# CYNAPSUS THERAPEUTICS INC.
(Formerly Cannasat Therapeutics Inc.)

("A Development Stage Company")

# THIRD QUARTER REPORT
# SEPTEMBER 30, 2010

**Unaudited**

# CYNAPSUS THERAPEUTICS INC.
# September 30, 2010

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# CYNAPSUS THERAPEUTICS INC.



## Unaudited Interim Balance Sheet

| | | September 30, 2010 | | December 31, 2009 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| CURRENT | | | | |
| Cash and cash equivalents | $ | 347,720 | $ | 483,197 |
| Sundry receivables (Note 5(a)) | | 91,159 | | 113,903 |
| | | 438,879 | | 597,100 |
| EQUIPMENT (Note 6) | | 11,387 | | 14,249 |
| OTHER INTANGIBLE ASSETS (Note 8) | | 141,667 | | 150,000 |
| | $ | 591,933 | $ | 761,349 |
| **LIABILITIES** | | | | |
| CURRENT | | | | |
| Accounts payable and accrued liabilities (Notes 9 and 10) | $ | 982,277 | $ | 765,491 |
| LONGER TERM | | | | |
| Debentures payable (Note 11) | $ | 547,577 | $ | - |
| | $ | 1,529,854 | $ | 765,491 |
| COMMITMENTS AND CONTINGENCIES (Note 10) | | | | |
| GOING CONCERN (Note 2) | | | | |
| **SHAREHOLDERS' DEFICIENCY** | | | | |
| SHARE CAPITAL (Note 7(b)) | | 9,164,930 | | 8,961,130 |
| WARRANTS (Note 7(c)) | | 236,183 | | 294,444 |
| CONTRIBUTED SURPLUS (Note 7(f)) | | 2,024,570 | | 1,841,596 |
| (DEFICIT) | | (12,363,604) | | (11,101,312) |
| | | (937,921) | | (4,142) |
| | $ | 591,933 | $ | 761,349 |

APPROVED BY THE BOARD:

"Ronald Hosking", Director        "Rochelle Stenzler", Director

# CYNAPSUS THERAPEUTICS INC.
## Unaudited Interim Statements of Operations, Comprehensive Loss and Deficit

| | Three Months Ended September 30, 2010 | Three Months Ended September 30, 2009 | Nine Months Ended September 30, 2010 | Nine Months Ended September 30, 2009 |
|---|---|---|---|---|
| REVENUE | | | | |
| Interest income | $ - | $ 5,027 | $ 1,015 | $ 17,812 |
| EXPENSES | | | | |
| General and administrative | 303,004 | 290,737 | 921,499 | 819,971 |
| Research and development | 168,151 | 49,211 | 317,047 | 522,790 |
| Amortization of equipment and intangible assets | 3,732 | 3,553 | 11,195 | 10,158 |
| Stock option compensation expense | 31,115 | 35,050 | 124,713 | 142,713 |
| Recovery on scientific research | (106,074) | (34,593) | (111,147) | (155,541) |
| | 399,928 | 343,958 | 1,263,307 | 1,340,091 |
| NET (LOSS) AND COMPREHENSIVE (LOSS) FOR THE PERIOD | (399,928) | (338,931) | (1,262,292) | (1,322,279) |
| (DEFICIT), BEGINNING OF PERIOD | (11,963,676) | (10,289,110) | (11,101,312) | (9,311,316) |
| (DEFICIT), END OF PERIOD | $(12,363,604) | $ (10,628,041) | $ (12,363,604) | $ (10,633,595) |
| (LOSS) PER SHARE - basic and diluted | $ (0.00) | $ (0.01) | $ (0.01) | $ (0.01) |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | 91,850,854 | 83,586,594 | 90,401,770 | 79,401,148 |

