



Afexa Life Sciences Inc.

FIRST QUARTER REPORT

Interim Consolidated
Financial Statements (Unaudited)
For the three months ended June 30, 2011

Interim Consolidated Statement of Financial Position

As at <i>(in thousands of Canadian dollars) (unaudited)</i>	June 30 2011	March 31 2011 restated (note 29)	April 1 2010 restated (note 29)
Assets			
Current			
Cash	\$ 219	\$ 3,691	\$ 17,685
Accounts receivable (note 6)	1,073	768	998
Inventory (note 7)	13,881	11,956	9,676
Prepaid expenses and deposits	1,005	470	502
Income taxes receivable	5,667	4,854	239
	21,845	21,739	29,100
Non-current			
Intangible assets (note 9)	1,274	1,307	1,298
Property and equipment (note 10)	12,014	12,225	13,004
Deferred tax assets (note 8)	1,172	965	1,067
Inventory, non-current (note 7)	–	–	243
	\$ 36,305	\$ 36,236	\$ 44,712
Liabilities			
Current			
Demand operating line of credit (note 12)	\$ 2,715	\$ –	\$ –
Accounts payable and accruals (note 11)	8,216	7,822	9,418
Provisions (note 15)	38	65	113
Customer deposits (note 14)	1,621	1,628	2,094
Current portion of long-term debt (note 12)	–	–	710
	12,590	9,515	12,335
Non-current			
Other long-term liabilities	299	287	381
Obligations under finance lease (note 13)	858	843	789
Deferred revenue	–	–	180
Long-term debt (note 12)	–	–	4,528
	13,747	10,645	18,213
Shareholders' Equity			
Share capital (note 16)	22,720	22,727	23,011
Contributed surplus (note 17)	8,844	8,733	8,531
Deficit	(9,006)	(5,869)	(5,043)
	22,558	25,591	26,499
	\$ 36,305	\$ 36,236	\$ 44,712

Commitments (note 28)

See accompanying Notes to the Interim Consolidated Financial Statements

Interim Consolidated Statement of Loss and Comprehensive Loss

<i>For the three months ended</i>	June 30	June 30
<i>(in thousands of Canadian dollars except per share amounts) (unaudited)</i>	2011	2010
		restated (note 29)
Revenue (note 27)	\$ 4,574	\$ 1,758
Cost of goods sold (note 19)	1,682	951
	2,892	807
Operating expenses		
Sales and marketing (note 19)	2,783	2,314
General and administration (note 19)	2,574	2,334
Research and development (notes 19 and 21)	1,625	1,643
Other expenses (note 19)	14	6
	6,996	6,297
Loss before finance items and income taxes	(4,104)	(5,490)
Finance items (note 22)		
Finance costs	32	80
Finance income	(3)	(17)
	29	63
Loss before income taxes	(4,133)	(5,553)
Income tax (recovery) expense (note 8)		
Current	(788)	(1,730)
Deferred	(208)	287
	(996)	(1,443)
Net loss and comprehensive loss	(3,137)	(4,110)
Loss per share, basic and diluted (note 18)	\$ (0.03)	\$ (0.04)
Weighted average number of shares outstanding		
Basic and diluted	103,198,513	104,504,670
<i>See accompanying Notes to the Interim Consolidated Financial Statements</i>		

Interim Consolidated Statement of Changes in Equity

<i>(in thousands of Canadian dollars) (unaudited)</i>	Share Capital	Contributed Surplus	Deficit	Total Shareholders' Equity
Balance at April 1, 2010	\$ 23,011	\$ 8,531	\$ (5,043)	\$ 26,499
Net loss for the three-month period	–	–	(4,110)	(4,110)
Share-based compensation related to share options granted	–	149	–	149
Balance at June 30, 2010	\$ 23,011	\$ 8,680	\$ (9,153)	\$ 22,538
Net income for the nine-month period commencing July 1, 2010 and ended March 31, 2011	–	–	3,284	3,284
Share-based compensation related to share options granted	–	456	–	456
Common shares repurchased and cancelled under the NCIB	(288)	(401)	–	(689)
Exercise of options	4	(2)	–	2
Balance at March 31, 2011	\$ 22,727	\$ 8,733	\$ (5,869)	\$ 25,591
Net loss for the three-month period	–	–	(3,137)	(3,137)
Share-based compensation related to share options granted	–	116	–	116
Common shares repurchased and cancelled under the NCIB	(7)	(5)	–	(12)
Balance at June 30, 2011	\$ 22,720	\$ 8,844	\$ (9,006)	\$ 22,558

