# SQI Diagnostics Inc.

## Consolidated Financial Statements

## For the Years Ended September 30, 2010 and 2009

Collins Barrow
Chartered Accountants

Collins Barrow Toronto LLP
Collins Barrow Place
11 King Street West
Suite 700, Box 27
Toronto, Ontario
M5H 4C7 Canada

T. 416.480.0160
F. 416.480.2646

www.collinsbarrow.com

## AUDITORS' REPORT

**To the Shareholders of**
**SQI Diagnostics Inc.**

We have audited the consolidated balance sheets of SQI Diagnostics Inc. as at September 30, 2010 and 2009 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at September 30, 2010 and 2009 and the results of its operations and its cash flows for the years then ended, in accordance with Canadian generally accepted accounting principles.

Collins Barrow Toronto LLP

Licensed Public Accountants
Chartered Accountants
November 19, 2010
Toronto, Ontario

**SQI Diagnostics Inc.**
**Consolidated Balance Sheets**
**As at September 30, 2010 and 2009**
(Amounts are in thousands of dollars)

| | | 2010 | | 2009 |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current** | | | | |
| Cash and cash equivalents | $ | 9,408 | $ | 3,180 |
| Amounts receivable | | 3 | | 40 |
| Inventory (Note 4) | | 260 | | 322 |
| Prepaids and deposits | | 165 | | 67 |
| Due from related party (Note 5) | | 66 | | 40 |
| | | 9,902 | | 3,649 |
| **Due from related party** (Note 5) | | 32 | | 65 |
| **Property and equipment** (Note 6) | | 2,731 | | 2,097 |
| **Patents and trademarks** | | 469 | | 394 |
| | $ | 13,134 | $ | 6,205 |
| **Liabilities** | | | | |
| **Current** | | | | |
| Accounts payable and accrued liabilities | $ | 972 | $ | 369 |
| **Shareholders' Equity** | | | | |
| **Capital stock** (Note 8) | | 35,026 | | 22,366 |
| **Warrants** (Note 9) | | 1,799 | | 461 |
| **Employee share purchase loan** (Note 8) | | (10) | | (10) |
| **Contributed surplus** (Note 11) | | 8,832 | | 8,431 |
| **Deficit** | | (33,485) | | (25,412) |
| | | 12,162 | | 5,836 |
| | $ | 13,134 | $ | 6,205 |

**Approved by the Board** **"Peter Winkley"** Director **(Signed)** **"Eric Schneider"** Director **(Signed)**

See accompanying notes

## SQI Diagnostics Inc.
**Consolidated Statements of Operations and Deficit**
**Years Ended September 30, 2010 and 2009**
(Amounts are in thousands of dollars, except per share amounts)

| | | **2010** | | 2009 |
|---|---|---|---|---|
| **Revenue** | | | | |
| Product sales | **$** | **5** | $ | 5 |
| Consulting fees (Note 7) | | **30** | | 27 |
| | | **35** | | 32 |
| **Expenses** | | | | |
| Salaries and wages | | **556** | | 469 |
| General and administrative (Note 7) | | **471** | | 447 |
| Professional and consulting fees | | **659** | | 436 |
| Sales and marketing | | **474** | | 409 |
| Stock based compensation (Note 13) | | **402** | | 380 |
| Research and development costs (Note 15) | | **5,059** | | 3,362 |
| Amortization - property and equipment | | **415** | | 417 |
| Amortization - patents and trademarks | | **100** | | 98 |
| | | **8,136** | | 6,018 |
| **Loss before the undernoted items** | | **(8,101)** | | (5,986) |
| Interest income | | **32** | | 121 |
| Interest expense | | **(4)** | | (45) |
| | | **28** | | 76 |
| **Net loss** | | **(8,073)** | | (5,910) |
| **Deficit, beginning of year** | | **(25,412)** | | (19,502) |
| **Deficit, end of year** | **$** | **(33,485)** | $ | (25,412) |
| **Loss per share** | | | | |
| Basic and diluted | **$** | **(0.27)** | $ | (0.23) |
| **Weighted average number of common shares outstanding** | | | | |
| Weighted average number of shares | | **30,349** | | 25,158 |

