ARCH BIOPARTNERS INC.

Consolidated Financial Statements

Years Ended September 30, 2011 and 2010

ARCH BIOPARTNERS INC.

Index to Consolidated Financial Statements

Years Ended September 30, 2011 and 2010

THE EXCHANGE

chartered accountants LLP

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Arch Biopartners Inc.

We have audited the accompanying consolidated financial statements of Arch Biopartners Inc., which comprise the consolidated balance sheets as at September 30, 2011 and 2010, and the consolidated statements of loss, deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Arch Biopartners Inc. as at September 30, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 1 - Description of Business and Going Concern Assumption in the financial statements which indicates that the entity has a shareholders' deficiency of $174,133 for the year ended September 30, 2011 and, as of that date, the Company has no revenue. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern.

The Exchange

chartered accountants LLP
Winnipeg, Manitoba
January 26, 2012

ARCH BIOPARTNERS INC.

Consolidated Balance Sheet

September 30, 2011 and 2010

	2011	2010 *(Restated)*
ASSETS		
CURRENT		
Cash	**$ 205,567**	$ 506,249
Prepaid expenses	**5,353**	10,981
	210,920	517,230
INTANGIBLE ASSETS *(Net of accumulated amortization) (Note 2)*	**11,122**	13,902
NON-CONTROLLING INTEREST *(Note 4)*	**1**	4,151
	$ 222,043	$ 535,283
LIABILITIES AND SHAREHOLDERS' DEFICIENCY		
CURRENT		
Accounts payable and accrued liabilities	**$ 40,059**	$ 34,301
Due to related party *(Note 7)*	**356,961**	343,010
	397,020	377,311
SHAREHOLDERS' DEFICIENCY		
Share capital *(Note 8)*	**7,476,704**	7,476,704
Contributed surplus *(Notes 2, 8)*	**113,319**	-
Deficit	**(7,765,000)**	(7,318,732)
	(174,977)	157,972
	$ 222,043	$ 535,283

COMMITMENTS *(Note 10)*

ON BEHALF OF THE BOARD

___*"Richard Muruve"*_____________ *Director*

___*"Andrew Bishop"*_____________ *Director*

ARCH BIOPARTNERS INC.

Consolidated Statement of Loss

Years Ended September 30, 2011 and 2010

	2011	2010 *(Restated)*
EXPENSES		
Advertising and promotion	**$ 10,776**	$ -
Amortization of intangible assets *(Note 2)*	**2,780**	-
Interest and bank charges *(Note 7)*	**14,364**	5,090
Marketing	**20,070**	6,204
Meetings and conventions	**2,260**	-
Office	**6,507**	1,014
Transfer agent fee	**17,713**	38,325
Patent expense *(Note 2)*	**111,193**	32,010
License expense	**38,564**	-
Materials	**9,779**	4,036
Research	**31,353**	3,333
Professional fees	**51,472**	38,777
Stock based compensation *(Note 8)*	**113,319**	-
Travel	**12,537**	19,137
	442,687	147,926
LOSS FROM OPERATIONS	**(442,687)**	(147,926)
FOREIGN EXCHANGE GAIN	**569**	27
LOSS BEFORE OTHER ITEMS	**(442,118)**	(147,899)
OTHER ITEMS		
Goodwill impairment	**-**	7,075,176
Non-controlling interest impairment *(Note 4)*	**13,560**	-
Non-controlling interest	**(9,410)**	(4,151)
	4,150	7,071,025
NET LOSS	**$ (446,268)**	$ (7,218,924)
BASIC AND DILUTED LOSS PER SHARE	**$ (0.0094)**	$ (0.2075)
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING	**47,360,179**	34,766,779

ARCH BIOPARTNERS INC.

Consolidated Statement of Deficit

Years Ended September 30, 2011 and 2010

	2011	2010
DEFICIT - BEGINNING OF YEAR		
As previously reported	**$ (7,311,834)**	$ (99,808)
Prior period adjustments *(Note 9)*	**(6,898)**	-
As restated	**(7,318,732)**	(99,808)
NET LOSS FOR THE YEAR	**(446,268)**	(7,218,924)
DEFICIT - END OF YEAR	**$ (7,765,000)**	$ (7,318,732)

ARCH BIOPARTNERS INC.

