_3. The Company sold 110 and 170 STERIZONE® VP4 Sterilizers in 2016 and 2017 respectively. In November 2017, the Company indicated that over 50 STERIZONE® VP4 Sterilizers had been delivered to end users in Canada and in the United States.

On January 25, 2018, the Company entered into a co-commercialization agreement (the "Co-commercialization Agreement") with Getinge allowing the Company to sell its STERIZONE® VP4 Sterilizers and associated products and services directly into the United States and Canada. The Co-commercialization Agreement also include an obligation for the Company to repurchase not less than 100 STERIZONE® VP4 Sterilizers for $3.3 million.

The parties have also agreed to begin immediate negotiations on additional modifications to the distribution relationship. The Co-commercialization Agreement and the Getinge Agreement will terminate on August 1, 2018 unless extended by mutual agreement. If agreement between the parties is not reached, TSO_3 has agreed, by July 1, 2019, to repurchase Getinge's remaining STERIZONE® VP4 Sterilizers at the same unit price in the Co-commercialization Agreement.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

2. Accounting Policies (cont'd)

Going Concern (cont'd)

While good faith negotiations have begun by both parties to either replace or amend the existing agreements, with the stated mutual goal to work toward a new and improved business arrangement, there is no guarantee that such a replacement or amendment will be achieved under favourable terms to the Company or at all.

The performance requirements in the Getinge Agreement involve minimum annual unit purchase commitments from Getinge and fulfillment obligations by TSO_3. Getinge must provide a purchase order to be obligated to buy units under its minimum annual commitments, and Getinge has not yet provided such a purchase order for 2018. There is no guarantee that Getinge will purchase additional STERIZONE® VP4 Sterilizers or other products or services.

As of March 31, 2018, the Company had positive working capital of $10.0 million, an accumulated deficit of $107.7 million and a net loss of $4.5 million for the quarter ended March 31, 2018. The attainment of profitable operations is dependent upon future events, including generating revenues from the sale of its products that will support its cost structure through its own distribution network and/or through a successful distribution agreement and gaining market acceptance for its products. The uncertainties related to these various conditions may cast doubt on the Company's ability to continue as a going concern.

In the event that the Company would not achieve its expected sales, the Company may be required to reduce or delay operating expenses as deemed appropriate to in order to conserve cash or to raise additional capital or financing within the next year, in order to continue the production and commercialization of its products and to continue to fund operations at the current cash expenditure levels.

Our interim consolidated financial statements as of March 31, 2018 have been prepared under the assumption that we will continue as a going concern for the next twelve months. Our ability to continue as a going concern is dependent upon our ability to generate additional revenue from the sale of units by the Company, attain further operating efficiencies, obtain additional equity and or debt financing and or to reduce expenditures. Our interim consolidated financial statements as of March 31, 2018 did not include any adjustments that might result from the outcome of this uncertainty.

New standard adopted by the Company

IFRS 9 Financial Instruments

In 2014, the IASB completed its project to replace IAS 39 Financial Instruments: Recognition and Measurement with IFRS 9. IFRS 9 introduces new requirements for 1) the classification and measurement of financial assets and financial liabilities, 2) impairment for financial assets and 3) general hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018.

TSO_3 adopted IFRS 9 in its financial statements from January 1, 2018 applying the transition provisions set out in IFRS 9. The Company elected not to restate comparatives and therefore the effect of applying the standard was recognized at the date of initial application (January 1, 2018). For classification and measurement, the requirements of IFRS 9 were applied to financial assets that have not been derecognized as at 1 January 2018. There was no material impact to the Company's financial position, statement of loss and comprehensive loss, or cash flows as a result of the adoption. The new accounting policies section is described below.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

2. Accounting Policies (cont'd)

New standard adopted by the Company (cont'd)

IFRS 15 Revenue from Contracts with Customers

The IASB also published IFRS 15 Revenue from Contracts with Customers, which replaces IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations. IFRS 15 is effective for annual periods beginning on or after January 1, 2018.

