

Convenience translation

BioCancell Ltd.

**Consolidated Financial Statements
December 31, 2017**

Consolidated Financial Statements as at December, 2017

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Auditors' Report to the Shareholders of BioCancell Ltd.

We have audited the accompanying consolidated statements of financial position of BioCancell ("the Company") as at December 31, 2017 and 2016 and the consolidated statements of income, other comprehensive income, changes in equity (loss), and cash flows, for each of the three years in the period ended December 31, 2017. These financial statements are the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including standards prescribed by the Auditors Regulations (Manner of Auditor's Performance), 1973. Such standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and Management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a fair basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company and its subsidiaries as at December 31, 2017 and 2016, and the results of operations, changes in equity (loss) and cash flows for each of the three years in the period ended on December 31, 2017, in accordance with International Financial Reporting Standards (IFRS) and the Israel Securities Regulations (Annual Financial Statements), 2010.

Without qualifying our above opinion, we draw attention to Note 1B to the financial statements, regarding the fact that the Company is in the stages of research and development, and the continuation of the development stages and the disposal of the assets related to the planned activities depend on future events, including raising of additional capital and achieving operating profit in the future. These factors, together with the other factors described in this Note, raise substantial doubt about the Company's ability to continue as a going concern. The management's plans regarding these issues are described in this Note. At this stage, the final outcome of the aforesaid cannot be assessed at this stage. The financial statements do not include any adjustments for assets and liabilities and their classification that might be required if the Company is unable to continue as a going concern.

Somekh Chaikin
Certified Public Accountants

March 5, 2018

Consolidated Statements of Financial Position as at December 31

NIS thousands

	Note	2017	2016
Assets			
Cash and cash equivalents	4	5,040	17,550
Receivables	5	1,388	3,336
Total current assets		6,428	20,886
Long-term prepaid expenses		37	25
Asset for employee benefits, net		11	10
Fixed assets, net		760	821
Total non-current assets		808	856
Total assets		7,236	21,742
Liabilities			
Trade payables		559	410
Other payables	6	8,254	8,117
Short-term employee benefits		536	542
Total current liabilities		9,349	9,069
Total liabilities		9,349	9,069
Contingent liabilities and commitments	7		
Capital			
Ordinary share capital	8	9,613	7,400
Share premium		219,280	203,015
Translation reserve of foreign operations		(133)	(11)
Capital reserve for share-based payments	9	7,183	5,094
Cumulative deficit		(238,056)	(202,825)
Total capital (deficit)		(2,113)	12,673
Total liabilities and capital		7,236	21,742

Lawrence Howard
Chairman of the Board

Frank Haluska
CEO

Jonathan Burgin
CFO and COO

Approval date of the financial statements: March 5, 2018

The accompanying notes are integral part of the consolidated financial statements.

Consolidated Statements of Income for the Year Ended December 31

NIS thousands (unless stated otherwise)

	Note	2017	2016	2015
Research and development expenses	11	22,340	9,142	23,277
General and administrative expenses	12	11,374	8,642	4,432
Loss from ordinary operations		33,714	17,784	27,709
Financial income	13	(5)	(164)	(4)
Financing expenses	13	365	25	1,437
Financing expenses (income), net		360	(139)	1,433
Loss before income tax		34,074	17,645	29,142
Income tax	14	1,157	523	-
Net loss attributable to: Shareholders of the Company		35,231	18,168	29,142
Loss per ordinary share (NIS)	15			
Basic and diluted loss		0.39	0.33	0.64

The accompanying notes are integral part of the consolidated financial statements.

Consolidated Statements of Other Comprehensive Loss for the Year Ended December 31

NIS thousands

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Loss for the year	35,231	18,168	29,142
Other comprehensive loss items to be reclassified to profit or loss after initial recognition in comprehensive income			
Foreign currency translation differences for foreign operations	<u>122</u>	<u>11</u>	<u>-</u>
Items of other comprehensive loss not to be transferred to profit or loss			
Remeasurement of a defined benefit plan		<u>-</u>	<u>18</u>
Total comprehensive loss for the year attributable to shareholders of the Company	<u>35,353</u>	<u>18,179</u>	<u>29,160</u>

The accompanying notes are integral part of the consolidated financial statements.

Consolidated Statements of Changes in Equity (Loss) for the Year Ended December 31

NIS thousands

	Ordinary share capital	Premium on shares	Translation reserve of foreign operations	Capital reserve for share- based payments	Cumulative deficit	Total capital (deficit)
Balance as at January 1, 2017	7,400	203,015	(11)	5,094	(202,825)	12,673
Issue of shares	2,213	15,728	-	-	-	17,941
Expiry of options	-	537	-	(537)	-	-
Share-based payment	-	-	-	2,626	-	2,626
	<u>2,213</u>	<u>16,265</u>	<u>-</u>	<u>2,089</u>	<u>-</u>	<u>20,567</u>
Comprehensive loss for the year	-	-	(122)	-	-	(122)
Loss for the year	-	-	-	-	(35,231)	(35,231)
	<u>-</u>	<u>-</u>	<u>(122)</u>	<u>-</u>	<u>(35,231)</u>	<u>(35,231)</u>
Balance as at December 31, 2017	9,613	219,280	(133)	7,183	(238,256)	(2,113)
Balance as at January 1, 2016	4,889	183,935	-	4,179	(184,657)	8,346
Issue of shares	2,511	18,957	-	-	-	21,468
Expiry of options	-	123	-	(123)	-	-
Share-based payment	-	-	-	1,038	-	1,038
	<u>2,511</u>	<u>19,080</u>	<u>-</u>	<u>915</u>	<u>-</u>	<u>22,506</u>
Comprehensive loss for the year	-	-	(11)	-	-	(11)
Loss for the year	-	-	-	-	(18,168)	(18,168)
	<u>-</u>	<u>-</u>	<u>(11)</u>	<u>-</u>	<u>(18,168)</u>	<u>(18,179)</u>
Balance as at December 31, 2016	7,400	203,015	(11)	5,094	(202,825)	12,673
Balance as at January 1, 2015	3,005	167,730	-	4,180	(155,497)	19,418
Issue of shares	1,884	15,945	-	-	-	17,829
Share-based payment	-	260	-	(1)	-	259
	<u>1,884</u>	<u>16,205</u>	<u>-</u>	<u>(1)</u>	<u>-</u>	<u>18,088</u>
Comprehensive loss for the year	-	-	-	-	(18)	(18)
Loss for the year	-	-	-	-	(29,142)	(29,142)
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(29,160)</u>	<u>(29,160)</u>
Balance as at December 31, 2015	4,889	183,935	-	4,179	(184,657)	8,346

The accompanying notes are integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows for the Year Ended December 31

NIS thousands

	Note	2017	2016	2015
Cash flows from operating activities				
Loss for the year		(35,231)	(18,168)	(29,142)
Finance costs, net	13	933	213	1,270
Depreciation for fixed assets		185	156	86
Share-based payments	9	2,626	1,038	259
Income tax	14	1,157	523	-
Change in other receivables	5	735	447	(2,208)
Change in liabilities to trade payables		157	(1,884)	1,644
Change in other payables	6	165	3,610	(750)
Change in employee benefits		(7)	(230)	158
Change in long-term prepaid expenses		(12)	2	15
Change in liability for refund of a grant		-	-	41
Taxes paid		(1,303)	-	-
Interest paid		-	-	(57)
Interest received	13	8	2	7
Net cash used in operating activities		(30,587)	(14,291)	(28,677)
Cash flows from investment activities				
Change in other investments		-	589	4,687
Purchase of property, plant and equipment		(121)	(291)	(339)
Net cash from financing activities (used for activities)		(121)	298	4,348
Investment		(121)	298	4,348
Cash flow from financing activities				
Repayment of a liability for a grant		-	-	(447)
Proceeds from the issue of share capital	8	20,696	24,854	18,024
Issuing costs		(1,545)	(1,679)	(195)
Net cash provided by financing activities		19,151	23,175	17,382
Increase (decrease) in cash and cash equivalents		11,557	9,182	(6,947)
Cash and cash equivalents at the beginning of the year		17,550	8,595	16,822
Effect of fluctuations in the rate of exchange on cash and cash equivalents		(953)	(227)	(1,280)
Cash and cash equivalents at the end of the year	4	5,040	17,550	8,595