# CYNAPSUS THERAPEUTICS INC.



## Unaudited Interim Statements of Cash Flows

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| OPERATING | | | | |
| Net loss for the period | $ (399,928) | $ (338,931) | $(1,262,292) | $(1,322,279) |
| Items not affecting cash | | | | |
| Amortization of equipment and intangible assets | 3,732 | 3,553 | 11,195 | 10,158 |
| Stock option compensation expense | 31,115 | 35,050 | 124,713 | 142,713 |
| Accretion expense for debentures (Note 11) | 32,377 | - | 32,377 | - |
| Shares issued for license option (Note 12) | 75,000 | - | 75,000 | - |
| Deferred financing costs from previous period | 35,977 | - | - | - |
| | (221,727) | (300,328) | (1,019,007) | (1,169,408) |
| Changes in non-cash operating working capital items | | | | |
| Sundry receivables | (19,552) | 125,233 | 22,744 | 25,067 |
| Accounts payable and accrued liabilities | (106,028) | (106,529) | 216,786 | 237,223 |
| | (347,307) | (281,624) | (779,477) | (907,118) |
| INVESTING | | | | |
| Acquisition of equipment | - | (2,705) | - | (9,524) |
| FINANCING | | | | |
| Share and warrant issuances, net of issue costs | - | 808,239 | - | 922,594 |
| Debentures, net of capital discount | 644,000 | - | 644,000 | - |
| | 644,000 | 808,239 | 644,000 | 922,594 |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 296,693 | 523,910 | (135,477) | 5,952 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 51,027 | 287,170 | 483,197 | 805,128 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | $ 347,720 | $ 811,080 | $ 347,720 | $ 811,080 |
| CASH AND CASH EQUIVALENTS CONSIST OF: | | | | |
| Cash | $ 347,720 | $ 431,080 | $ 347,720 | $ 431,080 |
| Cash equivalents | - | 380,000 | - | 380,000 |
| | $ 347,720 | $ 811,080 | $ 347,720 | $ 811,080 |

SUPPLEMENTARY CASH FLOW INFORMATION (Note 13)

The accompanying notes are an integral part of these financial statements

## 1. DESCRIPTION OF BUSINESS

Cynapsus Therapeutics Inc. (the "Corporation" or "Cynapsus") is a publicly traded (CTH: TSX-V) specialty clinical development pharmaceutical company targeting diseases of the brain. Cannasat Pharmaceuticals Inc. was incorporated under the Canada Business Corporations Act on January 16, 2004 and changed its name to Cannasat Therapeutics Inc. ("Cannasat") on January 25, 2005. Cannasat and Lonsdale Public Ventures Inc. ("Lonsdale"), a capital pool company, were amalgamated on March 15, 2006 under the Business Corporations Act (Canada) and continued as one company with the name "Cannasat Therapeutics Inc." On April 15, 2010, Cannasat changed its name to Cynapsus Therapeutics Inc. The Corporation is in the development stage as defined by the Canadian Institute of Chartered Accountants ("CICA") Accounting Guideline 11 "Enterprises in the Development Stage".

## 2. ACCOUNTING POLICIES AND GOING CONCERN

These interim financial statements are unaudited and have not been reviewed by the Corporation's auditors. The management of the Corporation has prepared these interim financial statements in accordance with Canadian Generally Accepted Accounting Principles for the preparation of interim financial information and follow the same accounting policies and methods of application as the audited financial statements of the Corporation for the year ended December 31, 2009. These statements should be read in conjunction with the audited financial statements of the Corporation for the year ended December 31, 2009. The disclosure in these interim financial statements does not conform in all respects to Generally Accepted Accounting Principles in Canada for annual financial reporting.

In the opinion of management, all adjustments considered necessary for fair presentation have been included in these interim financial statements. Operating results for the nine months ended September 30, 2010 may not be indicative of the results that may be expected for the full year ending December 31, 2010.

