Court File No.

***ONTARIO***

**SUPERIOR COURT OF JUSTICE**

**COMMERCIAL LIST**

**IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED**

**AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF ACERUS PHARMACEUTICALS CORPORATION, ACERUS BIOPHARMA INC., ACERUS LABS INC., AND ACERUS PHARMACEUTICALS USA, LLC**

# REPORT OF THE PROPOSED MONITOR

**DATED JANUARY 25, 2023**

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**(**each an **"Applicant"** and collectively, the **"Applicants")**

**REPORT OF THE PROPOSED MONITOR**

**DATED JANUARY 25, 2023**

## INTRODUCTION

1. Ernst & Young Inc. ("**EYI**" or the "**Proposed Monitor**") understands that the Applicants have brought an application (the "**CCAA Application**") before this Court returnable on January [26], 2023, seeking an initial order (the "**Proposed Initial Order**") pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**") to, among other things, obtain a stay of proceedings to allow them an opportunity to restructure their business and affairs. The Applicants propose that EYI be appointed as Monitor of the Applicants in these CCAA proceedings (in such capacity, the "**Monitor**").

2. This report (the "**Pre-Filing Report**") has been prepared by the Proposed Monitor prior to its appointment as Monitor, should this Court grant the Proposed Initial Order, to provide information to this Court for its consideration in respect of the Applicants' CCAA Application.

## PURPOSE

3. The purpose of this Pre-Filing Report is to provide information to the Court on:

    a) EYI's qualifications to act as the Monitor;

b) an overview of the Applicants;

c) background on the circumstances leading to the Applicants' decision to commence the CCAA proceedings, including a strategic review process conducted by the Applicants;

d) an overview of the Applicants' 13-week cash flow forecast on a consolidated basis for all of the Applicants (the "**Cash Flow Forecast**") and the Proposed Monitor's comments regarding the reasonableness thereof;

e) the Applicant's proposed debtor-in-possession financing;

f) the proposed appointment of FAAN Advisors Group Inc. ("**FAAN**") as Chief Restructuring Officer ("**CRO**"); and

g) certain other relevant matters about the relief sought in the Proposed Initial Order.

**TERMS OF REFERENCE**

4. In preparing this Pre-Filing Report and making the comments herein, the Proposed Monitor has been provided with, and has relied upon, audited and unaudited financial information, books and records prepared by the Applicants, discussions with management of the Applicants ("**Management**"), and information from other third-party sources (collectively, the "**Information**"). Except as described in this Pre-Filing Report in respect of the Cash Flow Forecast:

a) the Proposed Monitor has reviewed the Information for reasonableness, internal consistency and use in the context in which it was provided. However, the Proposed Monitor has not audited or otherwise attempted to verify the accuracy or completeness of such information in a manner that would wholly or partially comply with Canadian Auditing Standards ("**CAS**") pursuant to the Chartered Professional Accountants Canada Handbook and, accordingly, the Proposed Monitor expresses no opinion or other form of assurance contemplated under CAS in respect of the Information; and

b) some of the information referred to in this Pre-Filing Report consists of forecasts and projections. An examination or review of the financial forecast and projections, as outlined in the Chartered Professional Accountants Canada Handbook, has not been performed.

5. Future oriented financial information referred to in this Pre-Filing Report was prepared based on Management's estimates and assumptions. Readers are cautioned that since projections are based upon assumptions about future events and conditions that are not ascertainable, the actual results will vary from the projections, even if the assumptions materialize, and the variations could be significant.

6. Unless otherwise indicated, the Proposed Monitor's understanding of factual matters expressed in this Pre-Filing Report concerning the Applicants and their business is based on the Information, and not independent factual determinations made by the Proposed Monitor.

7. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars.

## EYI'S QUALIFICATION TO ACT AS MONITOR

8. EYI is a licensed insolvency trustee within the meaning of section 2 of the *Bankruptcy and Insolvency Act* (Canada). EYI is not subject to any of the restrictions set out in section 11.7(2) of the CCAA on who may be appointed as Monitor.

9. As discussed in further detail later in this Pre-Filing Report, EYI together with an affiliated Ernst & Young member firm, Ernst & Young Orenda Corporate Finance Inc., ("**EYO**", and together with EYI, "**EY**"), have been assisting the Applicants with a strategic review process since August 2022. EYI has developed a detailed understanding of the Applicants' operations and cash flow, and will be in a position to efficiently and seamlessly perform its responsibilities as Monitor, if appointed.

10. The Proposed Monitor has retained Fasken Martineau DuMoulin LLP to act as its independent legal counsel.

## OVERVIEW OF THE APPLICANTS

### Overview

11. This Pre-Filing Report should be read in conjunction with the Affidavit of Naveed Z. Manzoor sworn January 25, 2023 (the "**Manzoor Affidavit**") for additional background and financial

information with respect to the Applicants. Any terms not expressly defined herein are otherwise defined in the Manzoor Affidavit.

12. Headquartered in Mississauga, Ontario, the Applicants carry on a specialty pharmaceutical business focused on the research, development, commercialization and distribution of innovative prescription products primarily in the fields of urology and men's health.

**Corporate Structure**

13. Acerus Pharmaceuticals Corporation **("APC**") was incorporated under the *Ontario Business Corporations Act* (the "**OBCA**"). APC's shares are traded on the Toronto Stock Exchange (the "**TSX**") under the ticker "ASP.TO" and the OTCQB Exchange in the United States under the ticker "ASPCF". First Generation Capital Inc. ("**FGC**") holds approximately 89.3% of APC's outstanding shares. FGC is affiliated with the Chairman of the Board of Directors of APC (the "**Board**").

