Accounting principles

Amounts in SEK unless otherwise stated.

The consolidated financial statements of Xbrane Biopharma AB (publ) (Xbrane) have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and RFR 1 Supplementary Accounting Rules for Groups. Xbrane has been complying with IFRS since July 1, 2017. The Parent Company's accounts have been prepared in accordance with RFR 2, Accounting for Legal Entities and the Annual Accounts Act.

The 2015 financial year was the first year in which Xbrane prepared consolidated accounts.

Critical assessments
IFRS and GAAP require that Xbrane make assessments and assumptions that affect the company's reported assets, liabilities, income and expenses as well as other information. These assessments are based on historical experience and other factors deemed reasonable under prevailing circumstances. Actual outcomes may differ from these assessments if other assumptions are made or other conditions exist.

Key ratio definitions

Net sales

Comprised of income from goods sold and services performed which are included in the company's normal operations.

Gross margin
Gross margin is calculated as gross profit in relation to net sales. Gross profit is net sales minus cost of goods sold.

EBITDA
EBITDA is calculated as operating profit before depreciation.

Operating profit
Comprises the difference between operating income and operating expenses.

Research and development costs as a percentage of operating expenses
Calculated as research and development refers to expenses divided by total operating expenses.

Balance sheet total

The total of all assets or the total of all liabilities and equity.

Equity/assets ratio

Comprised of how great a proportion of the assets that are financed with equity in order to show the company's long-term solvency, that is to say, equity through total assets.

Valuation principles

Assets, provisions and liabilities have been evaluated based on acquisition value unless indicated otherwise below.

Depreciation

Depreciation is implemented lineally across the estimated useful life of the asset, since it reflects the expected depletion of the asset's future economic benefits. The depreciation is expensed in the income statement.

Tangible assets

Machinery and other technical facilities are written off in 10 years

Inventories, tools, fixtures and installations are written off in 3 to 5 years

Leases

Leases that mean that the financial risks and benefits of ownership of an asset are essentially transferred from the lease to an enterprise are classified in the consolidated financial statements as finance leases. Financial leases entail that rights and obligations are reported as assets and liabilities in the balance sheet. The asset and liability is initially valued at the lower of the asset's fair value and the present value of the minimum lease payments. Expenses directly attributable to the lease are added to the value of the asset. Leasing fees are allocated on interest and amortization according to the effective interest rate method. Variable fees are recognized as an expense in the period they arise. The leased asset is depreciated on a straight-line basis over the estimated useful life.

Leasing fees under operating leases, including increased first-time rent but excluding expenses for services such as insurance and maintenance, are recognized as costs linearly over the lease period.

Consolidation principles and business combinations

Subsidiary

Subsidiaries are companies that are under the controlling influence of the Parent Company. Continuing influence means a direct or indirect right to design a company's financial and operational strategies in order to obtain financial benefits. Subsidiaries' financial statements are included in the consolidated financial statements from the date of acquisition to the date on which the controlling interest expires.

The Italian company Primm Pharma s.r.l was acquired in September 2015. The consolidated financial statements have been prepared in accordance with the acquisition method. The acquisition date is the time when the controlling influence is obtained. Identifiable assets and liabilities are initially valued at fair value at the acquisition date. Minority's share of the acquired net assets is valued at fair value. Goodwill consists of the difference between the acquired identifiable net assets at the acquisition date and the acquisition value including the value of the minority interest, and is initially valued at acquisition value. Intercompany transactions between group companies are eliminated in their entirety. Subsidiaries in other countries prepare their annual accounts in foreign currency. At the consolidation, the items in these companies' balance sheet and income statements are translated at the closing date and average exchange rate during the period. The exchange rate differences that arise are reported in the translation difference in the Group's equity. Translation differences arising from foreign currency translation of foreign operations are reported in other comprehensive income and accumulated in a separate component of equity, referred to as translation reserve. Upon disposal of a foreign operation, the accumulated translation differences attributable to the business are realized, reclassifying them from the translation reserve in equity to the profit for the year. In cases where divestment occurs but controlling influence persists, the proportionate share of accumulated translation differences from other comprehensive income is transferred to non-controlling interest.