*Going concern*
While the financial statements have been prepared on the basis of accounting principles applicable to a going concern, several adverse conditions and events cast substantial doubt upon the validity of this assumption. The Corporation has used cash of $9,135,434 in operating activities from inception to September 30, 2010 and has an accumulated deficit of $12,363,604 as at September 30, 2010. The Corporation will be pursuing further financings. Management believes it will be successful in raising the necessary funding to continue operations in the normal course of business, however, there is no assurance that these funds will be available on terms acceptable to the Corporation or at all. The Corporation's continued existence is dependent upon its ability to obtain additional financing as needed and to attain profitable operations.

If the going concern assumption were not appropriate for these financial statements, adjustments would be necessary to the carrying values of assets and liabilities, the reported net loss and the balance sheet classifications used. Such adjustments could be material.

## 3. CHANGES IN ACCOUNTING POLICIES

*(a) Recent Accounting Pronouncements*

*(i) International Financial Reporting Standards*

In January 2006, the Canadian Accounting Standards Board ("AcSB") announced its decision to replace Canadian GAAP with IFRS. On February 13, 2008, the AcSB confirmed January 1, 2011 as the mandatory changeover date to IFRS for all Canadian publicly accountable enterprises. This means that the Corporation will be required to prepare IFRS financial statements for the interim and fiscal year ends beginning in 2011. The Corporation continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS on its results of operations, financial position and disclosures.

*(ii) Business Combinations*

CICA handbook Section 1582 "Business Combinations", replaces Section 1581 "Business Combinations", and provides the Canadian equivalent to International Financial Reporting Standards 3 "Business Combinations". This applies to a transaction in which the acquirer obtains control of one or more businesses. Most assets acquired and liabilities assumed, including contingent liabilities that are considered to be improbable, will be measured at fair value. Any interest in the acquiree owned prior to obtaining control will be re-measured at fair value at the acquisition date, eliminating the need for guidance on step acquisitions. Additionally, a bargain purchase will result in recognition of a gain and acquisition costs must be expensed. Section 1582 is effective for fiscal years beginning on or after January 1, 2011. The adoption of this standard is not expected to have a significant impact on the Corporation's financial statements.

*(iii) Consolidations and Non-Controlling Interests*

CICA handbook Sections 1601 "Consolidated Financial Statements", and 1602 "Non-Controlling Interests" replace Section 1600 "Consolidated Financial Statements". These new sections provide the Canadian equivalent to International Accounting Standard 27 "Consolidated and Separate Financial Statements". Sections 1601 and 1602 are effective for fiscal years beginning on or after January 1, 2011. The adoption of this standard is not expected to have a significant impact on the Corporation's financial statements.

## 4. CAPITAL MANAGEMENT

The Corporation manages its capital structure and makes adjustments to it, based on the funds available to the Corporation, in order to support its research and development activities. The Corporation's capital consists of share capital, warrants and contributed surplus. The Board of Directors does not establish quantitative return on capital criteria for management but rather relies on the expertise of the Corporation's management to sustain future development of the business.

The products which the Corporation currently has in its pipeline are in the research and development stage; as such the Corporation is dependent on external financing to fund its activities. In order to carry out the planned research and development and pay for administration costs, the Corporation will spend its existing working capital and raise additional amounts as needed.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Corporation, is reasonable. The Corporation is not subject to externally imposed requirements on its capital.

There were no changes in the Corporation's approach to capital management during the period ended September 30, 2010.

## 5. FINANCIAL RISK FACTORS

The Corporation's risk exposures and the impact on the Corporation's financial instruments are summarized below:

*(a) Credit Risk*

The Corporation has no significant concentration of credit risk arising from operations. Financial instruments included in sundry receivables consist of goods and services and harmonized sales tax due from the Federal Government of Canada and amounts due from the Ontario portion of the Scientific Research and Experimental Development (SRED) tax incentive program. Management believes that the credit risk concentration with respect to these financial instruments is remote.

*(b) Liquidity Risk*

The Corporation's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due (See Note 2 regarding Going Concern uncertainty). As at September 30, 2010, the Corporation had cash and cash equivalents of $347,720 and sundry receivables of $91,159 (December 31, 2009 - $483,197 and $113,903) to settle current liabilities of $982,277 (December 31, 2009 - $765,491). All of the Corporation's financial liabilities have contractual maturities of less than 30 days and are subject to normal trade terms.