**SQI Diagnostics Inc.**
**Consolidated Statements of Cash Flows**
**Years Ended September 30, 2010 and 2009**
(Amounts are in thousands of dollars)

| | | **2010** | | 2009 |
|---|---|---|---|---|
| **Cash provided by (used in)** | | | | |
| **Operations** | | | | |
| Net loss | **$** | **(8,073)** | $ | (5,910) |
| Items not affecting cash | | | | |
| Amortization - patents and trademarks | | **100** | | 98 |
| - property and equipment | | **415** | | 417 |
| Patents written off | | **-** | | 97 |
| Stock-based compensation | | **402** | | 380 |
| Interest accrual | | **(2)** | | (1) |
| | | **(7,158)** | | (4,919) |
| Net changes in non-cash working capital | | | | |
| Amounts receivable | | **37** | | (15) |
| Inventory | | **(568)** | | (211) |
| Prepaids and deposits | | **(98)** | | (7) |
| Accounts payable and accrued liabilities | | **604** | | (16) |
| Investment tax credits recoverable | | **-** | | 1,075 |
| Due from related party | | **7** | | - |
| | | **(7,176)** | | (4,093) |
| **Investing** | | | | |
| Purchase of property and equipment | | **(418)** | | (113) |
| Additions to patents and trademarks | | **(175)** | | (186) |
| | | **(593)** | | (299) |
| **Financing** | | | | |
| Repayment of loans payable | | **-** | | (732) |
| Proceeds from private placement and exercise of warrants and stock options, net of share issuance costs | | **13,997** | | 5,213 |
| | | **13,997** | | 4,481 |
| **Net change in cash and cash equivalents** | | **6,228** | | 89 |
| **Cash and cash equivalents, beginning of year** | | **3,180** | | 3,091 |
| **Cash and cash equivalents, end of year** | **$** | **9,408** | $ | 3,180 |

| **Non-cash Investing Activity** | | | | |
|---|---|---|---|---|
| Equipment reallocated from inventory and segregated for use by the Company | **$** | **631** | $ | - |

| **Supplemental Disclosure** | | | | |
|---|---|---|---|---|
| Cash paid for interest | **$** | **4** | $ | 44 |

See accompanying notes

## 1. NATURE OF OPERATIONS

SQI Diagnostics Inc., (the "Company"), has its head office and development centre in Toronto, Ontario. The Company is a medical systems company that develops proprietary technology in multiplexing, miniaturization and automation. The Company provides laboratories the ability to simultaneously analyse multiple biomarkers, deliver accurate and quantitative patient results in less time, significantly reduce labour cost, and increase profits when compared with current diagnostic instrumentation.

During fiscal 2009 the Company obtained Health Canada licenses and self authorization to sell in the EU and during fiscal 2010 received United States Food & Drug Administration ("FDA") clearance of its SQiDworks and IgXPLEX Rheumatoid Arthritis (RA) system. During fiscal 2010 the Company obtained a Health Canada license for its IgXPLEX Celiac™ microarray test kits that run on the Company's automated SQiDworks™ platform. The Company has earned limited revenues from its IgXPLEX RA™ and IgXPLEX Celiac™ test kits run on installed SQiDworks™ platforms to date and as such is considered to be a development stage company. The Company has a pipeline of additional autoimmune diagnostic products in various stages of development and commercialization. The Company expects to generate revenues from its IgXPLEX RA and IgXPLEX Celiac products as it grows its installed base of customers as well as from products to be launched as they complete commercialization. The continuation of the Company's research, development and commercialization activities is dependent upon the Company's ability to successfully generate product revenues, or, to finance its cash requirements through further equity financings.

## 2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles, within the framework of the significant accounting policies summarized below:

### Basis of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary. Inter-company balances and transactions are eliminated upon consolidation.

### Cash and Cash Equivalents

Cash and cash equivalents include bank deposits and highly liquid money market investments such as bankers acceptance notes, treasury bills, cashable money market funds, and cashable guaranteed investment certificates.

### Inventory

Inventory is valued at the lower of cost and replacement cost, with cost determined on a first-in, first-out basis.