The accompanying notes are integral part of the consolidated financial statements.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 1 – GENERAL

- A. The Company was incorporated and registered in Israel on September 22, 2011, in accordance with the Companies Law, 1999 ("the Companies Law"), as a private company limited by shares called BioCancell Ltd. ("the Company"). The official address of the Company is 1/3 High Tech-Village, Edmond J. Safra Campus, Givat Ram, Jerusalem. The Company is a continuing company of BioCancell Therapeutics Inc., which was incorporated in 2004 and began trading on the Tel Aviv Stock Exchange in 2006. The controlling shareholder of the Company is Clal Biotechnology Industries Ltd. ("CBI") of the Access Industries Group (the ultimate parent company), which holds 44.09% of the Company (as at the approval date of the financial statements).

In May 2016, BioCancell Therapeutics Israel Ltd. established a wholly-owned subsidiary in Delaware, United States, called BioCancell USA Inc. for the purpose of operating in the United States. This company is subject to the tax laws of the state of Delaware.

B. Reporting entity

- (1) The consolidated financial statements of the Company as at December 31, 2017 include those of the Company, BioCancell Therapeutics Israel Ltd. and BioCancell USA Inc., which is wholly-owned by the Company.
- (2) The Group is involved in research and development of drugs for treatment of cancer. The Group's products are in the research and development stage, and therefore there is no certainty regarding the Group's ability to complete product development, obtain regulatory approvals and achieve marketing success. Continuation of the development stages and disposal of assets related to the planned activities depend on future events, including raising additional capital and achieving operational profitability in the future. The Group is taking steps to raise the capital required for the continuation of its operations, however as at the reporting date, there is significant doubt as to the Group's ability to continue to operate as a going concern. As at the signing date of the financial statements and based on the Group's assessments, the Group's financial resources (including a USD 1 million bridge loan from CBI described in Note 17) are expected to suffice until March 2018. Should CBI extend the Company additional bridge loans totaling USD 2 million, at CBI's exclusive discretion, the Group's financial resources would be expected to suffice until April 2018. And to the extent that a full USD 25 million private placement whose Term Sheet is described in Note 17 is successfully concluded, the Group's financial resources would be expected to suffice until the third quarter of 2019. The financial statements do not include any measurement or presentation adjustment for assets and liabilities that would be required if the Group does not continue operating as a going concern.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 1 – GENERAL (CONTD.)**C. Separate financial information in accordance with Regulation 9C**

In February 2015, the Israel Securities Authority (no action) confirmed that the Company periodic financial statements for 2014 should not include separate financial information in accordance with Regulation 9C and the Tenth Schedule to the Israel Securities Regulations (Periodic and Immediate Reports), 1970, following the reorganization in the Company in previous years, and repayment and conversion of the convertible loans and exercise of the options, such that subsequent to these processes, most of the Group's operations are performed in the subsidiaries, and therefore the separate financial statements will not include any additional material information for the reasonable investor that is not already included in the consolidated financial statements.

The Company assessed, quantitatively and qualitatively, the negligibility of the additional information derived from the financial information compared to the consolidated financial statements according to the following parameters:

- The percentage of the Company's assets out of the total consolidated assets of the Group
- The percentage of the Company's liabilities out of the total consolidated liabilities of the Group
- The percentage of the Company's cash flow from operating activities out of the total cash flow from operating activities in the consolidated financial statement

For further information about relationships and agreements between the parent company and the subsidiaries, see Note 18 (Transactions and Balances with Interested and Related Parties).

D. Definitions

In these financial statements -

- (1) The Company – BioCancell Ltd
- (2) The Group – BioCancell Ltd. and its subsidiaries
- (3) Subsidiaries – the subsidiary of the Company, BioCancell Therapeutics Israel Ltd. and its subsidiary BioCancell USA, Inc., the financial statements of which are fully consolidated with those of the Company and which are fully owned and controlled by the Company
- (4) Related party - Within its meaning in IAS 24 (2009), Related Party Disclosures
- (5) Interested parties - Within their meaning in Paragraph (1) of the definition of an “interested party” in Section 1 of the Israel Securities Law – 1968

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 2 - BASIS OF PREPARATION**A. Statement of compliance**

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The financial statements have also been prepared in accordance with the Securities Regulations (Annual Financial Statements), 2010.

The consolidated financial statements were authorized for issue by the Company's Board of Directors on March 22, 2018.

B. Functional and presentation currency

These consolidated financial statements are presented in NIS, which is the Group's functional currency, and have been rounded to the nearest thousand. The NIS is the currency that represents the principal economic environment in which the Group operates.

C. Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following assets and liabilities: share-based payment and assets and liabilities for employee benefits

D. Operating cycle

The regular operating cycle of the Company is one year. As a result, current assets and current liabilities also include items the realization of which is intended to take place within the period of the Company's regular operating cycle.

E. Classification of expenses recognized in the statement of income

The classification of expenses recognized in the statement of income is based on the nature of the expense. Additional information regarding the nature of the expense is included, as relevant, in the Notes to the financial statements.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 2 - BASIS OF PREPARATION (CONTD.)**F. Use of estimates and judgments**

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

The preparation of accounting estimates used in the preparation of the Group's financial statements requires that management of the Company makes assumptions regarding circumstances and events that involve considerable uncertainty. Management of the Company prepares the estimates on the basis of past experience, various facts, external circumstances, and reasonable assumptions according to the pertinent circumstances of each estimate.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

G. Determination of fair value

Preparation of the financial statements requires the Group to determine the fair value of certain assets and liabilities.

Note 9D, Share-based Payment, includes further information about the assumptions that were used to

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently by Group entities for all periods presented in these consolidated financial statements.

A. Basis of consolidation

A subsidiary is an entity controlled by the Company. The consolidated financial statements of the subsidiary are included in the consolidated financial statements from the date that control is gained. The accounting policies of the subsidiary are aligned with the policies adopted by the Group.

Transactions eliminated on consolidation

Intra-group balances and any unrealized income and expenses arising from intra-group transactions, are eliminated in the preparation of the consolidated financial statements.

B. Foreign currency

Transactions in foreign currencies are translated to the functional currency of the Group at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. Exchange rate differences are recognized in profit or loss.

C. Foreign operations

The assets and liabilities of a foreign operation were translated to NIS in at the exchange rate in effect at the reporting date. The income and expenses of the foreign operation are translated to NIS at exchange rates at the dates of the transactions. Foreign currency differences arising on translation are recognized in other comprehensive income and are presented in equity in the translation reserve of the foreign operation – ("Fund of Translation Differences in Foreign Operations").

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)**D. Financial instruments (contd.)****(1) Non-derivative financial assets**

Non-derivative financial assets include cash and cash equivalents, trade receivables and trade payables. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

A financial asset is recognized when the Group accepts the contractual conditions of the instrument. A financial asset is derecognized when the Group's contractual rights to receive the cash flows deriving from the financial asset expires, or the Group transfers the financial asset to others without maintaining control of the asset or transfers all the risks and rewards deriving from the asset. Regular way purchases and sales of financial assets are recognized on the date of the transaction, meaning on the date the Group undertook to purchase or sell the asset. Financial liabilities are derecognized when the obligation of the Group, as specified in the agreement, expires or when it is discharged or cancelled.

Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, receivables are measured at amortized cost using the effective interest method, taking into account transaction costs and less impairment losses.