Start-up costs of companies

Start-up costs of companies are expensed in accordance with IFRS. This principle was implemented on July 1, 2017.

Translation to foreign currency

Monetary items in foreign currency are translated at the rate on the balance sheet date. Non-monetary items are not translated, but are reported at the rate at the time of acquisition.

Functional currency and report currency

The parent company's accounting currency is SEK. The subsidiary's accounting currency is EUR, translation to SEK takes place in the group.

Transactions and balance sheet items

Transactions in foreign currency are translated to SEK according to the exchange rates which apply on the balance sheet date for balance sheet items or alternatively the average rate during the period for profit/loss items. Exchange rate gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at the balance sheet date rate are reported in the income statement. Exchange rate differences on lending and borrowing are reported in the net interest income/expense, while other exchange rate differences are included in the earnings before interest and tax.

Intangible fixed assets

Research and development

Expenditure for research is reported as an expense when it arises in the group.

An intangible asset which arises through development or in the development phase of an internal project, can be recognised as an intangible asset only if all the below conditions are met:

a) It is technically possible to complete the development of the product so that it will be available for use

b) The management intends to complete the product, use or sell it

c) There is a possibility of using or selling the product

d) It can be demonstrated that it is likely the product will generate future economic benefits

e) There are adequate technical, economic and other resources to complete the development and to use or sell the product

f) The expenditure that is assignable to the intangible asset during its development

According to the above mentioned criteria, no internally developed intangible assets in Xbrane have been reported, however, equivalent costs are reported in the income statement. An assessment is made at each major milestone in the company's product development and Xbrane AB may capitalize development expenditure in the future. Development expenditure has been capitalized in Primm pharma s.r.l. Besides capitalized development, there is goodwill in the group.

Goodwill

Goodwill arising from acquisition of subsidiaries is reported at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested at least annually for impairment or when there is an indication of impairment. This can be done, for example, by calculating net present value (NPV).

The acquisition of the subsidiary Primm Pharma s.r.l. were based on a valuation in EUR and the translation differences arising on the valuation of Goodwill on the balance sheet date are included in other comprehensive income under "Items transferred or included in profit or loss" and in “Translation reserves" in equity. This accounting principle has been implemented since July 1, 2017.

Tangible fixed assets

All tangible fixed assets are reported at acquisition cost less deductions for depreciation. Historical cost includes expenses directly attributable to the acquisition of the asset.

Additional expenses are added to the asset's carrying amount or recognised as a separate asset, depending on which is appropriate, only when it is probable that future economic benefits associated with the item will flow to the company and the historical cost of the asset can be measured reliably. Reported value for the part compensated is removed from the balance sheet. All other types of repairs and maintenance are reported as expenses in the income statement in the period in which they occur.

The assets' residual values and useful lives are tested at the end of each reporting period and adjusted as necessary. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount exceeds its estimated recoverable amount.

Profits and losses on disposal are determined by a comparison between the sales revenue and the carrying amount and are recognised in other operating income and operating expenses respectively in the income statement.

Financial assets and liabilities

Financial assets are valued at initial recognition at cost, including any transaction costs directly attributable to the acquisition of the asset. Financial current assets are valued after the initial recognition at the lower of cost and net realizable value on the balance sheet date. Accounts receivable and other receivables constituting current assets are valued individually to the amount that is expected to flow. Financial assets are valued after initial recognition at acquisition cost less any write-downs and with the addition of any revaluations. Interest-bearing financial assets are valued at accrued acquisition value using the effective interest rate method. When evaluating the minimum value of the valuation and assessing impairment requirements, the company's financial instruments held for risk spreading are considered to be part of a securities portfolio and are therefore valued as an item. Derivative instruments that constitute financial assets and for which hedge accounting has not been applied is valued at the lower of acquisition cost and net realizable value at the balance sheet date after the first reporting date.

