WESTAIM

Third Quarter Report to Shareholders for the quarter ended September 30, 2014

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"Westaim" or the "Company" in this Management's Discussion and Analysis ("MD&A") refers to The Westaim Corporation on a consolidated basis. This MD&A, which has been approved by the Board of Directors of Westaim, should be read in conjunction with Westaim's unaudited consolidated financial statements including notes for the three and nine months ended September 30, 2014 and 2013 as set out on pages 14 to 29 of this quarterly report. Financial data in this MD&A has been derived from the unaudited consolidated financial statements for the three and nine months ended September 30, 2014 and 2013 and is intended to enable the reader to assess Westaim's results of operations for the three and nine months ended September 30, 2014 and financial condition as at September 30, 2014. The Company reports its consolidated financial statements using accounting policies consistent with International Financial Reporting Standards ("IFRS"). All amounts are in Canadian dollars unless otherwise indicated. The following commentary is current as of November 14, 2014. Additional information relating to Westaim is available on SEDAR at www.sedar.com. Certain totals, subtotals and percentages may not reconcile due to rounding.

Adoption of IFRS for Investment Entities

Westaim qualifies as an investment entity under IFRS and uses fair value as the key measure to monitor and evaluate its investments. The Company commenced reporting its financial results in accordance with IFRS applicable to investment entities, on a prospective basis, effective July 1, 2014. See Section 11, *Critical Accounting Policies and Recently Adopted and Pending Accounting Pronouncements* of this MD&A.

Non-GAAP measures

Westaim uses both IFRS and non-generally accepted accounting principles ("non-GAAP") measures to assess performance. The Company cautions readers about non-GAAP measures that do not have a standardized meaning under IFRS and are unlikely to be comparable to similar measures used by other companies. Management believes these measures allow for a more complete understanding of the underlying business. These measures are used to monitor Westaim's results and should not be viewed as a substitute for those determined in accordance with IFRS. Reconciliations of such measures to the most comparable IFRS figures are included herein. Book value per share represents shareholders' equity at the end of the period, determined on an IFRS basis, divided by the total number of common shares outstanding on the same date. The Company believes that this is a useful measurement as the relative increase or decrease from period to period in book value per share should approximate over the long term the relative increase or decrease in the intrinsic value of the business, but is not necessarily equivalent to the net realizable value of the Company's assets per share.

Cautionary Statement Regarding the Valuation of Investments in Private Entities

In the absence of an active market for its investments in private entities, fair values for these investments are determined by management using the appropriate valuation methodologies after considering the history and nature of the business, operating results and financial conditions, outlook and prospects, general economic, industry and market conditions, capital market and transaction market conditions, contractual rights relating to the investment, public market comparables, private market transactions multiples and, where applicable, other pertinent considerations. The process of valuing investments for which no active market exists is inevitably based on inherent uncertainties and the resulting values may differ from values that would have been used had an active market existed. The amounts at which the Company's investments in private entities could be disposed of may differ from the fair value assigned and the differences could be material.

Cautionary Statement Regarding Financial Information of Houston International Insurance Group, Ltd.

Selected financial information (the "HIIG Financial Information") concerning Houston International Insurance Group, Ltd. ("HIIG") contained in this MD&A has been derived from the interim unaudited consolidated financial statements of HIIG for the nine months ended September 30, 2014 and 2013. Such statements are the responsibility of the management of HIIG, are unaudited, have been prepared in accordance with United States generally accepted accounting principles ("US GAAP"), and are presented in United States dollars.

The HIIG Financial Information should be read in conjunction with Westaim's historical financial statements including the notes thereto and the related MD&A as well as Westaim's other public filings.

The HIIG Financial Information has been provided solely by HIIG. Although Westaim has no knowledge that would indicate that any of the HIIG Financial Information contained herein is untrue or otherwise misleading, neither Westaim nor any of its directors or officers assumes any responsibility for the accuracy or completeness of such information, or for any failure by HIIG to disclose to Westaim events or facts which may have occurred or which may affect the significance or accuracy of any such financial information but which are unknown to Westaim.

Westaim disclaims and excludes all liability (to the extent permitted by law), for losses, claims, damages, demands, costs and expenses or whatever nature arising in any way out of or in connection with the HIIG Financial Information, its accuracy, completeness or by reason of reliance by any person on any of it.

Future Oriented Financial Information

This MD&A may contain forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from these forward-looking statements as a result of various factors, including those discussed hereinafter. Please refer to the cautionary note in Section 14 of this MD&A.

1. THE COMPANY

The Westaim Corporation (TSXV: WED) is a Canadian investment company specializing in providing long-term capital to businesses operating primarily within the global financial services industry. The Company invests, directly and indirectly, through acquisitions, joint ventures and other arrangements, with the objective of providing its shareholders with capital appreciation and real wealth preservation.

Westaim's strategy is to pursue investment opportunities with a focus towards the financial services industry and grow shareholder value over the long-term.

On July 31, 2014, the Company, in combination with third party investors, completed the acquisition of a significant interest in Houston International Insurance Group, Ltd. ("HIIG") through Westaim HIIG Limited Partnership (the "Partnership"), an Ontario limited partnership managed by a subsidiary of the Company. HIIG is a U.S. based diversified specialty insurance provider and managing general insurance agent covering risks across the United States and certain niche global markets. For additional information on the acquisition and related financing transactions, see discussion in Section 3, *Investments in Private Entities*, Section 4, *Equity Financings* of this MD&A and the Business Acquisition Report related to the acquisition available on SEDAR at www.sedar.com.

On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the comparative periods have been adjusted to reflect this change.

2. OVERVIEW OF PERFORMANCE

Highlights (millions except share and per share data)	Three months ended September 30 2014	 2013 (1)	Nine months ended September 30 2014	 2013 (1)
Revenue	$ 0.6	$ 0.1	$ 0.7	$ 0.3
Net results of investments	13.0	-	13.0	-
Recovery of expenses (expenses) excluding share-based compensation	2.8	(0.5)	(1.7)	(2.0)
Share-based compensation	-	(0.1)	(0.1)	(0.1)
Income tax recovery	-	-	-	0.1
Profit or loss and other comprehensive income	$ 16.4	$ (0.5)	$ 11.9	$ (1.7)
Earnings per share				
Profit or loss and other comprehensive income – basic and diluted	$ 0.31	$ (0.04)	$ 0.44	$ (0.12)
Number of common shares outstanding - at September 30	70,297,342	13,902,937	70,297,342	13,902,937
Book value per share - at September 30	$ 2.64	$ 2.37	$ 2.64	$ 2.37

(1) Adjusted to reflect a 50:1 share consolidation completed on October 1, 2013.

For the three and nine months ended September 30, 2014, the Company reported profit of $16.4 million and $11.9 million (2013 - loss of $0.5 million and loss of $1.7 million).

Revenue for the three and nine months ended September 30, 2014 of $0.6 million and $0.7 million (2013 - $0.1 million and $0.3 million) consisted of interest income of $0.4 million and $0.5 million (2013 - $0.1 million and $0.3 million) and advisory fees of $0.2 million and $0.2 million (2013 - $nil), respectively. Net results of investments were $13.0 million for the three and nine months ended September 30, 2014 (2013 - $nil), representing an unrealized gain on investments in private entities recognized by the Company related to its investment in the Partnership. See discussion in Section 3, *Investments in Private Entities* of this MD&A. Expenses (recovery of expenses) for the three and nine months ended September 30, 2014 of $(2.8) million and $1.8 million (2013 - $0.6 million and $2.1 million) included share-based compensation expense of $nil and $0.1 million (2013 - $0.1 million and $0.1 million), site restoration provision expense of $0.2 million and $1.0 million (2013 - $nil), foreign exchange gain of $0.8 million and $0.1 million (2013 - $nil), other corporate costs of $0.9 million and $3.9 million (2013 - $0.5 million and $2.0 million), and a recovery of professional fees of $3.1 million and $3.1 million (2013 - $nil).

3. INVESTMENTS IN PRIVATE ENTITIES

Investment in Houston International Insurance Group, Ltd.

On July 31, 2014, the Partnership completed the acquisition of approximately 70.8% of the issued and outstanding shares of common stock of HIIG, an international specialty insurance company headquartered in Houston, for an aggregate purchase price of approximately US$138.7 million

3. INVESTMENTS IN PRIVATE ENTITIES (continued)

(the “Acquisition”). See discussion in Section 4, *Equity Financings* of this MD&A regarding related equity financing arrangements completed in the three months ended September 30, 2014.

The Acquisition involved:

(i) the purchase by the Partnership of an aggregate of 16,588,865 shares of common stock in the capital of HIIG (“HIIG Shares”) from certain shareholders of HIIG (the “Sellers”) for an aggregate purchase price of US$53.7 million; and

(ii) the purchase by the Partnership from HIIG of an aggregate of 18,702,673 HIIG Shares from treasury for an aggregate purchase price of US$85.0 million.

In order to complete the Acquisition and to provide working capital, the Partnership received funding of approximately US$141.1 million. This funding was provided as to (i) US$75.7 million by Westaim, (ii) US$24.3 million and US$22.9 million by affiliates of Everest Re Group, Ltd. and Catlin Group Limited, respectively, (iii) US$10.0 million by Stephen L. Way, Chairman and Chief Executive Officer of HIIG, and/or certain investors affiliated with Mr. Way, and (iv) US$8.2 million by certain other existing shareholders of HIIG and other investors.

The Company’s investment in the Partnership at closing was US$75.7 million, or $82.5 million, representing a 53.3% ownership interest in the Partnership.

The Company was reimbursed $3.1 million in transaction and related costs incurred in connection with the Acquisition and the formation of the Partnership, and $1.0 million in share issuance costs related to its investment in the Partnership.

Westaim has determined that it qualifies as an investment entity under IFRS and uses fair value as the key measure to monitor and evaluate its investments. Accordingly, the investment in HIIG, through the Partnership, is accounted for at fair value through profit or loss (“FVTPL”). See note 2 to the Company’s unaudited consolidated financial statements for the three and nine months ended September 30, 2014 and 2013 for the Company’s adoption of IFRS applicable to investment entities, on a prospective basis, effective July 1, 2014.