The Corporation believes movement in interest rates is "reasonably possible" over the next 12 months. Since cash and cash equivalents have varying terms and rates, sensitivity to a plus or minus 1% change in rates could affect its net loss by approximately $3,500.

*(c) Market Risk*

*(i) Interest rate risk*

The Corporation has cash and cash equivalent balances as at September 30, 2010. The Corporation's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions bearing interest at 0.5% per annum. The Corporation periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. The Corporation considers interest rate risk to be minimal as investments are short term. As at September 30, 2010, the Corporation has $700,000 in debentures bearing 8% interest per annum. The debentures are due and payable before December 30, 2011.

*(ii) Foreign currency risk*

The Corporation's functional currency is the Canadian dollar and most purchases are transacted in Canadian dollars. The Corporation funds certain research and development expenses in the United States and Europe on a cash call basis using the US Dollar and the EURO currency converted from its Canadian dollar bank accounts held in Canada. Management believes the foreign exchange risk derived from currency conversions is negligible and therefore does not hedge its foreign exchange risk. The Corporation does not hold significant balances in foreign currencies to give rise to exposure to foreign exchange risk.

(iii) *Price risk*

The Corporation is exposed to price risk with respect to Active Pharmaceutical Ingredient (API) prices used in research and development activities. The Corporation monitors API prices in the United States, Europe and Asia to determine the appropriate course of action to be taken by the Corporation. Management believes that the price risk concentration with respect to API is remote.

Continued

## 5. FINANCIAL RISK FACTORS (continued)

*(d) Fair value*

The Corporation has designated its cash and cash equivalents as held-for-trading, measured at fair value. Sundry receivables are classified as loans and receivables, which are measured at amortized cost. Accounts payable, accrued liabilities and debentures payable are classified as other financial liabilities, which are measured at amortized cost.

The carrying amounts for cash and cash equivalents, sundry receivables and accounts payable and accrued liabilities on the balance sheet approximate fair value because of the limited term of these instruments.

As at September 30, 2010, the Corporation's financial instruments that are carried at fair value, consisting of cash and cash equivalents have been classified as Level 1 within the fair value hierarchy.

## 6. EQUIPMENT

| | September 30, 2010 | | |
|---|---|---|---|
| | Cost<br>$ | Accumulated Amortization<br>$ | Net Book Value<br>$ |
| Computer equipment | 15,270 | 7,786 | 7,484 |
| Furniture and fixtures | 9,317 | 5,414 | 3,903 |
| Total | 24,587 | 13,200 | 11,387 |

**7. SHARE CAPITAL**

*a) Authorized*

Unlimited number of common shares with no par value

*b) Issued and outstanding common shares*

The number of common shares outstanding as at September 30, 2010 is as follows:

| | Number of Shares # | Value $ |
|---|---|---|
| **Balance, December 31, 2009** | 89,665,219 | 8,961,130 |
| Issued | 3,326,000 | 203,800 |
| **Balance, September 30, 2010** | 92,991,219 | 9,164,930 |

On July 19, 2010, Cynapsus announced that it completed a financing of secured debentures in the aggregate amount of $520,000 (See Note 11). As part of the financing, the Corporation issued 1,913,600 common shares to the debenture holders at a price of $0.05 per share.

On August 4, 2010, Cynapsus announced that it completed a second financing of secured debentures in the aggregate amount of $180,000 (See Note 11). As part of the financing, the Corporation issued 662,400 common shares to the debenture holders at a price of $0.05 per share.

On September 14, 2010 Cynapsus issued 750,000 common shares to Adagio Pharmaceuticals Ltd. ("Adagio") based on a deemed value of $75,000 and a price of $0.10 per share. The shares were issued in relation to the July 26, 2010 announcement that the Corporation had entered into a License Option Agreement with Adagio granting Cynapsus the option to execute a proposed exclusive, worldwide agreement to license all intellectual property relating to APL-130277, a reformulation of an approved Parkinson's drug (See Note 12).