TSO_3 adopted IFRS 15 in its financial statements from January 1, 2018. The adoption of the new standard was applied using the modified retrospective method, with the effect of initially applying this standard recognized at the date of initial application (January 1, 2018). There was no impact to the Company's financial position, statement of loss and comprehensive loss, or cash flows as a result of the adoption. The new accounting policies section is described below.

New accounting policies applicable starting January 1, 2018

Revenue Recognition

The Company recognizes revenue from the following major sources:

- Sale of sterilizers and associated license fees;
- Related spare parts, consumable supplies and accessories
- Maintenance services

Sale of sterilizers and associated license fees

The Company sells sterilizers to Getinge and directly to customers. Revenue is recognized when control of the goods are transferred to Getinge or the customers, being at the point the goods are delivered.

The Company signed a 5 year exclusive distribution agreement with Getinge Infection Control AB ("Getinge") in 2015 that includes the sale of sterilizers under a formula for minimum unit shipments in exchange for an upfront licensing fee for the exclusive distribution right and a per unit fee payable upon delivery of sterilizers over the term. Revenue is measured based on the consideration specified in this agreement. The upfront fee has been recognized as revenue on the basis of estimated future expected sales of sterilizers and has been recorded as revenue when control of the sterilizers transfers to the customer which is upon delivery at Getinge's location.

No sterilizers were delivered to Getinge during the quarter and, as the parties have entered into renegotiation, the Company has deferred recognition of license fee revenue in the period. The Company expects to recognize revenue in the future a manner appropriately in reflection of the outcome of the negotiations with Getinge.

Related spare parts, consumable supplies and accessories

The Company sells related spare parts, consumable supplies and accessories to Getinge and directly to customers.

Revenue is recognized when control of the goods are transferred to Getinge or the customers, being at the point the goods are delivered.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

2. Accounting Policies (cont'd)

New standard adopted by the Company (cont'd)

Maintenance services

This service relates to maintenance work that may be required on the sterilizers. Revenue relating to the maintenance services is recognized when the service is performed.

Financial Income

Financial Income from a financial asset is recognized when it is probable that the economic benefits will flow to the Company and the amount of income can be measured reliably. Financial income is accounted for on an accrual basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Financial instruments:

Financial assets and financial liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially recognized at fair value except for trade receivables which are recognized at the transaction price. All recognized financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortized cost or fair value on the basis of the Company's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets.

The following illustrates the classification and measurement of financial assets and liabilities under IFRS 9 and IAS 39 at the date of initial application:

Financial assets/liabilities	Original measurement category (IAS 39)	New measurement category (IFRS 9)
Cash	Loans and Receivables	Amortized Cost
Cash Equivalents	Fair value through profit or loss	Fair value through profit or loss
Investments	Fair value through profit or loss	Fair value through profit or loss
Accounts Receivable	Loans and Receivables	Amortized Cost
Accounts Payable and Accrued Liabilities	Other Liabilities	Other Liabilities

Cash and Cash Equivalents

Cash and cash equivalents include cash and investments with maturities of three months or less from the date of acquisition. These investments are highly liquid and are held for the purpose of meeting short and long term cash commitments. Therefore the cash equivalent is recorded at fair value through profit or loss. Increases and decreases in fair value are recognized as investment income.

Investments

Investments are instruments presented at fair value through profit or loss because they will be used for short and long-term cash commitments. These investments are recorded at fair value. Increases and decreases in fair value are recognized as investment income.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

2. Accounting Policies (cont'd)

New standard adopted by the Company (cont'd)

Accounts Receivables

Accounts receivables as outlined in note 7 are measured at amortized cost using the effective interest method.

Accounts payable and Accrued Liabilities

Accounts payable and accrued liabilities are accounted for at amortized cost using the effective interest method.