Consolidated Statement of Cash Flows

Years Ended September 30, 2011 and 2010

	2011	2010 *(Restated)*
OPERATING ACTIVITIES		
Cash paid to suppliers and employees	**$ (300,268)**	$ (205,547)
Interest paid	**(414)**	(162)
Cash flow used by operating activities	**(300,682)**	(205,709)
INVESTING ACTIVITY		
Cash received upon consolidation	**-**	1,252
FINANCING ACTIVITIES		
Advances to shareholders	**-**	(18,265)
Issuance of shares	**-**	699,456
Cash flow from financing activities	**-**	681,191
INCREASE (DECREASE) IN CASH FLOW	**(300,682)**	476,734
CASH - BEGINNING OF YEAR	**506,249**	29,515
CASH - END OF YEAR	**$ 205,567**	$ 506,249

1. DESCRIPTION OF BUSINESS AND GOING CONCERN ASSUMPTION

Arch Biopartners Inc. (the "Company"), formerly “Foccini International Inc” prior to May 3, 2010, is incorporated under the Business Corporation Act (Ontario) with continuance under the CBCA. On May 7, 2010, the Company was restructured into a biotechnology firm following a reverse take over transaction (“RTO”) involving three private Canadian biotechnology firms: Arch Biotech Inc, Arch Biophysics Ltd (Formerly “1495628 Alberta Ltd”) and Arch Cancer Therapeutics Ltd (formerly “1502440 Alberta Ltd”), collectively, the “Acquirers”. In September 2010, the Company became two-thirds owner of Colorado Cancer Therapeutics, a U.S. based corporation incorporated in the State of Delaware.

Arch Biopartners Inc. is a portfolio based biotechnology company established to develop new products and technology for sale to pharmaceutical and industrial companies.

At present, the Company has four areas of focus:

- Novel treatments for brain tumours (the focus of Arch Cancer Therapeutics Ltd.);

- Novel treatments for chronic kidney and bowel diseases caused by non-infectious inflammation; (the focus of Arch Biotech Inc.);

- Binding of peptides to solid surfaces (the focus of Arch Biophysics); and

- Novel anti-cancer compounds which have shown pre-clinical efficacy in slowing the progression of pancreatic cancer, non small cell lung cancer, and prostate cancer (the focus of Colorado Cancer Therapeutics).

The Company owns, or has exclusive licence on intellectual property emanating from its four research programs. Continuing research work is being conducted at the Universities of Calgary, Alberta and Colorado. Both of the Canadian universities became shareholders of the Company upon formation of Arch Biopartners Inc. on May 7, 2010. The University of Colorado has a pending minority stake in the Company subject to a licensed product reaching certain commercial milestones.

The current balance sheet of the Company does not show a build up of material assets such as buildings and equipment as any facilities used for continuing research have been owned by the universities. Nor has the company accumulated any material liabilities to date as a result of its research activities. In the future, scientific research may also be conducted in private labs. The corporate headquarters are located in Toronto, Ontario.

The Company is in the process of performing further research and development, and has not yet determined whether costs incurred are economically recoverable. The Company's continuing operations are dependent upon any one of:

1. the existence of economically recoverable medical or industrial solutions;

2. the ability of the Company to obtain the necessary financing to complete the research; or

3. future profitable production from, or proceeds from the disposition of intellectual property.

Although there are no assurances that management's plan will be realized, management believes the Company will be able to secure the necessary financing to continue operations into the future. The financial statements do not include any adjustments to the recoverability and classification of recorded assets, or the amounts of, and classification of liabilities that would be necessary if the going concern assumption were not appropriate. Such adjustments could be material.

