2018 Quarterly Report

July, August, September

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Message from the President and Chief Executive Officer

Dear Shareholders,

Today in North America we have 59 sterilizers installed with an additional nine units already shipped to customers and scheduled for installation. In addition, we currently have a backlog of 22 sterilizers meaning that we have received purchase orders (P.O.s) or commitment letters with scheduled delivery dates in the future. TSO_3 currently has 90 units which are installed or planned to be installed.

In the third quarter, TSO_3 received purchase orders for sterilizers from US and Canadian customers. Subsequent to the end of the quarter, additional business has been awarded. Some of this business relates to two tenders from provinces in Canada, the first new growth in our Canadian business in two years. Additionally, TSO_3 has received commitment for another seven units in the US as a result of our independent sales efforts subsequent to the close of the third quarter. We continue to drive actions that we believe will assist in aggressively placing new sterilizers in key accounts across North America.

In the third quarter, as previously disclosed, TSO_3 assumed opportunities representing over 200 units from its former distributor. These included potential customers that have a defined need and a purchase timeline that ranges from 90 days to 12 months. As is the case with such opportunities, some are more likely to produce results than others. Each however have now been transitioned to TSO_3's sales representatives and are being requoted consistent with their expected time to close and are tracked in TSO_3's pipeline.

TSO_3 started the year with five sales representatives calling on over approximately 500 accounts that had not been previously prioritized or targeted by our former distributor. Presently, TSO_3 has eight sales representatives trained and, in the field, and expected to have a total of 11 in the US and Canada by the end of 2018. In addition to our own dedicated sales team, the Company also has agreements with multiple independent sales and service organizations to facilitate opportunity identification and acquisition and increase our service footprint. This team is targeting more than 5,000 accounts in the US and Canada.

The Company has established an aggressive goal to gain commitment for all 200+ units in our inventory by year-end 2019. To achieve this goal the Company is employing strategies intended to accelerate sterilizer placement in high use, high visibility hospitals. TSO_3 has recently initiated a series of programs that are designed to gain market share and take advantage of the value proposition inherent in its product offering. These new approaches have, in the past weeks, been introduced to our customers through our sales team. These include pay-per-cycle and guaranteed savings proposals. Some of the early success in the fourth quarter has been a result of strategies like these. During the quarter, the Company also implemented a limited trial program in which a sterilizer is placed within a facility to demonstrate real world benefits to the health systems contemplating a purchase. One health system that is participating in the trial program is contemplating the acquisition of multiple sterilizers. The Company believes that trials may be another opportunity to offer direct comparisons between the benefits of the sterilizer and that of our competition and expects to see increased use of trials as the sales teams settle into their territories.

The Company is also investing in its service capabilities. It currently has seven service technicians on staff, both factory and field based. In addition, it has supplemented this team with seven independent service organizations that can collectively provide established accounts with field service that includes 4-hour telephone support and 24-hour on-site response.

With its additional investments in sales, marketing and technical service, the Company is taking action to control its other expenditures. This shift will enable the Company to focus on sale of the inventory it has in stock, while shifting resources from other areas, such as product development and assembly operations. At the end of the third quarter of 2018, the Company had $16.1 million in cash, cash equivalents and short-term investments.

The Company has a value proposition that is compelling to hospital systems, namely the Company offers the ability to sterilize the same volume of instruments using fewer sterilization cycles, and fewer sterilizers, all of which contribute to lower cost. The Company continues to advocate for improved healthcare practices through its presence on committees to support enhancements in processing. Recent Association for the Advancement of Medical Instrumentation (AAMI) working group meetings suggest that sterilization of complex devices such as duodenoscopes may become the norm and not the exception. TSO_3 is the first in the industry to have FDA cleared claims for terminal sterilization of endoscopes that include duodenoscopes, and is poised to facilitate the adoption of this new healthcare practice.

With direct control over our business and the communications which outline our progress, the Company recognizes that more frequent information is being requested by which to measure this progress. As we move forward, the Company will increase its effort to use its website to highlight customer experiences and sales progress. In addition, the Company will increase the frequency by which it will communicate with investors to aid in information flow.

In summary, in the past 90 days, the Company has assumed full control of its commercial operations, including the installed customer base. It has hired key resources required to support the targeted objective of aggressively accelerating the sale of its sterilizers to healthcare facilities and created a series of programs to incentivize customers to purchase our technology. The Company has set aggressive sales targets and is working multiple channels to meet its goals while we move resources towards the support of a sales-focused organization and simultaneously gauging the re-initiation of production of its sterilizer as our business grows.

R.M. (Ric) Rumble

Overview

General Description

TSO_3 Inc. ("TSO_3" or the "Company") was founded in June 1998 in Québec City, Canada and employs 64 people as at September 30, 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. All initial STERIZONE® 125L+ Sterilizers have been upgraded to the improved 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 extend its claims in that country. The new claims included the ability to terminally sterilize 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 (IFUs) of its STERIZONE® VP4 Sterilizer to include multi-channel flexible endoscopes of up to 3.5 meters in length and four or fewer 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.

TSO_3 established laboratory data validating that 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. On May 9, 2018, the Company announced that it received expanded clearance from US regulators for its most recent 510(k) submission. The new clearances allow a hospital to terminally sterilize gastrointestinal endoscopes that have dimensions within the cleared intended use, such as certain colonoscopes, duodenoscopes and gastroscopes.

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, duodenoscopes and gastroscopes;
- 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, duodenoscopes, gastroscopes and other multi-channel flexible scopes, consistent with the cleared claims of the sterilizer, which previously required treatment 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 thoroughly destroys all types of microbiological organisms with a sterility assurance level of 10^{-6} (SAL^{-6}), including bacterial spores.

The Company's extended claims further expand its technology leadership – offering enhanced patient protection in applications where terminal sterilization was not previously possible – and correspond to increasing scrutiny by regulatory authorities over medical device reprocessing, particularly for colonoscopes, duodenoscopes 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 even after cleaning and processing by high-level disinfection. Published reports confirm the significant health risk of device-related transfer of antibiotic resistant microbes, including patient injury or death.

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 increasing 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.

Recently, a legacy technology, ethylene oxide (ETO), has seen some renewed interest based on its claim (albeit limited) to sterilize complex, multi-channeled flexible endoscopes. This renewed interest was created when US regulators suggested, in a document circulated in 2015, that ETO may be used as a supplemental method when reprocessing duodenoscopes as a means to render the devices more safe for next patient use. ETO is a flammable, toxic, carcinogenic chemistry which is registered as an environmental pollutant. Due to the properties of the chemistry, the sterilization cycle is elongated in an attempt to remove the carcinogenic residuals from the instrument being sterilized. This adds significant time and cost to the reprocessing of instruments. Lastly, ETO inflicts increased damage on delicate flexible instruments, further increasing the cost associated with its use.

Other methods that play a role in a sub-segment of low temperature reprocessing include liquid high-level disinfection and liquid chemical sterilization. These are just-in-time methods of reprocessing and are not considered terminal sterilization. They are used 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 cost-effective and high throughput reprocessing 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's 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.

Regulatory Status

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 extend its claims in that country.

On July 4, 2016, TSO_3 announced that the FDA had cleared TSO_3's expanded IFUs 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. 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.

Additionally, on May 9, 2018, the Company announced that it had received expanded clearance from US regulators for its most recent 510(k) submission for the terminal sterilization of multi-channeled flexible endoscopes using its STERIZONE® VP4 Sterilizer. The new clearance allows a hospital to

terminally sterilize gastrointestinal endoscopes that have dimensions within the cleared intended use, such as certain colonoscopes, duodenoscopes and gastroscopes.