## 2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

### Property and Equipment

Property and equipment are recorded at cost and are amortized on the straight-line basis over their estimated useful lives as follows:

| | | |
|---|---|---|
| Computer hardware | - | 3 years |
| Computer software | - | 3 years |
| Laboratory fixtures and equipment | - | 10 years |
| Office equipment | - | 10 years |
| Leasehold improvements | - | 10 years |

### Patents and Trademarks

The costs relating to initial patent and trademark fees are deferred and amortized over 10 years on a straight-line basis. Patents and trademarks are recorded net of accumulated amortization of $627,000 (2009 - $527,000). At year end all patents and trademarks were reviewed and were related to the Company's current systems under development. Net capitalized costs of $97,000 related to three abandoned patents were written off in fiscal 2009, with the write off included in general and administrative expense.

### Research and Development Costs

Research costs are charged to operations in the period in which they are incurred. Development costs are expensed as incurred or deferred if they meet the criteria for deferral under Canadian generally accepted accounting principles and are expected to provide future benefits with reasonable certainty.

At September 30, 2010, the Company was developing IgXPLEX diagnostics assays for celiac, vasculitis, lupus (SLE), Crohn's (IBD), antiphospholipid syndrome and our second generation, fully quantitative IgXPLEX RA assay. The Company continued its work to complete scientific discovery and assay design work for a diagnostic assay to detect and measure infliximab (also referred to as anti-TNF) in the blood of autoimmune patients. Deferral criteria have not been met, and accordingly, all development costs have been expensed in the period.

### Impairment of Long-Lived Assets

Long-lived assets comprise property and equipment and intangible assets with finite lives (patents and trademarks). The Company recognizes an impairment loss for a long-lived asset when events or changes in circumstances cause its carrying value to exceed the total undiscounted cash flows expected from its use and eventual disposition. An impairment loss is measured as the excess of the carrying value of the asset over its fair value.

### Revenue Recognition

Product sales are recognized upon the shipment of products to customers, if a signed contract exists, the sales price is fixed and determinable, collection of the resulting receivables is reasonably assured and any uncertainties with regard to customer acceptance are insignificant. Sales are recorded net of discounts and sales returns.

## 2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

The Company also provides consulting services from time to time. Consulting fee revenue is recognized when services are completed, amounts are invoiced to customers and collectability is reasonably assured.

### Stock-Based Compensation and Other Stock-Based Payments

The Company applies a fair value based method of accounting for all stock-based payments. Accordingly, stock-based payments are measured at the fair value of the consideration received or the fair value of the equity instruments issued or liabilities incurred, whichever is more reliably measurable. Stock-based compensation is charged to operations over the vesting period and the offset is credited to contributed surplus. Consideration received upon the exercise of stock options is credited to share capital at which time the related contributed surplus is transferred to share capital.

### Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at rates of exchange in effect at each transaction date. Revenue and expenses are translated at the rate of exchange at each transaction date. Gains or losses on translation are included in operations.

### Income Taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on temporary differences between financial reporting and tax bases of assets and liabilities, as well as for the benefit of losses available to be carried forward to future years for tax purposes. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future income tax assets are recorded in the financial statements if realization is considered more likely than not.

### Investment Tax Credits

Investment tax credits are accrued when qualifying expenditures are incurred and there is reasonable assurance that the credits will be realized. Investment tax credits earned with respect to current expenditures for qualified research and development activities are included in the statements of operations as a reduction of research and development costs. Investment tax credits associated with capital expenditures are reflected as reductions in the carrying amounts of capital assets.

During the year ended September 30, 2010, the Company recorded an amount of $295,000 (2009 - $87,000) as a reduction in research and development costs.

## 2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

### Financial Instruments

Financial instruments are measured initially at fair value and thereafter based on their classification.

The Company has classified and measured its financial instruments as follows:

| Financial Instrument | Classification | Measurement Basis |
|---|---|---|
| Cash and cash equivalents | Held-for-trading | Fair value |
| Amounts receivable | Loans and receivable | Amortized cost |
| Due from related party | Loans and receivable | Amortized cost |
| Accounts payable and accruals | Other financial liabilities | Amortized cost |

### Comprehensive Income

The Company has not presented a statement of comprehensive income as it has no other comprehensive income.