Transaction Costs

Transaction costs related to financial assets presented at fair value are expensed as incurred. Transaction costs related to other liabilities and to the financial assets presented at amortized cost are added to the carrying value of the asset or are netted against the carrying value of the liability and are then recognized over the expected life of the instrument using the effective interest method.

Fair Value

The fair value of a financial instrument is defined as the price that would be received to sell an asset or pay to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities approximates their carrying values due to the short-term maturities of these items.

Impairment of financial assets

In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss (ECL) model as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires the Company to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition of the financial assets. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognized.

Specifically, IFRS 9 requires the Company to recognize a loss allowance for expected credit losses on debt investments subsequently measured at amortized cost or at FVTOCI. In particular, IFRS 9 requires the Company to measure the loss allowance for a financial instrument at an amount equal to the lifetime ECL if the credit risk on that financial instrument has increased significantly since initial recognition, or if the financial instrument is a purchased or originated credit-impaired financial asset. IFRS 9 also provides a simplified approach for measuring the loss allowance at an amount equal to lifetime ECL for trade receivables in certain circumstances.

3. Future Accounting Changes

On September 16, 2014, the IASB published an amendment to IFRS 10 – Consolidated Financial Statements and to IAS 28 - Investments in Associates and Joint Ventures. The amendment "Sale or Contribution of Assets between an Investor and its Associate or Joint Venture" clarifies the accounting for the gain or loss resulting from loss of control or from transfer of assets following a transaction with an associate or joint venture. Originally, the provisions of this amendment were supposed to apply prospectively to financial statements beginning on or after January 1, 2016.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

3. Future Accounting Change (cont'd)

The Company closely monitors both new accounting standards and amendments to existing accounting standards issued by the IASB. The Company is currently assessing how adoption of new and amended IASB accounting standards will impact the consolidated financial statements. Aside from the adoption of IFRS 9 and IFRS 15 on January 1, 2018, there have been no significant updates to the future accounting policy changes disclosed in Note 3 to the audited annual consolidated financial statements for the year ended December 31, 2017.

4. Financial expenses (income)

	First Quarter	
	2018	2017
	$	$
Financial Income		
Investment Income	**(27)**	(77)
Foreign Exchange Gain	**(1)**	-
	(28)	(77)
Financial Expenses		
Bank Charges	**13**	14
Factoring Cost	**1**	18
Foreign Exchange Loss	**-**	7
	14	38
Total Financial Income	**(14)**	(39)

5. Additional Information on the Consolidated Statements of Loss and Comprehensive Loss

Expenses in cost of sales, research and development as well as selling, general and administrative include the following:

	First Quarter	
	2018	2017
	$	$
Salary and Other Benefits	**2,268**	1,865
Share-based compensation expense	**371**	609
Depreciation of Property, Plant and Equipment	**267**	123
Amortization of Intangible Assets	**48**	45
Research and Development Tax Credits	**(33)**	(31)

Cost of sales includes $0.4 million of overhead as of March 31, 2018.

6. Financial Instruments

Cash and Cash Equivalents

	March 31, 2018	December 31, 2017
	$	$
Cash and cash equivalents	**5,521**	8,044

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

6. Financial Instruments (cont'd)

Investments

	March 31, 2018 $	December 31, 2017 $
Short-term Investments		
Bonds	**4,430**	6,764
	4,430	6,764

Accounts Receivable

	March 31, 2018 $	December 31, 2017 $
Accounts Receivable	**582**	651

Accounts Payable and Accrued Liabilities

	March 31, 2018 $	December 31, 2017 $
Accounts Payable and Accrued Liabilities	**2,025**	2,430

Investments were rated A- or better and had an average yield of 2.17% as at March 31, 2018.

Bonds held by the Company are classified as level 1 under IFRS 13 because their valuation model is based on quoted prices included in Level 1 that are observable for the assets. Their fair value is calculated using the market value on the measurement date.