TSO_3 is actively engaged in the future of healthcare delivery as part of the AAMI, which is the primary source of national and international consensus standards for the medical device industry. With participation on thirteen committees, TSO_3 is influencing all aspects of medical device sterilization to ensure our dual sterilant technology is represented in relevant standards, including those for biological and chemical indicators, sterilization containers and packaging, sterility assurance, and reusable device reprocessing. In addition, the STERIZONE® VP4 Sterilizer's clearances for sterilization of multi-channel flexible endoscopes are shaping the current standard for flexible endoscope processing by providing a solution to an unmet need in endoscopy, which is the safe and effective sterilization of these complex devices that have been repeatedly linked to patient outbreaks and deaths.

Third Quarter 2018 and Recent Activities

Financing

On August 1, 2018, the Company announced that it and a fund, of which Courage Capital Management LLC ("Courage") is the investment advisor, had entered into a binding $20 million debt financing to fund commercialization initiatives for its STERIZONE® VP4 Sterilizer. Courage is a Nashville, TN headquartered alternative asset management firm with a 20-year track record of investments in health care services, medical devices, and pharmaceuticals.

The $20 million financing is provided in two separate but concurrent transactions in the form of a $15 million first lien convertible note (the "Convertible Note") and a $5 million first lien term loan (the "Term Loan").

The $15 million Convertible Note is a five-year term non-callable note convertible into common shares of the Company at a price of US$0.82 per common share and bears interest at a rate of 10% per annum, accruing as of the closing date until full repayment, compounded quarterly and payable in cash, at or prior to the maturity date of the Convertible Note at the option of the Company.

The $5 million term loan is a 5-year loan callable after two years that bears interest at a maximum rate of 12% per annum, which begins accruing immediately, compounds quarterly and is payable in cash, at or prior to the maturity date of the Term Loan. The Company may at its entire discretion decide to reduce the rate of interest payable under the Term Loan provided it decides, on a quarterly basis, to pay a portion or the entirety of a quarterly payment of interest in cash or in common shares of the Company.

Board of Directors

On August 29, 2018 Mr. Martin J. Madden joined the Company's board of directors. Mr. Madden has a broad background in medical device innovation and new product development. Mr. Madden spent thirty years with Johnson & Johnson's Medical Device organization, and, as an executive and a vice-president of Johnson & Johnson, Mr. Madden served on the management boards of Johnson & Johnson's Global Surgery Group, Ethicon, Ethicon Endo-Surgery, DePuy-Synthes, and Cordis, and was also Chairman of Johnson & Johnson's Medical Device Research Council, with responsibility for talent strategy and technology acceleration. Mr. Madden's leadership experiences spanned internal start-ups, executing turn-arounds, and leading large portfolio and technology intensive research organizations.

Commercial Activities

On November 25, 2015, TSO_3 and Getinge Infection Control AB ("Getinge") (together, "the Parties") entered into an agreement (the "Getinge Agreement") which granted Getinge exclusive worldwide global distributor rights to TSO_3's STERIZONE® VP4 Sterilizer. In association with the Getinge

Agreement, TSO_3 shipped a total of 280 STERIZONE® VP4 Sterilizers to Getinge in 2016 and 2017, and none in 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 allowed the Company to sell its STERIZONE® VP4 Sterilizers and associated products and services directly into the United States within accounts not previously targeted by Getinge and repurchase not less than 100 STERIZONE® VP4 Sterilizers for $33,000 per sterilizer.

At that time, the Company began independent commercialization activities, including direct sales, marketing and product support, while the Parties entered negotiations regarding modifications to their distribution relationship, either through a new agreement or a modification of the Getinge Agreement. Both agreements between the Parties were set to terminate on August 1, 2018. In the event agreement was not reached, TSO_3 agreed, by July 1, 2019, to repurchase Getinge's remaining STERIZONE® VP4 Sterilizers at $33,000 per sterilizer, and Getinge's licensing and other rights made available by the agreement would cease.

On August 1, 2018, the Parties announced that they mutually decided not to renew the distribution agreements between them, and agreed: 1) to provide TSO_3 unrestricted independent commercialization of its STERIZONE® VP4 sterilizers; 2) that the Company would purchase approximately 230 STERIZONE® VP4 Sterilizers for $33,000 per sterilizer; 3) to transfer Getinge's existing sales pipeline to TSO_3 in exchange for shared economics at the completion of sale; and 4) to transition to TSO_3 the service, maintenance and consumables sales of all existing STERIZONE® VP4 sterilizer customers in the United States and Canada. The Company has substantially completed the transition on the STERIZONE® VP4 Sterilizer business from Getinge, and is actively and independently focused on selling the 237 STERIZONE® VP4 Sterilizers in its inventory to leading healthcare facilities in Canada and the United States.

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 September 30, 2018, TSO_3 had 187 patents or patent applications pending, with 92 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.

In 2010 and subsequently, TSO_3 filed initial patent applications and then several divisional patent applications in various countries, seeking patent protection for its various innovations related to hydrogen peroxide alone and hydrogen peroxide and ozone sterilization systems and methods.

The majority of patents, most of which cover fundamental aspects of TSO_3's STERIZONE® sterilization system technology, have now been issued, while the remaining applications are still pending.

In 2014 and subsequently, TSO_3 filed new distinct patent applications in various countries on its innovative methods to further improve compatibility under differing load conditions for surgical instruments and accessories. Patents have already been issued in some countries, while others are still pending in the United States, Europe, Canada, Japan and other countries.

In 2015 and subsequently, TSO_3 also filed new patent applications in the United States and other countries related to biological indicators (BI) used to monitor effectiveness of a sterilization process.

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

During the second quarter of 2018, the US Patent Office informed the Company of its intent to grant a new patent on the Company's recent innovative methods to further improve compatibility under different load conditions.

The European Patent Office also delivered to the Company a notice of acceptation for an additional patent covering a core aspect of TSO_3's technology embedded in the STERIZONE® Sterilization System.

The Canadian Patent Office and the Patent Office of South Korea each allowed to the Company an additional patent covering the STERIZONE® Sterilization System.

The Patent Office of Brazil also informed the Company of its intent to grant 7 patents, most of them covering aspects of TSO_3's technology embedded in the STERIZONE® Sterilization System.

During the third quarter of 2018, TSO_3 filed a new divisional patent application in Europe for another aspect of TSO_3's STERIZONE® sterilization system technology.

TSO_3 also filed a new divisional patent application in the United States on its methods to further improve compatibility under differing load conditions.

TSO_3's patented 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 and 2019 Focus

TSO_3 has substantially completed the transition of the STERIZONE® business from its former distributor, has regained sole ownership and control of all its commercial and service activities for all customers, and has repurchased and paid for 230 STERIZONE® VP4 Sterilizers at favourable pricing. Approximately 98% of the North American units that were transitioned from the former distributor remain in service. The Company is now focused on selling and installing its STERIZONE® VP4 Sterilizer inventory and providing existing and future customers with industry leading service and support.

The Company is targeting leading medical facilities in the United States and Canada to add to its current base of 59 installed units. In addition, an additional nine units have been shipped to customers and are waiting for installation, and the Company has a further backlog of 22 sterilizers for which we have received purchase orders or other written commitments and which are scheduled for future delivery and installation. Ten units of this backlog came subsequent to the third quarter of 2018 as a result of TSO_3's independent direct sales efforts. Thus, the sum of the Company's total installed units, units shipped but not yet installed, and sterilizer unit backlog equals 90 units.