Cash and cash equivalents

Cash comprises cash balances available for immediate use and call deposits. Cash equivalents comprise short-term highly liquid investments with original maturities of three months or less, which are readily convertible into known amounts of cash and are exposed to insignificant risks of change in value.

Non-derivative financial liabilities

Non-derivative financial liabilities include trade and other payables.

(2) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognized as a deduction from equity.

Incremental costs directly attributable to an expected issuance of an instrument that will be classified as an equity instrument are recognized as an asset (deferred issuance expenses) in the statement of financial position under receivables. The costs are deducted from the equity upon the initial recognition of the equity instruments, or are amortized as general and administrative expenses in the statement of income when the expected issuance is for a period exceeding six months from the incremental costs are incurred.

E. Property and equipment**Recognition and measurement**

Fixed asset items are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset. Depreciation is a systematic allocation of the depreciable amount of an asset over its useful life.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)**F. Intangible assets****Research and development**

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognized in profit or loss when incurred. Development activities involve a plan or design for the production of new or substantially improved products and processes. Development expenditure is recognized as an intangible asset only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Group has the intention and sufficient resources to complete research and development and to use or sell the asset.

None of the Company's development costs meet the above conditions, therefore are recognized in the statement of income as incurred.

See also Note 3(J) below regarding the offset of grants for participation in research and development expenses

G. Impairment**(1) Financial assets**

A financial asset is tested for impairment when objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

Impairment losses are recognized in profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost, the reversal is recognized in profit or loss.

(2) Non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the recoverable amount of the asset is estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs of disposal. In assessing value in use, the Group discounts the future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, the assets are grouped together into the smallest group of assets that generates cash from continuing use that are largely independent of other assets or groups of assets ("the Cash-Generating Unit").

An impairment loss is recognized if the carrying amount of an asset or cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)**H. Employee benefits**

The Group has a number of post-employment benefit plans.

(1) Employee benefit plans

The Group's net obligation in respect of defined benefit pension plans, up to April 1, 2014, is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is presented at its present value, and the fair value of any plan assets is deducted. The discount rate is the yield at the reporting date on high-quality linked corporate debentures, that have maturity dates approximating the terms of the Group's obligations and that are denominated in NIS. The calculations are performed by an actuary.

Remeasurements of the net defined benefit liability (asset) comprise actuarial gains and losses, the return on the plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). Remeasurements are recognized immediately, directly in retained earnings through other comprehensive income. The liability for a benefit accumulated until the date of change of this plan is NIS 708 thousand, and is presented net of the fair value of plan assets in the amount of NIS 719 thousand.

On April 1, 2014, the Company entered into an agreement with Israeli employees whereby as from that date they are eligible for severance pay under Section 14 of the Severance Pay Law, 1963, and as of that date, it classified as a defined contribution plan. A defined contribution plan is a post-employment benefit plan under which the Group pays fixed contributions into a separate entity and has no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognized as an expense in profit or loss in the periods during which related services are rendered by employees.

(2) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided or upon the actual absence of the employee when the benefit is not accumulated (such as maternity leave).

The employee benefits are classified as short-term benefits or as other long-term benefits depending on when the Group expects the benefits to be wholly settled,

A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(3) Termination benefits

Termination benefits are recognized as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment.

(4) Share-based payments

The fair value on the grant date of share-based payment awards granted to employees is recognized as a salary expense, with a corresponding increase in equity, over the period that the employees become eligible for the awards. The amount recognized as an expense, conditional upon meeting service conditions, is adjusted to reflect the number of awards that are expected to vest. For share-based payment awards with non-vesting conditions or with market performance vesting conditions, the grant date fair value of the share-based payment awards is measured to reflect such conditions, and therefore the Group recognizes an expense in respect of the awards whether or not the conditions have been met.

In transactions in which the parent company or the subsidiaries grant their employees rights to the equity instruments of the parent company, the Group accounts for the award as equity-settled share-based payment transactions.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)**I. Provisions**

A provision is recognized if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Legal claims

A provision for claims is recognized if, as a result of a past event, the Company has a present legal or constructive obligation and it is more likely than not that an outflow of economic benefits will be required to settle the obligation and the amount of obligation can be estimated reliably. When the value of time is material, the provision is measured at its present value.

Commitments to pay royalties

The Group does not recognize commitments to pay royalties until the event underlying the commitment occurs.

J. Participation grants in research and development expenses

Grants are recognized initially at fair value when there is reasonable assurance that they will be received and the Group will comply with the conditions associated with the grant. Grants that compensate the Group for expenses incurred are presented as a deduction from the corresponding expense.

Grants from the Chief Scientist in respect of research and development projects are accounted for as forgivable loans according to IAS 20. Grants received from the Chief Scientist are recognized as a liability according to their fair value on the date of their receipt, unless on that date it is reasonably certain that the amount received will not be refunded. The amount of the liability is reexamined each period, and any changes in the present value of the cash flows discounted at the original interest rate of the grant are recognized in profit or loss. The Group operates in the biotechnology industry and there is significant uncertainty (due to the preliminary stage it is in and the substantial financing that is required) regarding the success of the products under development and the return of the grant. The Company believes that as at the reporting date, the conditions for recognition of the commitment have not been fulfilled. Accordingly, the Group did not record a liability for the receipt of these grants.

K. Leases

The Group's leases are classified as operating leases and the leased assets are not recognized in the Group's statement of financial position. Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease.

L. Financing income and expenses

Financing income comprises interest income on funds invested and exchange rate differences. Interest income is recognized as it accrues using the effective interest method.

Financing expenses include bank and other commissions. Borrowing costs are recognized in profit or loss using the effective interest method.

In the statements of cash flows, interest received and interest paid are presented as cash flows from investing activities

Foreign currency gains and losses are reported on a net basis as either financing income or financing expenses depending on foreign currency fluctuations.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 3 – SIGNIFICANT ACCOUNTING POLICIES (CONTD.)**M. Loss per share**

The Company presents basic and diluted loss per share data for its ordinary shares. Basic loss per share is also the diluted loss calculated by dividing the loss attributable to ordinary shareholders of the Group by the weighted average number of ordinary shares outstanding during the period.

N. Income tax expenses

Income tax comprises current and deferred tax. Current and deferred taxes are recognized in the statement of income except to the extent that it relates to a business combination, or are recognized directly in equity or in other comprehensive income to the extent they relate to items recognized directly in equity or in other comprehensive income.

Current taxes

Current tax is the expected tax payable (or receivable) on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date.

Offsetting current tax assets and liabilities

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

O. New standards and interpretations not yet adopted**IFRS 9 (2014), Financial Instruments (in this section: "IFRS 9 (2014)")**

IFRS 9 (2014) replaces the current provisions in IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 (2014) includes revised guidance on the classification and measurement of financial instruments.

The standard will be implemented for annual periods starting on January 1, 2018, with the possibility of early adoption.

The Group has assessed the implications of adopting the standard and in the Group's opinion, adoption of the standard is not expected to have a material effect on the financial statements.

IFRS 16, Leases ("IFRS 16")

IFRS 16 replaces IAS 17, Leases and its related interpretations. For lessees, the new standard presents a unified model for the accounting treatment of most leases according to which the lessee has to recognize an asset and a lease liability in its financial statements.

IFRS 16 is applicable for annual periods as of January 1, 2019, with the possibility of early adoption, so long as the Company has also early adopted IFRS 15, Revenue from Contracts with Customers.

IFRS 16 includes various alternative transitional provisions, so that companies can choose between one of the following alternatives at initial application: full retrospective application or recognizing a cumulative effect, which means application (with the possibility of certain practical expedients) as from the mandatory effective date with an adjustment to the balance of retained earnings at that date.