14. The Manzoor Affidavit describes in detail the other Applicants, all of which are APC's wholly-owned subsidiaries and are financially dependant on APC. Set out below is a summary of those other Applicants:

a) Acerus Biopharma Inc. ("**ABI**") **-** Incorporated under the OBCA, ABI is the principal operating entity holding intellectual rights to Natesto™ and certain early-stage research and development projects, including two products in development: Tefina and TriVair, all as described further herein.

b) Acerus Labs Inc. ("**ALI**") - Incorporated under the OBCA, ALI is the principal operating entity holding certain early-stage research and development projects related to the intranasal delivery of various botanical and synthetic cannabinoids formulations.

c) Acerus Pharmaceuticals USA, LLC ("**APL**", formerly Serenity Pharmaceuticals LLC, ("**Serenity**")) - APL was incorporated under the laws of the State of Delaware, U.S.A. APL owns the global rights to Noctiva™ as described further herein.

15. The Applicants head office and management are located in Mississauga, Ontario and all operations are directed from that location.

**Portfolio and Operations**

16. As described in greater detail in the Manzoor Affidavit, the Applicants' portfolio of products include:

    a) two prescription drugs that have been approved by the U.S. Food and Drug Administration ("**FDA**"): Natesto™ and Noctiva™. These two FDA-approved drugs represent the most valuable assets of the Applicants;

    b) the exclusive licensing and commercial agreements with respect to distributing Avanafil in the Canadian market; and

    c) Other pipeline products in research and development stages.

*Natesto™*

17. Natesto is a prescription treatment in the form of low dose nasal gel for testosterone replacement therapy in males diagnosed with hypogonadism (i.e., reduction or absence of hormone secretion). Natesto uses patented gel technology designed to achieve short acting, increases in testosterone levels. All rights and interests in Natesto are owned by ABI.

18. In addition to the U.S. market, Natesto has been approved by Health Canada and several other countries and regions for distribution. For the nine months ended September 30, 2022, Natesto generated net revenues of approximately US$2.1 million in the U.S. and US$179,000 from Canada and other markets.

19. As described in detail in the Manzoor Affidavit and APC's public filings, following the receipt of FDA approval in May 2014, APC entered into two successive licensing arrangements with third parties for the distribution of Natesto in the U.S. market. APC bought back the licensing rights to Natesto.

20. From April 2021 until late in 2022, the Applicants used a sales service provider, Syneos Health, to market and distribute Natesto in the U.S. market.

21. APC has a contract manufacturing arrangement with Haupt GmbH, which produces and packages the final Natesto gel product at its facility in Regensburg, Germany.

*Noctiva™*

22. Noctiva is the first FDA-approved, low-dose Desmopressin Nasal Spray for the treatment of Nocturia due to nocturnal polyuria (i.e., overproduction of urine at night).

23. The Applicants acquired the global rights to Noctiva as a result of the acquisition of Serenity in March 2022, as described further herein.

24. Following the receipt of FDA approval in March 2017, Noctiva was distributed in the U.S. market for a short period of time by a third party under a licensing agreement with Serenity. APC is working toward relaunching Noctiva in the U.S. market. APC has contracted with Renaissance Lakewood LLC as the contract manufacturer for Noctiva.

*Avanafil™*

25. Petros Pharmaceuticals has given APC the exclusive license to distribute Avanafil in the Canadian market only. Avanafil is used for the treatment of erectile dysfunction, and is currently available in the U.S. market under the name "Stendra".

*Other Pipeline Products*

26. The Applicants own the following pipeline products that are still in research and development stages:

    a) Lidbree, a topical anaesthesia for moderate acute pain;

    b) Tefina, a nasal, low-dose gel formulation of testosterone to treat female sexual dysfunction; and,

    c) TriVair, a disposable single-unit dose dry powder inhalation technology platform. This technology is currently licensed to a third party who has the primary responsibility for developing this technology.

**Employees**

27. As outlined in the Manzoor Affidavit, the Applicants currently employ ten employees and contractors. Nine of these individuals are employed or contracted in Canada, and one is employed in the United States.

**FUNDED DEBT OBLIGATIONS**

**FGC Loan Facilities**

28. At the time of this Pre-Filing Report, the Applicants were indebted to FGC in the amount of US$47.945 million of principal under a fully-drawn secured loan facility, bearing interest at a fixed rate of 8% per annum. Initially entered on April 30, 2021, this facility has been amended multiple times to increase borrowing capacity, as described in detail in the Manzoor Affidavit. This facility matures on December 31, 2024. Prior to December 31, 2024, the interest payments and principal repayments are subject to certain exceptions related to APC's market capitalization.

29. In addition, the Applicants owe US$2.0 million of principal to FGC under a separate secured credit facility entered on December 21, 2022 (the "**Second FGC Facility**"), bearing an interest rate of 8% per annum. The Second FGC Facility does not require any principal and interest payments until the maturity date on December 31, 2024. As described in detail in the Manzoor Affidavit, due to certain regulatory requirements, APC sought and obtained approval from TSX regarding the accrual of interest under the Second FGC Facility.

**The Serenity Acquisition and the Serenity Note**

30. In March 2022, APC completed its acquisition of Serenity (the "**Serenity Acquisition**"), including the global rights to Noctiva, from Torreya Capital LLC ("**TCL**"). As part of the purchase consideration, APC delivered to the former securityholder of Serenity an unsecured promissory note (the "**Serenity Note**").

31. Following multiple amendments, APC currently owes US$7.75 million under the Serenity Note, the repayment of which is to be made in thirteen quarterly payments commencing after the first commercial sale of Noctiva in the United States.

32. Under the Serenity Acquisition, APC has also agreed to pay to the former securityholders of Serenity the following contingent consideration upon Noctiva achieving certain revenue targets:

a) newly issued shares of APC; and

b) certain milestone payments.

**Other Unsecured Liabilities**

33. As outlined in the Manzoor Affidavit, in addition to the aforementioned liabilities, the Applicants' unaudited consolidated financial statements show other unsecured liabilities totalling approximately US$15.74 million as at September 30, 2022

**CIRCUMSTANCES LEADING TO THE APPLICANTS' CCAA FILING**

34. The Applicants have incurred significant costs in pursuing the commercialization plan of their products, resulting in large operating losses and cash outflows in prior years. In the years of 2020, 2021 and the first nine months of 2022, APC reported net losses of approximately US$24.4 million, US$33.8 million and US$19.1 million, respectively.