### Loss Per Share

Basic loss per share is computed using the weighted average number of common shares outstanding during the year. Diluted loss per share is computed using the weighted average number of common and potential common shares outstanding during the year. Potential common shares consist of the incremental common shares issuable upon the exercise of stock options and warrants determined using the treasury stock method.

### Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions 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 amount of revenue and expenses during the year. Actual results could differ from those estimates.

Significant areas requiring the use of management estimates relate to the determination of the useful lives of property and equipment and patents and trademarks for amortization purposes, valuation of ITC's receivable, valuation of stock options and warrants and valuation allowance on future tax assets.

## 3. RECENT ACCOUNTING PRONOUNCEMENTS ISSUED AND NOT YET APPLIED

### Business Combinations

In January 2009, the CICA issued Section 1582, Business Combinations, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. In addition, the CICA issued Sections 1601, Consolidated Financial Statements, and 1602, Non-Controlling Interests, which replaces the existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements, while section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

These standards apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier application permitted. The Company is currently evaluating the new sections to determine the potential impact of any future transactions on its consolidated financial statements.

### International Financial Reporting Standards

The CICA plans to converge Canadian Generally Accepted Accounting Principles with International Financial Reporting Standards ("IFRS") over a transition period expected to end in 2011, when IFRS will be fully adopted. The transition date of October 1, 2010 for the Company will require restatement for comparative purposes of amounts reported by the Company for the year ended September 30, 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS on its financial statements.

## 4. INVENTORY

Inventory consists of component parts that are to be used in the future production of SQiDworks™ Platform and IgXPLEX consumable assays.

## 5. DUE FROM RELATED PARTY

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Amount due from an officer and director, secured, bearing interest as described in note (i), principal amount of $98,000 repayable in three equal payments on September 1, 2010, 2011 and 2012. Accrued interest is due on September 1, 2011 | **$ 98** | $ 105 |
| Less: Current portion | **(66)** | (40) |
| | **$ 32** | $ 65 |

(i) Terms of the promissory note were amended on April 16, 2010 as follows: interest bearing at Canada Revenue Agency prescribed rate for taxable benefits to employees and shareholders on interest-free and low-interest loans, which was 1% per annum at September 30, 2010. Prior to amendment, the loan was bearing interest at 4.25% per annum during the year ended December 31, 2009 and non-interest bearing from October 1, 2009 to April 15, 2010.

(ii) As at September 30, 2010, the first payment of $33,000 is in arrears.

## 6. PROPERTY AND EQUIPMENT

| **As at September 30, 2010:** | **Cost ($000s)** | **Accumulated Amortization ($000s)** | **Net ($000s)** |
|---|---|---|---|
| Computer hardware | **$ 193** | **$ 141** | **$ 52** |
| Computer software | **153** | **130** | **23** |
| Laboratory fixtures and equipment | **4,172** | **1,670** | **2,502** |
| Office equipment | **176** | **128** | **48** |
| Leasehold improvements | **263** | **157** | **106** |
| | **$ 4,957** | **$ 2,226** | **$ 2,731** |

| As at September 30, 2009: | Cost ($000s) | Accumulated Amortization ($000s) | Net ($000s) |
|---|---|---|---|
| Computer hardware | $ 141 | $ 114 | $ 27 |
| Computer software | 125 | 106 | 19 |
| Laboratory fixtures and equipment | 3,255 | 1,349 | 1,907 |
| Office equipment | 147 | 112 | 35 |
| Leasehold improvements | 240 | 131 | 109 |
| | $ 3,908 | $ 1,812 | $ 2,097 |

## 7. RELATED PARTY TRANSACTIONS

Transactions with related parties occur in the normal course of business and are measured at the exchange amount. Related party transactions have been listed below, unless they have been disclosed elsewhere in the financial statements.

Included in general and administrative expense for the year ended September 30, 2010 is $49,000 (2009 - $50,000) , related to recovery of occupancy costs, from a corporation in which an officer of the Company is also an officer. Consulting fee revenue of $30,000 for the year ended September 30, 2010 (2009 - $27,000) was earned from this corporation. At year end, $1,000 (2009 - $6,000) due from this corporation is included in amounts receivable.