7. Accounts Receivable

	March 31, 2018 $	December 31, 2017 $
Receivables from Clients and Related Parties	**287**	217
Government Credits Receivable	**295**	434
	582	651

There were no bad debt allowances as at March 31, 2018 nor as at December 31, 2017.

8. Property, Plant and Equipment

During the three-month period ended March 31, 2018, the Company acquired a total of $0.1 million in property, plant and equipment. During the year ended December 31, 2017, the Company acquired $1.2 million in equipment and tools, marketing demonstration equipment, medical devices in the Company's laboratories in Canada and in the United States, computer equipment and leasehold improvements; and also capitalized $0.3 million for STERIZONE® VP4 Sterilizers used internally and externally.

Notes to the Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

9. Intangible Assets

During the three-months period ended March 31, 2018, the Company acquired $0.04 million of new patents and software. During the year ended December 31, 2017, the Company acquired $0.2 million in patents and software.

10. Deferred Revenues

On November 25, 2015, the Company and Getinge entered into an exclusive distribution agreement (the Getinge Agreement) to distribute the STERIZONE® VP4 Sterilizer worldwide. Included in this agreement was an upfront license fee payment of $7.5 million from Getinge to the Company. The Getinge Agreement includes performance requirements for five years as well as a formula for minimum unit shipments.

Sales under the Getinge Agreement are made in US dollars to Getinge.

Current deferred revenues also include the unamortized portion of prepaid service contracts covering a part of the installed base of STERIZONE® Sterilizers in Canada.

11. Share Capital

Authorized:

The authorized capital of the Company consists of an unlimited number of common shares and an unlimited number of preferred shares.

The common shares are voting, participating and without par value.

The preferred shares are non-voting and without par value. They have priority over the common shares for dividends and a distribution of their capital upon liquidation of the Company, and are issuable in series, each series bearing the number of shares, designation, rights, privileges, restrictions and conditions determined by the Board of Directors upon their issue.

Issued:

	March 31, 2018		December 31, 2017	
Issued and Paid	**Number of Common Shares**	**$**	Number of Common Shares	$
Balance at Beginning	**92,854,304**	**111,215**	91,977,214	110,406
Options Exercised	**37,000**	**39**	877,090	809
Balance at the End	**92,891,304**	**111,254**	92,854,304	111,215

During the first quarter ended March 31, 2018, pursuant to the Company's Stock Option Plan, 37,000 stock options were exercised for an aggregate cash consideration of $0.04 million. During the year ended December 31, 2017, 877,090 options were exercised for an aggregate cash consideration of $0.5 million.

Employee Stock Purchase Plan

On May 2, 2007, the Company set up an employee stock purchase plan for employees and executives. Eligible participants may contribute, in the form of payroll deductions, up to 5% of their base salary. The Company contributes an amount equal to 50% of the participant's total monthly contribution. Each month, the participants' and Company's contributions are transferred to an investment dealer who purchases, on the open market and promptly upon reception of the contributions, shares for a total purchase price equal to the amount of such contributions.

Notes to the Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

11. Share Capital (cont'd)

Deferred Share Unit Plan

DSUs are awarded in connection with the 2016 Stock Incentive Compensation Plan. Under this plan, each eligible person receives a portion of his or her compensation in the form of DSUs. DSUs awarded pursuant to the Company's plan generally vest 50% at award date and the other 50% vest over a period of one year. DSUs are payable on the termination of service of the participant. The value of a DSU is determined based on the closing price of the Common Shares of the Company for the last trading day. The DSUs are settled in cash or in common share at the discretion of the Company when a person ceases to be eligible under the plan. For the purpose of repurchasing DSUs, the value of a DSU is determined based on the closing price of the Common Shares of TSO_3 for the last trading day prior to the repurchase of the DSUs.

As at March 31, 2018, no new DSUs were awarded (0.1 million as at March 31, 2017). During the three-month period ended March 31, 2018, TSO_3 recorded a compensation expense of $0.02 million ($0.01 million as at March 31, 2017) for its deferred share unit plan.