35. For the reasons summarized below, the Applicants require continued access to significant amounts of capital in order to advance the commercialization of Natesto and Noctiva.

a) The commercialization of Natesto remains in early stages due to various delays including the termination of the previous out-licensing arrangements as well as the negative impact caused by the pandemic. APC requires continued funding to expand marketing and distribution efforts. In the meantime, APC is required to complete certain clinical trials and pay various fees to preserve the future commercialization efforts.

b) The pre-launch preparation work for Noctiva will include:

i. producing commercial batches of the product;

ii. building and deploying a larger sales team to support a combined Natesto and Noctiva sales effort; and,

iii. education campaigns to increase disease and brand awareness among target patients and healthcare practitioners.

36. The Applicants have relied on the loans from FGC as the primary capital source in the past two years. As described further herein, despite their extensive efforts to explore strategic alternatives, including conducting a strategic review process since September 2022, the Applicants have not been able to conclude an actionable strategic transaction or secure other financing alternatives. The Proposed Monitor understands that FGC is unwilling to provide any additional financing outside of a CCAA proceeding, among other conditions.

37. By or around January 2023, the Applicants had depleted their liquidity and would not be able to maintain operations without immediate funding.

38. Pursuant to the Proposed Initial Order, the Applicants are seeking a stay of proceedings up to and including February 4, 2023 (the "**Stay Period**"), which they will seek to extend in a proposed Amended and Restated Initial Order (the "**ARIO**") at their comeback motion, to be heard on or before February 3, 2023 (the "**Comeback Motion**").

39. For the reasons set out in the Manzoor Affidavit, if this Court grants the Proposed Initial Order, the Applicants intend to commence ancillary insolvency proceedings under chapter 15 of title 11 of the United States Code in the United States Bankruptcy Court for the District of Delaware.

**PRE-FILING SOLICITATION EFFORTS**

40. Prior to the commencement of these CCAA proceedings, the Applicants, with the assistance of advisors, expended significant time and effort in exploring strategic transaction opportunities, including raising additional capital.

41. The Proposed Monitor understands that the Applicants began to explore capital market options starting in or around September 2021. Following the Serenity Acquisition, the Applicants increased their solicitation efforts by contacting known parties in the speciality pharmaceutical industry, as well as parties known to be interested in making investments in speciality pharmaceutical companies.

42. These informal marketing efforts did not result in any executable transaction. As the Applicants' capital needs became increasingly pressing, the Applicants engaged EY as

financial advisor in August 2022 to initiate a comprehensive strategic review process (the "**Strategic Review Process**") of all capital and business alternatives in an accelerated timeframe, including a possible debt or equity financing, asset sale, M&A, or licensing transaction. The Board formed a committee of independent directors to oversee the Strategic Review Process. As discussed further herein, FAAN was engaged around the same time to support these efforts and the finance functions of the Applicants.

43. On September 21, 2022, the Applicants sent out a press release announcing the Strategic Review Process. EY began to reach out to prospective financial and strategic transaction parties on or around the same day.

44. During the Strategic Review Process, the Applicants, with the assistance of EY, performed a formal market canvass, and also continued or reengaged in discussions with certain parties that had previously expressed interest in transacting with the Applicants.

45. Despite having received several expressions of interest, the Applicants were unable to reach agreement with any of the prospective parties on the terms of an actionable transaction prior to the commencement of the CCAA proceedings.

46. Based on information from the Strategic Review Process, the Applicants intend to seek court approval of a sale and investment solicitation process that will leverage off the work already commenced in the Strategic Review Process. The Applicants with the supervision of the Monitor may also reengage with certain parties that participated in the Strategic Review Process prior to the sale and investment solicitation process being approved by the Court to determine whether there are any actionable transactions for discrete assets or drugs of the Applicants.

47. The Proposed Monitor will provide a more detailed summary of activities during the Strategic Review Process in a further report.

**THE PROPOSED CRO APPOINTMENT**

48. In or around August 2022, the Applicants engaged FAAN initially as Chief Strategic Officer to support strategic initiatives and finance functions. Naveed Manzoor was retained as Chief Financial Officer in or around November 2022. FAAN has provided extensive financial

leadership and assistance with respect to a variety of functions, including liaising between stakeholders and advisors, internal controls, financial reporting, forecasting and vendor discussions.

49. The Proposed Monitor understands that FAAN's role is set to evolve should the CCAA Proceedings commence, to that of CRO. The Proposed Monitor has reviewed the terms of the engagement letter between APC and FAAN regarding the CRO services. The scope of these services is described in detail in the Manzoor Affidavit. A copy of the FAAN engagement letter with certain commercially sensitive information redacted is attached hereto as **Appendix "A"**, accompanied by a unredacted copy attached hereto as **Confidential Appendix "B"**. The unredacted engagement letter is proposed to be sealed as it contains commercially sensitive information that, if disclosed, could be detrimental to the CRO's ability to obtain market rates in future engagements. The redactions in the FAAN engagement letter are designed to only protect commercially sensitive information.

50. The Proposed Monitor believes that the powers, responsibilities and duties of the CRO set out in the Proposed Initial Order are important to the Applicants in these CCAA proceedings. EYI is of the view that the scope of the engagement letter appears appropriate in the circumstances and, in EYI's experience, the terms of the engagement letter are reasonable and consistent with comparable engagements in today's market. It is the Proposed Monitor's observation that FAAN is qualified to act as the CRO, given its knowledge and experience in advising and participating in corporate reorganizations. The Proposed Monitor also believe such appointment should occur immediately upon commencement of the CCAA Proceedings given the significant personnel turmoil the Applicants have experienced as described in the Manzoor Affidavit. The appointment of the CRO will help stabilize management and leadership of the Applicants.

## RELEVANT MATTERS ADDRESSED IN THE PROPOSED INITIAL ORDER

51. The Proposed Initial Order provides for three super-priority charges (collectively, the "**Charges**") on the current and future assets, undertakings and properties of the Applicants, wherever located, including all proceeds thereof that rank in the following order (each as defined and discussed below):

- first, the Administration Charge;
- second, the DIP Charge; and
- third, the Directors' Charge.