See accompanying Notes to the Interim Consolidated Financial Statements

Interim Consolidated Statements of Cash Flows

<i>For the three months ended</i> <i>(in thousands of Canadian dollars)(unaudited)</i>	June 30 2011	June 30 2010
Operating activities		
Net loss and comprehensive loss	\$ (3,137)	\$ (4,110)
Items not affecting cash:		
Share-based payments (note 16)	69	151
Deferred income taxes	(208)	287
Depreciation and amortization (notes 9 and 10)	282	338
Amortization of lease inducements	(6)	(7)
Accreted interest on long-term debt and land under capital lease	15	23
Loss on disposal of property and equipment	1	4
Impairment of intangible assets	9	4
	(2,826)	(3,310)
Change in non-cash operating working capital (note 26)	(3,149)	(5,540)
Change in non-current inventory	–	135
Cash used in operating activities	(6,124)	(8,715)
Investing activities		
Purchase of property and equipment	(20)	(183)
Purchase of intangible assets	(31)	(38)
Proceeds on disposal of property and equipment	–	3
Cash used in investing activities	(51)	(218)
Financing activities		
Share purchase under normal course issuer bid (note 16a)	(12)	–
Repayment of long-term debt (note 12)	–	(177)
Cash used in financing activities	(12)	(177)
Decrease in cash and cash equivalents	(6,187)	(9,110)
Cash and cash equivalents, beginning of period	3,691	17,685
Cash and cash equivalents, end of period	\$ (2,496)	\$ 8,575
Cash and cash equivalents is comprised of:		
Cash	\$ 219	\$ 8,575
Demand operating line of credit	(2,715)	–
	\$ (2,496)	\$ 8,575
Supplemental cash flow information:		
Interest paid	\$ 32	\$ 80
Interest received	7	21
Income taxes paid	–	1,846
Income taxes received	133	1,155
Property and equipment additions – included in accounts payable and accruals at period end	2	27

See accompanying Notes to the Interim Consolidated Financial Statements

Notes to the Interim Consolidated Financial Statements

For the Three Months Ended June 30, 2011

All amounts are in thousands of Canadian dollars, except share and per share amounts

1. NATURE OF OPERATION

Afexa Life Sciences Inc. (“Afexa” or “the Company”) is a publicly traded company that develops and sells biopharmaceutical products. The Company has developed, commercialized and patented a proprietary technology, known as ChemBioPrint, which is used in the discovery and biological standardization of natural products that deliver consistent, verifiable and provable health benefits. Using the ChemBioPrint® product discovery and standardization platform, Afexa’s scientists are able to identify precisely the chemical profile and biological activity of natural products. The process involves a combination of chemical and biological fingerprinting to ensure that the creation and scientific substantiation of our natural health products are safe, effective and consistent. Afexa is committed to using a pharmaceutical model (involving rigorous drug discovery and testing methods) to develop natural medicines for health maintenance and disease prevention. Afexa’s lead commercial product, COLD-FX®, is designed to aid in the prevention and relief of colds and flu by strengthening the immune system.

Afexa is incorporated under the Business Corporations Act (Alberta). The Company’s common shares are traded on the Toronto Stock Exchange under the symbol FXA. The head office and research centre for the Company is located in Edmonton, Canada. The Company’s registered office is 9604-20th Avenue NW, Edmonton, Alberta, Canada, T6N 1G1.

The Company has two wholly owned subsidiary companies. COLD-FX Pharmaceuticals (USA) Inc. is incorporated in the United States, and fX Life Sciences AG is incorporated in Switzerland under the Swiss Code of Obligations.

The interim consolidated financial statements are not necessarily indicative of results on an annual basis due to seasonal and short-term variations. Revenue from the Company’s lead product, COLD-FX, exhibits a seasonal sales pattern tied to the frequency and severity of colds and flu, as well as other factors including weather. This typically results in higher revenue during the quarters ending September 30 and December 31 of each fiscal year compared to the other quarters of the year.

The unaudited interim consolidated financial statements of the Company for the three months ended June 30, 2011 were authorized for issue in accordance with a resolution of the directors on August 18, 2011.

2. BASIS OF PRESENTATION

The unaudited interim consolidated financial statements for the three months ended June 30, 2011 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”). IFRS has replaced Canadian generally accepted accounting principles (“Canadian GAAP”) for publicly accountable enterprises for years beginning on or after January 1, 2011. Accordingly, the Company has commenced reporting on this basis in these interim consolidated financial statements ending June 30, 2011.