## 8. CAPITAL STOCK

(a) Authorized

unlimited common shares

Issued - common shares

| | Number (000s) | | **Value ($000s)** |
|---|---|---|---|
| Balance, September 30, 2008 | 22,217 | $ | **17,323** |
| Warrants exercised | 1,111 | | **689** |
| Issued in connection with a private placement (i) | 3,732 | | **4,664** |
| Option exercised | 133 | | **35** |
| Share issuance cost (i) | - | | **(345)** |
| Balance, September 30, 2009 | 27,193 | $ | **22,366** |
| Warrants exercised (Note 9(i)) | 970 | | **2,008** |
| Issued in connection with a private placement (ii) | 4,678 | | **12,295** |
| Allocated to warrants | - | | **(1,424)** |
| Options exercised | 917 | | **755** |
| Share issuance costs (ii) | - | | **(974)** |
| **Balance, September 30, 2010** | 33,758 | **$** | **35,026** |

(i) On December 23, 2008, pursuant to a private placement, the Company issued 2,400,000 shares at a price of $1.25 per share, resulting in gross proceeds of $3,000,000. The Company paid a finder's fee in relation to the private placement satisfied through the issuance of 236,800 warrants with an exercise price of $1.90 and expiring on December 23, 2011, valued at $127,000. Total share issuance costs were $127,000.

On January 21, 2009, pursuant to a private placement the Company issued 1,331,500 shares at a price of $1.25 per share, resulting in gross proceeds of $1,664,000. The Company paid a finder's fee in relation to the private placement satisfied through the issuance of 106,520 warrants with an exercise price of $1.25 and expiring on December 23, 2011, valued at $60,000 and a cash payment of $133,000. Total share issuance costs were $193,000.

Additional share issue costs amounted to $25,000.

## 8. CAPITAL STOCK (Cont'd)

(ii) On December 4, 2009, pursuant to a private placement, the Company issued 2,398,104 units at a price of $2.75 per unit, each unit comprised one common share of the Company and one-half common share purchase warrant, resulting in gross proceeds of $6,595,000. Each whole warrant has an exercise price of $4.00 per share and expires on December 4, 2011. The value of capital stock includes value attributable to the warrants in the amount of $846,000, which has been included in warrant capital (see Note 9).

The Company paid a finder's fee in relation to the private placement satisfied through a cash payment of $453,000 and the issuance of 143,886 compensation unit warrants with an exercise price of $2.75 per unit and expiring on December 4, 2010, valued at $125,000. Each unit entitles the purchaser to purchase one common share and one-half common share purchase warrant with an exercise price of $4.00 per share, expiring on December 4, 2010. Total share issuance costs were $611,000.

On August 12, 2010, pursuant to a private placement the Company issued 2,280,000 units at a price of $2.50 per unit, each unit comprised one common share of the Company and one-half common share purchase warrant, resulting in gross proceeds of $5,700,000. Each whole warrant has an exercise price of $5.00 and expires on August 12, 2012. The value of capital stock includes value attributable to the warrants in the amount of $578,000, which has been included in warrant capital (see Note 9).

The Company paid a finder's fee in relation to the private placement satisfied through a cash payment of $260,000 and the issuance of 57,000 compensation unit warrants with an exercise price of $2.50 per unit and expiring on August 12, 2012, valued at $62,000. Each unit entitles the purchaser to purchase one common share at and one-half common share purchase warrant with an exercise price of $5.00 per share, expiring on August 12, 2012. The total share issuance costs were $363,000.

(b) During the period ended September 30, 2007, the Company made a non-interest bearing loan to its officer, which was used to acquire 100,000 common shares. The loan has been accounted for as a share purchase loan and, accordingly, the $10,000 loan balance has been deducted from share capital.