**Administrative Charge**

52. The Proposed Initial Order provides for a charge up to a maximum amount of $150,000 (the "**Administration Charge**") in favour of counsel to the Applicants, the Proposed Monitor and the Proposed Monitor's independent legal counsel, and CRO in respect of its monthly work fee as security for the professional fees and disbursements incurred prior to and after the commencement of the CCAA proceedings. Professional fee obligations secured by the Administration Charge will be paid in the ordinary course from funding provided by, among other things, the DIP Facility (as defined below).

53. The Applicants, at the Comeback Motion, will seek to increase the Administration Charge to $300,000 under the proposed ARIO.

*Recommendation*

54. The Proposed Monitor is of the view that given the current liquidity constraints of the Applicants, the proposed Administration Charge is required and reasonable in the circumstances for the initial stay period pending the Comeback Motion. The Proposed Monitor believes the quantum of the Administration Charge is reasonable in the circumstances based upon a review and assessment of the anticipated professional costs to be incurred during this matter.

**DIP Facility Agreement and DIP Charge**

55. In order to provide the required liquidity to fund operations and these restructuring proceedings, the Applicants are seeking the approval of the execution of a debtor-in-possession financing agreement entered into on January 25, 2023 (the "**DIP Facility Agreement**") between APC and APL, as co-borrowers, and FGC, as DIP lender (the "**DIP Lender**"). Pursuant to the DIP Facility Agreement, the DIP Lender has agreed to provide a super-priority, interim, non-revolving credit facility up to a maximum principal amount of US$7 million (the "**DIP**

**Facility**"), with an initial borrowing limit of US$500,000 for the first 10-day period. A copy of the DIP Facility Agreement is attached as Exhibit "S" to the Manzoor Affidavit.

56. The following is a summary of the material terms of the DIP Commitment Letter:

a) Each DIP advance shall be in the minimum amount of US$250,000 as approved by the Monitor.

b) The DIP Facility is conditional upon, among other things, FAAN being appointed as CRO.

c) The DIP Facility proceeds are to be used for: (i) ordinary course working capital and other general corporate purposes of the Borrowers in accordance with, and subject to, a rolling 13-week cash flow forecast satisfactory to the DIP Lender and court orders in these CCAA proceedings; and (ii) paying the fees and expenses incurred by the Applicants' counsel, the Proposed Monitor and its counsel, CRO, and DIP Lenders' advisors in connection with the DIP Facility and the CCAA proceedings;

d) the DIP Facility matures on the earliest of (i) December 31, 2024, (ii) the date on which the Proposed Initial Order expires without being extended or on which the CCAA proceedings are terminated, and (iii) an Event of Default as defined in the DIP Loan Agreement.

e) Interest shall be compounded monthly and payable in kind quarterly, at a rate of 8% per annum.

57. The Proposed Initial Order also provides for the creation of a priority charge (the "**DIP Charge**") over all of the assets, undertakings and properties of the Applicants in favour of the DIP Lender to secure advances up to US$500,000 that may be drawn from the DIP Facility, plus potential accruing interest. At the Comeback Motion, the Applicants will seek to increase the borrowing limit to US$7 million under the proposed ARIO.

*Recommendation*

58. In light of the current capital market conditions, the nature and stages of the Applicants' products, and the challenges facing the continued commercialization, the Applicants believe that the terms being offered in the DIP Facility Agreement are reasonable in the circumstances

and it is highly unlikely that any third party lenders would provide financing on better terms given the collateral available in the Applicants' assets. The Applicants, therefore, considered it unnecessary to canvass the market for DIP financing alternatives. The Proposed Monitor is of the same view based on feedback received by it when EY conducted the Strategic Review Process as well as a review of the terms of the DIP Facility Agreement.

59. The Applicants have a critical need for interim financing. Based on the Monitor's review of the Cash Flow Forecast and discussions with the Applicants, the advances of US$500,000 may be required in the initial 10-day stay period for the Applicants to continue operating in the ordinary course. There is a high risk that unfavourable variances in collections would exhaust the Applicants' remaining liquidity buffer and cause significant disruptions if the Applicants have no immediate access to the DIP Facility. The DIP Facility funds will be made available to all the Applicants through APC. The Proposed Monitor is of the view that the Applicants' request for approval of the DIP Facility Agreement and the DIP Charge is necessary and reasonable in the circumstances prior to the Comeback Motion.

**Directors' Charge**

60. The Proposed Initial Order provides for a charge in an amount not to exceed $200,000 (the "**Directors' Charge**") to secure an indemnity in favour of the current directors and officers of the Applicants (the "**Director and Officers**") against obligations and liabilities that they may incur as directors or officers of the Applicants after the commencement of these CCAA proceedings, except to the extent that the obligation or liability is incurred as a result of such director's or officer's gross negligence or willful misconduct.

61. The Directors and Officers shall only be entitled to the benefit of the Directors' Charge to the extent that they do not have coverage under any directors' and officers' insurance policy, to the extent such coverage is insufficient to pay an indemnified amount as described above, or to the extent that such coverage is denied by the insurance provider.

62. The Proposed Monitor assisted the Applicants in the calculation of the Directors' Charge, taking into consideration the estimated payroll-related costs, payroll cycles and the estimated vacation accrual. This analysis estimates the Directors' and Officers' exposure in respect of accrued payroll costs and vacation pay in the first 10-day period and thereafter.

*Recommendation:*

63. The Proposed Monitor is of the view that the Directors' Charge is required and is reasonable under the circumstances.

## OVERVIEW OF APPLICANTS' THIRTEEN-WEEK CASH FLOW PROJECTION

64. The Applicants, with the assistance of FAAN, and in consultation with the Proposed Monitor, have prepared a Cash Flow Forecast for the 11-week period from January 23, 2023 to April 9, 2023 (the "**Cash Flow Period**"). A copy of the Cash Flow Forecast is attached as **Appendix "C"** to this Pre-Filing Report.