12. Reserve – Share-Based Compensation

The Company's Board of Directors adopted the 2016 Stock Incentive Compensation Plan which includes the award of stock options. The plan was approved by the shareholders. The total number of common shares that can be issued under this plan for all forms of award from the Company's share capital was 9.3 million as at March 31, 2018, (9.3 million as at December 31, 2017). The options awarded pursuant to this plan generally vest over a three-year period and may be exercised within a maximum of 10 years from the date of award.

During the three-month period ended March 31, 2018, the Company awarded 0.4 million stock options, (0.4 million for the same period in 2017) at a weighted average exercise price of $0.94 or CAD$1.21 ($2.31 or CAD$3.08 for the same period in 2017). The weighted average fair value of these stock options was $0.56 or CAD$0.73 for the three-month period of 2018 ($1.44 or CAD$1.92 for the same period in 2017).

The share-based compensation expense pertaining to the award of options is amortized using the graded vesting method and represents a share-based compensation expense of $0.4 million for the three-month period ended March 31, 2018 ($0.6 million for the same period in 2017) presented in the Interim Condensed Consolidated Statements of Loss and Comprehensive Loss in the functions based on the option holders.

The fair value of the stock options awarded is estimated using the Black-Scholes option pricing model under the following weighted average assumptions:

US$	**March 31, 2018 $**	December 31, 2017 $
Weighted Average Share Price	**$0.94**	$2.20
Exercise Price	**$0.94**	$2.20
Risk Free Interest Rate	**2.79%**	1.76%
Estimated Share Price Volatility	**60%**	61%
Expected Life	**7 years**	8 years
Expected Dividend Yield	**0%**	0%

Notes to the Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

12. Reserve – Share-Based Compensation (cont'd)

The share-based compensation expenses take into account an estimate of the number of options and DSUs that will actually vest and be exercised. In addition, option pricing models such as the Black-Scholes model require highly subjective assumptions, including the assumed stock price volatility of the underlying shares. Option's volatility was estimated for the 2018 and 2017 awards on the basis of the historical volatility of the Company's share price prior to the date of award. Any change in the assumptions can materially affect the fair value estimates.

	March 31, 2018		December 31, 2017	
US$	**Number**	**Weighted Average Exercise Price $**	Number	Weighted Average Exercise Price $
Outstanding at beginning	**7,909,953**	**1.71**	7,024,231	1.39
Granted	**425,000**	**0.94**	2,977,080	2.13
Exercised	**(37,000)**	**0.63**	(877,090)	0.65
Expired	**(14,000)**	**1.85**	(19,600)	2.03
Forfeited	**(542,337)**	**2.24**	(1,194,668)	2.19
Outstanding at end	**7,741,616**	**1.60**	7,909,953	1.71
Exercisable at end	**3,435,896**	**1.26**	3,177,566	1.33

The following table summarizes certain information regarding the stock options of the Company as at March 31, 2018:

	Outstanding Options		**Exercisable Options**	
Exercise Price in US$	**Number**	**Average Remaining Contractual Life (year)**	**Number**	**Average Remaining Contractual Life (year)**
$0.00 (DSU's)	**138,134**	**Undetermined**	**102,802**	**Undetermined**
$0.01 to $0.80	**848,667**	**2.45**	**848,667**	**0.42**
$0.81 to $1.69	**3,139,400**	**6.77**	**1,905,892**	**1.39**
$1.70 to $2.89	**3,615,415**	**9.28**	**578,535**	**2.27**
	7,741,616	**8.65**	**3,435,896**	**1.26**

The following table summarizes certain information regarding the stock options of the Company as at December 31, 2017:

	Outstanding Options		**Exercisable Options**	
Exercise Price in US$	**Number**	**Average Remaining Contractual Life (year)**	**Number**	**Average Remaining Contractual Life (year)**
$0.00 (DSU's)	138,134	Undetermined	102,802	Undetermined
$0.01 to $0.80	875,667	2.76	875,667	2.76
$0.81 to $1.69	2,574,233	6.45	1,537,894	5.39
$1.70 to $2.89	4,321,919	9.38	661,203	8.45
	7,909,953	8.81	3,177,566	7.40