These interim consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including International Accounting Standard (“IAS”) 34 and IFRS 1. Subject to certain transition elections disclosed in note 29, the Company has consistently applied the same accounting policies in its opening IFRS statement of financial position at April 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 29 discloses the impact of the transition to IFRS on the Company’s reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Company’s annual consolidated financial statements for the year ended March 31, 2011. Comparative figures for fiscal 2011 in these interim consolidated financial statements have been restated to give effect to these changes.

The policies applied in these interim consolidated financial statements are based on IFRS issued and outstanding as of August 18, 2011. Any subsequent changes to IFRS, that are given effect in the Company’s annual consolidated financial statements for the year ending March 31, 2012 could result in restatement of these interim consolidated financial statements, including the transition adjustments recognized on change over to IFRS.

The interim consolidated financial statements should be read in conjunction with the Company's Canadian GAAP annual consolidated financial statements for the year ended March 31, 2011. Note 29 discloses IFRS information for the year ended March 31, 2011 that is material to an understanding of these interim consolidated financial statements.

BASIS OF MEASUREMENT

The interim consolidated financial statements have been prepared on a historical cost basis, except for share-based payment arrangements that have been measured at fair value, and land under finance lease and building that have been measured at fair value as deemed cost at the transition date.

The interim consolidated financial statements are presented in Canadian dollars (\$) and rounded to the nearest thousands of Canadian dollars, except share and per share amounts or where otherwise indicated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF CONSOLIDATION

These consolidated interim financial statements consolidate the accounts of Afexa and its wholly owned subsidiaries: COLD-FX Pharmaceuticals (USA) Inc. and fX Life Sciences AG.

All intercompany transactions and balances have been eliminated. All companies included in the interim consolidated financial statements have adopted March 31 as the financial position date and use consistent accounting policies.

REVENUE RECOGNITION

Revenue from the sale of goods is recognized when all of the following criteria have been met:

- Evidence of a sales arrangement exists;
- Significant risks and rewards of ownership has transferred to the customer, which is generally at the time the goods are delivered;
- Product returns can be reasonably estimated or the right of return has expired;
- The Company retains neither continued managerial involvement nor control over the goods sold;
- The amount of revenue and costs incurred can be reliably measured; and
- Economic benefits associated with the transaction will flow to the Company.

Allowances for estimated returns are made when revenue is recognized. When future returns cannot be reasonably estimated, revenue is not recognized until the risk of return has been substantially eliminated. This risk is substantially eliminated when the final customer purchases the product from the retailer or the right of return has expired or been eliminated. The Company relies on third-party information to estimate when the final customer has completed a purchase. Product shipped where the risk of return cannot be reasonably estimated is included in inventories as product shipped with right of return.

Customer discounts, rebates and incentive allowances, which do not result in a sufficiently separable benefit from the sale, are recorded as a reduction in revenue. If they are separable, they are recorded in either cost of goods sold or in sales and marketing expense, depending on the nature of the expense. For discounts, rebates and incentive allowances to be sufficiently separable from the sale of the goods, the benefit must be identifiable, available from a party other than a purchaser of the Company's products and the fair value must be reasonably estimable.

Customer discounts, rebates and incentive allowances are recognized at the later of the date on which the Company recognizes the related revenue or the date the Company offers the discount, rebate or incentive. If the related revenue is not recognized and the discount is not recoverable in the event of return, the discount is recognized at the later of the date on which the specific activity occurs or the customer recognizes the discount, rebate or incentive allowance.

The Company may also enter into agreements where goods are exchanged for goods or services from vendors. When goods or services are exchanged or swapped for goods or services which are of a similar nature and value, the exchange is not regarded as a transaction which generates revenue. When goods or services are exchanged for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue. The revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents transferred. When the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services provided, adjusted by the amount of any cash or cash equivalents transferred.

CASH AND CASH EQUIVALENTS

Cash includes balances with banks, net of outstanding cheques, and the demand operating line of credit.

INVENTORY

Inventories of raw and packaging materials, work-in-progress, finished goods and product shipped with risk of return are valued at the lower of cost and net realizable value. Work-in-progress costs include direct materials, labour and an allocation of overhead which are determined on a weighted average basis. For product shipped with risk of return, displays and packaging materials normally included in the value of the inventory, which the Company does not expect to recover, are expensed when the product is initially shipped to the customer. Inventory is reviewed for obsolescence at least on a quarterly basis, and where identified, the excess of carrying amount over net realizable value is expensed to cost of goods sold. Previous write-downs to inventory are reversed when economic changes support an increased net realizable value. Inventory not reasonably expected to be realized in cash during the normal operating cycle is classified as non-current inventory.

INTANGIBLE ASSETS

Intangible assets, including patents, registered trademarks, and computer software, are measured on initial recognition at cost and are carried at cost less accumulated amortization and any impairment losses. Patents and registered trademarks are typically considered internally generated assets and computer software is considered acquired from third parties. All intangible assets are considered to have finite useful lives.