65. The Cash Flow Forecast is presented on a weekly basis during the Cash Flow Period and represents the estimates of Management of the projected cash flow during the Cash Flow Period. The Cash Flow Forecast has been prepared by the Applicants using probable and hypothetical assumptions (the "**Assumptions**") set out in the notes to the Cash Flow Forecast.

66. The Proposed Monitor has reviewed the Cash Flow Forecast through inquiries, analytical procedures and discussions, and review of documents related to the Information supplied to it by certain key members of Management and employees of the Applicants. Based on the Proposed Monitor's review, nothing has come to its attention that causes it to believe, in all material respects, that:

- the Assumptions are not consistent with the purpose of the Cash Flow Forecast;
- as at the date of this Pre-Filing Report, the Assumptions are not suitably supported and consistent with the plans of the Applicants or do not provide a reasonable basis for the Cash Flow Forecast, given the probable and hypothetical assumptions; or
- the Cash Flow Forecast does not reflect the Assumptions.

67. The Cash Flow Forecast shows that during the Cash Flow Period, the Applicants project total combined receipts of approximately $2.391 million and combined disbursements totalling approximately $8.604 million, resulting in a net outflow of $6.213 million. Based on the available cash on hand, supplemented by access to the proposed DIP Facility, subject to Court approval, the Applicants are projected to have sufficient liquidity during the Cash Flow Period.

## CONCLUSIONS AND RECOMMENDATIONS

68. The Proposed Monitor has reviewed the Applicants' CCAA application materials and has consented to act as the Monitor of the Applicants, should this Court grant the Proposed Initial Order.

69. For the reasons stated herein, the Proposed Monitor believes it is appropriate for the Applicants to be granted protection under the CCAA and respectfully requests that the Court grants the Proposed Initial Order.

All of which is respectfully submitted this 25th day of January 2023.

**ERNST & YOUNG INC., in its capacity as Proposed Monitor of the Applicants, and not in its corporate or personal capacity.**

**per:**

**Alex Morrison, CPA, CA**
**Senior Vice-President**

# Appendix “A”

# to the Pre-filing Report of the Proposed Monitor

20 Adelaide Street
East, Unit 920
Toronto, Ontario,
M5C 2T6

January 25, 2023

Acerus Pharmaceuticals Corporation
7025 Langer Drive, Suite 205
Mississauga, Ontario L5N 0E8

Attention: Mr. Steve Gregory

Dear Mr. Gegory:

Re: **Acerus Pharmaceuticals Corporation, Acerus Biopharma Inc., Acerus Labs Inc., and Acerus Pharmaceuticals USA, LLC** (collectively, the "**Company**")

This letter confirms and sets forth the terms and conditions of the engagement between FAAN Advisors Group Inc. ("**FAAN**") and the Company, including the scope of the services to be performed and the basis of compensation for those services. Upon execution of this letter by each of the parties below and receipt of the retainer described below, this letter will constitute an agreement between the Company and FAAN (the "**Agreement**").

1. Description of Services.

The Company hereby engages FAAN, and FAAN shall provide the services to serve as Chief Restructuring Officer the Company ("**CRO**"). This engagement will be led by FAAN's managing director, Naveed Z. Manzoor, with support, as required, to be provided by other FAAN personnel. FAAN, including its personnel, are collectively referred to as the "**Engagement Personnel**".

The Engagement Personnel shall be responsible for the following duties.

(a) Assisting the Company in the required preparations for potentially commencing an insolvency proceeding under the Companies' Creditors Arrangement Act ("**CCAA Proceedings**");

(b) Serving as the Company's primary contact with and providing information to the proposed CCAA monitor, Ernst & Young Inc., and other professionals involved in the CCAA Proceedings regarding the business and affairs of the Company;

(c) Assisting in the preparation of and evaluating the Company-prepared projected cash flows and financing requirements in the context of its planned CCAA Proceedings;

(d) Negotiating with prospective purchasers and other interested parties during the Company's sale and investment solicitation process in the CCAA Proceedings;

(e) Managing the CCAA Proceedings on the Company's behalf, including dealing with the administration of financing including updating forecasts and information that may be required for financing, and dealing with any insolvency related claims and reconciliation process during the CCAA;

(f) Dealing with other key stakeholders including employees lenders, vendors and suppliers;

(g) Providing information to and serving as a contact with the Company's Canadian and US legal advisors;

(h) Participating in the Company's management and executive team;

(i) Making decisions with respect to the day-to-day aspects of the management and operations of the Company's business;

(j) Overseeing the Company's finance department, including acting a signing authority over the Company's bank accounts;

(k) Overseeing the Company's accounts payable payment processing; and

(l) Other such other services as requested or directed by the Company's Board of Directors, which services are to be agreed to by FAAN and not duplicative of work others are performing for the Company.

During the performance of this Agreement, FAAN shall be an independent contractor and not an agent or employee of the Company and this Agreement is not intended and will not operate to make any Engagement Personnel an employee of the Company for any purpose.

Unless as amended pursuant to a Court order, the Engagement Personnel shall report to and operate under the direction of the Company's Board of Directors.

Upon Court-approval of FAAN's appointment as CRO in the CCAA Proceedings, the Consulting Agreement dated November 14, 2022 between FAAN and the Company shall terminate.

2. Information Provided by Company and Forward-Looking Statements. The Company shall: (i) provide the Engagement Personnel with access to management and other representatives of the Company; and (ii) furnish all data, material and other information concerning the business, assets, liabilities, operations, cash flows, properties, financial condition and prospects of the Company that the Engagement Personnel reasonably request in connection with the services to be provided to the Company. The Engagement Personnel shall rely, without further independent verification, on the accuracy and completeness of all publicly available information and information that is furnished by or on behalf of the Company and otherwise reviewed by Engagement Personnel in connection with the services performed for the Company. The Company acknowledges and agrees that the Engagement Personnel are not responsible for the accuracy or completeness of such information and shall not be responsible for any inaccuracies or omissions therein. The Engagement Personnel are under no obligation to update data submitted to them or to review any other areas unless specifically requested to do so.