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1. DESCRIPTION OF BUSINESS AND GOING CONCERN ASSUMPTION *(continued)*

Basis of Consolidation

Effective May 7, 2010 the Company completed a transaction with Foccini International Inc., Arch Biotech Inc., 1495628 Alberta Ltd. and 1502440 Alberta Ltd. This transaction was accounted for as a RTO as the control of the Company was acquired by the former management of Arch Biotech Inc. In connection to this transaction, the Company's name was changed to Arch Biopartners Inc. These consolidated financial statements include the accounts of the Company and its subsidiaries from May 7, 2010. Prior period results and comparatives are those of Arch Biotech Inc. Although legally, Arch Biopartners Inc. (formerly Foccini International) is regarded as the parent or continuing company, Arch Biotech Inc., whose management have control of the company, was treated as the acquirer under Canadian generally accepted accounting principles.

Consequently, Arch Biopartners Inc. (formerly Foccini International Inc) is deemed a continuation of Arch Biotech and control of the assets and business of Arch Biopartners Inc. (formerly Foccini International Inc) is deemed to have been acquired in consideration for the issuance of the shares. On September 21, 2010 the company formed a new American subsidiary, Colorado Cancer Therapeutics ("CCT"). This company is considered to be an integrated foreign subsidiary and is consolidated using the temporal method. This foreign subsidiary is two thirds owned by Arch Biopartners, with the remaining one third accounted for as a non-controlling interest.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of financial statements for a period necessarily involves the use of estimates which have been made using careful judgment. The financial statements have, in management's opinion, been properly prepared within the reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

Changes in accounting policies

Business Combinations

In January 2009, the CICA issued Section 1582, "Business Combinations," which will replace Section 1581 of the same title, and issued Sections 1601 "Consolidated Financial Statements" and 1602 "Non-Controlling Interests". These standards will harmonize Canadian GAAP with IFRS. The amendments establish principles and requirements for determining how an enterprise recognizes and measures the fair value of certain assets and liabilities acquired in a business combination, including non-controlling interests, contingent considerations and certain acquired contingencies. The amendments also require that acquisition related transaction expenses and restructuring costs be expensed as incurred rather than capitalized as a component of the business combination. These amendments are effective for business combinations with an acquisition on or after January 1, 2011 and early adoption is permitted. The Company has not entered into any business combinations since these amendments have come into affect.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Financial instruments

The Company classifies its financial instruments into one of the following categories based on the purpose for which the asset was acquired or liability incurred. The Company's accounting policy for each category is as follows:

Assets held-for-trading

Financial instruments classified as assets held-for-trading are reported at fair value at each balance sheet date, and any change in fair value is recognized in excess (deficiency) of revenue over expenses in the period during which the change occurs. Transaction costs are expensed when incurred.

In these financial statements, cash has been classified as held-for-trading.

Available-for-sale investments

Financial instruments classified as available-for-sale are reported at fair value at each balance sheet date, and any change in fair value is recognized in net assets in the period in which the change occurs. All transactions related to marketable securities are recorded on a settlement date basis.

In these financial statements, no assets have been classified as available-for-sale.

Held-to-maturity investments

Financial instruments classified as held-to-maturity are financial assets with fixed or determinable payments and fixed maturities that the Company's management has the positive intention and ability to hold to maturity. These assets are initially recorded at fair value and subsequently carried at amortized cost, using the effective interest rate method. Transaction costs are included in the amount initially recognized.

In these financial statements, no assets have been classified as held-to-maturity.

Loans and receivables and other financial liabilities

Financial instruments classified as loans and receivables and other financial liabilities are carried at amortized cost using the effective interest method. Transaction costs are expensed when incurred.

In these financial statements no assets have been classified as loans and receivables. Accounts payable and accrued liabilities and amounts due to related party have been classified as other financial liabilities.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Capital disclosures

Capital is comprised of the Company's shareholders' equity and any debt that it may issue. As at September 30, 2011, the company's shareholders' deficiency was $174,133 and its only debt, other than trade payables, related to amounts due to related parties (See Note 7 for further details). The Company's objectives when managing capital are to continue as a going concern to protect its ability to meet its on going liabilities, and to maximize returns for shareholders over the long term. Protecting the ability to pay current and future liabilities includes maintaining capital above minimum regulatory levels, current financial strength rating requirements and internally determined capital guidelines based on risk management policies.