## 9. WARRANT CAPITAL

The following summarizes the change in warrants:

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Balance, beginning of period | **$ 461** | $ 274 |
| Issued on private placement (Note 8(ii)) | **1,424** | - |
| Finder warrants (Note 8) | **187** | 187 |
| Exercise of warrants (Note 10 (i)) | **(213)** | - |
| Expiry of warrants (Note 10 (i)) | **(60)** | - |
| Balance, end of period | **$ 1,799** | $ 461 |

## 10. WARRANTS

The Company had the following warrants outstanding at September 30, 2010:

| Number of Warrants (000s) | Purchase Price | Expiry Date |
|---|---|---|
| 144 | $ 2.750 | December 4, 2010 (ii) |
| 107 | $ 1.250 | January 22, 2011 |
| 1,199 | $ 4.000 | December 4, 2011 |
| 237 | $ 1.900 | December 23, 2011 |
| 1,140 | $ 5.000 | August 12, 2012 |
| 57 | $ 2.500 | August 12, 2012 |
| **2,884** | | |

(i) During the year ended September 30, 2010, 194,200 warrants with an expiry of June 3, 2010 were exercised resulting in the issuance of 194,200 shares and net proceeds of $291,000, 576,563 warrants with an expiry of June 29, 2010 were exercised resulting in the issuance of 576,563 shares and net proceeds of $1,384,000 and 199,493 warrants with an expiry of April 26, 2010 were exercised resulting in the issuance of 199,493 shares and net proceeds of $120,000. On exercise, $213,000 (2009 - $Nil) was transferred from warrant capital to share capital. The remaining 1,207,213 warrants with an expiry date of June 29, 2010 expired unexercised. On expiry, $60,000 (2009 - $Nil) was transferred from warrant capital to contributed surplus.

(ii) Subsequent to the year ended September 30, 2010, these warrants expired unexercised.

## 11. CONTRIBUTED SURPLUS

The following summarizes the change in contributed surplus:

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Balance, beginning of period | **$ 8,431** | $ 8,068 |
| Stock-based compensation (Note 13) | **402** | 380 |
| Options exercised (Note 12 (i)) | **(61)** | (17) |
| Warrants expired (Note 9(i)) | **60** | - |
| Balance, end of period | **$ 8,832** | $ 8,431 |

## 12. STOCK OPTIONS

The Company maintains a Stock Option Plan (the "Plan") for the benefit of directors, officers, employees and consultants. The aggregate number of common shares reserved for issuance under the Plan, together with any other employee stock option plans, options for services and employee share purchase plans, will not exceed 3,200,000. Options granted pursuant to the Plan will have terms not to exceed five years, and are granted at an option price which will not be less than the fair market price at the time the options are granted. All options granted to individual optionees, other than consultants, generally vest in six equal installments over a period of 18 months.

The following summarizes the stock option activities under the Plan:

| | **September 30, 2010** | | September 30, 2009 | |
|---|---|---|---|---|
| | **Number of Options (000s)** | **Weighted Average Exercise Price** | Number of Options (000s) | Weighted Average Exercise Price |
| Beginning balance | **2,368** | **$ 1.20** | 2,624 | $ 1.18 |
| Granted | **384** | **$ 2.41** | 80 | $ 1.08 |
| Exercised (i) | **(850)** | **$ 0.75** | (133) | $ 0.13 |
| Expired | **-** | **$ -** | (36) | $ 0.60 |
| Forfeited | **(138)** | **$ 1.73** | (167) | $ 0.60 |
| Ending balance | **1,764** | **$ 1.75** | 2,368 | $ 1.20 |
| Exercisable | **985** | **$ 1.60** | 1,792 | $ 1.09 |

(i) On exercise of stock options, $61,000 (2009 - $17,000) was transferred from contributed surplus to share capital.

In addition to the options exercised included in the table, there were 66,667 options that were not granted under the Plan that were exercised at a price of $0.90 per share during the year ended September 30, 2010.

There are no other options outstanding that are not part of the Plan.

## 12. STOCK OPTIONS (Cont'd)

The Company had the following stock options outstanding under the Plan at September 30, 2010:

| Number of Options (000s) | Exercise Price | Expiry Date |
|---|---|---|
| 33 | $ 1.200 | June 29, 2011 |
| 67 | $ 1.200 | August 29, 2011 |
| 180 | $ 1.740 | August 7, 2012 |
| 50 | $ 1.500 | October 23, 2012 |
| 758 | $ 1.600 | February 26, 2013 |
| 269 | $ 1.750 | August 26, 2013 |
| 80 | $ 1.300 | May 22, 2014 |
| 25 | $ 3.260 | November 3, 2014 |
| 68 | $ 2.250 | February 22, 2015 |
| 60 | $ 2.100 | May 27, 2015 |
| 175 | $ 2.500 | August 16, 2015 |
| **1,764** | | |

## 13. STOCK-BASED COMPENSATION

The fair value of the options granted during the year ended September 30, 2010 was $591,000 (2009 - $67,000), which will be recognized over the vesting period of 18 to 36 months. The total compensation expense for the year ended September 30, 2010 was $402,000 (2009 - $380,000). The total amount credited to contributed surplus for the year ended September 30, 2010 was $402,000 (2009 - $380,000).