   The Company understands that the services to be rendered by the Engagement Personnel may include the review and preparation of projections and other forward- looking statements, and numerous factors can affect the actual results of the Company's operations, which may materially and adversely differ from those projections. In addition, Engagement Personnel will be relying on information provided by the Company and other professionals engaged by the Company in the preparation and review of those projections and other forward-looking statements.

3. Limitation of Duties. Neither FAAN, nor the Engagement Personnel make any representations or guarantees that, inter alia, (i) an appropriate restructuring proposal or strategic alternative can be formulated for the Company, (ii) any restructuring proposal or strategic alternative presented to the Company's management will be more successful than all other possible restructuring proposals or strategic alternatives, (iii) a restructuring is the best course of action for the Company, or (iv) if formulated, that any proposed restructuring plan or strategic alternative will be accepted by any of the Company's creditors, shareholders and other constituents. Further, the Engagement Personnel will not assume any responsibility for the Company's decision to pursue, or not pursue any business strategy, or to effect, or not to effect any transaction.

4. Compensation. FAAN will be paid by the Company for the services of the CRO at a monthly work fee of [redacted] plus applicable taxes and out-of-pocket expenses reasonably incurred in connection with or arising out of FAAN's activities under or contemplated by this Agreement. Out-of-pocket expenses shall include, but not be limited to, fees, disbursements and other charges associated with the Engagement Personnel's reasonable travel and lodging expenses, reasonable legal services provided to FAAN (if any), and other necessary expenses. FAAN shall invoice the Company bi-weekly and invoices are payable upon receipt.

(a) In addition to the monthly fee set out above, FAAN shall be entitled to a fee (the "**Success Fee**") in the [redacted] upon closing of:

i. Any transaction or series of transactions that constitute a material recapitalization or restructuring of the equity and/or senior secured debt of the Company, including accrued and/or accreted interest thereon, which recapitalization or restructuring is in each case effected pursuant to an exchange transaction, tender offer, or a plan of arrangement or compromise under the CCAA or other applicable similar legislation or statute; and/or

ii. Any transaction or series of transactions that is accepted and approved by the Court that constitutes a material disposition to one or more parties (including, without limitation, any person, group of persons, partnership, corporation or other entity, and also including, among others, any of the existing creditors of the Company) of (a) all or a majority of the equity securities of any entity comprising the Company which contain all or substantially all of the assets of the Company , and/or (b) all or substantially all of the material assets or operations of the entities comprising the Company, which (a) and (b) shall include, without limitation, a sale or exchange of assets, capital stock with or without a purchase option, a merger, consolidation or other business combination, an exchange or tender offer, a recapitalization, reverse vesting order transaction, the formation of a joint venture, partnership or similar entity, or any similar transaction, and including any credit bid by any secured lenders of the Company or any acquisition by existing shareholders or employees.

(b) The Success Fee shall apply to the event(s) noted in paragraph 4(i) or 4(ii) that occurs (a) during the term or this Agreement; or (b) within twelve (12) months following the end of the term (unless the Agreement has been terminated by the Company for cause) and will be paid upon closing of the event(s) noted above. For greater certainty, the Success Fee (a) shall only be earned once (i.e. not for every transaction); and (b) if the

event(s) referred to in (i) and (ii) occur as a series of transactions, be payable upon closing of the last of such transaction.

(c) The Company shall promptly remit to FAAN, a retainer in the amount [redacted] (plus applicable taxes), which shall be credited against any amounts due and owing to FAAN at the successful conclusion of this mandate or the termination of this Agreement. Any portion of the retainer remaining after being credited against the fees owed will be returned to the Company upon the satisfaction of all obligations hereunder.

(d) In the event the Company initiates a debtor-in-possession bankruptcy, insolvency or creditor enforcement proceeding (an "**Restructuring Proceeding**") under the Companies' Creditors Arrangement Act, the Bankruptcy and Insolvency Act or otherwise, the Company shall seek and obtain the approval of the Court of the retention of FAAN as the CRO of the Company, in its initial application for a Restructuring Proceeding and on terms acceptable to FAAN, and shall seek the Court's approval of this Agreement (including, without limitation, the payment of FAAN's fees and expenses and the provision of indemnification to FAAN) failing which FAAN may suspend or discontinue its efforts on behalf of the Company.

5. Termination.

(a) This Agreement will commence on the date the services referred to in Section 1 begin and may be terminated by the Company without cause by providing 30-days' written notice to FAAN. In the case of just cause, this Agreement may be terminated immediately by the Company.

(b) FAAN normally does not withdraw from an engagement unless the Company misrepresents or fails to disclose material facts, fails to pay fees or expenses, or makes it unethical or unreasonably difficult for FAAN to continue performance of the engagement, or other just cause exists. In the event that FAAN intends to withdraw from this engagement without cause, it shall provide 30 days' written notice.

(c) On termination of the Agreement, any fees and expenses due to FAAN for services provided up to and including the effective date of termination shall be remitted promptly by the Company (including fees and expenses that accrued prior to, but invoiced subsequent to, the effective date of termination).

(d) The provisions of this Agreement that expressly state that they are to continue in effect after the termination of this Agreement, or which by their nature would survive the termination of this Agreement shall survive and continue to bind the parties.

6. No Audit. The Company acknowledges and agrees that Engagement Personnel are not being requested to perform an audit, review or compilation, or any other type of financial statement reporting engagement that is subject to the rules of the CICA, ICAO, OSC, AICPA, SEC or other state or national professional or regulatory body.

7. No Third Party Beneficiary. The Company acknowledges that all advice (written or oral) provided by FAAN to the Company in connection with this Agreement is intended solely for the benefit and use of the Company in considering the matters to which this Agreement relates. The Company may choose to reproduce, disseminate, quote or refer to such information as it wishes, in its sole and absolute discretion, provided that in no event may such information be attributed to FAAN. The Company may communicate any information

concerning the services of FAAN and the advice provided by FAAN to its legal and financial advisors.