**7. SHARE CAPITAL (continued)**

c) *Warrants*

The number of warrants outstanding as at September 30, 2010 is as follows:

| | Number of Warrants # | Estimated Grant Date Fair Value $ | Weighted Average Price/Share |
|---|---|---|---|
| **Balance, December 31, 2009** | 13,338,350 | 294,444 | 0.153 |
| Expired February 8, 2010 | (1,175,000) | (58,261) | 0.220 |
| **Balance, September 30, 2010** | 12,163,350 | 236,183 | 0.140 |

Warrants outstanding and exercisable as at September 30, 2010 are as follows:

| Number of Warrants # | Number of shares issuable on exercise of Warrants # | Effective Strike Price $/share | Estimated Grant Date Fair Value $ | Expiry Date |
|---|---|---|---|---|
| 1,935,000 | 1,935,000 | 0.150 | 54,809 | February 26, 2011 |
| 7,509,500 | 7,509,500 | 0.150 | 130,874 | August 6, 2011 |
| 750,950 | 750,950 | 0.100 | 15,634 | August 6, 2011 |
| 1,789,000 | 1,789,000 | 0.150 | 31,038 | August 31, 2011 |
| 178,900 | 178,900 | 0.100 | 3,828 | August 31, 2011 |
| 12,163,350 | 12,163,350 | | 236,183 | |

Continued

**7. SHARE CAPITAL (continued)**

*d) Stock options*

The Corporation has in place a stock option plan for the purchase of common shares for its directors, officers, employees and other service providers. The aggregate number of common shares reserved for issuance under the stock option plan is a maximum of 10% of the issued and outstanding common shares of the Corporation. No one person shall be granted options representing more than 5% of the issued and outstanding common shares of the Corporation in a 12-month period. Option grants to persons providing consulting and investor services may not exceed 2% of the issued and outstanding common shares of the Corporation in any 12-month period. The options are non-assignable and non-transferable and may be granted for a term not exceeding ten years. The exercise price of the options is fixed by the board of directors of the Corporation and shall not be lower than the discounted market price (as defined by the the TSX Venture) of the shares at the time of grant, subject to all applicable regulatory requirements.

The number of stock options outstanding as at September 30, 2010 is as follows:

| | Number of Options # | Number of Shares Issuable on Exercise of Options # | Weighted Exercise Price/Share $/share |
|---|---|---|---|
| Options outstanding as at December 31, 2009 | 6,283,750 | 8,225,829 | 0.215 |
| Expired | (807,084) | (1,015,829) | 0.244 |
| Granted | 1,725,000 | 1,725,000 | 0.100 |
| Options outstanding as at September 30, 2010 | 7,201,666 | 8,935,000 | 0.190 |

On January 8, 2010, 33,333, 66,667 and 100,000 stock options exercisable into 33,333, 66,667 and 100,000 shares with exercise prices of $0.250, $0.200 and $0.100 per share respectively, expired unexercised.

On March 3, 2010 the Corporation granted stock options to acquire 425,000 common shares. The stock options were granted to an employee, an officer and a director of the Corporation at an exercise price of $0.10 per share for a term of 5 years from date of grant. Of the total, 100,000 options vested immediately, 125,000 vest in 6 months, 100,000 vest in 12 months, and 100,000 vest in 18 months.

On April 8, 2010, 33,334, 66,666 and 150,000 stock options exercisable into 33,334, 66,666 and 150,000 shares with exercise prices of $0.200, $0.250 and $0.300 per share respectively, expired unexercised.

On June 25, 2010, 200,000 stock options exercisable into 200,000 shares with an exercise price of $0.200 per share expired unexercised.

On June 30, 2010, 41,667 stock options exercisable into 125,000 shares with an exercise price of $0.283 per share expired unexercised.