The fair value of each option granted has been estimated at the date of grant or the date when it became measurable using the Black-Scholes option pricing model with the following weighted average assumptions at the measurement date:

| | **2010** | 2009 |
|---|---|---|
| Dividend yield | 0% | 0% |
| Expected volatility | 80% | 80% |
| Risk-free interest rate | 2.00% | 1.98% |
| Expected life (years) | 5.00 | 5.00 |
| Weighted average grant date fair value | $1.540 | $0.842 |

The Company has assumed no forfeiture rate as adjustments for actual forfeitures are made in the year they occur.

## 14. INCOME TAXES

### (a) Income Tax Expense

The following table reconciles income taxes calculated at combined Canadian federal/ provincial tax rates with the income tax expense in the financial statements:

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Loss before income taxes | **$ (8,073)** | $ (5,910) |
| Statutory rate | **31.75 %** | 33.00 % |
| Expected income tax recovery | **$ (2,563)** | $ (1,950) |
| Effect on income taxes of unrecognized future income tax assets relating to deductible temporary differences on: | | |
| Change in valuation allowance related to operations | **1,971** | 1,325 |
| Change in future tax rates | **1,150** | 121 |
| Impact of SR&ED filings | **(689)** | 302 |
| Non-deductible expenses and other items | **131** | 202 |
| Income tax expense | **$ -** | $ - |

### (b) Future Income Taxes

The temporary differences that give rise to future income tax assets and future income tax liabilities are presented below:

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Amounts related to tax loss and other credits carry forwards | **$ 8,646** | $ 6,448 |
| Property and equipment and intangibles | **(279)** | (276) |
| Share issue costs | **280** | 231 |
| Net future tax asset | **8,647** | 6,403 |
| Less: Valuation allowance | **(8,647)** | (6,403) |
| | **$ -** | $ - |

## 14. INCOME TAXES (Cont'd)

### (c) Loss and Tax Credit Carryforwards

As at September 30, 2010, the Company has non-capital losses of approximately $18,128,000 expiring as follows:

| | |
|---|---|
| 2013 | $ 879,000 |
| 2014 | 766,000 |
| 2025 | 1,146,000 |
| 2026 | 516,000 |
| 2027 | 1,154,000 |
| 2028 | 2,537,000 |
| 2029 | 3,287,000 |
| 2030 | 7,843,000 |
| | **$ 18,128,000** |

The Company has undeducted scientific research and experimental development costs of approximately $9,726,000 and investment tax credits relating to scientific research and development costs of approximately $2,046,000 available to apply against future taxable income.

The potential tax benefit relating to the non-capital losses and tax credit carryforwards has not been reflected in these financial statements.

## 15. RESEARCH AND DEVELOPMENT COSTS

The Company's autoimmune diagnostic research and development programs focus primarily on the following technology platforms:

(a) Platform: The Company develops various platforms to enable its customers to run and analyze the Company's immunoassay IgXPLEX ™ and QuantiSpot test kits. The Company's SQiDworks™ is a fully automated, multi plate system used to process up to three IgXPLEX ™ or QuantiSpot test kits. SQiDworks™ is a fully load-and-go device that completes all sample handling, biochemistry, plate scanning and data analysis. SQiDman is a semi automated system used to process single IgXPLEX ™ or QuantiSpot test kits. The Company's Platform research and development activities focus on continuous improvement to the Platforms, novel applications, required modifications for the Company's pipeline IgXPLEX ™ and QuantiSpot content as well as the evolution of the Platform to meet customer needs and market demands. SQiDworksLITE™, in the concept stage in 2010, is designed to address customers' requirements for smaller, less costly, fully automated systems and is intended to address the IVD markets as well as the research and drug development markets.