The capital for the Company's current expansion plan has been raised primarily from net proceeds from the recent issuance of common shares and loans from related parties. The net proceeds raised will only be sufficient to identify and evaluate a limited number of research projects.

The Company does not have any externally imposed capital requirements with which it has not complied.

Intangible assets

The incorporation costs are being amortized on a straight-line basis over their estimated useful lives of five years.

Patent fees

The Company has expensed all costs incurred with the review of patentability of intellectual property. Patent fees paid for approved patent applications are expensed, since recoverability is uncertain. Future patent costs may be capitalized if future recoverability is readily estimable.

Loss per share

The Company uses the treasury stock method to calculate earnings (loss) per share. Basic earnings (loss) per common share is computed by dividing net income (loss) available to common shareholders by the weighted average number of common shares outstanding for the period. To calculate diluted earnings per share, all options and warrants whose average exercise price is less than or equal to the average share price for the year are assumed to be exercised. Also under this method, certain shares are considered contingently issuable, such as escrowed shares subject to release based on performance criteria, are excluded from the calculation of weighted average common shares. For the year ended September 30, 2011, potentially dilutive common shares (relating to outstanding options) totaling 350,000 (September 30, 2010 - 100,000) were not included in the computation of loss per share because their effect was anti-dilutive. Therefore, diluted loss per share is the same as basic loss per share.

Revenue recognition

Revenue and cost recoveries on the sales, assignment and transfer of rights of patents are recorded in the period in which the agreement relates.

Interest income is recognized as earned.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Stock based compensation

Compensation costs attributable to all stock options granted are measured at fair value at the grant date, using the Black-Scholes Model, and are expensed over the vesting period with a corresponding increase to contributed surplus. The Black-Scholes Model requires the input of highly subjective assumptions including expected stock price volatility. Differences in input assumptions can materially affect the fair value estimate and therefore the existing models do not necessarily provide a reliable single measure of the fair value of any stock options granted.

Upon the exercise of the option, consideration received together with the amount previously recognized in contributed surplus is recorded as an increase to share capital.

Income taxes

The asset and liability method of tax allocation is used in accounting for income taxes. Under this method, future tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities, and measured using the substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is recorded to the extent that future assets are more likely than not to be realized.

Future changes in significant accounting policies

International Financial Reporting Standards ("IFRS")

In February 2008, the CICA Accounting Standards Board ("AcSB") confirmed the changeover to IFRS from Canadian GAAP will be required for publicly accountable enterprises effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The eventual changeover to IFRS represents changes to new accounting standards. The transition from current Canadian GAAP to IFRS is a significant undertaking that may materially affect the Company's reported financial position and results of operations.

3. FINANCIAL INSTRUMENTS

In the normal course of business, the company uses various financial instruments which by their nature involve risk, including market risk, interest rate risk, liquidity risk and credit risk of non performance by counter parties. These financial instruments are subject to normal credit standards, financial controls, risk management as well as monitoring procedures.

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3. FINANCIAL INSTRUMENTS *(continued)*

Fair value of recognized financial instruments

The following table sets out the fair values of recognized financial instruments using the valuation methods and assumptions described below:

	Carrying and fair values	
	September 30, 2011	September 30, 2010
Financial Assets Held for Trading		
Cash	$ 205,567	$ 506,249
Financial Liabilities at Amortized Cost		
Accounts payable and accrued liabilities	40,058	34,301

Three-level hierarchy

The Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3862 "Financial Instruments - Disclosures" requires the disclosure of a three-level hierarchy for the fair value measurements based upon transparency of inputs to the valuation of financial instruments measured at fair value on the balance sheet date are as follows:

As at September 30, 2011	Level 1	Level 2	Level 3	Total
Assets				
Cash	$205,567			$205,567

The three levels are defined as follows:

Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - inputs to valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Determination of fair value

The following methods and assumptions were used to estimate the fair values of each class of financial instruments:

The carrying value of amounts due to related parties is based on amortized cost using the effective interest rate implicit in the loan. Fair value of the loan is not readily determinable since there are no set repayment terms.

The carrying amounts of cash and accounts payable and accrued liabilities, approximate their fair values due to the short maturity of these financial instruments.