On July 28, 2010, 48,750 stock options exercisable into 40,829 shares with an exercise price of $0.239 per share expired unexercised.

**7. SHARE CAPITAL (continued)**

*d) Stock options (continued)*

On August 12, 2010 the Corporation granted stock options to acquire 1,300,000 common shares. The stock options were granted to directors and officers of the Corporation at an exercise price of $0.10 per share for a term of 5 years from date of grant. Of the total, 200,000 options vest in 6 months, 433,331 vest in 12 months, 200,000 vest in 18 months, 233,331 vest in 24 months, and 233,338 vest in 36 months.

On August 31, 2010, 66,667 stock options exercisable into 200,000 shares with an exercise price of $0.317 per share expired unexercised.

The weighted average grant date fair value of the stock options issued during the period ended September 30, 2010 is $0.04. The fair value of the options granted during the period ended September 30, 2010, has been estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions: expected dividend yield of 0%, expected volatility of 123%, risk free rate of return interest rates of 2.09% and an expiry period of 5 years.

Stock options issued and outstanding as at September 30, 2010 are as follows:

| Number of Options # | Number of Shares Issuable on Exercise of Options # | Effective Strike Price ($/share) | Expiry Date |
|---|---|---|---|
| 100,000 | 100,000 | 0.300 | December 3, 2010 |
| 41,666 | 125,000 | 0.283 | December 31, 2010 |
| 50,000 | 150,000 | 0.283 | March 23, 2011 |
| 208,333 | 625,000 | 0.283 | June 30, 2011 |
| 66,667 | 200,000 | 0.317 | August 31, 2011 |
| 50,000 | 150,000 | 0.283 | August 31, 2011 |
| 250,000 | 750,000 | 0.283 | November 1, 2011 |
| 116,667 | 350,000 | 0.283 | December 31, 2011 |
| 260,000 | 260,000 | 0.250 | May 24, 2012 |
| 750,000 | 750,000 | 0.250 | June 25, 2012 |
| 16,667 | 50,000 | 0.283 | June 30, 2012 |
| 66,666 | 200,000 | 0.317 | August 31, 2012 |
| 600,000 | 600,000 | 0.200 | April 4, 2013 |
| 700,000 | 700,000 | 0.200 | June 25, 2013 |
| 250,000 | 250,000 | 0.200 | August 28, 2013 |
| 1,450,000 | 1,450,000 | 0.100 | August 31, 2014 |
| 500,000 | 500,000 | 0.100 | November 16, 2014 |
| 425,000 | 425,000 | 0.100 | March 3, 2015 |
| 1,300,000 | 1,300,000 | 0.100 | August 12, 2015 |
| 7,201,666 | 8,935,000 | | |

The total number of common shares that are issuable pursuant to stock options that are exercisable as at September 30, 2010 is 7,868,333. The weighted average exercise price of stock options that are exercisable as at September 30, 2010 is $0.190.

The weighted average contractual life remaining for options at September 30, 2010 was 2.33 years.

## 7. SHARE CAPITAL (continued)

*e) Escrowed shares*

On March 15, 2006, Cynapsus amalgamated with Lonsdale Public Ventures ("Lonsdale"), a capital pool company. Immediately following the amalgamation, 38,705,837 common shares of the Corporation were subject to escrow. 34,608,879 of these escrowed shares are to be released over a period of 72 months on the basis of 5% to be released six months after the final Exchange bulletin (March 23, 2006), 5% to be released every six months thereafter for the next 18 months and 10% to be released every six months thereafter for the next 48 months. At September 30, 2010, 10,382,673 of the 72-month release shares are still subject to escrow. The remaining 4,096,958 escrowed shares were released over a period of 36 months ending on March 23, 2009.