In determining the valuation of investments in private entities, the Company uses generally accepted valuation methodologies, including the original purchase price, the capitalized cash flow method, reviews of comparable arm’s length transactions, and reviews of comparable publicly traded company valuations.

The capitalized cash flow approach is one of estimating the present value of the projected cash flows to be generated from the business and theoretically available (though not necessarily paid) to the capital providers of the investee company. A discount rate is applied to the projected future cash flows to arrive at a present value. The discount rate is intended to reflect all risks of ownership and the associated risks of realizing a stream of projected future cash flows. The capitalized cash flow method generally involves the estimation of future maintainable operating pre-debt cash flows which are then capitalized using a capitalization rate based on a weighted average cost of capital. It is a present value calculation of future operating cash flow expectations. The enterprise value is then reduced for the debt outstanding. Historical net operating earnings of the Company (adjusted for unusual items), and current performance and prospects are used to estimate its future operating cash flows. For a full description of the Company’s valuation techniques, see note 5 to the Company’s unaudited consolidated financial statements for the three and nine months ended September 30, 2014 and 2013.

In determining the valuation of the Company’s investment in the Partnership at the end of each reporting period, the Company uses the capitalized cash flow method to prepare a valuation of HIIG and the Partnership, and reviews comparable arm’s length transactions and comparable publicly traded company valuations.

In arriving at the fair value of Westaim’s investment in the Partnership at July 31, 2014, the Company also considered the acquisition cost of the Partnership’s 70.8% investment in HIIG. Given certain seller motivations and the desire of the Sellers to provide limited indemnifications and no reserve guarantees, the purchase of HIIG Shares from the Sellers was completed at an approximate 29% discount to the December 31, 2013 adjusted book value of HIIG (“Discount Purchase”). The purchase of HIIG Shares from treasury was completed at a valuation equal to approximately 100% of the December 31, 2013 adjusted book value of HIIG and was, due to the factors outlined above, considered to be a better indicator of value. This indication of value is also based on implied valuation multiples related to the equity financing completed by the Company, implied valuation multiples drawn from comparable public companies and targets of precedent transactions operating in the specialty insurance market, and a supporting discounted cash flow approach. As a result of the determination that the purchase of HIIG Shares from the Sellers constituted a Discount Purchase, the Company recognized an unrealized gain on its investment in the Partnership of $10.4 million at July 31, 2014. An additional unrealized gain of $2.6 million was recognized in the three months ended September 30, 2014, reflecting a change in the fair value of the investment in the Partnership from August 1, 2014 to September 30, 2014 resulting from a strengthening of the U.S. dollar against the Canadian dollar. The combined unrealized gain of $13.0 million has been included in profit of the Company for the three months ended September 30, 2014.

3. INVESTMENTS IN PRIVATE ENTITIES (continued)

Selected Financial Information of Houston International Insurance Group, Ltd. for the nine months ended September 30, 2014 and 2013

As disclosed above, as an investment entity under IFRS, the Company uses fair value as the key measure to monitor and evaluate its investments. Accordingly, the financial results of HIIG are not consolidated by the Company. However, at this time, the Company considers certain financial results of HIIG to be important measures for investors in assessing the Company's financial position and performance. In particular, premium volumes provide a measure of HIIG's growth, net income and loss & LAE (loss adjustment expense) ratios provide a measure of HIIG's profitability, and shareholders' equity is a measure that is generally used by investors to determine the value of insurance companies.

Set out below is certain selected financial information relating to HIIG that has been derived from the interim consolidated financial statements of HIIG. Such statements are the responsibility of the management of HIIG. The information below is unaudited, is presented in accordance with United States generally accepted accounting principles ("US GAAP") and is in United States dollars. Readers are cautioned that the HIIG financial information has not been reconciled to IFRS and so may not be comparable to the financial information of issuers that present their financial information in accordance with IFRS.

(prepared in accordance with US GAAP)	**For the three months ended**		**For the nine months ended**	
(US$000's)	**30-Sep-14**	**30-Sep-13**	**30-Sep-14**	**30-Sep-13**
	(unaudited)		**(unaudited)**	
Income Statement				
Gross written premium	$ 95,842	$ 83,359	$ 350,030	$ 299,936
Net premiums written	$ 72,518	$ 67,751	$ 224,762	$ 202,527
Net premiums earned	$ 84,322	$ 61,002	$ 240,299	$ 156,471
Net Income	$ 7,172	$ 917	$ 15,634	$ 2,408
Segmented Information				
Net premiums written:				
Construction	$ 10,570	$ 7,283	$ 34,428	$ 23,242
Energy	14,902	12,376	41,550	25,155
Specialty	36,639	30,807	104,555	93,840
Professional	8,601	7,755	22,993	21,618
Property	2,134	6,307	17,916	27,999
Non-continuing lines and other	(328)	3,223	3,320	10,673
	$ 72,518	$ 67,751	$ 224,762	$ 202,527
Net loss & LAE ratio:				
Construction	65%	60%	62%	61%
Energy	55%	11%	55%	43%
Specialty	64%	77%	69%	76%
Professional	59%	56%	60%	46%
Property	33%	18%	35%	32%
Non-continuing lines and other	n.m.(1)	n.m.(1)	n.m.(1)	n.m.(1)
	63%	66%	65%	69%

Balance Sheet Information	**As at 30-Sep-14**	**As at 31-Dec-13**
	(unaudited)	**(audited)**
Investment Portfolio	$ 643,391	$ 528,388
Stockholders' Equity	$ 239,375	$ 140,229

Notes:

(1) Not meaningful, but included in the aggregate ratios below.

4. EQUITY FINANCINGS

In connection with the Acquisition, on April 23, 2014, Westaim completed the sale of an aggregate of 50,995,385 subscription receipts (the "Subscription Receipts") at a purchase price of $2.65 per Subscription Receipt (the "Subscription Receipt Offering"). On July 29, 2014, an aggregate of 50,995,385 common shares of Westaim ("Westaim Shares") were issued upon the conversion of the Subscription Receipts for aggregate gross proceeds of approximately $135.1 million. An additional 5,399,020 Westaim Shares were issued on July 31, 2014 to certain funds and co-investors (collectively, the "Investors") pursuant to subscription agreements entered into by the Investors on April 23, 2014 (the "Additional Private Placement"). In connection with the Additional Private Placement, Westaim received additional gross proceeds of approximately $14.3 million.

On July 31, 2014, the Company used US$75.7 million of the proceeds from the Subscription Receipt Offering and the Additional Private Placement (collectively, the "Offerings") to purchase Class A Limited Partnership Units in the Partnership to enable the Partnership (together with funds committed by other investors in the Partnership) to complete the Acquisition. The Partnership completed the Acquisition and acquired 70.8% of HIIG for approximately US$138.7 million (see discussion in Section 3, *Investments in Private Entities* of this MD&A). The remaining net proceeds of the Offerings will be used by the Company for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership).

Immediately following the issuance of the common shares under the Offerings, the Company had 70,297,342 common shares outstanding, with a stated capital of $346.8 million.

5. ANALYSIS OF FINANCIAL RESULTS

Details of the Company's operating results are as follows:

(millions)	Three months ended September 30 2014	Three months ended September 30 2013	Nine months ended September 30 2014	Nine months ended September 30 2013
Revenue	$ 0.6	$ 0.1	$ 0.7	$ 0.3
Net results of investments	13.0	-	13.0	-
Expenses				
Salaries and benefits	0.2	0.2	0.6	0.9
Office expenses	0.3	0.1	0.8	0.6
Professional fee (recovery) expense	(2.7)	0.2	(0.6)	0.5
Site restoration provision expense	0.2	-	1.0	-
Share-based compensation	-	0.1	0.1	0.1
Foreign exchange gain	(0.8)	-	(0.1)	-
Total expenses	(2.8)	0.6	1.8	2.1
Income tax recovery	-	-	-	0.1
Profit (loss)	$ 16.4	$ (0.5)	$ 11.9	$ (1.7)

5.1 Revenue

Revenue for the three and nine months ended September 30, 2014 of $0.6 million and $0.7 million (2013 - $0.1 million and $0.3 million) consisted of interest income of $0.4 million and $0.5 million (2013 - $0.1 million and $0.3 million) and advisory fees of $0.2 million and $0.2 million (2013 - $nil), respectively.

The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., entered into a management services agreement ("MSA") with HIIG commencing on closing, whereby Westaim HIIG GP Inc. will be entitled to receive from HIIG an ongoing fee of US$1.0 million annually for the first three years of the agreement and US$0.5 million annually for the next two years relating to advisory services provided under the agreement. The Company received fees of $0.5 million under the MSA, of which $0.2 million was earned in the three months ended September 30, 2014 and $0.3 million was recorded as deferred revenue in the statement of financial position at September 30, 2014.

5.2 Net Results of Investments

The Company determined that the purchase of HIIG Shares from the Sellers was a Discount Purchase and not representative of the value of HIIG, and that the purchase of HIIG Shares from treasury was a better indicator of value. As a result of the determination that the purchase of HIIG Shares from the Sellers constituted a Discount Purchase, the Company recognized an unrealized gain on its investment in the Partnership of $10.4 million at July 31, 2014.

5. ANALYSIS OF FINANCIAL RESULTS (continued)

An additional unrealized gain of $2.6 million was recognized in the three months ended September 30, 2014, reflecting a change in the fair value of the investment in the Partnership from August 1, 2014 to September 30, 2014 resulting from a strengthening of the U.S. dollar against the Canadian dollar. The combined unrealized gain of $13.0 million has been included in the statement of profit or loss and other comprehensive income for the three months ended September 30, 2014.

5.3 Expenses

Expenses (recovery of expenses) for the three months ended September 30, 2014 were $(2.8) million (2013 - $0.6 million). The decrease in total expenses of $3.4 million in the third quarter of 2014 compared to the same period in the prior year was mainly due to a recovery of professional fees in the three months ended September 30, 2014. Following the completion of the Acquisition on July 31, 2014, the Company was reimbursed $3.1 million in transaction and related costs previously expensed by the Company. The increase in corporate expenses of $0.5 million was offset by a foreign exchange gain of $0.8 million recorded in the three months ended September 30, 2014.