The Company's sales and marketing team is focused on selling and providing support to end users in the central sterilization department ("CSSD") of acute care hospitals and hospital systems, establishing and supporting new industry partnerships, as well as developing additional opportunities in the gastrointestinal reprocessing market segment.

The Company's initial focus has been to directly support North American customers and launch a limited but targeted campaign which focused on a STERIZONE® core value: to significantly lower healthcare reprocessing operating costs. Additionally, in the past several months the Company lead the response to government tenders in the Provinces of Quebec and British Columbia, has initiated promotions and been a sponsored speaker at key industry trade events.

TSO_3 assumed opportunities representing over 200 sterilizers from its former distributor. These include potential customers that have a defined need and could lead to a low temperature sterilizer purchase in the near term. These quotes have been transitioned to TSO_3 sales representatives, requoted by TSO_3, and now are included in our pipeline.

TSO_3 began the year with five sales representatives calling on over approximately 500 accounts not previously prioritized or targeted by our former distributor. Presently, TSO_3 has eight sales representatives trained and, in the field, and expects to have a total of 11 in the US and Canada by the end of 2018. In addition to our own dedicated sales team, the Company also has agreements with multiple independent sales organizations to facilitate opportunity identification and acquisition. This team is targeting more than 5,000 accounts in the US and Canada.

The Company is employing strategies intended to accelerate sterilizer placement in high use, high visibility hospitals, and has recently initiated a series of programs that are designed to gain market share and take advantage of the value proposition inherent in its product offering. In addition, new approaches have been created and have, in the past weeks, been introduced to our customers through our sales team. These include pay-per-cycle and guaranteed savings proposals. During the quarter, the Company also implemented a limited trial program in which a sterilizer is placed within a facility to demonstrate real world benefits to health systems contemplating a purchase. One health system that is participating in the trial program is contemplating the acquisition of multiple sterilizers. The Company believes that trials may be another opportunity to offer direct comparisons between the benefits of the sterilizer and that of our competition and expects to see increased use of trials as the sales teams settle into their territories.

The Company is also investing in its service capabilities. It currently has seven service technicians on staff and has supplemented this team with seven independent service organizations that can collectively provide established accounts with field service that includes 4-hour telephone support and 24-hour on-site response.

With its additional investments in sales, marketing and technical service, the Company is taking action to reduce other expenditures to control its expenses. This shift will enable the Company to focus on sales, and while shifting resources from other areas, such as product development and assembly operations.

At the end of the third quarter of 2018, the Company had $16.1 million in cash, cash equivalents and short-term investments. Under the terms of the Courage financing, the Company is not required to pay interest immediately, but may elect to accrue the interest for up to the life of the underlying financing instruments. The Company currently plans to elect to defer payment of all interest relating to all debt throughout the end of 2019.

The Company's goal is to gain commitment, in the form of purchase orders or contracts, for 200+ sterilizers by year-end 2019. The Company's financial models assume that a sterilizer, once installed and running with a US customer, if used three or more cycles per working day, could generate an average of between $20,000-$30,000 in annual consumables revenue at a relatively high contribution margin. Such revenues would for shipments made directly to hospitals, and therefore would be at higher average selling prices and contribution margins than the Company has recorded when shipping to its distributor in prior periods. The Company recorded $0.2 million of consumables revenue in the third quarter of 2018 as it transitioned from its formed distributor and recorded in excess of approximately $0.1 million in consumables revenue in October 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 and nine-month periods ended September 30, 2018, and to compare them with the three-month and nine-month periods ended September 30, 2017. This information is dated November 6, 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 ability for the Company to market and sell its products;
- The success of sales and marketing partners and suppliers;
- The ability for the Company to deploy TSO_3's products to end customers;
- Business and economic conditions;
- The ability to obtain regulatory authorizations that are required to market its product;
- The ability to attract and retain skilled staff;
- The ability for the Company to attract capital and other financial risks;
- Regulatory Approvals;
- Competition;
- Tax benefits and tax rates;

- Foreign currency exchange rates;
- The compatibility of medical instruments with the Company's technology.
- The ability to obtain sufficient quantities of supplies and materials when needed;
- The ability to complete research and development work.

These forward-looking statements involve risks and uncertainties relating to, among other things, limited history of commercialization, commercial operations, compatibility, biocompatibility, research and development projects, dependency on key personnel, 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 November 6, 2018, the date of filing for the third 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 September 30, 2018 and 2017 (Unaudited, IFRS Basis, in thousands of US dollars, except per share amounts)

	Third Quarter		Nine months	
	2018	2017	**2018**	2017
	$	$	**$**	$
Revenues	**782**	5,105	**1,410**	13,946
Cost of sales	**(394)**	3,102	**451**	8,613
	1,176	2,003	**959**	5,333
Expenses				
Research and development	**1,260**	1,562	**4,452**	4,456
Selling, general and administrative	**2,608**	2,131	**7,681**	6,735
Financial (income) expenses	**(599)**	48	**(624)**	58
Total Expenses	**3,269**	3,741	**11,509**	11,249
Net loss before income taxes	**(2,093)**	(1,738)	**(10,550)**	(5,916)
Income taxes	**11**	33	**18**	89
Net loss and comprehensive loss	**(2,104)**	(1,771)	**(10,568)**	(6,005)
Weighted average number of outstanding shares (in thousands)	**93,208**	92,842	**93,009**	92,258
Basic and diluted net loss per share	**(0.02)**	(0.02)	**(0.11)**	(0.07)
Basic and diluted net comprehensive loss per share	**(0.02)**	(0.02)	**(0.11)**	(0.07)

Results Analysis

Below, the Company discusses the variations of certain accounts for the third quarters of 2018 and 2017 and within the nine-month periods ending September 30, 2018 and 2017.

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

REVENUES

For the third quarter of 2018, revenues equalled $0.8 million, as compared to $5.1 million in the third quarter of 2017. TSO_3 revenues in the third quarter of 2018 reflect sales of sterilizers, consumables, accessories and service parts. The Company shipped four sterilizers to hospitals in the third quarter of 2018 as opposed to 44 sterilizers to Getinge in the same period last year. For the nine-month period ended September 30, 2018, revenues equalled $1.4 million, as compared to $13.9 million for the same period in 2017. The Company shipped four sterilizers to hospitals in the first nine-months of 2018 as compared to 120 units shipped to Getinge in 2017.

Sales of the Company's proprietary consumables, accessories and service parts in the third quarter and nine-month period of 2018 were higher compared to the same period in 2017, reflecting increased installations of its STERIZONE® VP4 Sterilizers in medical facilities. The Company recorded $0.2 million in consumables revenue in the third quarter of 2018, which reflects a period of transition from distribution to a direct sales model, along with inventory adjustments. The Company expects consumables consumption and revenue run rates to normalize in future periods at direct-to-customer average selling prices which are higher than under the distributor model.

The Company did not record license fee revenue in the third quarter and first nine-months of 2018, as compared to $0.2 million recorded in the third quarter of 2017 and $0.6 million recorded in the first nine-months of 2017. In the third quarter of 2018, the Company allocated the $6.0 million balance in deferred license fee associated with the Getinge Agreement against inventories and will amortize it against cost of sales over the 230 units bought from Getinge as TSO_3 ships these units.