The Group has commenced assessing the implications on the financial statements of adopting the standard.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 4 – CASH AND CASH EQUIVALENTS

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
	<u>NIS thousands</u>	
NIS:		
Cash	1,052	920
Cash equivalents	62	40
Foreign currency:		
Cash	3,926	16,590
	<u>5,040</u>	<u>17,550</u>

The Group's exposure to interest rate risk, foreign currency risk and a sensitivity analysis in respect of cash and cash equivalents balances is included in Note 10 on financial instruments.

NOTE 5 – OTHER RECEIVABLES

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
	<u>NIS thousands</u>	
Value added tax authorities	253	496
Deferred acquisition expenses	918	2,150
Prepaid expenses	163	651
Others	54	39
	<u>1,388</u>	<u>3,336</u>

For the Group's exposure to foreign currency and liquidity risks for trade receivables, see Note 10.

NOTE 6 – OTHER PAYABLES

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
	<u>NIS thousands</u>	
Institutions and employees for salary	333	550
Expenses payable	7,921	7,567
	<u>8,254</u>	<u>8,117</u>

For the Group's exposure to exchange and liquidity risks for other payables, see Note 10, Financial Instruments.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 7 – CONTINGENT LIABILITIES AND AGREEMENTS**A. Liability for royalty payments to the Chief Scientist**

The Group has financed part of its research and development activities with grants from the Office of the Chief Scientist in the Ministry of Trade and Industry ("the OCS"). In return for OCS grants, royalties of 3%-5% are payable by the Group on revenues derived from the product, which was developed with the support of a grant from the OCS, up to the full payment of the grant, linked to the USD exchange rate. As from 2013, no new applications were submitted to the OCS.

As at December 31, 2017, the Group's maximum liability for repayment of the royalties is estimated at USD 3.9 million. The transfer of its all or part of production outside of Israel requires higher payments of royalties, of up to 2% of the total liability. The Group has yet to start paying royalties. The financial statements do not include a liability for royalties for these grants, since the conditions for recognition of the liability have not been fulfilled (see also Note 3J above).

B. Royalties agreement

The research and development activities of the Group are based on an exclusive license granted to the Group to use patent-protected technology and/or applications for the registration of patents developed by the Group.

The rights to these patents originally belonged to Yissum Technology Transfer, the research development company of The Hebrew University of Jerusalem ("Yissum"). Under the 2005 license agreement between Yissum and the Group, and the amendments to the agreement ("the License Agreement"), Yissum granted an exclusive license to the Group for the global development, use, manufacture and commercialization of products that are based on the patents. In return, the Group undertook to pay royalties to Yissum at the following rates:

- (1) 4% of sales net of distribution costs
- (2) 10% of the total consideration received by the Group from any third party obtaining a sub-license to use the Group's technologies

The rate of royalties from sales in countries where a patent has not been registered, in which a third party sells identical products, will be reduced by 50%.

The Group does not recognize a liability for royalties until the event underlying the liability actually occurs and therefore the financial statements do not include a liability for these royalties.

Regarding the payment period of the royalties, it was determined that for the country in which the patent was registered, the payment period of the royalties will continue until the later of: (A) the expiry date of the patent in that country; (B) the expiry of the exclusivity period (set by an authorized entity in that country) for a product based on the patent; or (C) nine years from the date of the first commercial sale in that country. For countries in which no patent has been registered with success, the payment period of the royalties for sales in a specific country will continue until the later of: (A) the expiry date of the regulatory exclusivity in that country; or (b) nine years from the date of the first commercial sale in that country.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 7 – CONTINGENT LIABILITIES AND AGREEMENTS (CONTD.)**B. Royalties agreement (contd.)**

The license will remain valid for all countries after the end of the royalty period as well, whether for countries in which a patent was registered or countries in which a patent was not registered, when the Group will have an irrevocable, unlimited license which is exempt from payment of royalties (for sales in that country).

The Group has undertaken to indemnify Yissum and The Hebrew University of Jerusalem, their employees, officers, representatives and any person acting on their behalf ("the Indemnitees") from any liability, including product liability, damages, losses, expenses, fees and reasonable legal expenses ("the Damages") that they may incur due to the acts and omissions of the Group, and/or arising from the use, development, production, marketing, sale and/or grant of a biotechnology sublicense, unless the Damages were due to gross or malicious negligence by the Indemnitees. In addition, before the clinical trials started and prior to the first commercial sale, the Group undertook to purchase comprehensive liability insurance for product liability and the Group's undertaking for their indemnification and to add Yissum as an additional insured party. The Group also undertook to purchase, at its expense, when the clinical trials begin, a liability insurance policy for clinical trials in an appropriate amount and in accordance with commercial practice. The Group acquired insurance for the clinical trials it finances.

C. Agreements for clinical trials ("the Research Agreements") between the Group and medical centers ("the Hospitals")

The Group has signed Research Agreements with medical centers, according to which the Hospitals will perform clinical trials to assess the effect of the drug under development by the Group. In accordance with the Research Agreements, the Group will finance the clinical trials, including the supply of the drug used in the trial. The consideration for the Hospitals depends on the number of patients participating in the trials, the duration of their treatment, and the number of hospital visits by the patient. The Group undertook to indemnify the Hospitals, including the medical teams participating in the trials, against any claim arising from the trials, as long as the trials were carried out in accordance with the Research Agreements, and the damage was not caused by the negligence of the Hospitals. The Group undertook to insure the hospitals, including the directors and employees involved in the trials, in a liability insurance policy of at least USD 5,000,000 per case. These liabilities will also continue to be in effect after the termination of the Research Agreements. Payments for the insurance policies are recorded as a current expense in the statement of income as expenses for clinical trials under research and development.

D. Research and development services agreement

Most of the Group's research and development are performed by the research laboratory staff at The Hebrew University of Jerusalem. The Group signed an agreement for research and development services with Yissum on January 1, 2015, which expired in December 2017. As from the beginning of 2018, the Group continues to carry out research and development through employees that it employs directly.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 8 – CONTINGENT LIABILITIES AND AGREEMENTS (CONTD.)**E. Car rentals**

The Group has agreements to lease five cars for 12-36 months each. In respect of these agreements, the Company has made deposits to secure future lease commitments. As at the balance sheet date, the balance of these deposits is NIS 40 thousand. The deposits are linked to the CPI and do not bear interest.

At the end of the reporting period, the minimum rent to be paid for the lease agreements is as follows:

	<u>NIS thousands</u>
2018	183
2019	110
2020	50
	<hr/>
	343
	<hr/>

F. Office rental

In November 2013, the Company signed a new rental agreement with MPNAT in the Edmund J. Safra High-Tech Village in Givat Ram, Jerusalem, from March 2014 to September 2016, which was extended until September 2021. The total monthly rental fees will be NIS 16 thousand. Under the agreement, a guarantee of NIS 63 thousand was provided through Bank Leumi in favor of the property owner. The minimum future rental fee for the rental agreements is NIS 48 thousand. In January 2018, the Group signed an agreement to rent offices and new laboratories (for further information, see Subsequent Events see note 17).

In addition, in July 2016, the subsidiary BioCancell USA Inc. and Vedantra Pharmaceuticals, Inc. signed a one-year rental agreement for offices in the United States with monthly rental fees of USD 5 thousand. This agreement was extended for another year. The minimum future rental under the rental agreements is USD 33 thousand.

G. Commitment to pay royalties to the Jerusalem Development Authority

In 2009, the Company received a grant of NIS 135 thousand from the Jerusalem Development Authority. In return for the grant, the Company is required to pay royalties of 4% of revenues from sales, until the CPI-linked grant is fully repaid. The financial statements do not include a liability for this grant because there is significant uncertainty regarding the repayment of the grant.

H. Production agreements and development of production processes

In October 2017, the Group signed a new binding order with the European pharmaceutical manufacturer Boehringer Ingelheim ("BI"), for production of BC-819 ("the Drug") for EUR 2.6 million in 2018. According to the terms of the order, if the Group cancels all or part of the order, BI may charge the Group cancellation fees at rates that are a function of the proximity between the cancellation date and the planned date for performing of the work.