*f) Contributed Surplus*

Contributed surplus represents the fair value of unexercised and expired warrants as well as the unexercised grant date fair value of stock option compensation earned by directors, officers, employees and certain consultants of the Corporation as follows:

| | |
|---|---|
| Balance December 31, 2009 | $ 1,841,596 |
| Compensation earned during the period – employee | 123,963 |
| Compensation earned during the period – non-employee | 750 |
| Expiry of warrants, February 8, 2010 | 58,261 |
| Balance September 30, 2010 | $ 2,024,570 |

## 8. OTHER INTANGIBLE ASSETS

On June 10, 2005, the Corporation entered into a license agreement with a research and development company. The license fee of $200,000 was satisfied by the execution and delivery of two promissory notes on June 30, 2005 in the aggregate principal amount of $100,000 plus interest and the issuance of 117,648 Class A common shares at an aggregate subscription price of $100,000. In addition to the acquisition costs, the Corporation has agreed to pay a combination of milestone-based payments and royalties. The license is for patents that have been issued in certain jurisdictions and are currently pending in others.

| | September 30, 2010 | | |
|---|---|---|---|
| | Cost<br>$ | Accumulated Amortization<br>$ | Net Book Value<br>$ |
| License | 200,000 | 58,333 | 141,667 |

## 9. RELATED PARTY TRANSACTIONS

Related party transactions during the periods ended September 30, 2010 and 2009 are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Management fees | $36,000 | $25,500 | $106,000 | $97,833 |
| Director fees | 4,300 | 4,300 | 34,050 | 20,400 |
| Consulting fees paid to a director | - | - | 28,000 | - |
| | $40,300 | $29,800 | $168,050 | $118,233 |

At September 30, 2010, included in accounts payable and accrued liabilities is $137,175 (December 31, 2009 - $98,560) due to officers and directors of the Corporation. These amounts are unsecured, non-interest bearing with no fixed terms of repayment. These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

On July 19, 2010, Cynapsus announced that it completed a financing of secured debentures in the aggregate amount of $520,000 (See Note 11). Included in this total, was a $50,000 debenture from a director who was also issued 184,000 common shares at a price of $0.05 per share.

On September 14, 2010 Adagio was issued 750,000 common shares in the capital of Cynapsus based on a deemed value of $75,000 and a price of $0.10 per share. An officer of the Corporation is also a director, officer and majority shareholder of Adagio, a private holding company for the APL-130277 asset only.

## 10. COMMITMENTS AND CONTINGENCIES

The Corporation is party to certain management contracts for its executive officers. Minimum management contract termination commitments remaining under the agreements are approximately $131,167 and are all payable within one year. In addition, the Corporation is party to certain management contracts which require that additional payments of approximately $108,000 be made upon the occurrence of certain events such as a change of control. As the likelihood of these events taking place is not determinable, the contingent payments have not been reflected in these financial statements.

The Corporation is subject to additional termination and stock option commitments, contingent upon the Corporation raising a cumulative of $5 million post November 15, 2009. From November 15, 2009, to September 30, 2010, $644,000 has been raised. Once $5 million is raised, the Corporation will have additional management contract termination commitments of $285,400 and will be required to issue 3,733,163 stock options priced at the then fair market value, but not less than $0.10 per share.

On November 15, 2009, the former CEO resigned and is due $216,500 over a twelve month period, contingent upon the Corporation raising a minimum of $2 million post November 15, 2009 and at the discretion of the Board. As the likelihood of these events taking place is not determinable, the contingent payments have not been reflected in these financial statements.

The Corporation has entered into a lease for its office premises in Toronto. Minimum rental commitments approximate $42,500 including $19,500 due within the current year and $23,000 due the year following.

The Corporation has one contractual dispute for claims against them totalling approximately $100,000. Included in accounts payable and accrued liabilities is $100,000 related to this dispute. Management believes this dispute will be settled before December 31, 2010.

On March 2, 2010, Cynapsus and IntelGenx Corp. signed a Letter of Intent to engage in a project to further develop tablets containing delta-9 tetrahydrocannabinol (“THC”) for sublingual or buccal delivery of THC. Once the formulations have been completed, one or more partners will be retained for clinical development and commercialization of the products. Upon successfully entering into a sub-licensing agreement with a marketing and/or commercialization partner, the parties agree to share royalties received from the sale of the products. In consideration of the rights and licenses to be granted by the Corporation to IntelGenx under the license agreement, IntelGenx would agree to forgive $230,688 in indebtedness owed by the Corporation to IntelGenx. The license agreement is currently in final stages of negotiations.