Amortization is recognized in earnings from the date that the assets are available for use, as this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Amortization expense on intangible assets is recognized on a straight-line basis over the remaining useful lives of the assets and are recorded in earnings in the expense category consistent with the function of the intangible asset.

Amortization is provided for using the following methods and rates:

Asset Class	Amortization Method
Patents	20 years straight-line
Computer software	3 years straight-line
Registered trademarks	10 years straight-line

The Company periodically reviews the estimated useful lives and carrying values of intangible assets for impairment. Gains or losses arising from the impairment or disposal of individual assets are recognized in earnings in the period of impairment or disposal.

PROPERTY AND EQUIPMENT

Property and equipment, including equipment under finance leases, is measured at cost less accumulated depreciation. Cost is determined by the amount paid to acquire the property and equipment including any freight and installation costs. Gains and losses arising on the disposal of individual assets are recognized within other expenses in the year disposed.

When components of property and equipment have different useful lives, they are accounted for as separate components of property and equipment.

Depreciation is not recorded until an asset is available for use and is calculated over the depreciable amount, which is the cost of the asset less residual value. The asset's residual value is the estimated amount that the Company would currently obtain from the disposition of the asset, net of estimated disposal costs, if the asset were already at the age and in the condition expected at the end of its useful life.

Depreciation is provided for using the following methods and rates:

Asset Class	Depreciation Method
Building and building improvements	15 to 25 years straight-line
Lab equipment	5 to 10 years straight-line
Furniture and equipment	5 years straight-line
Computer hardware	4 years straight-line
Leasehold improvements	Straight-line over term of lease

The cost for periodic repairs and maintenance is expensed to the extent the expenditures serve only to restore the assets to their normal operating condition without enhancing the service potential or extending their useful lives.

LEASES

Leases entered into by the Company in which substantially all of the benefits and risks of ownership are transferred to the Company are recorded as finance leases and classified as property and equipment and obligations under finance lease. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the assets are depreciated over the shorter of the lease term and their useful lives, unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. All other leases are classified as operating leases and leasing costs are expensed in the period in which they are incurred. Lease inducements received by the Company are deferred and depreciated on a straight-line basis over the term of the lease as a reduction in rental expense.

RESEARCH AND DEVELOPMENT COSTS

Research and development costs are charged to expense as incurred, net of related tax credits, unless a development project meets the criteria for capitalization and amortization. Research and development costs include the following direct operating expenditures: salaries and benefits, administration, contracting, consulting and professional fees, and share-based payments. Research and development costs also include an allocation of depreciation and amortization based on utilization of the Company's capital and intangible assets related to research and development activities.

Development costs are capitalized for clearly defined, technically feasible technologies which management intends on producing and promoting to an identified future market with existing or estimated future resources. The Company annually evaluates capitalized development costs to consider whether these costs continue to meet criteria for capitalization. The Company has not capitalized development costs during the periods presented.

GOVERNMENT GRANTS

Government grants received in relation to research activities are recognized at their fair value where there is reasonable assurance Afexa will comply with all attached conditions and will receive the funding. Government grants received for expense items are deducted from the related expense in the period the expense is incurred. For government grants received in relation to expenses of future accounting periods, Afexa recognizes the expense reduction in the period the expense is incurred. Government grants received for capital expenditures are treated as a reduction of the cost of the applicable asset.

Investment tax credits relating to qualifying scientific research and experimental development expenditures that are recoverable in the current period are accounted for as a reduction in research and development expenses or as a reduction in property and equipment depending on the nature of the expenditure. Investment tax credits not recoverable in the current period are accrued provided there is reasonable assurance that the credits will be realized.

COMPREHENSIVE INCOME

Comprehensive income is the change in equity (net assets) of the Company, during a period, from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period, except those resulting from investments by owners and distributions to owners. The Company does not have other comprehensive income, and accordingly, total comprehensive income and net earnings are equal.

FINANCIAL INSTRUMENTS

On acquisition, all financial assets are classified into the following four categories: held-to-maturity, loans and receivables, fair value through profit or loss or available-for-sale. The Company's financial instruments are classified as follows:

- Accounts receivable and cash and cash equivalents as loans and receivables
- Accounts payable and accruals and other long-term liabilities as other liabilities

All financial instruments are initially measured at fair value. Subsequent measurement depends on initial classification.

Loans and receivables

Financial instruments classified as loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Trade and other receivables are classified as receivables and are initially accounted for at fair value and subsequently adjusted for any allowance for doubtful accounts, with allowances reported in general and administration expenses.