8. Exclusivity and Conflicts. FAAN is an independent firm that has several clients and engagements, some of which will be active during the rendering of services by the Engagement Personnel in connection with this matter. FAAN is not currently aware of any relationship that would create a conflict of interest with the Company or those parties-in-interest of which you have made us aware. It is possible that FAAN may have rendered or will render services to, or have business associations with, other entities or people which had or have or may have relationships with the Company, including creditors of the Company. In the event the Company accepts the terms of this Agreement, FAAN will not represent, and has not represented, the interests of any entities or parties which are in conflict with the interests of the Company in connection with this matter.

9. Indemnification/Limitations on Liability. FAAN shall incur no liability for any acts or omissions of the Engagement Personnel related to the performance or non- performance of services at the direction of the Company and consistent with the requirements of this engagement and this Agreement, provided that such actions or omissions are not carried out in a manner that is dishonest or grossly negligent and/or the Engagement Personnel has not engaged in willful misconduct.

   The Company shall indemnify the Engagement Personnel acting as officers (the "Indemnified Professionals") to the same extent as the most favorable indemnification it extends to its officers or directors, whether under the Company's bylaws, its certificate of incorporation, by contract or otherwise, and no reduction or termination in any of the benefits provided under any such indemnities shall affect the benefits provided to the Indemnified Professionals. The provisions of this section are in the nature of contractual obligations and no change in applicable law or the Company's charter, bylaws or other organizational documents or policies shall affect the Indemnified Professionals' rights hereunder.

   In the context of any Insolvency Proceeding involving the Company, the Company shall also seek, as part of any plan confirmation, discharge order or final sale order, a full and final release of FAAN from all potentially affected parties, which release shall be consistent with the terms of other releases sought for professionals in respect of the CCAA Proceedings. The Company shall use reasonable commercial efforts to obtain such approval by the Court.

10. Miscellaneous. This Agreement: (a) shall be governed and construed in accordance with the laws of the Province of Ontario and the laws of Canada applicable therein without giving effect 'to such Province's rules concerning conflicts of laws that might provide for any other choice of law; (b) incorporates the entire understanding of the parties with respect to the subject matter hereof; (c) may not be amended or modified except in writing executed by each of the parties hereto; (d) may be executed by facsimile and in counterparts, each of which shall be deemed to be an original but all of which together shall constitute one and the same agreement; and (e) notwithstanding anything herein to the contrary, upon the completion of the restructuring process presently being undertaken in respect of the Company, FAAN may reference or list the Company's name and/or a general description of the services in FAAN's marketing materials.

If the foregoing is acceptable to you, kindly sign the enclosed copy to acknowledge your agreement with its terms.

Very truly yours,

**FAAN ADVISORS GROUP INC.**

Per:_____

Naveed Z. Manzoor, Managing Director

Accepted and agreed:

**ACERUS PHARMACEUTICALS CORPORATION**
**ACERUS BIOPHARMA INC.**
**ACERUS LABS INC.**
**ACERUS PHARMACEUTICALS USA, LLC**

Per: _____

(I have the authority to bind the above Corporations)

# Confidential Appendix “B”
# to the Pre-filing Report of the Proposed Monitor

# Appendix “C”

# to the Pre-filing Report of the Proposed Monitor

**Acerus Pharmaceuticals Corporation and Subsidiaries (collectively, the "Applicants")**
**Cash Flow Forecast for the Period January 23, 2023 to April 9, 2023**
**$CDN in Thousands**

| | Week # | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Ending | Jan 29 | Feb 05 | Feb 12 | Feb 19 | Feb 26 | Mar 05 | Mar 12 | Mar 19 | Mar 26 | Apr 02 | Apr 09 | Total |
| | Notes | | | | | | | | | | | | |
| **Receipts** | | | | | | | | | | | | | |
| Product Sales | 1 | $ - | $ 449 | $ 536 | $ 199 | $ 203 | $ 224 | $ 176 | $ 163 | $ 149 | $ 170 | $ 122 | $ 2,391 |
| **Total Receipts** | | **$ -** | **$ 449** | **$ 536** | **$ 199** | **$ 203** | **$ 224** | **$ 176** | **$ 163** | **$ 149** | **$ 170** | **$ 122** | **$ 2,391** |
| **Disbursements** | | | | | | | | | | | | | |
| Direct Selling Costs | 2 | 210 | 240 | - | - | 291 | 375 | 140 | 142 | 133 | 123 | 114 | 1,768 |
| Payroll & Contractor costs | 3 | 92 | 37 | 4 | 92 | - | 129 | 4 | 92 | - | 196 | 4 | 650 |
| Contract manufacturing costs | 4 | - | 261 | - | - | - | 72 | - | - | - | 838 | - | 1,172 |
| Other Product Related Expenses | 5 | 529 | 551 | 563 | 20 | 20 | 551 | 20 | 20 | 20 | 557 | 529 | 3,382 |
| Other SG&A | 6 | 5 | 24 | - | 5 | - | 24 | - | 5 | - | 24 | - | 88 |
| Professional Fees | 7 | 462 | 125 | 234 | 50 | 45 | 147 | 170 | 45 | 75 | 147 | 45 | 1,545 |
| **Total Disbursements** | | 1,299 | 1,238 | 801 | 168 | 356 | 1,298 | 334 | 305 | 228 | 1,885 | 692 | 8,604 |
| **Net cash receipts/(disbursements)** | | **$ (1,299)** | **$ (789)** | **$ (265)** | **$ 31** | **$ (152)** | **$ (1,074)** | **$ (158)** | **$ (143)** | **$ (79)** | **$ (1,715)** | **$ (570)** | **$ (6,213)** |
| **Cash Balance** | | | | | | | | | | | | | |
| Opening Balance | 8 | $ 1,662 | $ 363 | $ 252 | $ 1,343 | $ 1,375 | $ 1,222 | $ 1,504 | $ 1,347 | $ 1,204 | $ 1,125 | $ 2,123 | $ 1,662 |
| Net Cash Receipts/(disbursements) | | (1,299) | (789) | (265) | 31 | (152) | (1,074) | (158) | (143) | (79) | (1,715) | (570) | $ (6,213) |
| DIP draws/(repayment) | | - | 678 | 1,356 | - | - | 1,356 | - | - | - | 2,713 | 678 | $ 6,782 |
| **Ending Cash Balance** | | **$ 363** | **$ 252** | **$ 1,343** | **$ 1,375** | **$ 1,222** | **$ 1,504** | **$ 1,347** | **$ 1,204** | **$ 1,125** | **$ 2,123** | **$ 2,231** | **$ 2,231** |
| **DIP Facility** | | | | | | | | | | | | | |
| Opening Balance | 9 | $ - | $ - | $ 678 | $ 2,035 | $ 2,035 | $ 2,035 | $ 3,391 | $ 3,391 | $ 3,391 | $ 3,391 | $ 6,104 | $ - |
| DIP Draws/(Repayment) | 9 | - | 678 | 1,356 | - | - | 1,356 | - | - | - | 2,713 | 678 | $ 6,782 |
| **Closing Balance** | | **$ -** | **$ 678** | **$ 2,035** | **$ 2,035** | **$ 2,035** | **$ 3,391** | **$ 3,391** | **$ 3,391** | **$ 3,391** | **$ 6,104** | **$ 6,782** | **$ 6,782** |