Prior to the termination of the Getinge agreement on August 1, 2018, Getinge represented substantially all of the Company's source of revenue. As a result of the transition of the STERIZONE® VP4 Sterilizer business from Getinge to TSO_3, the Company is now recording revenue to sales of products and services to end users and does not expect to record significant revenue from sales to Getinge.

NET LOSS

In the third quarter of 2018, net loss and comprehensive loss totaled $2.1 million or ($0.02) per share, as compared to $1.8 million or ($0.02) per share of net loss and comprehensive loss in the third quarter of 2017. For the nine-month period ended September 30, 2017, net loss and comprehensive loss totaled $10.6 million or ($0.11) per share, as compared to $6.0 million or ($0.07) per share during the same period in 2017.

In the third quarter of 2018, gross profit decreased by $0.8 million, as compared to the same period last year and by $4.4 million for the nine-month period, mainly related to the decrease of sterilizer sales to Getinge and the lack of deferred license fee revenue recognition. The investments made in research and development activities were lower by $0.4 million for the third quarter of 2018 as compared to the same period last year and by $0.1 million for the nine-month period and higher by $0.5 million in sales, general and administrative activities to support the business for the third quarter of 2018 and $0.9 million for the nine-month period.

In addition, during the third quarter of 2018, the Company closed a $15 million Convertible Note financing as part of a $20 million financing package. The Convertible Note contains two components: debt and embedded derivative, the latter of which is the right to convert the Convertible Note into common shares of the Company at US$0.82 per share. In accordance with IFRS 9, the Company shall revalue the embedded derivative on a quarterly basis and record the difference in liabilities and in financial income or loss. The value of the underlying derivative, and subsequent revaluations, has no cash impact on the Company. As a result of the revaluation of the derivative in association with the Convertible Note, the Company recorded a non-cash financial gain of $1.1 million in the third quarter and nine-month periods of 2018, respectively.

For the third quarter of 2018, the Company incurred no material events which would have impacted it's 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

			2018				2017
$000's	**Q3**	Q2	Q1	Q4	Q3	Q2	Q1
Net loss	**(2,104)**	(3,952)	(4,512)	(1,449)	(1,771)	(2,254)	(1,980)
Financial (income) expenses	**(599)**	(12)	(14)	74	48	49	(39)
Amortization and depreciation	**270**	292	315	246	331	221	168
Share-based compensation expense	**688**	627	371	301	632	592	609
Income taxes	**11**	7	-	(59)	33	29	27
Adjusted Ebitda	**(1,734)**	(3,038)	(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 third quarter of 2018, total expenses denominated in Canadian dollars were CAD$1.5 million, as compared to CAD$4.0 million in the third quarter of 2017. The average USD/CAD foreign exchange rate in the third quarter of 2018 was 0.7652 as compared to 0.7983 in 2017, which is reflected in a decrease in CAD denominated expenses of 4% year over year upon conversion to USD.

From a quarterly sequential perspective, the USD/CAD foreign exchange rate in the third quarter of 2018 was 0.7652 as compared to 0.7747 in the second quarter of 2018, which is reflected in a decrease in CAD denominated expenses of 1% quarter over quarter upon conversion to USD.

In the third quarter of 2018, total cost of sales related expenses denominated in Canadian dollars were CAD$0.2 million, as compared to CAD$3.1 million in the third quarter of 2017. Total research and development expenses denominated in Canadian dollars were CAD$0.5 million in the third quarter of 2018, as compared to CAD$0.6 million in the third quarter of 2017. In the third quarter of 2018, total SG&A expenses denominated in Canadian dollars were CAD$0.8 million, representing the same amount in the third quarter of 2017.

Cost of sales

Cost of sales includes inventory costs and 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 September 30, 2018, cost of sales amounted to ($0.4) million, as compared to $3.1 million for the same period in 2017. For the nine-month period ended September 30, 2018, cost of sales equaled $0.5 million, as compared to $8.6 million in the same period in 2017. In the third quarter of 2018 and for the nine-month period of 2018, TSO_3 shipped four STERIZONE® VP4 Sterilizers to hospitals as opposed to 44 sterilizers to Getinge in the third quarter of last year and 120 sterilizers to Getinge in the nine-month period of last year. Cost of sales in the third quarter and in the nine months period of 2018 included a $0.8 million reversal of the warranty provision accrual following the termination of the agreement with Getinge in August 2018 and the repurchase of the STERIZONE® VP4 Sterilizers for which the warranty accrual was recorded in prior periods.

Gross profit was $1.2 million in the third quarter of 2018, as compared to $2.0 million in the third quarter of 2017. For the nine-month period ended September 30, 2018, gross profit was $1.0 million, as compared to $5.3 million for the same period in 2017. Gross profit in the third quarter and nine-month period of 2018 declined despite a $0.8 million reversal of warranty provision associated with inventory purchased from Getinge, as the Company shipped four STERIZONE® VP4 Sterilizers in the periods and did not recognize licencing fee revenue.

Research and development

For the quarter ended September 30, 2018, research and development expenses were $1.3 million as compared to $1.6 million in 2017 and for the nine-month period ended September 30, 2018, these expenses were $4.5 million (same amount in the same period in 2017). For the three-month period ended September 30, 2018, the Company reduced by $0.2 million expenses related to material purchases, equipment maintenance, depreciation and building expenses to run the laboratories. The Company also reduced salary, share-based compensation, travelling expenses and professional fees by $0.2 million in the third quarter of 2018 as compared to the same period last year.

The Company reduced its research and development expenditures as it focused more of its investments on selling and marketing activities.

Selling, General and Administrative (SG&A)

Selling, general and administrative (SG&A) include marketing, sales, service and administrative expenses. SG&A expenses were $2.6 million for the quarter ended September 30, 2018, as compared to $2.1 million for the same period in 2017. For the nine-month period ended September 30, 2018, these expenses were $7.7 million, as compared to $6.7 million in 2017.

During the third quarter and first nine-month of 2018, as compared to the same periods in 2017, the Company incurred an additional $0.4 million and $1.7 million, respectively, in salary, share-based compensation, travelling, recruiting fees and professional fees relating to in marketing, sales and service. The Company also accrued $0.1 million of commissions payable. This increase is offset by a decrease in general and administration expenditures during the third quarter and first nine-months of 2018, as compared to the same periods in 2017, of $0.1 million and $1.0 million in salary, share-based compensation, travelling and recruiting fees.

Share-based compensation expense

For the quarter ended September 30, 2018, non-cash share-based compensation amortization amounted to $0.7 million, as compared to $0.6 million for the same period in 2017. For the nine-month period ended September 30, 2018, these expenses amounted to $1.7 million, as compared to $1.8 million for the same period in 2017.

As at September 30, 2018, the Company had 7.3 million stock options and other equity-based compensation instruments oustanding, as compared to 6.2 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) expenses

For the quarter and nine-month period ended September 30, 2018, financial income amounted to $0.6 million, as compared to $0.1 million for the same periods in 2017. The Company recorded a non-cash gain of $1.1 million on the Company's Convertible Note embedded derivative offset by $0.5 million of accrued interest expense related to the $20.0 million debt financing obtained on August 1, 2018.

Financial Position Analysis

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

	September 30, 2018	December 31, 2017
	$	$
Cash, cash equivalents and investments	**16,082**	14,808
Accounts receivable	**855**	651
Inventories	**3,976**	2,040
Property, plant and equipment	**2,592**	3,184
Intangibles assets	**1,839**	1,886
Accounts payable, accrued liabilities, current and deferred income tax liabilities	**2,083**	2,515
Warranty provision	**251**	1,263
Deferred revenues (short and long term)	**16**	6,050
Equity	**4,175**	12,891

Liquid Assets

As at September 30, 2018, cash, cash equivalents and investments amounted to $16.1 million, as compared to $14.8 million as at December 31, 2017.