The Company's loans and receivables are presented as current assets or non-current assets depending on their maturity.

Other liabilities

Other liabilities are initially recognized at fair value, net of any transaction costs incurred.

Financial liabilities are classified as current liabilities if payment is due within twelve months. Liabilities that have payments that extend beyond twelve months are considered non-current liabilities.

Transaction costs for demand debt obligations that are directly attributable to the acquisition or issuance of the financial liability are expensed by the Company. Transaction costs for long-term debt obligations are applied against the fair value of the liability when issued and amortized to interest expense using the effective interest rate method.

IMPAIRMENT OF LONG-LIVED ASSETS

The Company evaluates the carrying value of long-lived assets, including property and equipment, intangible assets and other assets subject to depreciation or amortization, at the end of each reporting period to determine whether there is any indication of impairment. Factors that the Company considers important which could trigger an impairment include, but are not limited to, significant underperformance relative to historical or projected future operating results, significant changes in the manner of use of the asset or the overall strategy of the business, significant negative industry or economic trends, a significant decline in the Company's share price for a sustained period and the Company's market capitalization relative to the net book value of its assets and liabilities.

Intangible assets with indefinite lives and intangible assets that are not yet in use are tested for impairment at least annually, and whenever there is an indication that the asset may be impaired.

Impairment of non-monetary long-lived assets is recognized when their carrying amount or cash generating unit ("CGU") exceeds its estimated recoverable amount and is recognized in earnings. The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate. For the purposes of impairment testing, assets that cannot be tested individually are grouped together into a CGU. CGUs are the smallest identifiable group of assets that generate cash inflows and are largely independent of the cash inflows of other assets.

Reversal of impairment costs

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

EARNINGS PER SHARE

The computation of basic earnings per share has been calculated by dividing net earnings by the weighted average number of common shares outstanding during the period.

Diluted earnings per share reflects the potential dilution that would occur if share options were exercised. The computation of diluted earnings per share has been calculated by dividing net earnings available to common shareholders by the sum of the weighted average number of common shares outstanding and all additional common shares that would have been outstanding arising from the exercise of potentially dilutive share options outstanding during the period.

The Company uses the treasury method for outstanding options which assumes that the proceeds that could be obtained upon exercise of options in computing diluted earnings per share are used to purchase the Company's common shares at the average market price during the period. Anti-dilutive amounts are not considered in computing diluted earnings per share.

INCOME TAXES

Income tax expense is comprised of current and deferred tax. Current income tax assets and liabilities for current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. Deferred taxes are determined based on differences between accounting and income tax bases of an asset and liability. Current tax and deferred tax are recognized in profit and loss except to the extent that they relate to items recognized directly in equity or in other comprehensive income. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred tax is not recognized for the following temporary differences: the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that the timing of the reversal of the temporary differences can be controlled and it is probable that they will not reverse in the foreseeable future. Deferred taxes are measured using the substantively enacted tax rates, regulations and laws in the Canada, United States, and Swiss tax jurisdictions that are anticipated to be in effect when the differences are expected to reverse.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

SHARE-BASED PAYMENT PLANS

The Company applies the fair value method of accounting for its share-based payment transactions. The fair value at grant date of share options is estimated using the Black-Scholes option pricing model. Share-based payment expense is recognized over the period that services are rendered. Any consideration paid upon exercise of share options is recorded as an increase in share capital and the recorded fair value of the related share option is reclassified from contributed surplus to share capital.

The Company has a Deferred Share Unit (“DSU”) plan, under which participants are eligible to receive an equivalent cash value of the common shares, at a future date subject to certain conditions. The value of the DSU is equal to the share price at the date of grant. Share-based payment expense is recognized as share-based payment on the date of grant as all DSUs vest on the date of grant. Changes in the amount of the liability due to share price changes after the initial grant date are recognized as share-based payments in the period in which the changes occur.

The Company also has a Restricted Share Unit (“RSU”) plan under which participants are eligible to receive an equivalent cash value of the common shares, at a future date subject to certain conditions. The value of the RSU is equal to the share price at the date of grant. In the case of RSUs granted for a prior service period, the compensation cost will be recognized in the period the RSU is granted. In the case of RSUs granted for current or future service periods, the fair value of the liability is recognized over the period that services are rendered. Changes in the amount of the liability due to share price changes are recognized as share-based payments in the period in which the changes occur.

PROVISIONS

Provisions represent liabilities of the Company for which the amount or timing is uncertain. Provisions are recognized when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are not recognized for future operating losses. Provisions are measured at the present value of the expected expenditures to settle the obligation. When the effect of the time value of money is material, provisions are discounted using a discount rate that reflects current market assessment of the time value of money and the risks specific to the obligation.