I. Agreement with an investment banker

The Company has an agreement with the US investment bank Raymond James & Associates, Inc., according to which it will provide investment banking services to the Company in return for 7% of the gross consideration of private placements (a fee of only 3.5% of the consideration of up to USD 5 million to be received from the Company's controlling shareholder). The aggregate fee for the US distributor will not, in any case, be less than USD 1 million.

J. Business development consultation agreement

The Company has signed an agreement with Locust Walk, a US business development advisory company, to promote strategic partnering for BC-819, the Company's lead product.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 8 – EQUITY

A. Share capital

	Number of ordinary shares	
	2017	2016
Ordinary shares of NIS 0.10 par value each		
Issued and paid up share capital as of January 1	73,997	48,892
Issued during the year	22,134	25,105
Issued and paid up share capital as of December 31	96,131	73,997
Registered capital	190,000	190,000

B. Issuances

Summary of the issuances for raising capital between 2015 and 2017:

Date	Class	Shares	Consideration (gross in NIS thousands)	Participation of the controlling shareholder (NIS thousands)	Issuance expenses (NIS thousands)	Benefit component [^]
April 2017	Public offering of shares (1)	22,134,300	20,696	-	2,755*	Not applicable
October 2016	Private placement (2)	23,076,922	22,805	-	# 3,236	Not applicable
June 2016	Rights issue (3)	2,028,047	2,048	2,000	150	-
March 2015	Rights issue	17,934,058	17,934	15,400	195	12.61%

[^] The benefit component is calculated as the ratio between the base trading price of the share ex-rights and the closing price of the share on the trading day preceding the ex date, which is the ratio that is the basis for the increase in the number of underlying shares from the Company's options at the time of the rights issue.

* Of this amount, NIS 1,214 thousand has not yet been paid in cash

** Of this amount, NIS 1,338 thousand has not yet been paid in cash.

- (1) In April 2017, the Company issued shares to the public pursuant to a shelf offering report. In the offering, the Company issued 22,134,300 ordinary shares to the public, at a price per share of NIS 0.935 (USD 0.26 at the USD exchange rate on that date) and for a gross consideration of NIS 20,696 thousand (USD 5,665 thousand). The actual issuance costs amounted to NIS 2,755 thousand.

To the best of the Company's knowledge and as it was informed, in the issuance, Palisade Capital Management LLC ("Palisade") and Patata Beroa LLC ("Patata"), acquired 18,482,000 and 769,300 ordinary shares, respectively, following their announcement to the Company in March 2017, according to which they reached agreements with Edgewater Partner Holdings Limited ("Edgewater"), a company incorporated in Samoa, whereby Edgewater will purchase 18,461,538 ordinary shares from Palisade for a consideration of USD 4.8 million, and will acquire 769,231 ordinary shares from Patata for a consideration of USD 0.2 million. It should be noted that the sold shares, which Palisade and Patata purchased from the Company in a private placement, are subject to the remaining lock-up periods set out in Section 15C of the Israel Securities Law.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 8 - EQUITY (CONTD.)**B. Issuances (contd.)**

- (2) In October 2016, the Company completed a private placement to two investors from the United States, in which the Company allotted 18,461,538 of the Company's ordinary shares of NIS 0.10 par value each to Palisade Medical Equity I LP (24.95% of the Company's equity and voting rights subsequent to the allotment, and 24.69%, fully diluted), in consideration for an investment of USD 4.8 million, plus 4,615,384 ordinary shares to Patata Beroa LLC (6.24% of the Company's equity and voting rights and 6.17%, fully diluted) in consideration for an investment of USD 1.2 million (jointly below: "the Private Placement"). The price paid per share amounted to USD 0.26. The total number of shares allotted to investors in the the Private Placement 31.19% of the Company's issued and paid-up share capital and voting rights in the Company subsequent to the Private Placement and 30.86%, fully diluted.
- (3) In June 2016, the Company raised a gross amount of NIS 2,048 thousand (of which NIS 2,000 thousand was from CBI) by way of a rights issue to shareholders, according to a shelf offering memorandum and in accordance with the Company's shelf prospectus of October 21, 2013. In accordance with the shelf offering memorandum, 23,008,128 of the Company's ordinary registered shares of NIS 0.10 par value each were offered to the Company's shareholders by way of rights, such that for every 102 ordinary shares, a shareholder in the Company was entitled to exercise one rights unit, which included 48 ordinary shares at NIS 1.01 per share (NIS 48.48 per unit). The rights holders purchased 2,028,047 of the Company's ordinary shares (42,251 rights units), representing 8.81% of the offered securities.

There were no placements in accordance with the Company's commitment to allot anti-dilutive shares between 2016 and 2017. It should be noted that the investor was offered 74,061 shares in 2015 and 250,266 shares in 2013, but the investor has not yet transferred the minimum consideration to the Company in accordance with the TASE bylaws. In addition, the Company has no commitments to issue anti-dilutive shares, and the Company has no valid agreements that include an anti-dilution provision.

Fully-diluted capital of the Company

As at December 31, 2017, the Company's fully diluted share capital consists of the securities described in Note 8A above and Note 9A below, only.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 9 - SHARE-BASED PAYMENTS

- A. The table below summarizes the terms of the grants and the number of options granted by the Company and not yet exercised, foreclosed or expired by December 31, 2017:

<u>Grant Date</u>	<u>Number of options</u>	<u>No. of underlying shares (1)</u>	<u>Exercise price per share (1)</u>	<u>Actual vesting date</u>	<u>Contractual life of options</u>
2008	335,000	39,448	NIS 10.78	3-4 years (2)	10 years
2009	38,000	4,475	NIS 26.92	4 years (2)	10 years
2010	30,000 *	3,533	NIS 26.92	3 years (3)	10 years
	140,000	16,486	NIS 24.20	3 years (3)	10 years
2011	300,000 *	35,327	NIS 24.63	4 years (2)	10 years
2013	150,000	17,663	NIS 8.66	4 years (2)	10 years
2014	130,000**	146,393	NIS 2.34	4 years (2)	10 years
2015	20,000	22,522	NIS 1.17	4 years (2)	10 years
	201,000**	201,000	NIS 1.21	4 years (2)	10 years
2016	5,627,816 *	5,627,816	USD 0.26	4 years (4)	10 years
2017	1,649,416**	1,649,416	USD 0.29	4 years (4)	10 years
	1,010,000**	1,010,000	USD 0.29	4 years (5)	10 years
	3,193,533**	3,193,533	NIS 0.91	4 years (5)	10 years
	40,000	40,000	USD 0.25	4 years (5)	10 years
	200,000	200,000	USD 0.39	2 years (6)	10 years
Total as of December 31 2017	<u>13,064,765</u>	<u>12,207,612</u>			

* These options were granted to interested parties or key managerial personnel in the Group (see also Note 16D).

** Some of the options were granted to interested parties and/or key managerial personnel in the Group (3,652,949 options in 2017; 60,000 options in 2015; and 40,000 options in 2014).

- (1) After historical adjustments in the Company's capital, mainly capital consolidation in 2013
- (2) The options will vest in 16 equal quarterly lots.
- (3) The options will vest in 12 equal quarterly lots.
- (4) The options will vest in four equal annual lots, one year after commencement of the transaction.
- (5) 25% of the options will vest after one year, and the remainder in 12 equal quarterly lots over 4 years.
- (6) The options will vest in 8 equal quarterly lots.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 9 - SHARE-BASED PAYMENT (CONTD.)