In the third quarter and for the nine-month period of 2018, the Company used approximately $1.7 million and $8.6 million respectively in cash for operations and excluding non-cash working capital, as compared to $0.8 million and $3.5 million for the same period in 2017. In the third quarter and for the nine-month period of 2018, the Company consumed $8.7 million and $9.8 million

respectively from changes in non-cash working capital, as compared to $0.2 million and $0.9 million generated in the same period last year from the early receipt of accounts receivables. Cash used from operations increased predominantly in the third quarter and nine-month period of 2018 relative to the comparable period due to the decrease in sales of sterilizers.

Accounts Receivable

As at September 30, 2018, accounts receivable amounted to $0.9 million, as compared to $0.7 million as at December 31, 2017. As at September 30, 2018, receivables were related to customer receivables, R&D and sales tax credits and a unsecured receivable outstanding from an executive in relation to an ordinary course income tax refund. In the nine-month periods of 2018, the Company used the automated receivable factoring program for almost all accounts receivable from its former distributor prior to August 1, 2018.

Inventories

As at September 30, 2018, inventories amounted to $4.0 million, as compared to $2.0 million as at December 31, 2017.

	September 30, 2018	December 31, 2017
	$	$
Raw Materials	**1,514**	1,137
Work in Progress	**2**	242
Finished Goods	**2,460**	661
	3,976	2,040

In the third quarter of 2018, the Company grew its raw material by $0.4 million and its finished goods by $1.8 million. During the third quarter, the Company bought from Getinge $0.3 million of accessories and $7.6 million representing 230 STERIZONE® VP4 Sterilizers for $33,000 per sterilizer for a total repurchase amount of $7.9 million. The Company also applied the remaining $6.0 million balance of deferred license fee associated with the Getinge Agreement against the finished goods the Company repurchased from Getinge. In addition, the Company also applied the repurchase provision of $0.5 million related to the upgrades of 47 STERIZONE® VP4 Sterilizers to Getinge against finished goods. In the second quarter of 2018, in lieu of recording revenue for such shipments and due to the potential repurchase of those upgraded sterilizers in accordance with the Co-commercialization Agreement, the Company recorded an associated $0.5 million repurchase provision and retained $0.3 million of associated upgrade costs of sales in inventory.

Property, Plant and Equipment

Property, plant and equipment, net of depreciation, amounted to $2.6 million as at September 30, 2018 which is $0.6 million lower compared to December 31, 2017. During the nine-month period, TSO_3 acquired a total of $0.1 million in property, plant and equipment. Depreciation was $0.7 million during the nine-month period of 2018.

Intangible Assets

Intangible assets, net of amortization, decreased from $1.9 million at the end of 2017 to $1.8 million as at September 30, 2018. During the nine-month period, the Company invested $0.1 million in patents and amortization was $0.2 million during the nine-month period of 2018.

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

As at September 30, 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 purchasing. Trade accounts payable amounted to $0.6 million as at September 30, 2018, compared to $1.3 million as at December 31, 2017.

Deferred Revenues

As at December 31, 2017, deferred revenues was representing almost exclusively the unamortized part of the deferred license revenue received under the Getinge Agreement. As at September 30, 2018, following the termination agreement with Getinge, the Company applied the $6.0 million balance of deferred license fee associated with the Getinge Agreement against inventories.

Shareholders' Equity

As at September 30, 2018, Shareholders' Equity amounted to $4.2 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 nine-month period of 2018, partially offset by $1.7 million in share-based compensation recognized during the same period.

As at September 30, 2018, the number of outstanding shares was 93,450,171 (92,854,304 as at December 31, 2017). As of November 6, 2018, the date of filing for the third fiscal quarter of 2018, the number of outstanding shares was 93,450,171.

Cash Flows Analysis

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

	Nine months	
	2018	2017
	$	$
Operating Activities	**(18,332)**	(2,457)
Investing Activities	**6,488**	6,861
Financing Activities	**19,882**	540

Operating Activities

In the third quarter and for the nine-month period of 2018, the Company used approximately $1.7 million and $8.6 million respectively in cash for operations and excluding non-cash working capital, as compared to $0.8 million and $3.5 million for the same period in 2017. In the third quarter and for the nine-month period of 2018, the Company consumed $8.7 million and $9.8 million respectively from changes in non-cash working capital, as compared to $0.2 million and $0.9 million generated in the same period last year from the early receipt of accounts receivables. Cash used from operations increased predominantly in the third quarter and nine-month period of 2018 relative to the comparable period due to the decrease in sales of sterilizers.

Investing Activities

For the nine-month period ended September 30, 2018, investing activities generated $6.5 million, as compared to $6.9 million generated during the same period in 2017, a decrease resulting from the net disposal of $6.7 million of short term investments and the purchase of $0.2 million of property, plant and equipment and intangible assets in the first nine-month of 2018, as compared to $11.0 million and $1.2 million respectively in the same period last year. In the third quarter of 2018, the Company generated $1.6 million from the net disposal of short term investments and used $0.03 million to purchase property, plant and equipment and intangible assets in 2018, as compared to $2.0 million and $0.2 million respectively in the same period in 2017.

Financing Activities

For the nine-month period ended September 30, 2018, financing activities generated $19.9 million as compared to $0.5 million for the same period in 2017. The amount generated in 2018 is related to a net $19.7 million financing provided in two separate but concurrent transactions in the form of a $15.0 million first lien convertible note and a $5.0 million first lien term loan. In addition, amount generated from options exercised is $0.2 million in 2018 and $0.5 million in 2017.

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
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Revenues	**782**	373	255	5,780	5,105	4,630	4,211	3,746
Net loss	**(2,104)**	(3,952)	(4,512)	(1,449)	(1,771)	(2,254)	(1,980)	(2,068)
Net loss per Share (basic, in $)	**(0.02)**	(0.04)	(0.05)	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)

Segmented Information

The Company has one operating segment.

	Third quarter		Nine months	
Revenues	**2018**	2017	**2018**	2017
	$	$	**$**	$
Canada and Worldwide	**120**	73	**272**	270
United States	**662**	5,032	**1,138**	13,676
	782	5,105	**1,410**	13,946

	September 30, 2018			December 31, 2017		
	Inventories	**Property, Plant and Equipment**	**Intangible Assets**	Inventories	Property, Plant and Equipment	Intangible Assets
Canada and Worldwide	**1,952**	**1,052**	**1,829**	1,616	1,306	1,870
United States	**2,024**	**1,540**	**10**	424	1,878	16
	3,976	**2,592**	**1,839**	2,040	3,184	1,886

For the third quarter of 2018, revenue from Getinge represented 21% of the Company's total revenues in conjunction with the Getinge Agreement (98% for the same period in 2017).

Off-Balance Sheet Arrangement

The Company made no off-balance sheet arrangement during the third 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 September 30, 2018, $26.2 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 September 30, 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 debt and equity financings and, to a small extent, through government grants and tax credits.

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 September 30, 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 September 30, 2018.

Limited History of Sales

The Company intends that its principal sources of revenue in the future will be from direct sales to customers of its STERIZONE® VP4 Sterilizers and associated products and services. The Company has limited sales and marketing experience and there is no assurance that the Company can keep its current customers or gain new ones.