Expenses for the nine months ended September 30, 2014 were $1.8 million (2013 - $2.1 million). The decrease in total expenses of $0.3 million in the nine months ended September 30, 2014 compared to the same period in 2013 resulted from a recovery of professional fees previously expensed by the Company of $3.1 million following the completion of the Acquisition on July 31, 2014, offset in part by a site restoration provision expense of $1.0 million and an increase in corporate expenses of $1.8 million in the nine months ended September 30, 2014.

6. ANALYSIS OF FINANCIAL POSITION

The Company's assets, liabilities and shareholders' equity consist of the following:

(millions)	September 30, 2014	December 31, 2013
Assets		
Cash and cash equivalents	$ 94.9	$ 35.4
Accounts receivable and other assets	0.5	0.2
Investments in private entities	95.5	-
	$ 190.9	$ 35.6
Liabilities		
Accounts payable and accrued liabilities	$ 1.5	$ 2.5
Deferred revenue	0.3	-
Site restoration provision	3.2	2.2
	5.0	4.7
Shareholders' equity	185.9	30.9
Total liabilities and shareholders' equity	$ 190.9	$ 35.6

6.1 Cash and Cash Equivalents

At September 30, 2014, the Company had cash and cash equivalents of $94.9 million compared to $35.4 million at December 31, 2013. In the three months ended September 30, 2014, the Company received the following: net proceeds from the equity financings of $142.1 million, reimbursements of $1.0 million in share issuance costs and $3.1 million in transaction and related costs incurred in connection with the Acquisition and the formation of the Partnership. The Company invested $82.5 million in the Partnership and will use the remaining net proceeds for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership). See also discussion in Section 8, *Liquidity and Capital Resources* of this MD&A.

6.2 Accounts Receivable and Other Assets

Accounts receivable and other assets at September 30, 2014 included $0.2 million in capital assets which were placed in use at the end of September 2014. Depreciation on the capital assets will commence in October 2014.

6.3 Investments in Private Entities

The Company's investments in private entities at September 30, 2014 consisted of its investment in HIIG, through the Partnership. The investment is accounted for at FVTPL and the fair value of the investment was determined to be $95.5 million at September 30, 2014. See discussion in Section 3, *Investments in Private Entities* of this MD&A.

6. ANALYSIS OF FINANCIAL POSITION (continued)

6.4 Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities were $1.5 million at September 30, 2014 and $2.5 million at December 31, 2013.

6.5 Deferred Revenue

Deferred revenue of $0.3 million was related to advisory fees received under the MSA which had not been earned at September 30, 2014.

6.6 Site Restoration Provision

The site restoration provision of $3.2 million at September 30, 2014 and $2.2 million at December 31, 2013 relates to costs associated with soil and groundwater reclamation and remediation costs. The increase during the three and nine months ending September 30, 2014 was related to a change in the long-term inflation rate assumption from 1.30% at December 31, 2013 to 1.58% at September 30, 2014 and a change in the discount rate due to a flattening of the yield curve during the second and third quarters. The Company conducts periodic reviews of the underlying assumptions supporting the provision, including remediation costs and regulatory requirements. Reimbursements of costs resulting from indemnifications provided by previous owners of the industrial sites have not been recognized in these consolidated financial statements. Future reimbursements will be recorded when received.

6.7 Shareholders' Equity

The details of shareholders' equity are as follows:

(millions)	September 30, 2014	December 31, 2013
Common shares	$ 346.7	$ 203.6
Contributed surplus	12.9	12.9
Deficit	(173.7)	(185.6)
Shareholders' equity	$ 185.9	$ 30.9

The Company issued 50,995,385 common shares under the Subscription Receipt Offering on July 29, 2014 and 5,399,020 common shares pursuant to the Additional Private Placement on July 31, 2014 for net proceeds of $143.1 million, after transaction costs of $6.3 million. At September 30, 2014, the Company had 70,297,342 common shares outstanding. See discussion in Section 4, *Equity Financings* of this MD&A.

The decrease in deficit of $11.9 million from December 31, 2013 to September 30, 2014 is due to the profit for the nine months ended September 30, 2014.

7. OUTLOOK

The Company's investment in HIIG, through the Partnership, which was completed during the third quarter of 2014, is consistent with Westaim's strategy to deploy capital at above average risk-adjusted returns. Westaim has partnered with third party investors and an experienced management team with a proven track record in the attractive global specialty P&C insurance market.

Westaim plans to use the remaining cash raised from the equity financings (see discussion in Section 4, *Equity Financings* of this MD&A) for general corporate purposes and to pursue future investments (including possible additional equity investments in the Partnership) consistent with its strategy.

The Company continues to seek additional investment opportunities to create meaningful shareholder value through partnering with aligned and capable management teams to build profitable businesses that generate attractive returns over the long term.

8. LIQUIDITY AND CAPITAL RESOURCES

<u>Capital Management Objectives</u>

The Company's guiding principles for capital management are to maintain the stability and safety of the Company for its stakeholders through optimal capital mix and an adequate level of capital, maintain a strong balance sheet, ensure the return on capital meets the Board of Directors' expectations relative to the risk taken, and minimize the after-tax cost of capital.

8. LIQUIDITY AND CAPITAL RESOURCES (continued)

Towards achieving these objectives, the Company employs a strong and efficient capital base and manages capital in accordance with policies established by the Board of Directors. These policies relate to capital strength and capital mix. The Company has a capital management process in place to measure, deploy and monitor its available capital to assess its adequacy on a continuous basis. Management develops the capital strategy and oversees the capital management processes of the Company. The Company's capital consists of its shareholders' equity.

Share Capital

The Company's authorized share capital consists of an unlimited number of common shares, Class A preferred shares and Class B preferred shares. On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the comparative period have been adjusted to reflect this change.

At December 31, 2013, the Company had 13,902,937 common shares outstanding. In the three months ended September 30, 2014, the Company issued 56,394,405 common shares in connection with the Subscription Receipt Offering and the Additional Private Placement for net proceeds of $143.1 million, after transaction costs of $6.3 million. See discussion in Section 4, *Equity Financings* of this MD&A. At September 30, 2014, the Company had 70,297,342 common shares outstanding, with a stated capital of $346.7 million

The Company had 5,000 stock options outstanding at September 30, 2014 and 6,000 options outstanding at December 31, 2013.

There were no Class A or Class B preferred shares outstanding at September 30, 2014 and December 31, 2013.

Dividends

No dividends were paid in the nine months ended September 30, 2014 and 2013.

Share-based Compensation Plans

At the annual and special meeting (the "Meeting") of the shareholders of the Company held on June 19, 2014, the Company's shareholders approved an amendment to the Company's comprehensive long-term equity incentive plan (the "Incentive Plan") to adopt substantially the form of long-term incentive plan of the Company in place prior to the Company's shares being listed on the TSX-V, with certain exceptions. The amendments included (a) providing for grants of restricted share units ("RSUs"), stock appreciation rights and other share-based awards in addition to DSUs, (b) providing the Board of Directors with the option of establishing a share purchase program; and (c) removing the ability of the Company to grant stock options under the Incentive Plan. Also at the Meeting, the shareholders of the Company approved the adoption of a stand-alone incentive stock option plan (the "Option Plan") in accordance with the policies of the TSX-V.

Unless increased in accordance with the terms of the plan and the rules of the TSX-V or any other applicable stock exchange, the maximum number of common shares which may be issued under the Incentive Plan is fixed at 7,042,150. The Option Plan is a "rolling plan" which provides that the aggregate number of common shares which may be reserved for issuance under the Option Plan is limited to not more than 10% of the aggregate number of common shares outstanding. However, each of the Incentive Plan and the Option Plan provide that under no circumstances shall there be common shares issuable under such plan, together with all other security-based compensation arrangements of the Company, which exceed 10% of the aggregate number of common shares outstanding.

The Company had 5,000 stock options outstanding at September 30, 2014 and 6,000 stock options outstanding at December 31, 2013. At September 30, 2014 and December 31, 2013, the company had 113,200 DSUs outstanding, issued to non-executive directors of the Company. The DSUs were issued at the market value of the Company's common shares at the date of grant. Vested DSUs are paid out in cash when the participant ceases to be a director, officer or employee. An amount of $0.3 million related to outstanding DSUs was included in accounts payable and accrued liabilities as at September 30, 2014.

On November 14, 2014, the Company approved the grant of an aggregate of 2,375,000 RSUs to certain officers, employees and consultants under the Incentive Plan. The RSUs vest over three years and are payable when vested with either cash or common shares of the Company.

Market for Securities

On January 9, 2013, Westaim's common shares commenced trading on the TSX-V under the symbol "WED". Until January 8, 2013, the common shares of Westaim were listed on the Toronto Stock Exchange (the "TSX") under the symbol "WED". The Westaim Board of Directors determined that a listing with the TSX-V was better suited for the Company at that time while providing continued trading liquidity for the Company's shareholders. The Company received approval of its listing on the TSX-V prior to voluntarily de-listing from the TSX.

8. LIQUIDITY AND CAPITAL RESOURCES (continued)

Cash Flow Objectives

The Company manages its liquidity with a view to ensuring that there is sufficient cash to meet all financial commitments and obligations as they fall due. The Company believes its liquidity requirements for the next year will be met with the cash and cash equivalents on hand. The Company has sufficient funds to meet its financial obligations and pursue other opportunities. As part of pursuing one or more new opportunities, the Company may from time to time issue shares from treasury.