Financial liabilities are valued at accrued acquisition value. Expenses directly attributable to borrowing correct the loan's acquisition value and accrued using the effective interest rate method. Derivative instruments with a negative value and for which hedge accounting has not been applied are reported as financial liabilities and valued at the amount that is most favorable for the company if the obligation is regulated or transferred on the balance sheet date.

Impairment of non-financial fixed assets

Tangible fixed assets and intangible assets, where depreciation does not occur or has not yet begun, is tested annually for impairment or as soon as an indication of impairment is required. Other assets are tested as soon as an indication exists that the reported value may be too high.
Write-downs are made at the recoverable amount if this is lower than the carrying amount. The recoverable amount is the higher of net realizable value and value in use. When assessing the value in use, future cash flows are discounted at present value using a discount factor before tax. The discount factor should reflect market assessments of the money's time value (real interest rate) and the special risks associated with the asset or cash-generating unit to which the asset can be attributed.

Income recognition

Income is recognized when it can be calculated in a reliable way and when fundamentally all risks and rights which are associated with ownership are transferred to the purchaser, which is normally in connection with delivery.

Interest income is recorded in accordance with the effective interest method.

Other operating income

Other operating revenues consist of revenues that are not the core business of the company. This reclassification of costs previously reported as net income was implemented on July 1, 2017.

Financial income and expenses
Financial income consists of interest income on cash and cash equivalents. Interest income on financial instruments is reported using the effective interest rate method. The effective interest rate is the interest rate that discount the estimated future payments and payments over a financial instrument's expected maturity to the net asset value of the financial asset or liability. The calculation includes all fees paid or received by the contracting parties that are part of the effective interest rate, transaction costs and all other upper and lower rates. Financial expenses consist of interest expenses on loans. Borrowing costs are recognized in profit or loss using the effective interest method except to the extent that they are directly attributable to the purchase, construction or production of assets that take a considerable amount of time to complete the intended use or sale, which are included in the acquisition value of the assets. Exchange rate gains and losses on assets and liabilities attributable to financing activities are reported net.

Taxes

Current taxes are valued based on the tax rates and tax rules applicable on the balance sheet date.

Tax on profit for the year in the income statement consists of current tax and deferred tax. Current tax is income tax for the current fiscal year relating to the taxable profit for the year and the portion of previous taxable income tax which has not yet been reported. Deferred tax is income tax for taxable income in respect of future fiscal years as a result of past transactions or events.

Deferred tax liability is recognized for all taxable temporary differences, but not for temporary differences arising from initial recognition of goodwill. Deferred tax assets are reported for deductible temporary differences and for the possibility of using tax loss carryforwards in the future. The valuation is based on how the reported value of the corresponding asset or liability is expected to be recovered and regulated respectively. The amount is based on the tax rates and tax rules that were decided on the balance sheet date and have not been calculated on a current basis.

Inventory

Inventories are measured at purchase value or net realizable value, whichever is the lower.

Receivables

Receivables are recorded in the amounts expected to be paid.

Provisions

The company makes a provision when there is a legal or informal undertaking and a reliable estimate of the amount can be made. There are provisions in the subsidiary Primm pharma s.r.l and they relate to severance pay for the CEO and other employees.

Liabilities

Liabilities are reported at their nominal amount.

Equity

The acquisition of Primm Pharma s.r.l was financed through the issuing of a convertible which is classified as equity. The convertible, which was held by Primm Pharma´s former owner, amounted to SEK 56 million and can be converted to shares equivalent to the issue price of SEK 42.5. Conversion can take place during a period up to 2020 provided that a total of 6 different milestones regarding the commercialization of Spherotide are achieved. The convertible is reported as equity in that the terms stipulate that it will always be converted to shares and it therefore does not entail any cash payment for the company. 10% of the convertible was converted to shares during 2016 as the first milestone in the agreement was reached.