The Company will have to expend material funds to promote and commercialize its products and to invest significant management resources. The Company's success in this regard will depend on its ability to develop and implement an effective sales and marketing strategy. Failure to achieve the marketing objectives could have a material adverse effect on the Company and on its results of operations.

Indebtedness risks

The recent $20.0 million secured debt financings restrict the Company's ability to sell its assets, incur secured or certain other indebtedness or engage in mergers or consolidations. These restrictions and covenants could impede access to capital or prevent the Company to pursue other business opportunities or implement its business strategy in the future.

The Company may need to use a large portion of its cash flow to repay principal and pay interest of these debts, which may reduce the amounts of fund available to finance its operations or its expansion.

The Company's ability to meet its obligations will depend on its future financial performance. Its existing capital resources and future cash flows from operations may not be sufficient to allow the Company to repay principal and pay interest. If these amounts are insufficient, the Company may be required to refinance part or all of these debts, sell assets, borrow more money or issue additional equity.

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 September 30, 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 September 30, 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 September 30, 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 and nine-month periods ended September 30, 2018 and 2017

Interim Condensed Consolidated Statements of Loss and Comprehensive Loss

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, except per share amounts)

		Third quarter		Nine months	
		2018	2017	**2018**	2017
	Notes	**$**	$	**$**	$
Revenues		**782**	5,105	**1,410**	13,946
Cost of sales	**5**	**(394)**	3,102	**451**	8,613
		1,176	2,003	**959**	5,333
Expenses					
Research and development		**1,260**	1,562	**4,452**	4,456
Selling, general and administrative		**2,608**	2,131	**7,681**	6,735
Financial (income) expenses	**4**	**(599)**	48	**(624)**	58
Total Expenses		**3,269**	3,741	**11,509**	11,249
Net loss before income taxes		**(2,093)**	(1,738)	**(10,550)**	(5,916)
Income taxes		**11**	33	**18**	89
Net loss and total comprehensive loss		**(2,104)**	(1,771)	**(10,568)**	(6,005)
Weighted average number of outstanding shares (in thousands)		**93,208**	92,842	**93,009**	92,258
Basic and diluted net loss per share	**17**	**(0.02)**	(0.02)	**(0.11)**	(0.07)
Basic and diluted net comprehensive loss per share	**17**	**(0.02)**	(0.02)	**(0.11)**	(0.07)

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	13	809	(269)	-	-	540
Share-based compensation	14	-	1,833	-	-	1,833
Net loss for the period		-	-	(6,005)	-	(6,005)
Balance at September 30, 2017		111,215	6,273	(101,737)	(1,712)	14,039
Balance at October 1, 2017		111,215	6,273	(101,737)	(1,712)	14,039
Options exercised	13	-	-	-	-	-
Share-based compensation	14	-	301	-	-	301
Net loss for the period		-	-	(1,449)	-	(1,449)
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	13	256	(90)	-	-	166
Share-based compensation	14	-	1,686	-	-	1,686
Net loss for the period		-	-	(10,568)	-	(10,568)
Balance at September 30, 2018		111,471	8,170	(113,754)	(1,712)	4,175

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	September 30, 2018 $	December 31, 2017 $
Current Assets			
Cash and Cash Equivalents	6	**16,082**	8,044
Short-term Investments	6	**-**	6,764
Accounts Receivable	7	**855**	651
Inventories	8	**3,976**	2,040
Prepaid Expenses		**238**	150
		21,151	17,649
Non-current Assets			
Property, Plant and Equipment	9	**2,592**	3,184
Intangible Assets	10	**1,839**	1,886
		4,431	5,070
		25,582	22,719
Current Liabilities			
Accounts Payable and Accrued Liabilities	6	**2,055**	2,430
Warranty Provision		**251**	1,263
Current Tax Liabilities		**11**	68
Deferred Revenues	11	**16**	6
		2,333	3,767
Non-current Liabilities			
Defered Tax Liabilities		**17**	17
Debt	12	**17,364**	-
Embedded Derivative	12	**1,693**	-
Deferred Revenues	11	**-**	6,044
		21,407	9,828
Equity			
Share Capital	13	**111,471**	111,215
Reserve – Share-based Compensation	14	**8,170**	6,574
Deficit		**(113,754)**	(103,186)
Accumulated Other Comprehensive Loss		**(1,712)**	(1,712)
		4,175	12,891
		25,582	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 September 30, 2018 and 2017 (Unaudited, in thousands of US dollars)

	Notes	Nine months 2018 $	2017 $
Cash flows from operating activities			
Net loss		**(10,568)**	(6,005)
Adjustments for:			
Depreciation and amortization		**877**	715
Loss on write-down of property, plant and equipment		**66**	39
Deferred income tax liabilities		**-**	89
Share-based compensation		**1,686**	1,833
Capitalized interest on long term debt		**445**	-
Embedded derivative (gain) recognized in net loss	12	**(1,103)**	-
Investment income	4	**(69)**	(138)
		(8,666)	(3,467)
Changes in non-cash operating working capital items	15	**(9,772)**	883
Interest received		**106**	127
Cash flows used in by operating activities		**(18,332)**	(2,457)
Cash flows from investing activities			
Acquisition of investments		**-**	(2,909)
Disposal of investments		**6,726**	11,015
Acquisition of property, plant and equipment	9	**(136)**	(1,057)
Acquisition of intangible assets	10	**(102)**	(190)
Proceed from disposal of property, plant and equipment		**-**	2
Cash flows generated by investing activities		**6,488**	6,861
Cash flows from financing activities			
Issuance of debt net of financing fees		**19,666**	-
Financing fee recognized in net loss		**50**	-
Options exercised	13	**166**	540
Cash flows generated by financing activities		**19,882**	540
Increase in cash and cash equivalents		**8,038**	4,944
Cash and cash equivalents at the beginning		**8,044**	2,698
Cash and cash equivalents at the end		**16,082**	7,642

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

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 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 September 30, 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.

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.

On August 1, 2018, the Company announced it had entered into a binding $20 million debt financing to fund commercialization initiatives for its STERIZONE® VP4 Sterilizer and announced that it had decided not to renew the distribution agreements with Getinge. As at September 30, 2018, $7.9 million has been used to repurchase 230 units and related accessories from Getinge.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

2. Accounting Policies (cont'd)

Going Concern (cont'd)

As of September 30, 2018, the Company had positive working capital of $18.8 million, an accumulated deficit of $113.3 million, and a net loss of $10.6 million for the nine-month period ended September 30, 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 September 30, 2018 have been prepared under the assumption that the Company will continue as a going concern for the next twelve months. The Company's ability to continue as a going concern is dependent upon its ability to generate additional revenue from the sale of sterilizers, attain further operating efficiencies, obtain additional equity and/or debt financing, and/or to reduce expenditures. Our interim consolidated financial statements as of September 30, 2018 do 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 January 1, 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 are described below.

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.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 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 (cont'd)

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 are 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 directly to customers. Revenue is recognized when control of the goods are transferred to customers, being at the point the goods are shipped.

The Company signed a five-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 has been 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.

Following the termination agreement with Getinge, the Company did recognize in the third quarter of 2018, the $6.0 million balance in deferred revenues as it related to deferred license fee associated with the Getinge Agreement against inventories.

Related spare parts, consumable supplies and accessories

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

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

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.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 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)

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
Debt		Amortized Cost
Embedded derivatives		Fair value through profit or loss

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 September 30, 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.