The following tables illustrate the duration of the financial assets of the Company compared to its financial obligations:

September 30, 2014 (millions)	One year or less	No specific date	Total
Financial assets:			
Cash and cash equivalents	$ 94.9	$ -	$ 94.9
Accounts receivable and other assets	0.5	-	0.5
Investments in private entities	-	95.5	95.5
Total financial assets	95.4	95.5	190.9
Financial obligations:			
Accounts payable and accrued liabilities	1.5	-	1.5
Deferred revenue	0.3	-	0.3
Site restoration provision	-	3.2	3.2
Total financial obligations	1.8	3.2	5.0
Financial assets net of financial obligations	$ 93.6	$ 92.3	$ 185.9

December 31, 2013 (millions)	One year or less	No specific date	Total
Financial assets:			
Cash and cash equivalents	$ 35.4	$ -	$ 35.4
Accounts receivable and other assets	0.2	-	0.2
Total financial assets	35.6	-	35.6
Financial obligations:			
Accounts payable and accrued liabilities	2.5	-	2.5
Site restoration provision	-	2.2	2.2
Total financial obligations	2.5	2.2	4.7
Financial assets net of financial obligations	$ 33.1	$ (2.2)	$ 30.9

The Company's investment guidelines stress preservation of capital and market liquidity to support payment of liabilities. The matching of the duration of financial assets and liabilities is monitored to ensure that all obligations will be met.

9. RELATED PARTY TRANSACTIONS

Management services agreement

The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., entered into an MSA with HIIG commencing on closing, whereby Westaim HIIG GP Inc. will be entitled to receive from HIIG an ongoing fee of US$1.0 million annually for the first three years of the agreement and US$0.5 million annually for the next two years relating to advisory services provided under the agreement. The Company received fees of $0.5 million under the MSA, of which $0.2 million was earned in the three months ended September 30, 2014 and $0.3 million was recorded as deferred revenue in the statement of financial position at September 30, 2014.

Transactions with key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly, and include executive officers and directors of the Company.

9. RELATED PARTY TRANSACTIONS (continued)

Compensation expenses related to key management personnel, including non-executive directors, are as follows:

	Three months ended September 30		Nine months ended September 30	
(millions)	2014	2013	2014	2013
Salaries and benefits	$ 0.2	$ 0.2	$ 0.6	$ 0.9
Share-based compensation	-	0.1	0.1	0.1
	$ 0.2	$ 0.3	$ 0.7	$ 1.0

On July 29, 2014, an aggregate of 3,400,000 common shares were issued to certain directors and officers of the Company for aggregate gross proceeds of $9.0 million pursuant to the Subscription Receipt Offering, on terms equivalent to the other participants in the Subscription Receipt Offering. See discussion in Section 4, *Equity Financings* of this MD&A.

10. CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

Preparation of the financial statements in conformity with IFRS requires management to make estimates and assumptions, some of which relate to matters that are uncertain. As more information becomes known, these estimates and assumptions could change and thus have a material impact on the Company's financial condition and results of operations in the future. The Company has established detailed policies and control procedures that are intended to ensure that management's judgments and estimates are well controlled, independently reviewed and consistently applied from period to period. Management believes that its estimates for determining the valuation of the Company's assets and liabilities are appropriate.

Valuation of Investments in Private Entities

In determining the valuation of the Company's investment in the Partnership at the end of each reporting period, the Company uses the capitalized cash flow method to prepare a valuation of HIIG and the Partnership, and reviews comparable arm's length transactions and comparable publicly traded company valuations. Due to the inherent uncertainty of valuation, management's estimated values may differ significantly from the values that would have been used had a ready market for the investment existed, and the differences could be material.

11. CRITICAL ACCOUNTING POLICIES AND RECENTLY ADOPTED AND PENDING ACCOUNTING PRONOUNCEMENTS

IFRS 10 "*Consolidated Financial Statements*" ("IFRS 10") provides an exception to the consolidation requirements for entities that meet the definition of an investment entity and requires such entities to measure its investments in particular subsidiaries at FVTPL instead of consolidating those subsidiaries in its consolidated and separate financial statements.

In accordance with IFRS 10, an investment entity is an entity that: (i) obtains funds from one or more investors for the purpose of providing them with investment management services, (ii) commits to its investors that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both, and (iii) measures and evaluates the performance of substantially all of its investments on a fair value basis. In addition, IFRS 10 clarifies that an investment entity may earn fee income from the provision of investment-related services to external parties.

The Company has adopted the strategy to co-invest alongside third party capital in its investment vehicles, the first such vehicle being the Partnership, with the objective of growing shareholder value through capital appreciation in its investments and generating investment income. The Company uses fair value as the key measure to monitor and evaluate its investments. The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., also earns fees from providing advisory services to HIIG. As a result, Westaim has determined that it qualifies as an investment entity under IFRS, and commenced reporting its financial results in accordance with IFRS applicable to investment entities, on a prospective basis, effective July 1, 2014. Adopting the investment entity accounting rules in IFRS 10 did not have an impact on the Company's consolidated financial statements, except that fair value is used to measure its investments.

A full description of the Company's accounting policies and other recently adopted and pending accounting pronouncements are disclosed in note 2 and note 3, respectively, to the unaudited consolidated financial statements for the three and nine months ended September 30, 2014 and 2013.

12. QUARTERLY FINANCIAL INFORMATION

(millions)	Q3 2014	Q2 2014	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012
Revenue	$ 0.6	$ -	$ 0.1	$ 0.1	$ 0.1	$ 0.1	$ 0.1	$ 0.1
Net results of investments	13.0	-	-	-	-	-	-	-
Expenses (recovery)	(2.8)	2.9	1.7	2.1	0.6	0.8	0.6	1.1
Profit or loss and other comprehensive income	16.4	(2.9)	(1.6)	(2.0)	(0.5)	(0.7)	(0.5)	(1.0)

Revenue in the three months ended September 30, 2014 consisted of investment income of $0.4 million and advisory fee income of $0.2 million. Prior to the third quarter of 2014, quarterly revenue comprised investment income. Net results of investments of $13.0 million in the three months ended September 30, 2014 represented an unrealized gain on investments in private entities recognized by the Company related to its investment in the Partnership. Expenses included transaction and related costs incurred in connection with the investment in HIIG, through the Partnership, of $0.1 million in the third quarter of 2014, $0.5 million in the second quarter of 2014, $1.2 million in the first quarter of 2014 and $2.0 million in the fourth quarter of 2013, with $3.1 million reimbursed to the Company in the third quarter of 2014. The Company recorded a foreign exchange gain of $0.8 million in the third quarter of 2014. In the second quarter of 2014, the Company also recorded a site restoration provision expense of $0.8 million and a foreign exchange loss of $0.8 million. In the fourth quarter of 2013, the Company recorded a site restoration provision recovery of $0.4 million.

13. RISKS

For a detailed description of risk factors associated with the Company and its business, refer to Section 11 “Risk Factors” of the Company’s MD&A dated August 14, 2014 in respect of the three and six months ended June 30, 2014 and 2013. The Company is not aware of any significant changes to its risk factors from those disclosed at that time.

14. CAUTIONARY NOTE REGARDING FUTURE ORIENTED FINANCIAL INFORMATION

Certain portions of this MD&A, as well as other public statements by the Company, contain forward-looking statements. In particular, the words "strategy", "may", "will", "continue", "developed", "objective", "potential", "exploring", "could", "expect", "expected", "expects", “tends”, "indicates", and words and expressions of similar import, are intended to identify forward-looking statements. Such forward-looking statements include but are not limited to statements concerning: strategies, alternatives and objectives to maximize value for shareholders; expectations and assumptions relating to the Company’s business plan; expectations and assumptions relating to HIIG’s business and operations; expectations regarding the Company’s assets and liabilities; the Company’s ability to retain key employees; management’s belief that its estimates for determining the valuation of the Company’s assets and liabilities are appropriate; the Company’s views regarding potential future remediation costs; the effect of changes to interpretations of tax legislation on income tax provisions in future periods; and the Company’s determination that the adoption of new accounting standards will not have a material impact on its consolidated financial statements.

These statements are based on current expectations that are subject to risks, uncertainties and assumptions and the Company can give no assurance that these expectations are correct. By their nature, these statements are subject to inherent risks and uncertainties that may be general or specific. A variety of material factors, many of which are beyond the Company’s control, may affect the operations, financial position, performance and results of the Company and its business, and could cause actual results to differ materially from the expectations expressed in any of these forward-looking statements.

The Company's actual results or financial position could differ materially from those anticipated by these forward-looking statements for various reasons generally beyond the Company’s control, including, without limitation, the following factors: the Company’s ability to implement its strategy or operate its business as management currently expects; the Company and/or HIIG may have undisclosed liabilities; the Company’s ability to obtain additional funding to pursue additional acquisitions or other investments; HIIG’s ability to accurately assess the risks associated with the insurance policies that it writes and to adequately reserve against future claims; unfavourable capital market developments or other factors which may affect the investments of the Company and/or HIIG; the cyclical nature of the P&C insurance industry; HIIG’s ability to accurately predict future claims frequency; government regulations designed to protect policyholders and creditors rather than investors; litigation and regulatory actions; periodic negative publicity regarding the insurance industry; intense competition and/or industry consolidation; HIIG’s reliance on brokers and third parties to sell its products to clients; HIIG’s ability to successfully pursue its acquisition strategy; HIIG’s ability to execute its business strategy; HIIG’s ability to achieve synergies arising from successful integration plans relating to acquisitions, as well as management's estimates and expectations in relation to resulting accretion, internal rate of return and debt-to-capital ratio; terrorist attacks and ensuing events; the occurrence of catastrophic events including weather related natural disasters; HIIG’s ability to maintain its financial strength and issuer credit ratings; access to debt financing and HIIG's ability to compete for large commercial business; HIIG’s ability to alleviate risk through reinsurance; HIIG’s ability to successfully manage credit risk (including credit risk related to the financial health of reinsurers); HIIG’s reliance on information technology and telecommunications systems; dependence by the Company and HIIG on key employees and certain third party service providers; changes in laws or regulations; general economic, financial and political conditions; HIIG’s dependence on the results of operations of its subsidiaries; the volatility of the stock market and other factors affecting the Company’s share price; future sales of a substantial number of the Company’s common shares; and other risk factors set forth herein or in the Company's annual report or other public filings.

14. CAUTIONARY NOTE REGARDING FUTURE ORIENTED FINANCIAL INFORMATION (continued)

The Company disclaims any intention or obligation to revise forward-looking statements whether as a result of new information, future developments or otherwise except as required by law. All forward-looking statements are expressly qualified in their entirety by this cautionary statement.