B. The table below presents the movement in options and the weighted average of the exercise price per share (after the required adjustments*):

	2017			2016			2015		
	Shares underlying options *	Weighted average of exercise price per share		Shares underlying options *	Weighted average of exercise price per share		Shares underlying options *	Weighted average of exercise price per share	
		NIS	USD		NIS	USD		NIS	USD
In circulation at the beginning of the period	6,330,522			816,519			437,965		
Addition due to issue of rights in 2015	-			-			55,228		
Granted during the year (NIS)	3,193,533	0.91	-	-	-	-	378,026	1.21	-
Granted during the year (USD)	2,899,416**	-	0.30	-	-	-	-	-	-
	*			5,627,816		0.26	-		-
Expired during the year	(14,277)	1.40	-	(86,020)	1.40	-	(23,068)	3.11	-
Expired during the year (NIS)	(187,451)	6.55	-	(21,993)	7.81	-	(31,632)	13.00	-
Expired during the year (USD)	(14,131)	-	5.07	(5,800)	-	0.68	-	-	-
Total shares arising from options in circulation at the end of the period	12,207,612			6,330,522			816,519		
Composition									
Average exercise supplement (NIS)	3,680,380	1.52	-	688,575	5.70	-	796,588	5.29	-
Average exercise supplement in USD	8,527,232	-	0.27	5,641,947	-	0.27	19,931	-	3.79

* Subsequent to consolidation of the Company's capital in a ratio of 10:1, the Company's rights issue of 2014, which included a benefit of 4.57%, and the Company's rights issue of 2015, which included a benefit of 12.61%

** The weighted average of the contractual life of the options in circulation as at December 31, 2017 is 8.8 years (as at December 31, 2016, 7.95 years).

*** Including 200,000 options, approved for allotment by the Company in 2017 and which were actually allotted in 2018.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 9 - SHARE-BASED PAYMENT (CONTD.)

- C. The table below presents information about the average exercise supplement for options exercisable at the end of the period:

	December 31, 2017		December 31, 2016		December 31, 2015	
	No. of underlying shares)	Exercise price per share	No. of underlying shares	Exercise price per share	No. of underlying shares	Exercise price per share
Options with an exercise price denominated in NIS	432,374	NIS 6.04	522,832	NIS 7.03	408,957	NIS 8.75
Options with an exercise price Denominated in USD	2,219,308	USD 0.27	14,131	USD 5.07	19,931	USD 3.79
Total shares arising from options	2,651,682		536,963		428,888	

- D. The fair value of the services received in consideration of the options granted, based on the fair value of the granted options, based on the Black and Scholes pricing model:

	Granted in 2017	Granted in 2016
Fair value at the grant date	(NIS 3,727 thousand)	USD 3,123 thousand
The following parameters were used in the model:		
Share price at the grant date	NIS 0.88 - NIS 1.36	USD 0.23
Adjusted exercise supplement	NIS 0.91 - NIS 1.36	USD 0.26
Expected fluctuations (1)	66.9% - 78.1%	69.23%
Expected life of the option (2)	5.13 - 7.06 years	7 years
Risk-free interest rate (3)	0.86% - 2.75%	2.06%
Rate of expected dividends	-	-

- (1) The anticipated fluctuations were based on historical fluctuations of the Company's share price.
- (2) For options granted to the CEO, the expected life is subject to certain conditions as set out Note 16E and will be assessed in each period in accordance with the probability of their occurrence.
- (3) The risk-free interest rate was based on the yield to maturity of Israeli government bonds for options with an NIS-linked exercise price linked and of US Treasury Securities for options with a USD-linked exercise price, with their duration to maturity equal to the expected life of the options.

- E. Salary expenses for share-based payment (see also Notes 11 and 12)

	Year ended December 31		
	2017	2016	2015
	NIS thousands	NIS thousands	NIS thousands
Share options granted in 2011, net	-	-	1
Share options granted in 2012, net	-	-	16
Share options granted in 2013, net	-	4	13
Share options granted in 2014, net	9	38	98
Share options granted in 2015, net	13	32	131
Share options granted in 2016, net	1,139	964	-
Share options granted in 2017, net	1,465	-	-
	2,626	1,038	259

Regarding options granted to related parties, see also Note 16 about transactions and balances with related parties and interested parties.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 10 - FINANCIAL INSTRUMENTS

The Group has exposure to the following risks from its use of financial instruments:

- * Credit risk
- * Liquidity risk
- * Market risk

A. Framework for risk management

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policy was formulated to identify and analyze the risks that the Group faces, to set appropriate limits for the risks and controls, and to monitor the risks and their compliance with the limits. The risk policy and risk management methods are reviewed regularly to reflect changes in market conditions and in the Group's operations. The Group acts to develop an effective control environment in which all employees understand their roles and commitment.

B. Credit risk

Credit risk is the risk of financial loss to the Group if a debtor or counterparty to a financial instrument fails to meet its contractual obligations, and arises mainly from the Company's receivables. The Group restricts exposure to credit risk by investing in bank deposits only.

Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was as follows:

	December 31	
	2017	2016
	Carrying amount	
	NIS thousands	NIS thousands
Cash and cash equivalents	5,040	17,550
Receivables	253	496
	5,293	18,046

C. Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group ensures that it has sufficient cash on demand to meet expected operational expenses, including amounts required to meet its financial obligations,

This does not take into account the potential effect of extreme circumstances that cannot reasonably be predicted.

See also Note 1B(2) regarding the comment on a going concern.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 10 - FINANCIAL INSTRUMENTS (CONTD.)

C. Liquidity risk (contd.)

The following are the contractual maturities of financial liabilities, including estimated interest payments:

	As of December 31, 2017		
	Carrying amount	Contractual cash	Up to 6 months
	NIS thousands	flows NIS thousands	NIS thousands
Finance liabilities			
Liabilities for trade payables	559	559	559
Other payables	7,921	7,921	7,921
	8,480	8,480	8,480

	As of December 31, 2016		
	Carrying amount	Contractual cash	Up to 6 months
	NIS thousands	flows NIS thousands	NIS thousands
Finance liabilities			
Liabilities for trade payables	410	410	410
Other payables	7,593	7,593	7,593
Total	8,003	8,003	8,003

D. Market risk

Market risk is the risk that changes in market prices, such as foreign currency exchange rates, the CPI, interest rates and the prices of capital instruments, will influence the Group's results or the value of its holdings in financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

Currency risk:

The Group is exposed to currency risk mainly for cash and purchases for R&D expenses that are denominated in USD and EUR. Therefore, the Company is exposed to exchange rate fluctuations in these currencies against the NIS and takes steps to reduce the currency risk by keeping its liquid resources in accordance with its future needs.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 10 - FINANCIAL INSTRUMENTS (CONTD.)

E. CPI and foreign currency risks

- (1) The table below presents the Group's exposure to CPI and foreign currency risks, based on notional amounts:

	December 31, 2017			
	Unlinked	CPI-linked	In foreign currency	Total
	NIS thousands			
Assets				
Cash and cash equivalents	1,115	-	3,925	5,040
Receivables	-	253	-	253
	1,115	253	3,925	5,293
Liabilities				
Trade payables and service providers	350	-	209	559
Other payables	1,736	-	6,185	7,921
	2,086	-	6,394	8,480
	December 31, 2016			
	Unlinked	CPI-linked	In foreign currency	Total
	NIS thousands			
Assets				
Cash and cash equivalents	960	-	16,590	17,550
Receivables	-	496	-	496
	960	496	16,590	18,046
Liabilities				
Trade payables and service providers	256	-	154	410
Other payables	1,651	-	5,942	7,593
	1,907	-	6,096	8,003

- (2) Sensitivity analysis

A change as of December 31 in the exchange rates of the USD and of the EUR against the NIS, as indicated below, and a change in the CPI would have increased (reduced) profit or loss and equity by the amounts presented below. The analysis below is based on foreign currency exchange rate and CPI variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

	December 31, 2017		December 31, 2016	
	Increase	Decrease	Increase	Decrease
	Capital and profit and loss	Capital and profit and loss	Capital and profit and loss	Capital and profit and loss
Change in the CPI of 5%	13	(13)	25	(25)
Change in the exchange rate of the USD by 5%	(165)	165	521	(521)
Change in the exchange rate of Euro at 5%	42	(42)	4	(4)

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 10 - FINANCIAL INSTRUMENTS (CONTD.)