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3. FINANCIAL INSTRUMENTS *(continued)*

Risk management policies

Credit Risk

Credit risk arises from the potential that a counter party will fail to perform its obligations. The Company is not exposed to any credit risk.

Market Risk

Market risk arises through changes in the value of assets that will occur due to the volatility of changing market prices in the economy.

Liquidity Risk

Liquidity risk is the risk that the Company will not have adequate cash flows to maintain operations. The company manages liquidity risk by maintaining adequate cash balances to pay liabilities as they become due in accordance with Note 2 (Capital Management). The Company continuously monitors both actual and forecasted cash flows and matches the maturity profile of financial assets and liabilities. The company does not have a current source of operating revenue. Without continued sources of external financing, the Company may not be able to discharge its liabilities in the normal course of operations.

Currency Risk

Currency risk is the risk to the Company's earnings that arise from fluctuations of foreign exchange rates and the degree of volatility of those rates. The Company is exposed to foreign currency exchange risk on cash, accounts payable and accrued liabilities held in U.S. dollars. The Company does not use derivative instruments to reduce its exposure to foreign currency risk. As of September 30, 2011, the Company had $2,341 in U.S. cash. Had the U.S. exchange rate been 5% higher/lower at September 30, 2011, the Company's operations for the year ended September 30, 2011 would have changed by $116.

Interest Rate Risk

Interest rate risk is the risk that the value of a financial instrument might be adversely affected by a change in the interest rates. The company is exposed to interest rate risk through its loan to shareholders. The Company does not use any derivatives to manage this exposure. Had interest rates been 1% higher/lower for the year ended September 30, 2011, the Company's operations for the year ended September 30, 2011 would have changed by $131.

4. NON-CONTROLLING INTEREST IMPAIRMENT

Non-controlling interest assets have arisen on the accumulated losses incurred in Colorado Cancer Therapeutics, a company owned two-thirds by Arch Biopartners Inc. Based on the fact that Colorado Cancer Therapeutics has not generated revenue to date, and based on the number of variables in determining the value of any potential recovery, management has valued the non-controlling interest assets at a nominal value of $1 and has recorded any resulting change in value for each quarter to the consolidated interim statement of loss.

5. PATENTS

As at September 30, 2011 it was difficult to determine the value and the future recoverability of patents owned by the Company. The Company has chosen to take a conservative approach, and expense all costs relating to patents. The total patent fee expense reflected in the statement of loss relates to professional fees incurred to obtain and file patents. Future patent costs may be capitalized if future recoverability is readily estimable.

6. NON-MONETARY TRANSACTIONS

The CEO, several principal scientists and directors have significant share holdings at this time that align their interests with those of all shareholders. Due to the Corporation's early stage of development and small size of the Corporation's management team and board, the Board's Nominating and Compensation Committee has maintained the Corporation's recent practice of not compensating executives or board members. As this compensation is not readily measurable, these expenses and the related services revenue has not been recorded.

7. DUE TO RELATED PARTY

The amount reflected as due to related party is payable to a director of the company. $2,805 of this balance does not bear interest or have any terms of repayment. The remaining amount of this balance bears interest at the Canadian prime lending rate plus 1%.

During the year ending September 30, 2011, interest expense of $13,108 has been recorded as a result of this loan.

8. SHARE CAPITAL

a) Details are as follows:

	# of shares		Amount
Issued:			
Issued and fully paid, common shares			
Balance September 30, 2009	**26,371,179**	$	13,269,387
Issued for cash - private placement	**1,400,000**		699,456
Net shares issued on RTO transaction	**19,589,000**		-
Cancellation under RTO accounting	**-**		(6,492,139)
Balance, September 30, 2010 and 2011	**47,360,179**	$	7,476,704

During the year ended September 30, 2010, the following occurred:

On May 7, 2010, the Company completed a non-brokered private placement of $700,000 by issuing 1,400,000 common shares in the capital of the Company at $0.50 per common share. Share issuance costs of $544 were accounted for as a reduction in share capital.