**In the Matter of the CCAA of Acerus Pharmaceuticals Corporation, Acerus Biopharma Inc., Acerus Labs Inc., and Acerus Pharmaceuticals Usa, LLC (collectively, the "Applicants")**

**Notes to the Unaudited Cash Flow Forecast of the Applicants**

**Disclaimer:**

In preparing this cash flow forecast (the "**Cash Flow Forecast**"), the Applicants with the assistance of FAAN Advisors Group Inc. ("**FAAN"**), and in consultation with Ernst & Young Inc. (the "**Proposed Monitor**"), have relied upon unaudited financial information and the Applicants have not attempted to further verify the accuracy or completeness of such information. The Cash Flow Forecast includes estimates concerning the operations of the Applicants and additional assumptions discussed below with respect to the requirements and impact of a *Companies' Creditors Arrangement Act* ("**CCAA**") filing (the "**Probable and Hypothetical Assumptions**" or the "**Assumptions**"). Since the Cash Flow Forecast is based on Assumptions about future events and conditions that are not ascertainable, the actual results achieved during the Cash Flow Forecast period will vary from the Cash Flow Forecast, even if the Assumptions materialize, and such variation may be material. There is no representation, warranty or other assurance that any of the estimates, forecasts or projections will be realized.

The Proposed Monitor has reviewed the Cash Flow Forecast to the standard required of a Court appointed Monitor pursuant to section 23(1)(b) of the CCAA, which requires a Monitor to review the debtor's cash flow statements as to its reasonableness and to file a report with the Court on the Monitor's findings.

Pursuant to this standard, the Proposed Monitor's review of the Cash Flow Forecast consisted of inquiries, analytical procedures and discussions related to information supplied to it by certain key members of the Applicants and other employees of the Applicants. Since the Probable and Hypothetical Assumptions need not be supported, the Proposed Monitor's procedures with respect to them were limited to evaluating whether they were consistent with the purpose of the Cash Flow Forecast. The Proposed Monitor also reviewed the support provided by the Applicants for the Probable and Hypothetical Assumptions and the preparation and presentation of the Cash Flow Forecast.

Based on the Proposed Monitor's review, nothing has come to the Monitor's attention that causes the Proposed Monitor to believe, in any material respect, that:

(a) The Probable and Hypothetical Assumptions are not consistent with the purpose of the Cash Flow Forecast;
(b) As at the date of this report, the Probable and Hypothetical Assumptions are not suitably supported and consistent with the plans of the Applicants or do not provide a reasonable basis for the Cash Flow Forecast, given the Probable and Hypothetical Assumptions; or
(c) The Cash Flow Forecast does not reflect the Probable and Hypothetical Assumptions.

**Overview:**

The Cash Flow Forecast includes the receipts and disbursements of the Applicants during the Cash Flow Forecast period. The Applicants, with the assistance of FAAN, and in consultation with the Proposed Monitor, have prepared the Cash Flow Forecast based primarily on estimated receipts and disbursements related to the ongoing operations and the CCAA proceedings.

**Assumptions:**

1. **Product Sales**
   The Cash Flow Forecast reflects the continued sale of Natesto™ during the CCAA Proceedings. Cash receipts are forecast based on accounts receivable and projected sales during the forecast period, before rebates and other direct selling costs, as described in Note 2.

2. **Direct Selling Costs**
   Represents rebates to health plans and co-pay card holders, fees charged by wholesalers and incentives offered to pharmacy partners.

3. **Payroll and Contractor Costs**
   Payroll and contractor payments are forecast based on historical run rates and anticipated staffing levels. Salaried employees receive semi-monthly pay. Included in Week 13 are anticipated payments under a proposed key employee retention plan, subject to court approval.

4. **Contract Manufacturing Costs**
   Represents estimated payments to third party contract manufacturers for the production of commercial batches of the Applicants' products.

5. **Other Product Related Expenses**
   Included in these expenses are fees charged by regulatory agencies, clinical trial costs, and costs to maintain intellectual property rights, and certain indirect selling costs.

6. **Other SG&A**
   Includes office lease, insurance and other administrative expenses.

7. **Restructuring Costs**
   Restructuring costs include primarily professional fee payments and expenses to the Applicants' Canadian and U.S. legal counsel, the proposed Monitor and its counsel and the proposed Chief Restructuring Officer in connection with the Applicants' restructuring proceedings.

8. **Beginning Balance**
   Represents the projected opening cash balance as at January 23, 2023.

9. **Debt in Possession Facility ("DIP") Draws and Repayments**
   Reflects projected draws and repayments under the DIP facility, subject to Court approval.