F. Interest rate risk

Type of interest

Type of interest for the Group's interest-bearing financial instruments:

	December 31	
	2017	2016
	NIS thousands	NIS thousands
Fixed-interest instruments		
Financial assets	253	496

G. Fair value

The carrying amounts of financial assets and liabilities, including cash and cash equivalents, other receivables, other short-term investments, trade payables and other payables are the same or proximate to their fair value.

NOTE 11 – RESEARCH AND DEVELOPMENT EXPENSES

	Year ended December 31		
	2017	2016	2015
	NIS thousands	NIS thousands	NIS thousands
Research:			
Sub-contractors	836	905	2,758
Salaries, wages and incidentals	1,340	1,716	2,331
Raw materials, components and consumer goods	254	224	168
Share-based payment	175	39	125
Patents	430	236	280
Amortization and depreciation	172	156	102
Others	193	175	185
	3,400	3,451	5,949
Development			
Development of production processes	6,438	3,876	7,087
Clinical trials development			
Trial management	2,755	749	1,571
Salaries, wages and incidentals	2,104	955	1,056
Materials	7,131	64	7,522
Share-based payment	473	-	19
Others	39	47	73
	12,502	1,815	10,241
Total research and development expenses	22,340	9,142	23,277

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 12 – GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended December 31		
	2017	2016	2015
	NIS thousands	NIS thousands	NIS thousands
Salaries, wages and incidentals	3,887	3,050	1,841
Share-based payment	1,978	999	115
Remuneration of directors	474	670	624
Professionals and experts	2,056	1,533	645
Rent, maintenance and insurance	896	504	477
Investor relations and business development	1,322	301	250
Issuing costs	-	843	-
Travel	583	497	307
Fees	71	127	77
Miscellaneous	107	118	96
	11,374	8,642	4,432

NOTE 13 - FINANCING EXPENSES, NET

	Year ended December 31		
	2017	2016	2015
	NIS thousands	NIS thousands	NIS thousands
Financing income			
Interest income from deposits	5	2	4
Net profit from change in exchange rate	-	162	-
Financing income recognized in profit or loss	5	164	4
Financing expenses			
Net loss from change in exchange rate	350	-	1,382
Interest expenses, bank fees and others	15	25	55
Financing income recognized in profit or loss	365	25	1,437

NOTE 14 – INCOME TAX

A. Information about the tax environment of the Group

(1) BioCancell Ltd. is taxed according to Israeli tax laws.

BioCancell Therapeutics Israel Ltd. is taxed according to Israeli tax laws.

BioCancell USA. Inc. is taxed according to US tax laws.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 15 – INCOME TAX (CONTD.)

A. Information about the tax environment of the Group (contd.)

(2) Rate of corporate tax

(A) Below are the tax rates relevant to Israeli companies in 2015-2017:

2015 - 26.5%

2016 - 25%

2017 - 24%

On January 4, 2016, the Knesset passed Amendment 216 to the Income Tax Ordinance, 2016, which prescribes a gradual decrease of 1.5% in the rate of corporate tax, as from January 1, 2016, to a rate of 25%.

In addition, on December 22, 2016, the Knesset plenum passed the Economic Efficiency Law (Legislative Amendments for Achieving Budget Objectives in 2017 and 2018) – 2016, which stipulates, among other things, a reduction in the corporate tax rate from 25% to 23% in two steps. The first step will be to a rate of 24% as from January 2017 and the second step will be to a rate of 23% as from January 2018.

(B) On January 12, 2012, Amendment 188 to the Tax Ordinance (New Version), 1961 was published in the Official Gazette ("the Ordinance"), which includes an amendment to section 87A, referring to a temporary order. In accordance with the temporary order, Israel Accounting Standard 29 - Adoption of International Financial Reporting Standards (IFRS) will not apply to determining taxable income for the 2007 to 2011 tax years, other than for the preparation of the financial statements ("the Temporary Order"). On July 31, 2014, Amendment 202 to the Ordinance was published, extending the Temporary Order for the 2012-2013 tax years.

(C) The relevant annual tax rates for 2017 for the company in the United States are up to 40%.

(3) Benefits under the Law for the Encouragement of Capital Investments - beneficiary enterprise

BioCancell Therapeutics Israel Ltd. has elected 2009 as the year of election, under the Law for the Encouragement of Capital Investments, 1959. The income generated by the "Beneficiary Enterprise" is exempt from tax over a period of 10 years. The benefits are contingent upon compliance with the terms of the Encouragement Law, including approval to be considered as a biotechnology company. The Company is taking steps to obtain such approval.

B. Tax assessments in Israel and the United States

The Company and BioCancell Therapeutics Israel Ltd. have final tax assessments up to and including the 2012 tax year, as well as deduction assessments that are considered final up to and including 2012.

BioCancell USA Inc. commenced operations in 2016 and the Company has filed its tax returns for this year only.

C. Carryforward tax losses

(1) The Company has carryforward tax losses of USD 13 million and carryforward capital losses of NIS 46 million from the liquidation of BioCancell Therapeutics Inc. (see (3) below).

(2) BioCancell Therapeutics Israel Ltd. has carryforward losses for tax purposes of NIS 175 million and carryforward capital losses of NIS 5 million (at the end of the 2016 tax year - NIS 152 million and carryforward capital losses of NIS 5 million).

(3) BioCancell Therapeutics Inc. was dissolved at the end of 2012 and therefore the Company estimates that its accumulated losses will not be utilized in the future.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 14 - INCOME TAX (CONTD.)

D. Unrecognized deferred tax assets

The Group companies do not create deferred taxes for temporary differences and carryforward losses that require recognition of deferred tax assets, as they do not expect to utilize them in the foreseeable future. According to Israeli tax laws, there is no time limitation on the utilization of losses for tax purposes.

E. Unrecognized deferred tax assets

Unrecognized deferred tax assets for the following items:

	December 31		
	2017	2016	2015
	NIS thousands		
Losses for tax purposes	188,225	161,502	135,832
Deductible temporary differences	24,400	14,389	22,130
Capital loss for tax purposes	51,408	51,408	51,408
	<u>264,033</u>	<u>227,299</u>	<u>209,370</u>

F. Reconciliation between the theoretical tax on pre-tax loss and the tax expenses

	Year ended December 31		
	2017	2016	2015
	NIS thousands		
Loss before income tax	(34,074)	(17,645)	(29,142)
Principal statutory tax rate of the Company	24%	25%	26.5%
Tax calculated at the Company's principal tax rate	(8,178)	(4,411)	(7,722)
Addition (saving) in tax liability for:			
Unrecognized expenses	223	265	72
Different tax rate in subsidiaries operating outside of Israel	463	199	-
Change in temporary differences for which deferred taxes were not recognized	2,009	(1,943)	1,346
Losses and benefits for tax purposes from the year for which deferred taxes were not recorded	6,640	6,413	6,304
Taxes on income from continuing operations	<u>1,157</u>	<u>523</u>	<u>-</u>

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 15 – LOSS PER SHARE

A. Basic loss per share

The calculation of the basic loss per share as of December 31, 2017 was based on the loss attributed to holders of ordinary shares in the amount of NIS 35,231 thousand (in 2016 and 2015): NIS 18,168 thousand and NIS 29,142 thousand, respectively), divided by the weighted average number of ordinary shares in circulation (including the benefit component for retroactive adjustment of a rights issue (Note 8B) of 90,298 thousand shares (in 2016 and 2015: 54,334 thousand shares and 45,538 thousand shares, respectively), calculated as follows:

Weighted average number of ordinary shares:

	Year ended December 31		
	2017	2016	2015
Ordinary shares of NIS 0.1 par value			
Balance as at January 1	73,996	48,892	32,542
Effect of shares issued in the year	16,252	5,442	12,996
Weighted average number of ordinary shares used to calculate basic loss per share	90,248	54,334	45,538

B. Diluted loss per share

The Company did not present data for the diluted loss per share due to the anti-dilutive effect of the convertible securities. See Notes 8 and 9 regarding information about options for the purchase of Company shares which may have a dilutive effect in the future.