TRANSLATION OF FOREIGN CURRENCIES

Transactions in currencies other than Afexa’s functional currency (Canadian dollars) are translated at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. Non-monetary assets and liabilities measured in terms of historical cost in foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. All gains and losses on foreign currency differences are recognized in profit or loss.

4. USE OF ESTIMATES AND MEASUREMENT UNCERTAINTY

The preparation of the financial statements in accordance with IFRS requires management to make various estimates and assumptions. Critical accounting estimates are those assumptions and estimates that are most important in the preparation of the interim consolidated financial statements. The selection of policies requires subjective and complex judgment from many alternatives and estimates involving matters that are inherently uncertain. Those assumptions and estimates affect the reported amounts of assets and liabilities and revenue and expenses during the periods presented. Actual results could differ from these estimates.

Management believes the following critical accounting policies affect the more significant judgments and estimates used in the preparation of the accompanying interim consolidated financial statements:

- Revenue recognition;
- Long-lived assets and impairment;
- Depreciation and amortization;
- Accrued liabilities;
- Provisions;
- Income taxes;
- Inventory valuation; and
- Share-based payments.

On an ongoing basis, management reviews its estimates to ensure that these values appropriately reflect changes in the Company's business and new information as it becomes available. Revisions to accounting estimates are recognized in the period in which the estimate is revised. Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the annual consolidated financial statements include, but are not limited to, the following:

REVENUE RECOGNITION

The Company establishes allowances for estimated rebates, charge-backs and product returns based on numerous qualitative and quantitative factors, which include:

- The number of and specific terms of arrangements with customers;
- Estimated levels of inventory in the distribution channel;
- Historical rebates, coupon redemption rates, charge-backs and returns of products;
- Direct communication with customers;
- Anticipated introduction of competitive products;
- Anticipated pricing strategy changes by the company and/or its competitors;
- Analysis of retail sell-through;
- The effect of regulatory changes; and
- The estimated remaining shelf life of products.

Consistent with industry practice, the Company periodically offers promotional discounts or allowances to the existing customer base. Where products are sold into new markets or new products are launched, Afexa's policy is to recognize revenue when the risk of return is substantially eliminated, which is typically based on estimates of sell-through to the end consumer.

Customer discounts and allowances are typically either a percentage of the current published list price or a fixed amount, and are treated as off-invoice allowances. Accordingly, discounts reduce revenue in the period the program is offered. Discounts and allowances vary by customer, marketing program and time of the year.

LONG-LIVED ASSETS AND IMPAIRMENT

Impairment exists when the carrying value of an asset or CGU exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for the next five years and do not include restructuring activities that the Company is not yet committed to or significant future investments that will enhance the asset's performance of the CGU being tested.

The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash-inflows and the growth rate used for extrapolation purposes. To arrive at cash flow projections, the Company uses estimates of economic and market information over the projection period, including growth rates in revenues, estimates of future expected changes in operating margins, and cash expenditures. Other significant estimates and assumptions include future estimates of capital expenditures and changes in future working capital requirements.

DEPRECIATION AND AMORTIZATION

The Company depreciates property and equipment and amortizes intangible assets over the estimated useful lives of the assets. The Company takes into account expectations of the in-service period of these assets in determining these estimates. The Company assesses the estimated useful life of these assets on an annual basis to ensure they match the anticipated life of an asset from a revenue producing perspective. If the Company determines that the useful life of an asset is different from the original assessment, changes to depreciation and amortization will be applied prospectively.

ACCRUED LIABILITIES

The Company engages a significant number of third party service providers, contract manufacturers and logistics organizations. Accruals are made based on estimated expenses and/or inventory production. Where possible, detective controls, such as confirmations, are used to verify significant accruals. The accruals depend on the issuance and accuracy of estimates in purchase orders and contracts, and the accuracy of estimates on the percentage of completion and costs incurred to the end of the reporting period.

INVENTORY VALUATION

Work-in-progress costs includes the Company's allocation of overhead. This allocation is based on estimated annual production levels. Production levels are substantially driven by current and future estimated demand for the Company's products, as well as the Company's supply chain strategy.

Inventories have a finite shelf life. Raw materials, work-in-progress and finished goods have expiry dates and are subject to competitive pricing, obsolescence, and spoilage. Inventory is reviewed for obsolescence at least on a quarterly basis, and where identified, the excess of carrying amount over net realizable value is expensed to cost of goods sold. Inventory valuation allowances primarily relate to packaging material and excess inventories that would not be useable with planned changes to product branding and current revenue forecasts.