## 11. DEBENTURES PAYABLE

On July 19, 2010, Cynapsus announced that it completed a financing of secured debentures in the aggregate amount of $520,000. The secured debentures bear interest at a rate of 8% per annum and are secured by a security interest in the assets of the Corporation. The secured debentures are payable by Cynapsus on December 30, 2011. As part of the financing, the Corporation paid an 8% capital discount to the debenture holders resulting in net proceeds to the Corporation of $478,400 and issued 1,913,600 common shares to the debenture holders at a market price of $0.05 per share. The estimated fair value on July 19, 2010 was $382,700 using an effective interest rate of 34%.

On August 4, 2010, Cynapsus announced that it completed a second financing of secured debentures in the aggregate amount of $180,000. The secured debentures bear interest at a rate of 8% per annum and are secured by a security interest in the assets of the Corporation. The secured debentures are payable by Cynapsus on December 30, 2011. As part of the financing, the Corporation paid an 8% capital discount to the debenture holders resulting in net proceeds to the Corporation of $165,600 and issued 662,400 common shares to the debenture holders at a market price of $0.05 per share. The estimated fair value on August 4, 2010 was $132,480 using an effective interest rate of 34%.

**Continuity Schedule of Debentures Outstanding**

| | **Debentures Issued on July 19, 2010** | **Debentures Issued on August 4, 2010** | **TOTAL** |
|---|---|---|---|
| Gross Proceeds | $ 520,000 | $ 180,000 | $700,000 |
| Capital Discount (8%) | (41,600) | (14,400) | (56,000) |
| | $ 478,400 | $ 165,600 | $ 644,000 |
| Bonus Shares Valuation | (95,680) | (33,120) | (128,800) |
| | $ 382,720 | $ 132,480 | $ 515,200 |
| Accretion Expense for the Period | $ 25,382 | $ 6,995 | $ 32,377 |
| **TOTAL** | **$ 408,102** | **$ 139,475** | **$ 547,577** |

## 12. LICENSE OPTION AGREEMENT

On July 26, 2010, Cynapsus announced that it entered into a License Option Agreement with Adagio Pharmaceuticals Ltd. (“Adagio”) granting Cynapsus the option to execute a proposed exclusive, worldwide agreement to license all intellectual property relating to APL-130277, a reformulation of an approved Parkinson’s drug. The two parties have also finalized an exclusive worldwide license that would result in Cynapsus assuming product development and commercialization rights to APL-130277 from Adagio in return for development milestones and royalties to Adagio, including common shares of Cynapsus. On September 14, 2010 Cynapsus issued 750,000 common shares to Adagio based on a deemed value of $75,000 and a price of $0.10 per share.

The license agreement includes an exclusive option period for the first 12 months which allows Cynapsus to conduct further due diligence and proof-of-concept studies for APL-130277 prior to executing the full license.

## 13. SUPPLEMENTARY CASH FLOW INFORMATION

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| Interest paid | 516 | 2,020 | 1,720 | 6,062 |
| The following significant transactions did not generate or use cash: | | | | |
| Change in contributed surplus | 31,114 | (59,156) | 182,974 | 126,714 |
| Change in compensation expense | (12,005) | (35,050) | (124,713) | (142,713) |
| Deferred financing costs reallocated to share and warrant costs | - | - | - | (251,040) |
| Value of shares issued for debenture bonus shares (Note 11) | (128,800) | - | (128,800) | -- |

## 14. SUBSEQUENT EVENT

On November 10, 2010 the Corporation granted stock options to acquire 200,000 common shares. The stock options were granted to directors of the Corporation at an exercise price of $0.10 per share for a term of 5 years from date of grant.