**15. RESEARCH AND DEVELOPMENT COSTS** (Cont'd)

(b) IgXPLEX™: The Company develops multiplex microarrays used to aid in the diagnosis of a variety of autoimmune diseases and with a goal of expanding the use of this technology into infectious diseases and allergens. The IgXPLEX™ research and development program includes basic and advanced research and development in materials science, surface chemistry, biochemistry, ELISA chemistry, multiplexing, antibody kinetics, autofluorescing anti body marker biochemistry and detection, multiplexed calibration and normalization, qualitative and quantitative measurement and automation of the assay biochemistry. The development of the core IgXPLEX™ technology was completed in parallel with the development of the Company's first QuantiSpot RA and IgXPLEX™ test kits licensed in Canada, cleared in the US and authorized in the EU to aid in the diagnosis of rheumatoid arthritis.

(c) Gastrointestinal ("GI"): The Company is developing a pipeline of IgXPLEX™ test kits targeted at autoimmune disorders of the digestive system. The first such test kit for Celiac disease has been licensed in Canada and is awaiting FDA approval in the United States. The IgXPLEX™ products currently in development include multiplex microarrays detecting and measuring serum antibodies to aid in the diagnosis of celiac disease and Crohn's/ulcerative colitis.

(d) Vascular: The Company is developing a pipeline of IgXPLEX™ test kits targeted at autoimmune disorders of the vasculature. The IgXPLEX™ products currently in development include multiplex microarrays detecting and measuring serum antibodies to aid in the diagnosis of vasculitis and Antiphospholipid Syndrome (APS).

(e) General Discovery Markers: The Company conducts discovery research as the first step in the development process. Discovery includes basic research to determine the suitability of candidate biomarkers that could be combined in marketable multiplex microarrays. The current research includes biomarkers used to aid in the diagnosis of autoimmune diseases and includes: lupus, thyroid disease, autoimmune hepatitis, autoimmune renal disease and food intolerance.

(f) Therapeutic Monitoring: The Company has initiated a program to develop monitoring tests used to aid in the therapeutic treatment of autoimmune diseases. These tests are used to measure biologic therapies in patient's blood to assist clinicians in their use of various clinical approaches. Therapeutic Monitoring may be used alone, or in combination with the Company's IgXPLEX™ products.

The following table summarizes the Company's research and development costs for the years ending September 30, 2010 and 2009:

| | **2010 ($000s)** | 2009 ($000s) |
|---|---|---|
| Platform | **$ 907** | $ 460 |
| IgXPLEX Technology | **1,431** | 2,050 |
| Gastrointestinal | **1,861** | 494 |
| Vascular | **345** | 217 |
| General Discovery Markets | **304** | 180 |
| Therapeutic Monitoring | **506** | 48 |
| | **5,354** | 3,449 |
| ITC Refund | **(295)** | (87) |
| | **$ 5,059** | $ 3,362 |

## 16. CONTINGENCIES

In the ordinary course of business, the Company may be contingently liable for litigation and claims with customers, suppliers, former employees or competitors. Management believes that adequate provisions have been recorded in accounts where required.

## 17. CAPITAL RISK MANAGEMENT

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern so that it can complete its lead assay commercialization efforts and receive the required regulatory approvals to sell and market its products and provide returns for shareholders and benefits for other stakeholders.

The capital structure of the Company consists of shareholders' equity. The Company is not subject to externally imposed capital requirements.

## 18. FINANCIAL RISK MANAGEMENT

### a) Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's cash and cash equivalents are exposed to credit risk. The credit risk on cash and cash equivalents is small because the counterparties are highly rated Canadian banks.

### b) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's cash and cash equivalents are exposed to cash flow interest rate risk as the Company invests cash and cash equivalents at floating rates of interest in highly liquid instruments. Fluctuations in interest rates would not significantly impact interest income.

### c) Currency Risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company is exposed to currency risk due to its purchases in US dollars. A 1% change in the foreign exchange rate would result in a change of approximately $16,000 in net loss.

### d) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company's accounts payable and accrued liabilities are all current. The Company ensures that it has sufficient capital to meet short term financial obligations after taking into account its cash on hand.

## 19. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current year's financial statement presentation.