The Westaim Corporation
Consolidated Statements of Financial Position
(unaudited)

(thousands of Canadian dollars)		September 30 2014		December 31 2013
ASSETS				
Cash and cash equivalents (note 8)	$	94,922	$	35,412
Accounts receivable and other assets (note 4)		567		159
Investments in private entities (note 5)		95,448		-
	$	190,937	$	35,571
LIABILITIES				
Accounts payable and accrued liabilities	$	1,519	$	2,450
Deferred revenue (note 5)		280		-
Site restoration provision (note 6)		3,208		2,219
		5,007		4,669
Commitments and contingent liabilities (note 7)				
SHAREHOLDERS' EQUITY				
Share capital (note 8)		346,775		203,640
Contributed surplus		12,890		12,890
Deficit		(173,735)		(185,628)
		185,930		30,902
	$	190,937	$	35,571

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

The Westaim Corporation
Consolidated Statements of Profit or Loss and Other Comprehensive Income
(unaudited)

(thousands of Canadian dollars except share and per share data)	Three Months Ended September 30 2014	Three Months Ended September 30 2013	Nine Months Ended September 30 2014	Nine Months Ended September 30 2013
Revenue				
Investment income	$ 374	$ 105	$ 461	$ 319
Fee income (note 5)	182	-	182	-
	556	105	643	319
Net results of investments				
Unrealized gain on investments in private entities (note 5)	12,997	-	12,997	-
Expenses				
Salaries and benefits	182	219	651	918
Office expenses	288	147	776	615
Professional fee (recovery) expense (note 5)	(2,704)	187	(650)	534
Site restoration provision expense (note 6)	172	7	989	21
Share-based compensation (note 9)	(22)	85	101	85
Foreign exchange gain	(781)	-	(120)	-
	(2,865)	645	1,747	2,173
Income (loss) before income tax	16,418	(540)	11,893	(1,854)
Income tax recovery	-	-	-	124
Profit or loss and other comprehensive income	$ 16,418	$ (540)	$ 11,893	$ (1,730)
Earnings per share (note 12)				
Profit or loss and other comprehensive income - basic and diluted	$ 0.31	$ (0.04)	$ 0.44	$ (0.12)
Weighted average number of common shares outstanding (in thousands)				
Basic and diluted	53,016	13,903	27,084	13,903

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

The Westaim Corporation
Consolidated Statements of Changes in Equity
(unaudited)

Nine months ended September 30, 2014

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Deficit	Total Equity
Balance at January 1, 2014	$ 203,640	$ 12,890	$ (185,628)	$ 30,902
Share capital issued and paid (note 8)	143,135	-	-	143,135
Profit or loss and other comprehensive income	-	-	11,893	11,893
Balance at September 30, 2014	$ 346,775	$ 12,890	$ (173,735)	$ 185,930

Nine months ended September 30, 2013

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Deficit	Total Equity
Balance at January 1, 2013	$ 203,640	$ 12,890	$ (181,918)	$ 34,612
Profit or loss and other comprehensive income	-	-	(1,730)	(1,730)
Balance at September 30, 2013	$ 203,640	$ 12,890	$ (183,648)	$ 32,882

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

The Westaim Corporation
Consolidated Cash Flow Statements
(unaudited)

(thousands of Canadian dollars)	Nine Months Ended September 30 2014	2013
Operating activities		
Profit (loss)	$ 11,893	$ (1,730)
Unrealized gain on investments in private entities	(12,997)	-
Share-based compensation	101	85
Site restoration provision expense	989	-
Lease expense	41	-
Income tax recovery	-	(124)
Income taxes paid	-	(1,406)
Net change in other non-cash balances	(1,018)	196
Cash used in operating activities	(991)	(2,979)
Investing activities		
Purchase of capital assets	(183)	-
Purchase of investment in private entities	(82,451)	-
Cash used in investing activities	(82,634)	-
Financing activities		
Issuance of share capital, net of issuance costs	143,135	-
Cash provided from financing activities	143,135	-
Net increase (decrease) in cash and cash equivalents	59,510	(2,979)
Cash and cash equivalents, beginning of period	35,412	39,164
Cash and cash equivalents, end of period	$ 94,922	$ 36,185
Cash and cash equivalents is comprised of:		
Cash	$ 94,922	$ 36,185

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

1 Nature of Operations

The Westaim Corporation (the "Company") was incorporated on May 7, 1996 by articles of incorporation under the Business Corporations Act (Alberta). The Company's head office is located at Suite 1700, 70 York Street, Toronto, Ontario, Canada. These financial statements were authorized for issue by the Board of Directors of the Company on November 14, 2014.

On July 31, 2014, the Company completed the acquisition of a significant interest in Houston International Insurance Group, Ltd. ("HIIG") through Westaim HIIG Limited Partnership (the "Partnership"), an Ontario limited partnership managed by a subsidiary of the Company and with its principal place of business situated at Suite 1700, 70 York Street, Toronto, Ontario, Canada. HIIG is a U.S. based diversified specialty insurance provider and managing general insurance agent covering risks across the United States and certain niche global markets. HIIG's principal place of business is situated at 6th Floor, 800 Gessner Road, Houston, Texas, United States. See notes 5 and 8 for additional information on the acquisition and related financing transactions.

On January 9, 2013, the Company's common shares commenced trading on the TSX Venture Exchange ("TSX-V") under the symbol WED. Until January 8, 2013, the Company's common shares were traded on the Toronto Stock Exchange under the symbol WED. Concurrent with the commencement of trading on the TSX Venture Exchange, the Company's common shares were voluntarily delisted from the Toronto Stock Exchange. On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the current and comparative periods have been adjusted to reflect this change.

2 Basis of Preparation and Summary of Significant Accounting Policies

Basis of Preparation and Adoption of IFRS for Investment Entities

These financial statements are prepared in compliance with International Financial Reporting Standards ("IFRS"), including International Accounting Standard ("IAS") 34 *"Interim Financial Reporting"*, and include, on a consolidated basis, the accounts of wholly-owned subsidiaries, Westaim Management GP Inc. and Westaim HIIG GP Inc.

IFRS 10 "*Consolidated Financial Statements*" ("IFRS 10") provides an exception to the consolidation requirements for entities that meet the definition of an investment entity and requires such an entity to measure its investments in particular subsidiaries at fair value through profit or loss ("FVTPL") instead of consolidating those subsidiaries in its consolidated financial statements.

In accordance with IFRS 10, an investment entity is an entity that: (i) obtains funds from one or more investors for the purpose of providing them with investment management services, (ii) commits to its investors that its business purpose is to invest funds solely for returns from capital appreciation, investment income, or both, and (iii) measures and evaluates the performance of substantially all of its investments on a fair value basis. In addition, IFRS 10 clarifies that an investment entity may earn fee income from the provision of investment-related services to external parties.

Westaim has adopted the strategy to co-invest alongside third party capital in its investment vehicles, the first such vehicle being the Partnership, with the objective of growing shareholder value through capital appreciation in its investments and generating investment income. The Company uses fair value as the key measure to monitor and evaluate its investments. The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., also earns fees from providing advisory services to HIIG. As a result, Westaim has determined that it qualifies as an investment entity under IFRS, and commenced reporting its financial results in accordance with IFRS applicable to investment entities, on a prospective basis, effective July 1, 2014. Adopting the investment entity accounting rules in IFRS 10 did not have an impact on the Company's consolidated financial statements, except that fair value is used to measure its investments.

All currency amounts are expressed in thousands of Canadian dollars except earnings per share data, unless otherwise noted.

Summary of Significant Accounting Policies

The significant accounting policies used to prepare these financial statements are as follows:

(a) Principles of consolidation

The financial statements of entities which are controlled by the Company through voting equity interests, other than those measured at FVTPL, are consolidated. The financial results of these entities, referred to as subsidiaries, are included in the consolidated financial statements from the date that control commences until the date that control ceases. Intercompany balances and transactions are eliminated upon consolidation.

2 Basis of Preparation and Summary of Significant Accounting Policies (continued)

(b) Use of estimates

The preparation of financial statements requires management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and changes in estimates are recorded in the reporting period in which they are determined. Key estimates are discussed in the following accounting policies and applicable notes.

(c) Judgments made by management

Key areas where management has made difficult, complex or subjective judgments in the process of applying the Company's accounting policies, often as a result of matters that are inherently uncertain, include valuation techniques for fair value determination of investments in private entities, site restoration provision and income taxes. For additional information on these judgments, see note 5 for investments in private entities, note 6 for site restoration provision and note 11 for income taxes.

(d) Foreign currency translation

The Canadian dollar is the functional and presentation currency of the Company. Transactions in foreign currencies are translated into Canadian dollars at rates of exchange prevailing at the time of such transactions. Monetary assets and liabilities are translated at current rates of exchange. Translation differences on investments in private entities measured at FVTPL are included in changes in the carrying value of the investments.

(e) Revenue Recognition

Investment income includes interest income and dividend income. Interest income is recognized on an accrual basis and dividend income is recognized on the ex-dividend date. Advisory fees are recorded as income on an accrual basis when earned.

(f) Cash and cash equivalents

Cash and cash equivalents consist of cash on deposit and highly liquid short-term investments with original maturities of 90 days or less.

Cash and cash equivalents are classified in the financial instrument category of loans and receivables for purposes of measurement. Cash and cash equivalents are valued at fair value at the issuance date and subsequently at amortized cost using the effective interest method. Carrying value is a reasonable approximation of fair value.

(g) Capital assets

The Company's capital assets are reported at cost less accumulated depreciation. Depreciation is calculated based on the estimated useful lives of the particular assets which is 3 to 10 years for furniture and equipment. Leasehold improvements are depreciated using the straight-line method over the lesser of the term of the lease or the estimated useful life of the assets. At the end of each reporting period, management reviews the carrying amounts of capital assets for indications of impairment. An impairment loss is recognized for the amount by which the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is the higher of fair value less cost to sell and value in use. Capital assets are included in accounts receivable and other assets in the statement of financial position.

(h) Investments

The Company's investments in marketable securities and private entities are classified as FVTPL and are carried at fair value. At initial recognition, the investments are measured at fair value, and gains and losses arising from changes in their fair value, including foreign exchange gains or losses, are included in the statement of profit or loss and other comprehensive income for the period in which they arise. Transaction costs on the investments are expensed as incurred. Fair value is determined in the manner described in note 5.