Debt

Debt is accounted for at amortized cost using the effective interest method.

Embedded derivatives

An embedded derivative is a feature within a contract, such that the cash flows associated with that feature behave in a similar fashion to a stand-alone derivative. Embedded derivatives that are separated from the host contract are accounted for at fair value through profit or loss.

The terms of the debt include an embedded conversion feature which provides for the conversion of the debt into common shares at a variable rate due to a price protection feature (down-round protection). The Company determined that the conversion feature was an embedded derivative liability that required separation from the financial liability host contract. The embedded derivative liability is recognized and measured at fair value at each reporting date with changes in fair value recorded in financial (income) expenses in the statement of loss and comprehensive loss in the period in which they arise. The liability component of the debt is determined at inception by reducing the fair value of the embedded derivative from the fair value of the instrument as a whole.

Effective interest method

The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest over the relevant period. The effective interest rate is the rate that discounts estimated future cash receipts (including transaction costs and other premiums or discounts) through the expected term of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

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.

Transaction costs that relate to the issue of the debt are allocated to the liability and embedded derivative components in proportion to the allocation of the gross proceeds. Transaction costs relating to the embedded derivative liability component are expensed directly in profit and loss and transaction costs relating to the financial liability component are included in the carrying amount of the liability component and are amortized over the expected lives of the convertible instrument using the effective interest method.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 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)

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.

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.

On January 13, 2016, the IASB issued IFRS 16, which will replace the following standards: IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases - Incentives, and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. This new standard sets out the requirements for recognizing and disclosing leases. The objective is to ensure that lessees and lessors provide relevant information that faithfully represents the transactions. The IFRS 16 is effective January 1, 2019 with earlier application permitted for companies that have also adopted IFRS 15, Revenue from Contracts with Customers. The Company has continued to advance on its IFRS 16 implementation project, however, it does not have a reliable estimate of the quantitative impact of the new standard at this time. The company will complete its assessment and quantification of the impact of the standard during the fourth quarter.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

4. Financial (income) expenses

	Third quarter		Nine months	
	2018	2017	**2018**	2017
	$	$	**$**	$
Financial Income				
Investment Income	**(6)**	(47)	**(69)**	(138)
Gain on re-measurment at fair-value on embedded derivative	**(1,103)**	-	**(1,103)**	-
	(1,109)	(47)	**(1,172)**	(138)
Financial Expenses				
Bank Charges	**12**	13	**44**	38
Factoring Cost	**2**	25	**5**	63
Interest on long term debt	**445**	-	**445**	-
Financing fees	**50**	-	**50**	-
Foreign Exchange Loss	**1**	57	**4**	95
	510	95	**548**	196
Total Financial (income) expenses	**(599)**	48	**(624)**	58

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:

	Third Quarter		Nine months	
	2018	2017	**2018**	2017
	$	$	**$**	$
Salary and Other Benefits	**1,738**	1,654	**5,977**	5,368
Share-based compensation expense	**688**	632	**1686**	1,833
Depreciation of Property, Plant and Equipment	**219**	276	**728**	575
Amortization of Intangible Assets	**51**	50	**149**	140
Research and Development Tax Credits	**(41)**	(85)	**(106)**	(145)
Warranty recorded in cost of sales	**(752)**	225	**(752)**	605

Cost of sales in both periods in 2018 included a $0.8 million reversal of the warranty provision accrual following the termination of the agreement with Getinge in August 2018 and the repurchase of the VP4 Sterilizers for which the warranty accrual was recorded in prior periods.

6. Financial Instruments

Cash and Cash Equivalents

	September 30, 2018	December 31, 2017
	$	$
Cash and cash equivalents	**16,082**	8,044

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

6. Financial Instruments (cont'd)

Investments

	September 30, 2018 $	December 31, 2017 $
Short-term Investments		
Bonds	**-**	6,764
	-	6,764

Accounts Receivable

	September 30, 2018 $	December 31, 2017 $
Accounts Receivable	**855**	651

Accounts Payable and Accrued Liabilities

	September 30, 2018 $	December 31, 2017 $
Accounts Payable and Accrued Liabilities	**2,055**	2,430

Debt and Embedded Derivative

	September 30, 2018 $	December 31, 2017 $
Debt	**17,364**	-
Embedded Derivative	**1,693**	-

Investments were rated A+ or better and had an average yield of 1.48% as at December 31, 2017. No investments as at September 30, 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

	September 30, 2018 $	December 31, 2017 $
Receivables from Clients and Related Parties	**550**	217
Government Credits Receivable	**305**	434
	855	651

There were no bad debt allowances as at September 30, 2018 nor as at December 31, 2017.

Notes to the Interim Condensed Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

8. Inventories

As at September 30, 2018, inventories amounted to $4.0 million, as compared to $2.0 million as at December 31, 2017.

	September 30, 2018 $	December 31, 2017 $
Raw Materials	**1,514**	1,137
Work in Progress	**2**	242
Finished Goods	**2,460**	661
	3,976	2,040

In the third quarter of 2018, the Company grew its raw material by $0.3 million and its finished goods by $1.8 million. During the third quarter, the Company bought from Getinge $0.3 million of accessories and $7.6 million of finished goods representing 230 STERIZONE® VP4 sterilizers for $33,000 per sterilizer for a total repurchase amount of $7.9 million. The Company also applied the remaining $6.0 million balance of deferred license fee associated with the Getinge Agreement against the finished goods the Company repurchased from Getinge. In addition, the Company also applied the repurchase provision of $0.5 million related to the upgrades of 47 VP4 sterilizers to Getinge against finished goods. In the second quarter of 2018, in lieu of recording revenue for such shipments and due to the potential repurchase of those upgraded sterilizers in accordance with the Co-commercialization Agreement, the Company recorded an associated $0.5 million repurchase provision and retained $0.3 million of associated upgrade costs of sales in inventory.

9. Property, Plant and Equipment

During the nine-month period ended September 30, 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.

10. Intangible Assets

During the nine-month period ended September 30, 2018, the Company acquired $0.1 million of new patents and software. During the year ended December 31, 2017, the Company acquired $0.2 million in patents and software.

11. Deferred Revenues

On November 25, 2015, the Company and Getinge entered into 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. On August 1, 2018, the Company and Getinge announced that they mutually decided not to renew the distribution agreements between the parties and the Company have agreed to repurchase 230 STERIZONE® VP4 Sterilizer for $33,000 per sterilizer to be reinserted in inventories. The $6.0 million remaining balance of the deferred license fee revenue has been applied against this repurchase of inventories.

As at September 30, 2018, current deferred revenues include the unamortized portion of prepaid service contracts covering a part of the installed base of STERIZONE® Sterilizers in Canada.

Notes to the Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

12. Debt

	September 30, 2018 $	December 31, 2017 $
Convertible, non-callable into convertible common shares of the Company at a price of US$0.82 per common share bearing interest at 10% per annum, compounded quarterly and payable in cash, at or prior to the maturity date of the Convertible Note at the option of the Company, maturing in August 2023.		
Debt balance	**12,204**	-
Imputed Interest	**345**	-
	12,549	-
Term loan, bearing interest at 12% per annum, compounded quarterly and payable in cash, at or prior to the maturity date of the Term loan, maturing in August 2023, callable after two years. The Company may at its entire discretion decide to reduce the rate of interest payable under the Term loan provided it decides, on a quarterly basis, to pay a portion or the entirety of a quarterly payment of interest in cash or in common shares of the Company.		
Debt balance	**5,000**	-
Imputed Interest	**100**	-
	5,100	-
Less financing fees	**(285)**	-
	17,364	-

The convertible note contains two components: debt and embedded derivative. The effective interest rate of the embedded derivative on initial recognition is 14.69% per annum.