Receivables and liabilities in foreign currency

The acquisition of Primm Pharma s.r.l. was financed through the issue of a convertible which is classified as equity. The convertible bond held by Primm Pharma's former owner amounted to MSEK 56 and can be converted into shares corresponding to the subscription price of SEK 42.5. Conversion can take place over a period of time up to 2020, provided that a total of 6 different milestones regarding the commercialization of Spherotide are achieved. Following the implementation of IFRS, the convertible bond was retroactively recognized as a short-term liability from when it arose until Xbrane shares were traded on Nasdaq OMX First North on February 3, 2016. After that, it was reclassified as equity as the terms mean that it will always converted into shares and thus will not involve any cash payment for the company. In 2016, 10% of the convertible bond was converted into shares after the first milestone in the agreement was reached. By 2017, another 40% of the convertible amount has been converted into shares when the second and third milestones in the agreement were reached.

Receivables and liabilities in foreign currency
Receivables and liabilities in foreign currencies have been valued at the closing date and unrealized exchange gains and losses are included in the income statement.

Advances from customers are taken at the rates prevailing when each advance was received, as repayment is not expected to occur.

Unrealized gains on long-term receivables and liabilities are offset against unrealized exchange losses, as excess gains or losses are reported in the income statement as a financial income or financial expense.

Exchange gains (losses) on operating-related receivables and liabilities are reported as other operating income (operating expenses).

Exchange rate differences relating to financial assets and liabilities are reported under results from financial investments.

Payments to employees

Short-term payments in the group consist of salaries, social insurance expenses, paid holidays, paid absence due to illness, healthcare and bonuses. Short-term payments are recognized as an expense and a liability when there is a legal or constructive obligation to make a payment.

Share Savings Program for Employees
In June 2017, a share saving program was initiated for all of the company's employees, which runs until December 2019. Employees' participation is based on investing up to SEK 150,000 in Xbrane shares on the market, so-called savings shares, by February 2018. By the end of the year In 2020, the participants are either offered, if approved by the Annual General Meeting 2020, to subscribe for shares 1 matching share per savings account to quota value and the opportunity to acquire up to 1 matching share per savings share, depending on the outcome of the set long-term goals. The incentive program is described in its entirety on the company's website. The cost of the program is calculated on the basis of assumptions about participation rate, staff turnover, annual price increases and outcomes of the targets on which performance shares are based and updated monthly. The estimated cost of the program and social costs for employees are expensed on a straight-line basis over the period from the start of the program until the end of the program and booked in equity.

Severance pay to employees
Provisions apply for severance pay to employees in Italy. Since 1 July 2017, current debt is calculated as the liability that arises. The debt is classified as long-term.

Parent company

Financial assets
Shares and participations in subsidiaries are reported at cost less any impairment losses. The acquisition value includes the purchase price paid for the shares as well as acquisition costs. Any capital contributions and group contributions are added to the acquisition value when they are submitted. Dividends from subsidiaries are reported as income.

Other accounting principles
The parent company applies the same accounting principles as the Group.
All leases are reported as finance leases.

Segment reporting
An operating segment is part of a group that operates, from which it can generate revenue and incur costs and for which there is independent financial information available. The performance of a business segment is monitored by the company's highest executive decision maker who decides on resources to be allocated to the segment and assesses its long and short-term financial results. The operating segments are reported in a manner that complies with the internal reporting provided to the business's highest decision makers. The Chief Executive Officer and CEO, who is responsible for all allocating resources and evaluating the performance of the operating segments, is the highest executive decision maker who makes strategic decisions.

The Group has two operating segments - "Biosimilars" whose operations are conducted in the Parent Company, Xbrane Biopharma AB, and "Long-term Injectable Drugs", conducted by the Italian subsidiary, Primm Pharma, Inc.. Segment reporting was implemented from 1 July 2017.

Function-based cost classification
Since the implementation of IFRS 1 July 2017, the Group has a function based cost classification. This is due to that the company operates an activity based on the research and development, production and administration functions.