Marketable securities are carried at fair value. Quoted market prices are used in determining the fair value of individual investments held. The Company records security purchases and sales on a trade date basis.

Investments in securities where no quoted market values are available are generally valued initially at the cost of acquisition on the basis that such cost is a reasonable estimate of fair value. Such investments are subsequently revalued using accepted industry valuation techniques such as a substantial arm's length transaction, earnings multiples of comparable publicly traded companies and discounted cash flow analysis. Any sale, size or other liquidity restrictions on the investment is considered by management in its determination of fair value. Due to the inherent uncertainty of valuation, management's estimated values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

2 Basis of Preparation and Summary of Significant Accounting Policies (continued)

(i) Income taxes

Income tax expense is recognized in the statement of profit or loss and other comprehensive income. Current tax is based on taxable income which differs from profit or loss and other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible.

Deferred tax assets are generally recognized for all deductible temporary income tax differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets and liabilities are determined based on the enacted or substantively enacted tax laws and rates that are anticipated to apply in the year of realization. The measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the Company expects to recover or settle the carrying amount of the related assets and liabilities. The carrying amount of the deferred tax asset is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Income tax assets and liabilities are offset when the Company intends to settle on a net basis and there is a legally enforceable right to offset.

(j) Site restoration provision

Future site restoration costs relate to industrial sites previously owned by the Company and are estimated taking into consideration the anticipated method and extent of the remediation consistent with regulatory requirements, industry practices, current technology and possible uses of the site. The estimated amount of future restoration costs is reviewed periodically based on available information. The amount of the provision is the present value of the estimated future restoration costs discounted using the rate of interest of a high quality government bond.

Recoveries of costs resulting from indemnifications provided by previous owners of the Company's industrial sites have not been recognized in these financial statements. Future recoveries of site restoration costs will be recorded when received.

(k) Contributed surplus

The cost of stock options is recognized over the period from the issue date to the vesting date and recorded as contributed surplus. When share capital of the Company is repurchased by the Company, the amount by which the average carrying value of the shares exceeds the cost to repurchase the shares is removed from share capital and included in contributed surplus.

(l) Share-based compensation

The Company maintains share-based compensation plans, which are described in note 9. Any consideration paid by stock option holders for the purchase of stock is credited to share capital. The cost of stock options is recognized over the period from the issue date to the vesting date and recorded as a component of equity in contributed surplus.

Obligations related to Deferred Share Units ("DSUs") are accrued as liabilities when issued. When a change in value occurs, it is recognized in share-based compensation expense in the applicable financial period.

(m) Earnings per share

Basic earnings per share is calculated by dividing profit or loss by the total of the weighted average number of common shares outstanding during the reporting period. Profit or loss equals profit or loss and other comprehensive income for the three and nine months ended September 30, 2014 and 2013.

Diluted earnings per share is calculated on the basis of the weighted average number of shares outstanding during the reporting period plus an estimate of the additional common shares that would have been outstanding if potentially dilutive common shares had been issued using the "treasury stock" method. No adjustments to profit or loss are required for dividends, interest or other changes in income for purposes of calculating diluted earnings per share.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

3 Recently Adopted and Pending Accounting Pronouncements

In December 2011, amendments to IAS 32 "*Financial Instruments: Presentation*" were issued to clarify the existing requirements for offsetting financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2014. The adoption of these amendments did not have an impact on the Company's interim consolidated financial statements.

In May 2013, International Financial Reporting Standards Interpretations Committee Interpretation 21: Levies ("IFRIC 21") was issued. IFRIC 21 addresses various accounting issues relating to levies imposed by a government. This interpretation is effective for annual periods beginning on or after January 1, 2014. The adoption of IFRIC 21 did not have an impact on the Company's interim consolidated financial statements.

In November 2009, the IASB issued IFRS 9 *"Financial Instruments"* ("IFRS 9") as part of its plan to replace IAS 39 *"Financial Instruments: Recognition and Measurement"*. IFRS 9 requires financial assets, including hybrid contracts, to be measured at either fair value or amortized cost. In October 2010, the IASB amended the requirements for classification and measurement of financial assets and liabilities. In November 2013, the IASB introduced a new hedge accounting model and allowed early adoption of the own credit provisions of IFRS 9. In July 2014, the IASB issued the final version of IFRS 9 incorporating a new expected loss impairment model and introducing limited amendments to the classification and measurement requirements for financial assets. This version supersedes all previous versions and is mandatorily effective for periods beginning on or after January 1, 2018 with early adoption permitted.

4 Capital Assets

The following capital assets were included in accounts receivable and other assets at September 30, 2014:

September 30, 2014	Cost	Accumulated Depreciation	Net Book Value
Leasehold improvements	$ 77	$ -	$ 77
Furniture	64	-	64
Computers	50	-	50
	$ 191	$ -	$ 191

The capital assets were placed in use at the end of September 2014 and the Company will commence depreciating the capital assets in October 2014. There were no capital assets at December 31, 2013.

5 Investments

<u>Fair value measurement</u>

The Company's investments are classified as FVTPL and are carried at fair value in the statement of financial position. Changes in fair value are reported under "Net results of investments" in the statement of profit or loss and other comprehensive income.

The table below summarizes the fair value hierarchy under which the Company's investments are valued. Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs). Inputs are considered as observable if they are developed using market data, such as publicly available information about actual events or transactions, and that reflect the assumption that market participants would use when pricing the asset or liability.

As at September 30, 2014	Fair value	Level 1	Level 2	Level 3
Investments in private entities	$ 95,448	$ -	$ -	$ 95,448

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

5 Investments (continued)

Changes in the fair value measurement of investments in private entities included in Level 3 of the fair value hierarchy for the three and nine months ended September 30, 2014 are as follows:

	Three months ended September 30, 2014	Nine months ended September 30, 2014
Opening balance	$ -	$ -
Purchase of investment in private entities	82,451	82,451
Unrealized gain included in income	12,997	12,997
Ending balance	$ 95,448	$ 95,448

There were no transfers between any levels during the three and nine months ended September 30, 2014.

Investment in private entities

Fair Value Determination

The fair value of financial assets that are not traded in an active market is determined by using valuation techniques. The Company uses a variety of methods and makes assumptions that are based on market conditions existing at each period end date. Valuation techniques used for non-standardized financial instruments include the use of initial acquisition cost, discounted cash flow analysis, comparable recent arm's length transactions, comparable publicly traded companies, reference to other instruments that are substantially the same, option pricing models and other valuation techniques commonly used by market participants.

For instruments for which there is no active market, the Company may use internally developed models, which are usually based on valuation methods and techniques generally recognized as standard within the industry. Valuation models are used primarily to value unlisted equity and debt securities for which markets were or have been inactive during the financial period. Some of the inputs to these models may not be observable and are therefore estimated based on assumptions.

The output of a model is always an estimate or approximation of a value that cannot be determined with certainty, and valuation techniques employed may not fully reflect all factors relevant to the positions the Company holds. Valuations are therefore adjusted, where appropriate, to allow for additional factors including model risk, liquidity risk and counterparty risk.

In determining the valuation of investments in private entities, the Company uses generally accepted valuation methodologies, including the original purchase price, the capitalized cash flow method, reviews of comparable arm's length transactions, and reviews of comparable publicly traded company valuations.

The capitalized cash flow approach is one of estimating the present value of the projected cash flows to be generated from the business and theoretically available (though not necessarily paid) to the capital providers of the investee company. A discount rate is applied to the projected future cash flows to arrive at a present value. The discount rate is intended to reflect all risks of ownership and the associated risks of realizing a stream of projected future cash flows.

The capitalized cash flow method generally involves the estimation of future maintainable operating pre-debt cash flows which are then capitalized using a capitalization rate based on a weighted average cost of capital. It is a present value calculation of future operating cash flow expectations. The enterprise value is then reduced for the debt outstanding. Historical net operating earnings of the Company (adjusted for unusual items), and current performance and prospects are used to estimate its future operating cash flows.

Investment in Houston International Insurance Group, Ltd. (HIIG)

On March 12, 2014, the Company announced that the Partnership had agreed to acquire an approximate 42.5% equity ownership interest in HIIG for aggregate consideration of US$75,000 (the "Initial Acquisition") through (i) the purchase of shares from certain existing shareholders of HIIG (the "Sellers") for US$15,000 and (ii) the subscription for stock from HIIG's treasury for US$60,000, subject to closing adjustments. The Company had agreed to provide a US$20,000 capital commitment to the Partnership to fund, in part, the Initial Acquisition.

Under a stock purchase agreement entered into in connection with, and as a condition to, the completion of the Initial Acquisition, the Partnership also had the right and obligation to purchase the remaining shares of HIIG owned by the Sellers (24.6% with the completion of the Acquisition) for an aggregate purchase price of approximately US$38,700, subject to closing adjustments (the "Second Acquisition", and together with the Initial Acquisition, the "Acquisition"). Completion of the Second Acquisition was conditional on the Partnership raising the funds necessary to complete such purchase on terms reasonably satisfactory to the Partnership. See note 8 regarding the related equity financing arrangements.

5 Investments (continued)

On April 30, 2014, the Board of Directors of the Company approved an additional equity investment in the Partnership of up to US$25,000 to fund (subject to the pre-emptive rights of other Partnership investors) the Partnership's subscription for additional stock from HIIG's treasury contingent on the closing of the Acquisition (the "Supplemental Treasury Purchase"). The Supplemental Treasury Purchase allowed the Partnership to increase its ownership in HIIG to 70.8% on July 31, 2014. Based on commitments received from certain of the Partnership's other investors, the contribution of the Company was approximately US$16,800.

The Acquisition was subject to the receipt of all requisite regulatory approvals, including TSX Venture Exchange approval, and other regulatory approvals required under applicable U.S. competition and insurance laws, including approval of the Departments of Insurance of the States of Texas and Oklahoma.

On July 31, 2014, the Company used a portion of the proceeds from the equity financing (described in note 8 below) to purchase Class A Limited Partnership Units in the Partnership and the Partnership (together with funds committed by other investors in the Partnership) completed the Acquisition and the Supplemental Treasury Purchase and acquired 70.8% of HIIG for US$138,683. The Company's investment in the Partnership at closing was US$75,712, representing a 53.3% ownership interest in the Partnership.