Interim reporting under IAS 34 specifies that price, efficiency, spending, and volume variances are recognized in earnings at interim reporting dates to the same extent that those variances are recognized in income at financial year end. Deferral of variances that are expected to be absorbed by year end is not appropriate because it could result in reporting inventory at the interim date at more or less than its portion of the actual cost to manufacture. Under IFRS, the Company still assesses normal capacity on an annual basis; however, any unallocated overhead variances have been recorded to cost of goods sold during the interim period.

SHARE-BASED PAYMENTS

The Company measures the cost of equity settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires the determination of the most appropriate valuation model, which is dependent on the terms and conditions of the grant. The Company uses a Black-Scholes option pricing model.

This fair value estimate also requires determining the most appropriate inputs to the valuation model including the estimated expected life of the share option, volatility, and dividend yield. The expected volatility is based on the historical volatility of the Company's shares over a period commensurate with the expected term of the share option. The risk-free interest rate for the expected life of the option is based on the yield available on government bonds, with an approximate equivalent remaining term at the end of the grant. Historical data is used to estimate the expected life of the option. As well, the Company estimates its forfeiture rate for equity settled transactions based on historical experience in order to determine the compensation expense arising from the share-based awards.

INCOME TAXES

The Company is subject to taxation in numerous jurisdictions. There are certain transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Company maintains provisions for uncertain tax positions that it believes appropriately reflect its risk with respect to tax matters under active discussion, audit, dispute or appeal with tax authorities, or which are otherwise considered to involve uncertainty. These provisions are made using the best estimate of the amount expected to be paid based on qualitative assessment of all relevant factors. The Company reviews the adequacy of these provisions at the end of each reporting period; however, it is possible that at some future date an additional liability could result from audits by taxing authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

5. FUTURE ACCOUNTING STANDARDS

IAS 12 INCOME TAXES — RECOVERY OF UNDERLYING ASSETS

This exposure draft was issued in September 2010 and contains a proposal by the IASB to amend IAS 12 Income Taxes (Deferred Tax: Recovery of Underlying Assets). The purpose of the amendments is to provide an exception to the principle that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities. The proposed amendments state that, in specified circumstances, the measurement of deferred tax liabilities and deferred tax assets should reflect a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale. This standard is required to be applied for accounting periods beginning on or after January 1, 2012, with earlier adoption permitted. The exception is currently meant to apply to only specified property and equipment or investment properties that apply the fair value or re-measurement model. The amendment to IAS 12 is not expected to have a significant impact on the Company's consolidated financial statements.

IFRS 7 FINANCIAL INSTRUMENTS: DISCLOSURES — ENHANCED DERECOGNITION DISCLOSURE REQUIREMENTS

The amendment requires additional disclosures about financial assets that have been transferred, but not derecognized, to enable the user of the Company's financial statements to understand the relationship with those assets that have not been derecognized and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognized assets to enable the user to evaluate the nature of and risks associated with, the entity's continuing involvement in those derecognized assets. The amendment becomes effective for annual periods beginning on or after July 1, 2011, with earlier adoption permitted. The amendment affects disclosure only and therefore has no impact on the Company's financial position or performance.

IFRS 9 FINANCIAL INSTRUMENTS: CLASSIFICATION AND MEASUREMENT

IFRS 9 as issued reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard is effective for annual periods beginning on or after January 1, 2015, with earlier adoption permitted. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The completion of this project is expected over the course of 2011. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Company's financial assets, but will potentially have no impact on classification and measurements of financial liabilities. The Company is currently in the process of evaluating the implications of this new standard.

IFRS 10 CONSOLIDATED FINANCIAL STATEMENTS

IFRS 10 replaces the portion of IAS 27 – Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also includes the issues raised in Standing Interpretations Committee (“SIC”) 12 – Consolidation – Special Purpose Entities. What remains in IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. IFRS 10 establishes a single control model that applies to all entities (including “special purpose entities”, or “structured entities”). The changes introduced by IFRS 10 will require management to exercise significant judgment to determine which entities are controlled, and therefore are required to be consolidated by a parent, compared with the requirements that were in IAS 27. Under IFRS 10, an investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee, and has the ability to affect those returns through its power over the investee. This principle applies to all investees, including structured entities. IFRS 10 is effective for annual periods commencing on or after January 1, 2013. The Company is currently in the process of evaluating the implications of this new standard.