At the end of 2017, there were options exercisable for 12,208 thousand shares (including 200,000 options not yet allotted), See Note 9(B) (in 2016 and 2015: options exercisable for 6,253 thousand ordinary shares and 817 thousand ordinary shares, respectively) were not included in the calculation of the weighted average number of ordinary shares (diluted), since their effect is anti-dilutive.

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 16 – TRANSACTIONS AND BALANCES WITH INTERESTED AND RELATED PARTIES**A. Subsidiaries**

The Company holds 100% of the share capital of BioCancell Therapeutics Israel Ltd., which holds 100% of the share capital of the BioCancell USA Inc. The Company has no significant restrictions on the transfer of resources (use of assets or settlement of liabilities) of the Group.

B. Substantial Relations, Agreements and Transactions with Investees**1. Capital note**

In the reporting period, BioCancell Therapeutics Israel Ltd. issued a capital note to the Company in the amount of NIS 27.7 million. The capital note is not linked to the CPI, bears no interest, and there is no intention to repay it before the end of five years. As from the establishment of the Company, capital notes in the amount of NIS 191 million were transferred under the terms mentioned above.

2. Agreement to provide services

As from October 2013, the Company provides management services and business support to its subsidiary, BioCancell Therapeutics Israel Ltd. The subsidiary is charged management fees for the consultancy services. In 2017, management fees amounted to NIS 656 thousand (in 2015-2016 - NIS 656 thousand).

3. Share-based payment

The Company has granted the employees of its subsidiaries options exercisable for Company shares. In 2017, the expenses for these options amounted to NIS 266 thousand (in 2016 - NIS 47 thousand, in 2015 - NIS 153 thousand) and were recorded in the subsidiary. The parent company also granted the sub-subsidiary BioCancell USA Inc. options amounting to NIS 2,152 thousand (in 2016 - NIS 967 thousand)

4. Agreement to provide services

As from May 2016, the subsidiary receives management and supervision services for clinical trials and management and public relations services from its sub-subsidiary BioCancell USA Inc..

Notes to the Consolidated Financial Statements as at December 31, 2017

NOTE 16 – TRANSACTIONS AND BALANCES WITH INTERESTED AND RELATED PARTIES (CONTD.)

C. Benefits for key managers (including directors)

The senior managers in the Group are eligible, in addition to their salary, to non-monetary benefits, such as the use of a company car. The Group contributes to defined post-employment benefit plans.

The senior managers also participate in the options plan for the Company's shares. See Note 9 for information about measurement of share-based payment.

Benefits for key managers (including three directors) employed in the Company include:

	Year ended December 31			
	2017		2016	
	No. of people in the year	Expenditure NIS thousands	No. of people in the year	Expenditure NIS thousands
Short-term employee benefits (including salaries)	3	3,491	4	2,397
Post-employment benefits	1	45	2	80
Share-based payments	5	2,261	5	996
Salary and insurance for outside directors מנעסקים	9	527	9	718
		<u>6,324</u>		<u>4,191</u>

D. Salary of the CEO

In September 2017, 1,649,416 options were allotted to the CEO in accordance with his employment agreement, at an exercise price of USD 0.29 (the fair value of the Company's shares on the approval date of the Board of Directors on this matter), vesting in four lots at the end of each year, from the beginning of his employment in May 2016, at a total cost of USD 292 thousand. 1,434,579 of the options were allotted in accordance with the approval of the general meeting of the Company's shareholders on November 17, 2016, while the remaining 214,837 options were allotted in accordance with the approval of the general meeting on July 20, 2017.

In addition, following the recommendation of the Company's compensation committee and Board of Directors, the general meeting approved the following mechanism for additional grants in the future: The Company will allot the number of additional nonqualified options that are required to bring the CEO's holding to 7% of the Company's fully diluted share capital (after the allotment and exercise of the option) after completion of any capital raising up to (and not including) the earlier of (A) a public offering of the Company in the United States, or (b) two years from the approval date of the general meeting. These allotments will vest in four annual lots from the date of the CEO's employment (May 2016), and the exercise price will be the fair value of the Company's shares at the approval date of the allotment by the Board of Directors, but no less than USD 0.26.

F. D&O insurance policies

In August 2017, the Company purchased D&O insurance policies for itself and for the subsidiary, within the liability limits of USD 10 million for one claim or in aggregate for each insurance period. The policy is valid until August 31, 2018. The annual insurance premiums of the policy are USD 21 thousand. Officers will not pay a deductible, while the Company will cover deductible expenses of USD 7.5 thousand worldwide, except for the United States and Canada, where the deductible is USD 35,000 (USD 100,000 in claims related to the US Securities and Exchange Commission).

NOTE 17 – SUBSEQUENT EVENTS

Notes to the Consolidated Financial Statements as at December 31, 2017

1. On January 22, 2018, the Company signed a term sheet with an investment fund for an investment of USD 25 million in the Company (private placement). According to the term sheet, the investment will be priced at NIS 1.60 per share, reflecting a Company valuation of USD 51 million (fully diluted) before the money. The investment fund will invest at least USD 7 million and may add additional investors to the amount of USD 8 million. Existing investors will invest at least USD 5 million. In return for the investment, the Company will allot ordinary shares of the Company to the investors ("the Allotted Shares"), as well as options for the Company's shares in an amount equal to 80% of the allotted shares, at an exercise price equal to 120% of the price of the allotted shares, and the investors will be granted price protection and other rights. The private placement is subject, among other things, to a definitive agreement between the parties, the approval of a general meeting of the Company's shareholders and the approval of the TASE. The allotted shares will represent 36% of the Company's share capital, subsequent to the private placement
2. In January 2018, the Company signed a new rental agreement with Har-Hotzvim Properties Ltd. on Kiryat HaMada Street in the Har-Hotzvim area of Jerusalem. The term of the agreement is five years with an option for an additional five years. The agreement will commence in the first half of 2018. As part of this agreement, the Group will lease a laboratory and offices with monthly rental fees (including management fees) of NIS 125 thousand. Under the agreement, a guarantee of NIS 355 thousand will be provided through Bank Leumi in favor of the property owner. The minimum annual rental fee for the rental agreements is NIS 1,500 thousand.
3. On February 7, 2018, the Company received a bridge loan of USD 1 million from CBI. The loan was received in accordance with a loan agreement between the parties, according to which CBI may also provide the Company, at CBI's sole discretion, additional bridge loans of up to USD 2 million, subject to the Company's request and subject to conditions set out in the loan agreement. Under the terms of the agreement, the unpaid balance of the loan will bear annual interest at the interest rate paid on US 3-Month Treasury Bills based on 360 days a year. The loan (principal and interest) will be repaid in one payment at the earliest of: (A) Four months after signing the loan agreement; (B) the date on which the Company will receive financing of any kind in the aggregate amount of USD 5 million (with the exception of loans under the loan agreement described in this report); (c) CBI determines, at its sole discretion, that there has been a material deterioration in the Company, as defined in the agreement. In addition, the Company is entitled to make early repayment, in whole or in part, of the loan (the unpaid balance of principal and interest at that time) at any time. The loan agreement contains standard grounds for the immediate repayment of the loan by CBI. The loan agreement was approved by the Company's audit committee and Board of Directors as an exempting transaction.