The Partnership exercises control over HIIG and its insurance subsidiaries through its ownership of 70.8% of the issued and outstanding shares of HIIG. Westaim is also considered to exercise control over HIIG and its insurance subsidiaries as Westaim HIIG GP Inc., a wholly-owned subsidiary of Westaim, is the general partner of the Partnership. The amount of dividends paid by the insurance subsidiaries of HIIG to HIIG may be subject to restrictions imposed by the insurance regulators in the United States, thereby limiting the amount of dividends HIIG can pay to its shareholders, including the Partnership. Payment of dividends from HIIG to the Partnership may also be restricted as a result of covenants in credit facilities entered into by HIIG from time to time.

The Company incurred and expensed transaction and related costs in connection with the Acquisition and the Supplemental Treasury Purchase of $1,942 in 2013, and $111 and $1,806 in the three and nine months ended September 30, 2014, of which $3,130 was reimbursed at closing and recorded as an offset to professional fees in the three months ended September 30, 2014.

The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., entered into a management services agreement ("MSA") with HIIG commencing on closing, whereby Westaim HIIG GP Inc. will be entitled to receive from HIIG an ongoing fee of US$1,000 annually for the first three years of the agreement and US$500 annually for the next two years relating to advisory services provided under the agreement. The Company received fees of $462 under the MSA, of which $182 was earned in the three months ended September 30, 2014 and $280 was recorded as deferred revenue in the statement of financial position at September 30, 2014.

The investment in HIIG, through the Partnership, is accounted for at FVTPL. The fair value of the Company's investment in the Partnership was determined to be $95,448 at September 30, 2014.

In determining the valuation of Westaim's investment in the Partnership at the end of each reporting period, the Company uses the capitalized cash flow method to prepare a valuation of HIIG and the Partnership, and reviews comparable arm's length transactions and comparable publicly traded company valuations.

In arriving at the fair value of Westaim's investment in the Partnership at July 31, 2014, the Company also considered the acquisition cost of the Partnership's 70.8% investment in HIIG. Given certain seller motivations and the desire of the Sellers to provide limited indemnifications and no reserve guarantees, the purchase of shares of HIIG from the Sellers was completed at an approximate 29% discount to the December 31, 2013 adjusted book value of HIIG ("Discount Purchase"). The purchase of shares of HIIG from treasury was completed at a valuation equal to approximately 100% of the December 31, 2013 adjusted book value of HIIG and was, due to the factors outlined above, considered to be a better indicator of value. This indication of value is also based on implied valuation multiples related to the equity financing completed by the Company, implied valuation multiples drawn from comparable public companies and targets of precedent transactions operating in the specialty insurance market, and a supporting discounted cash flow approach. As a result of the determination that the purchase of the shares of HIIG from the Sellers constituted a Discount Purchase, the Company recognized an unrealized gain on its investment in the Partnership of $10,355 at July 31, 2014.

An additional unrealized gain of $2,642 was recognized in the three months ended September 30, 2014, reflecting a change in the fair value of the investment in the Partnership from August 1, 2014 to September 30, 2014 resulting from a strengthening of the U.S. dollar against the Canadian dollar. The combined unrealized gain of $12,997 has been included in the statement of profit or loss and other comprehensive income for the three months ended September 30, 2014.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

6 Site Restoration Provision

The Company has provided indemnifications to third parties with respect to future site restoration costs to be incurred on industrial sites formerly owned by the Company. The site restoration provision is based on periodic independent estimates of costs associated with soil and groundwater reclamation and remediation of these industrial sites. The ultimate environmental costs are uncertain as they are dependent on the future use of the land and future laws and regulations.

Changes to the site restoration provision for the nine months ended September 30, 2014 and 2013 are as follows:

	Nine months ended September 30	
	2014	2013
Balance at January 1	$ 2,219	$ 2,663
Changes due to:		
Inflation	256	-
Passage of time and discount rates	733	21
Balance at September 30	$ 3,208	$ 2,684

Estimates of future expenditures could change as a result of periodic reviews of the underlying assumptions supporting the provision, including remediation costs and regulatory requirements.

Cash flows are estimated to take place over the next 150 years, with the majority to take place later than 50 years after September 30, 2014. To calculate the site restoration provision, the estimated cash flows were adjusted for inflation and discounted to September 30, 2014. For inflation and discounting calculations, all cash flows later than 50 years are treated as if the cash flow would occur at 100 years. Inflation is estimated at 1.58% per annum over the next 100 years. Discount rates are based on risk free rates which range from 1.0% to 2.7% over the next 30 years. The 30-year risk free rate is used for discounting cash flows that are estimated to occur later than 30 years after September 30, 2014.

Reimbursements of future costs resulting from indemnifications provided by previous owners of the industrial sites have not been recognized in these financial statements. Future reimbursements will be recorded when received.

7 Commitments and Contingent Liabilities

(a) In connection with the sale of the operations and assets of NUCRYST Pharmaceuticals Corp. (“Nucryst”) in 2009, Nucryst agreed to indemnify the purchaser against certain liabilities or losses as described in the asset purchase agreement to an aggregate maximum of US$11,000, subject to certain exclusions. The Company also agreed to indemnify the purchaser and the purchaser’s directors, officers and employees, for an indefinite period, from certain environmental liabilities and costs relating to the premises formerly leased by Nucryst in Fort Saskatchewan, Alberta. No claims have been made under, and no amounts have been accrued related to, these indemnities.

(b) The Company has operating leases in Toronto with remaining lease terms of up to 6 years. At September 30, 2014, the Company had a total commitment of $1,491 for future occupancy cost payments including payments due not later than one year of $282, payments due later than one year and not later than five years of $1,164, and payments due later than five years of $45.

(c) The Company may be involved in legal matters that arise from time to time in the ordinary course of the Company's business. At this time, the Company is not aware of any legal matters of this type that are believed to be material to the Company's results of operations, liquidity or financial condition.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

8 Share Capital

The Company's authorized share capital consists of an unlimited number of common shares with no par value, Class A preferred shares with no par value and Class B preferred shares with no par value.

The Company's share capital at September 30, 2014 and December 31, 2013 is as follows:

	Nine months ended September 30, 2014		Year ended December 31, 2013 [1]	
Common shares	Number	Stated Capital	Number	Stated Capital
As at January 1	13,902,937	$ 203,640	13,902,940	$ 203,640
Issued	56,394,405	143,135	-	-
Cancelled	-	-	(3)	-
	70,297,342	$ 346,775	13,902,937	$ 203,640

[1] Adjusted to reflect a 50:1 share consolidation completed on October 1, 2013.

On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the current and comparative periods have been adjusted to reflect this change.

No shares of the Company are held by the Company, and there were no Class A preferred shares or Class B preferred shares outstanding at September 30, 2014 and December 31, 2013.

On April 23, 2014, the Company completed the sale, on an underwritten private placement basis, of 47,180,380 subscription receipts (the "Subscription Receipts") of the Company at a price of $2.65 per Subscription Receipt for aggregate gross proceeds to the Company of $125,028 (the "Offering"). The Company also completed a concurrent non-brokered private placement of 3,815,005 Subscription Receipts on the same terms as the Offering for aggregate gross proceeds to the Company of $10,110 (the "Concurrent Private Placement"). Investors in the Concurrent Private Placement included primarily members of the Company's Board of Directors and management team.

Under the terms of the Offering and the Concurrent Private Placement, the net proceeds of the Offering and the Concurrent Private Placement were held in escrow pending satisfaction of certain escrow release conditions, including the satisfaction of all conditions required to complete the Acquisition (other than payment of the purchase price) and the receipt of all regulatory approvals (the "Escrow Release Conditions"). Upon satisfaction of the Escrow Release Conditions, each Subscription Receipt entitled the holder to receive, for no additional consideration, one common share of the Company.

Concurrent with the closing of the Offering and the Concurrent Private Placement, the Company also entered into irrevocable subscription agreements with certain funds and co-investors (collectively, the "Investors") for the subscription of 5,399,020 common shares of the Company at a price of $2.65 per share, for aggregate gross proceeds to the Company of $14,307 (the "Additional Subscription"). The Investors were shareholders of HIIG (and members of the Seller group) and they agreed to use the proceeds from the sale of their shares of HIIG to the Partnership pursuant to the Acquisition to fund the Additional Subscription. The conditions to the closing of the Additional Subscription were the same as the Escrow Release Conditions under the Offering and the Concurrent Private Placement.

The Escrow Release Conditions were satisfied on July 29, 2014 and the Subscription Receipts were exchanged for 50,995,385 common shares of the Company pursuant to the terms of the Offering and the Concurrent Private Placement when the Escrow Release Conditions were satisfied. Aggregate gross proceeds of the Offering and the Concurrent Private Placement to the Company, before share issuance costs, amounted to $135,138. The Company used $82,451 of the proceeds from the Offering and the Concurrent Private Placement to purchase Class A Limited Partnership Units in the Partnership to enable the Partnership (together with funds committed by other investors in the Partnership) to satisfy the cash consideration payable by the Partnership in connection with the Acquisition and the Supplemental Treasury Purchase. See note 5 for additional information on the investment in HIIG. On July 31, 2014, the Company completed the Additional Subscription. On closing, the Company issued 5,399,020 common shares of the Company to the Investors at a price of $2.65 per share for aggregate gross proceeds to the Company of $14,307, and the Company was reimbursed $1,034 in transaction and related costs. The remaining net proceeds will be used by the Company for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership).

The proceeds of the Offering, the Concurrent Private Placement and the Additional Subscription to the Company were $143,135, net of transaction costs of $6,310.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

9 Share-based Compensation

At the annual and special meeting (the “Meeting”) of the shareholders of the Company held on June 19, 2014, the Company’s shareholders approved an amendment to the Company’s comprehensive long-term equity incentive plan (the “Incentive Plan”) to adopt substantially the form of long-term incentive plan of the Company in place prior to the Company’s shares being listed on the TSX-V, with certain exceptions. The amendments included (a) providing for grants of restricted share units (“RSUs”), stock appreciation rights and other share-based awards in addition to DSUs, (b) providing the Board of Directors with the option of establishing a share purchase program; and (c) removing the ability of the Company to grant stock options under the Incentive Plan. Also at the Meeting, the shareholders of the Company approved the adoption of a stand-alone incentive stock option plan (the “Option Plan”) in accordance with the policies of the TSX-V.