Notes to the Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

13. Additional Information Relating to Cash Flows

	First Quarter	
	2018	2017
	$	$
Changes in Non-Cash Operating Working Capital Items		
Decrease (Increase) in Assets		
Accounts Receivable	**69**	(1,811)
Inventories	**(416)**	(372)
Prepaid Expenses	**(111)**	(88)
Increase (Decrease) in Liabilities		
Accounts Payable and Accrued Liabilities	**(405)**	476
Warranty Provision	**(81)**	153
Current Deferred Revenues	**(4)**	79
Non-current Deferred revenues	**-**	(294)
	(948)	(1,765)

14. Segmented Information

The Company is structured as a single operating segment.

Revenues	First Quarter	
	2018	2017
	$	$
Canada and Worldwide	**50**	110
United States	**205**	4,101
	255	4,211

	March 31, 2018			December 31, 2017		
	Inventories	**Property, Plant and Equipment**	**Intangible Assets**	Inventories	Property, Plant and Equipment	Intangible Assets
Canada and Worldwide	**1,967**	**1,246**	**1,865**	1,616	1,306	1,870
United States	**489**	**1,738**	**14**	424	1,878	16
	2,456	**2,984**	**1,879**	2,040	3,184	1,886

For the first quarter of 2018, revenue from Getinge represented 93% of the Company's total revenues in conjunction with Getinge and TSO_3's exclusive distribution agreement (99% for the same period in 2017).

Notes to the Consolidated Financial Statements

Periods ended March 31, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

15. Loss per Share

The following table reconciles the basic and diluted loss per share for the periods ended March 31:

In thousands of us $, except per share amounts	First Quarter 2018 $	2017 $
Net loss		
Basic and Diluted	**(4,512)**	(1,980)
Number of Shares		
Weighted Average Number of Outstanding Shares	**92,877**	91,995
Number of Shares		
Weighted Average Number of Outstanding Shares Diluted[(1)]	**92,877**	91,995
Loss per Share		
Basic and Diluted	**(0.05)**	(0.02)
Comprehensive loss per Share Basic and Diluted	**(0.05)**	(0.02)

1) If the Company had a profit, the weighted average number of outstanding shares diluted would have been increased by 2.1 million as at March 31, 2018 (6.4 million as of March 31, 2017) for the calculation of the diluted net loss per share.

16. Contractual Commitments

On January 25, 2018, the Company entered into the Co-commercialization Agreement with Getinge in a joint effort to increase sales to end users and optimize the customer experience. The Co-commercialization Agreement allows the Company to sell its STERIZONE® VP4 Sterilizers and associated products and services directly into the United States and Canada. The Company shall repurchase not less than 100 STERIZONE® VP4 Sterilizers for $3.3 million.

The parties are in negotiations on additional modifications to the distribution relationship, either through a new agreement or a modification of the Getinge Agreement, with the objective of further increasing the speed, flexibility and effectiveness of the relationship. The Co-commercialization Agreement and the Getinge Agreement will terminate on August 1, 2018 unless extended by mutual agreement. If agreement between the parties is not reached, TSO_3 has agreed, by July 1, 2019, to repurchase Getinge's remaining STERIZONE® VP4 Sterilizers at the same unit price in the Co-commercialization Agreement. In the event the Getinge Agreement terminates, Getinge would lose licensing and other rights made available by the agreement, and the Company's only other recourse against Getinge would be to retain in full the $7.5 million license fee payment made by Getinge when the Getinge Agreement was entered into and require Getinge to accept delivery and pay for units under any then outstanding purchase orders (see Note 2).

17. Approval of Financial Statements

The interim condensed consolidated financial statements were approved by the Board of Directors on May 8, 2018.