	September 30, 2018 $	December 31, 2017 $
Embedded Derivative reported as long-term liability as at August 1, 2018	**2,796**	-
Gain on re-measuremant at fair-value on embedded derivative	**(1,103)**	-
Embedded Derivative reported as long-term liability	**1,693**	-

Expenses associated with the embedded derivative consist of:

	September 30, 2018 $	December 31, 2017 $
Gain on re-measurment at fair-value on embedded derivative	**(1,103)**	-

Under the terms and conditions of the agreements on the debt with its lenders, the Company is subject to certain covenants. As at September 30, 2018, these covenants were met by the Company.

Notes to the Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

13. 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:

	September 30, 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	**595,867**	**256**	877,090	809
Balance at the End	**93,450,171**	**111,471**	92,854,304	111,215

During the three-month period ended September 30, 2018, pursuant to the Company's Stock Option Plan, 595,867 stock options were exercised for an aggregate cash consideration of $0.2 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.

Deferred Share Unit and Restricted Share Unit Plan

DSUs and RSUs 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 and RSUs. DSUs and RSUs are 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 and RSUs are payable on the termination of service of the participant. The value of a DSU or RSU is determined based on the closing price of the Common Shares of the Company for the last trading day. The DSUs and RSUs 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 or RSUs, the value of a DSU or RSU 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 or DSUs.

As at September 30, 2018, 0.5 million DSUs and RSUs were awarded (0.1 million as at September 30, 2017). During the nine-month period ended September 30, 2018, TSO_3 recorded a compensation expense of $0.2 million ($0.2 million as at September 30, 2017) for its deferred share unit plan.

Notes to the Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

14. Reserve – Share-Based Compensation

The Company's Board of Directors adopted the 2016 Stock Incentive Compensation Plan which includes the award of stock options, Deferred Share Units (DSUs) and Restricted Share Units (RSUs). 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 September 30, 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 nine-month period ended September 30, 2018, the Company awarded 0.5 million stock options, (0.7 million for the same period in 2017) at a weighted average exercise price of $0.87 or CAD$1.13 ($2.43 or CAD$3.03 for the same period in 2017). The weighted average fair value of these stock options was $0.53 or CAD$0.68 for the nine-month period of 2018 ($1.51or CAD$1.88 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 $1.5 million for the nine-month period ended September 30, 2018 ($1.8 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$	**September 30, 2018 $**	December 31, 2017 $
Weighted Average Share Price	**$0.87**	$2.20
Exercise Price	**$0.87**	$2.20
Risk Free Interest Rate	**2.11%**	1.76%
Estimated Share Price Volatility	**60%**	61%
Expected Life	**7 years**	8 years
Expected Dividend Yield	**0%**	0%

The share-based compensation expenses take into account an estimate of the number of options, DSUs and RSUs 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. Any change in the assumptions can materially affect the fair value estimates.

	September 30, 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	**960,754**	**0.87**	2,977,080	2.13
Exercised	**(595,867)**	**0.31**	(877,090)	0.65
Expired	**(21,000)**	**1.51**	(19,600)	2.03
Forfeited	**(915,337)**	**2.07**	(1,194,668)	2.19
Outstanding at end	**7,338,503**	**2.02**	7,909,953	1.71
Exercisable at end	**3,194,616**	**1.33**	3,177,566	1.33

Notes to the Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

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

The following table summarizes certain information regarding the share based compensation of the Company as at September 30, 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)	540,021	Undetermined	309,644	Undetermined
$0.01 to $0.80	423,667	5.55	348,667	4.62
$0.81 to $1.69	3,001,066	6.15	1,982,562	5.21
$1.70 to $2.89	3,373,749	8.81	553,743	8.28
	7,338,503	12.70	3,194,616	12.67

The following table summarizes certain information regarding the share based compensation 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

15. Additional Information Relating to Cash Flows

	Nine months	
	2018	2017
	$	$
Changes in Non-Cash Operating Working Capital Items		
Decrease (Increase) in Assets		
Accounts Receivable	**(204)**	1,705
Inventories	**(1,936)**	(892)
Prepaid Expenses	**(88)**	(63)
Increase (Decrease) in Liabilities		
Accounts Payable and Accrued Liabilities	**(375)**	392
Income Tax Payable	**(57)**	-
Warranty Provision	**(1,012)**	528
Current Deferred Revenues	**10**	99
Non-current Deferred revenues	**(6,044)**	(741)
Increase in Assets Transferred		
Property, Plant and Equipment Transferred to Inventories	**-**	26
Inventories transferred to Property, Plant and Equipment	**(66)**	(171)
	(9,772)	883
Reseach and Development Tax Credits Received	**-**	155

Notes to the Consolidated Financial Statements

Periods ended September 30, 2018 and 2017 (Unaudited, in thousands of US dollars, unless otherwise indicated)

16. Segmented Information

The Company is structured as a single operating segment.

	Third Quarter		Nine months	
	2018	2017	**2018**	2017
Revenues	**$**	$	**$**	$
Canada and Worldwide	**120**	73	**272**	270
United States	**662**	5,032	**1,138**	13,676
	782	5,105	**1,410**	13,946

	September 30, 2018			December 31, 2017		
	Inventories	**Property, Plant and Equipment**	**Intangible Assets**	Inventories	Property, Plant and Equipment	Intangible Assets
Canada and Worldwide	**1,952**	**1,052**	**1,829**	1,616	1,306	1,870
United States	**2,024**	**1,540**	**10**	424	1,878	16
	3,976	**2,592**	**1,839**	2,040	3,184	1,886

For the third quarter of 2018, revenue from Getinge represented 21% of the Company's total revenues (98% for the same period in 2017).

17. Loss per Share

The following table reconciles the basic and diluted loss per share for the periods ended September 30:

	Third Quarter		Nine months	
	2018	2017	**2018**	2017
In thousands of US $, except per share amounts	**$**	$	**$**	$
Net loss				
Basic and Diluted	**(2,104)**	(1,771)	**(10,568)**	(6,005)
Number of Shares				
Weighted Average Number of Outstanding Shares	**93,208**	92,842	**93,009**	92,258
Number of Shares				
Weighted Average Number of Outstanding Shares Diluted[(1)]	**93,208**	92,842	**93,009**	92,258
Loss per Share				
Basic and Diluted	**(0.02)**	(0.02)	**(0.11)**	(0.07)
Comprehensive loss per Share Basic and Diluted	**(0.02)**	(0.02)	**(0.11)**	(0.07)

1) If the Company had a profit, the weighted average number of outstanding shares diluted would have been increased by 0.7 million as at September 30, 2018 (6.2 million as of September 30, 2017) for the calculation of the diluted net loss per share.

18. Contractual Commitments

Consistent with the transfer of the STERIZONE business from Getinge to TSO3, the Company has agreed to pay Getinge commissions ranging from 10% to approximately 35% of certain product sales from specifically identified end customers formerly linked with Getinge. Such commissions only apply to funds received by the Company prior to December 31, 2019. Commission rates vary on the nature of such sales - with higher commission rates being associated with committed business and lower commissions being associated with non-binding commercial opportunities.

19. Approval of Financial Statements

The interim condensed consolidated financial statements were approved by the Board of Directors on November 6, 2018.