Unless increased in accordance with the terms of the plan and the rules of the TSX-V or any other applicable stock exchange, the maximum number of common shares which may be issued under the Incentive Plan is fixed at 7,042,150. The Option Plan is a “rolling plan” which provides that the aggregate number of common shares which may be reserved for issuance under the Option Plan is limited to not more than 10% of the aggregate number of common shares outstanding. However, each of the Incentive Plan and the Option Plan provide that under no circumstances shall there be common shares issuable under such plan, together with all other security-based compensation arrangements of the Company, which exceed 10% of the aggregate number of common shares outstanding.

Stock Options - Changes to the number of stock options for the nine months ended September 30, 2014 and 2013 are as follows:

	Nine months ended September 30, 2014		Nine months ended September 30, 2013 [(1)]	
Common share stock options	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Outstanding at January 1	6,000	$ 165.25	7,456	$ 153.50
Expired and forfeited	(1,000)	$ 197.50	(1,456)	$ 104.00
Outstanding at September 30	5,000	$ 158.80	6,000	$ 165.25

(1) Adjusted to reflect a 50:1 share consolidation completed on October 1, 2013.

Stock options outstanding are exercisable at prices ranging from $61.50 to $309.00 and at September 30, 2014 had an average remaining contractual life of 1.4 years.

Deferred Share Units - DSUs are granted to non-executive directors of the Company and are issued at the market value of the Company’s shares at the date of grant. Vested DSUs are paid out in cash when the participant ceases to be a director, officer or employee.

There were 113,200 DSUs outstanding at September 30, 2014 and December 31, 2013. There were no changes to the number of DSUs for the nine months ended September 30, 2014 and 2013.

For the three and nine months ended September 30, 2014, compensation (recovery) expense relating to DSUs was $(22) and $101 (2013 - $85 and $85). At September 30, 2014, a liability of $340 (December 31, 2013 - $239) has been accrued with respect to outstanding DSUs.

10 Related Party Transactions

The Company, through its wholly-owned subsidiary, Westaim HIIG GP Inc., entered into an MSA with HIIG commencing on closing, whereby Westaim HIIG GP Inc. will be entitled to receive from HIIG an ongoing fee of US$1,000 annually for the first three years of the agreement and US$500 annually for the next two years relating to advisory services provided under the agreement. The Company received fees of $462 under the MSA, of which $182 was earned in the three months ended September 30, 2014 and $280 was recorded as deferred revenue in the statement of financial position at September 30, 2014.

Transactions with key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly, and include executive officers and directors of the Company.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

10 Related Party Transactions (continued)

Compensation expenses related to key management personnel for the three and nine months ended September 30, 2014 and 2013 are as follows:

	Three months ended September 30		Nine months ended September 30	
	2014	2013	2014	2013
Salaries and other short-term employee benefits	$ 182	$ 219	$ 651	$ 918
Share-based compensation	(22)	85	101	85
	$ 160	$ 304	$ 752	$ 1,003

An aggregate of 3,400,000 common shares were issued to certain directors and officers of the Company pursuant to the Concurrent Private Placement completed on July 29, 2014 for aggregate gross proceeds of $9,010, on terms equivalent to the other participants in the Concurrent Private Placement. See note 8 for additional information on the Concurrent Private Placement.

11 Income Taxes

Income taxes are recognized for deferred income taxes attributed to estimated differences between the financial statement carrying values of assets and liabilities and their respective income tax bases.

Deferred tax (liabilities)/assets recognized in profit or loss in relation to:

	Three months ended September 30		Nine months ended September 30	
	2014	2013	2014	2013
Unrealized gain on investments in private entities	$ (1,640)	$ -	$ (1,640)	$ -
Non-capital loss carry-forwards	1,640	-	1,640	-
	$ -	$ -	$ -	$ -

As the realization of any related tax benefits is not probable, no deferred income tax assets have been recognized for the following:

	September 30, 2014	December 31, 2013
Non-capital loss carry-forwards	$ 45,574	$ 48,234
Capital loss carry-forwards	6,987	6,987
Deductible temporary differences	9,358	6,066
Corporate minimum tax credits	1,406	1,406
Investment tax credits	9,633	9,633

The unrecognized non-capital losses and investment tax credits will expire at various times to the end of 2034, as follows:

Non-capital losses by year of expiry:	
2026	$ 1,693
2027	6,151
2028	9,048
2029	103
2030	610
2031	20,609
2033	3,830
2034	3,530
	$ 45,574

Investment tax credits by year of expiry:	
2016	$ 961
2017	3,241
2018	888
2019	961
2020	823
2021	643
Beyond 2021	2,116
	$ 9,633

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

11 Income Taxes (continued)

The following is a reconciliation of income taxes calculated at the statutory income tax rate to the income tax expense included in the statements of profit or loss and other comprehensive income:

	Three months ended September 30		Nine months ended September 30	
	2014	2013	2014	2013
Profit (loss) before income tax	$ 16,418	$ (540)	$ 11,893	$ (1,854)
Statutory income tax rate	26.5%	26.5%	26.5%	26.5%
Income taxes at statutory income tax rate	4,351	(143)	3,152	(491)
Variations due to:				
Non-taxable portion of unrealized gain on investments in private entities	(1,640)	-	(1,640)	-
Tax losses allocated from the Partnership	(8)	-	(8)	-
Unrecognized temporary differences	(1,289)	(83)	(800)	(297)
Recognized tax losses	(1,640)	-	(1,640)	-
Unrecognized tax losses	226	226	936	788
Adjustment to prior year provision	-	-	-	(124)
Income tax recovery	$ -	$ -	$ -	$ (124)

12 Earnings per Share

The Company uses the treasury stock method to calculate diluted earnings per share. Following the treasury stock method, the numerator for the Company's diluted earnings per share calculation remains unchanged from the basic earnings per share calculation, as the assumed exercise of the Company's stock options does not result in an adjustment to profit or loss.

Stock options to purchase 5,000 common shares were outstanding at September 30, 2014 (December 31, 2013 – 6,000). These stock options were excluded in the calculation of diluted earnings per share because the exercise price of the stock options was greater than the weighted average market value of the common shares in the three and nine months ended September 30, 2014 and 2013.

13 Capital Management

The Company's capital consists of its shareholders' equity. The Company's objectives when managing capital are to maintain a strong balance sheet and maximize shareholder value. In order to achieve the Company's capital management objectives, it employs a strong and efficient capital base and manages capital in accordance with policies established by the Board of Directors. These policies relate to capital strength, capital mix, dividends and return on capital. The Company has a capital management process in place to measure, deploy and monitor its available capital to assess its adequacy on a continuous basis. Management develops the capital strategy and oversees the capital management processes. Capital is managed using internal metrics. Neither the capital of the Company or the Partnership is subject to any restrictions.

The insurance laws of each of Texas and Oklahoma generally prohibit any person from acquiring control (being 10% or more of the voting securities or securities convertible into voting securities) of a domestic insurance company or any entity that controls such insurance company unless that person has filed a notification with specified information with that state's Commissioner of Insurance (the "Commissioner") and has obtained the Commissioner's prior approval. Accordingly, any purchaser that acquires, directly or indirectly, 10% of more of the outstanding common shares of Westaim will be presumed to have acquired control of HIIG's domestic insurance companies unless, following application by that purchaser, the relevant Commissioner determines otherwise.

14 Financial Risk Management

The Company is exposed to a number of risks due to its business operations. The Company's statement of financial position at September 30, 2014 consists of short-term financial assets and financial liabilities with maturities of less than one year, investments in private entities and the site restoration provision. The most significant identified risks which arise from holding financial instruments include credit risk, liquidity risk and market risk (currency risk and interest rate risk). The Company has a comprehensive risk management framework to monitor, evaluate and manage the risks assumed in conducting its business.

<u>Credit risk</u>

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Company. The Company's credit risk arises primarily from its cash and cash equivalents. The Company manages such risk by maintaining bank accounts with a Schedule 1 bank in Canada.

14 Financial Risk Management (continued)

Liquidity risk

Liquidity risk is the risk that the Company may not be able to generate sufficient cash resources to settle its obligations in full as they fall due or can only do so on terms that are materially disadvantageous.

The Company has made investments in private entities which do not typically have an active market. Private investment transactions can be highly structured and the Company takes measures, where possible, to create defined liquidity events and as part of its strategy, the Company has sought to create or accelerate such liquidity events. However, such liquidity events are rarely expected in the first two or three years of making an investment and may not be realized as expected.

At September 30, 2014, the Company had no debt and its financial assets were significantly higher than its financial liabilities resulting in minimal liquidity risk.

Currency risk

The Company's investment in HIIG, through the Partnership, is exposed to foreign exchange risk as HIIG's operations are located in the United States and its functional currency is the U.S. dollar. The Company's functional currency is the Canadian dollar and any fluctuations in the U.S. dollar relative to the Canadian dollar may have a material impact on the fair value of its investment in HIIG, through the Partnership. An increase (a decrease) in the value of the U.S. dollar relative to the Canadian dollar increases (decreases) the value of the investment. A 10% strengthening of the U.S. dollar against the Canadian dollar would have resulted in an increase in the fair value of investments in private entities at September 30, 2014 by approximately $9,545 and an increase in the unrealized gain on investments in private entities by a corresponding amount. A similar weakening of the U.S. dollar would have had the opposite impact.

Interest rate risk

The Company is subject to nominal interest rate risk on its cash and cash equivalents. The Company does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates relative to interest rates on its cash and cash equivalents.

15 Subsequent Event

On November 14, 2014, the Company approved the grant of an aggregate of 2,375,000 RSUs to certain officers, employees and consultants under the Incentive Plan. The RSUs vest over three years and are payable when vested with either cash or common shares of the Company.

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