A further 18,013,000 common shares were issued to acquire all the issued and outstanding shares in the capital of Arch Biotech, 1495628 AB Ltd and 1502440 AB Ltd.

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8. SHARE CAPITAL *(continued)*

Additionally, in connection with the closing of the acquisition of Arch Biotech, the Company issued 1,576,000 common shares to the University of Calgary pursuant to the terms of agreement between Arch Biotech, the University of Calgary and the Company.

No shares were issued during the year ended September 30, 2011.

The Company has also reserved for issuance one million common shares in the event that it exercises its option to acquire the remaining one third interest in Colorado Cancer Therapeutics it does not already own. The option is exercisable after November 20, 2011 and no later than May 20, 2013.

The Company has a discretionary stock option plan under which the Company may grant options to its directors, officers, employees and consultants. The option plan is a rolling plan whereby the maximum number of common shares that may be reserved for issuance under the plan is a rolling amount fixed at 10% of the issued and outstanding common shares of the Company from time to time with no one optionee having shares reserved for issuance in excess of 5% of the outstanding number of shares in and twelve month period. The options granted under the plan are valid for a period not to exceed five years from the date of their grant and may be subject to certain vesting conditions as determined by the Board of Directors. The options are exercisable at the price determined by the Company which must not be less than the last closing price of the listed shares of the Company before the date of their grant, less any applicable discount.

	Number of Stock Options	Weighted Average Exercise Price	Expiry date
Balance, September 30, 2009	300,000	0.2	February 2013
Granted	-	-	
Exercised	-	-	
Forfeited	(200,000)	0.2	
Balance, September 30, 2010	100,000	0.2	February 2013
Granted	250,000	0.9	April 15, 2016
Exercised	-	-	
Forfeited	-	-	
Balance, September 30, 2011	350,000	0.7	

All issued options have fully vested and are exercisable as at September 30, 2011.

b) Stock-based compensation

During the year ended September 30, 2011, the Company granted 250,000 options to a director pursuant to terms of the Company's stock option plan.

For the year ended September 30, 2011, the total compensation expense, as calculated using the Black-Scholes option pricing model, for stock options granted to this director is $113,319. The expense relating to the issuance of these options is recorded in the Statement of Loss with an offsetting increase to contributed surplus.

(continues)

8. SHARE CAPITAL *(continued)*

The fair value of options that have vested during year is estimated on the date of grant using the Black-Scholes Option Pricing Model, with the following weighted average assumptions:

	September 30, 2011
Risk free interest rate	2.38 %
Expected dividend yield	NIL
Expected stock price volatility	1.03 %
Expected option life in years	5 years
Weighted average option exercise price	$ 0.90

Option pricing models require the input of highly subjective assumptions including the expected price volatility. Change in the subjective input assumptions can materially affect the fair value estimate, and therefore the existing models do not necessarily provide a reliable single measure of the fair value of the Company's stock options.

9. PRIOR PERIOD ADJUSTMENT

During the quarter ended December 31, 2010 unanticipated legal invoices relating to patents were received that related to the September 30, 2010 year end. As a result a prior period adjustment was made to reflect an increase in accounts payable and accrued liabilities as well as patent expense in the amount of $3,564 in the fourth quarter of the September 30, 2010 year.

During the quarter ended September 30, 2011, service contracts with terms dated from July 1, 2010 to December 31, 2011 were discovered to not have been accrued for in the September 30, 2010 year. As a result, accounts payable and accrued liabilities and research expenses were increased by $3,334 for the year ended September 30, 2010.

10. COMMITMENTS

The Company entered into an agreement with Renmark Financial Communications Inc. ("Renmark") to perform investor relations activities. The Company has agreed to a one year contract starting August 1, 2011 for a monthly fee of $4,000 per month. The contract was terminated by the company effective November 30, 2011.

The Company entered into two contract service agreements with the University of Calgary for research and development services. The Company has agreed to pay $10,000 for each of the service agreements, each of which have a term of July 1, 2010 to December 31, 2011.

The Company entered into an agreement with the University of Alberta for a research assistant. The agreement runs from September 1, 2011 to August 31, 2012 for a total fee of $25,308.