6. ACCOUNTS RECEIVABLE

	June 30 2011	March 31 2011	April 1 2010
Trade receivables	\$ 1,559	\$ 1,210	\$ 1,723
Allowance for doubtful accounts	–	–	(33)
	1,559	1,210	1,690
Other receivables	115	233	552
Discount and incentive allowances	(4,030)	(4,261)	(5,208)
Return allowances	(317)	(393)	(1,053)
Other provisions	(4)	(7)	(9)
	(2,677)	(3,218)	(4,028)
Net credit balances classified to accounts payable and accruals	3,750	3,986	5,026
	\$ 1,073	\$ 768	\$ 998

Trade receivables are non-interest bearing and are generally on 30-day terms. In cases when discount and incentive allowances and return allowances for customers exceed invoice balances due from the same customer, the credit customer balance is reclassified to accounts payable and accruals.

The Company identifies impairment of trade receivables through a review of specific accounts and provides an allowance for doubtful accounts based on the excess of their carrying value over their estimated realizable amount. After all efforts of collection have failed, the accounts receivable balance not collected is written off against the allowance for doubtful accounts. The Company recorded the following activity in its allowance for doubtful accounts for the periods presented:

	June 30 2011	March 31 2011	April 1 2010
Balance, beginning of period	\$ –	\$ 33	\$ 78
Provision for doubtful accounts	–	11	78
Recovery	–	(11)	(47)
Amounts written off as uncollectible	–	(33)	(76)
Balance, end of period	\$ –	\$ –	\$ 33

The aging analysis of trade receivables is as follows:

	Total	< 30 days	30 – 60 days	60 – 90 days	> 90 days
June 30, 2011	\$ 1,559	\$ 1,505	\$ 177	\$ 12	\$ (135)
March 31, 2011	1,210	893	352	9	(44)
April 1, 2010	1,690	150	832	667	41

The credit balances for trade receivables aged over 90 days relate to customer overpayments.

As at June 30, 2011, two customers (March 31, 2011 – two customers) represented 73% (March 31, 2011 – 61%) of accounts receivable. The Company has pledged trade receivables as collateral under the terms of the demand operating line of credit (note 12).

7. INVENTORY

	June 30 2011	March 31 2011	April 1 2010
Finished goods	\$ 8,096	\$ 4,689	\$ 5,669
Work-in-progress	5,338	6,991	3,559
Raw and packaging materials	292	138	204
Products shipped with risk of return	155	138	487
	13,881	11,956	9,919
Less non-current portion	–	–	243
	\$ 13,881	\$ 11,956	\$ 9,676

The cost of inventory recognized as an expense and included in cost of goods sold, prior to overhead variances, for the three months ended June 30, 2011 was \$893 (three months ended June 30, 2010 – \$370). Included in cost of goods sold for the three months ended June 30, 2011 were write-downs of inventory totalling \$224 (three months ended June 30, 2010 – \$236). No inventory write-downs recognized in previous periods were reversed in the current period (three months ended June 30, 2010 – \$nil). Included in finished goods inventory are promotional products not held for sale of \$138 (March 31, 2011 – \$140).

The Company has pledged inventory as collateral under the terms of the demand operating line of credit (note 12).

8. INCOME TAXES

	3 months ended June 30 2011	3 months ended June 30 2010
Current tax expense		
Current period	\$ (836)	\$ (1,924)
Adjustment for prior periods	48	194
	\$ (788)	\$ (1,730)
Deferred tax (recovery) expense		
Origination and reversal of temporary differences	\$ (237)	\$ 245
Reduction in tax rate	29	42
	\$ (208)	\$ 287

Income taxes differ from the amounts that would be computed by applying the federal and provincial income tax rates as follows:

	3 months ended June 30 2011	3 months ended June 30 2010
Provision for income taxes at statutory rates of 27.1% (June 30, 2010 – 28.1%)	\$ (1,120)	\$ (1,561)
Increase (decrease) resulting from:		
Income tax related to previous periods	(2)	41
Non-deductible amounts	14	13
Tax rate differences of foreign subsidiaries	9	8
Non-deductible stock-based compensation	32	42
Change in valuation allowance	2	3
Other	69	11
Income tax expense at effective tax rate of 24.0% (June 30, 2010 – 26.0%)	\$ (996)	\$ (1,443)

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are presented below:

	Balance June 30 2011	Earnings effect for three months ended June 30 2011	Balance March 31 2011	Earnings effect for twelve months ended March 31 2011	Balance April 1 2010
Deferred tax assets:					
Non-capital losses carried forward (expiring 2014 to 2031)	\$ 4,893	\$ (244)	\$ 4,649	\$ (1,402)	\$ 3,247
Accounts receivable	54	22	76	176	252
Deferred revenue	509	(153)	356	(52)	304
Amounts not tax deductible in the current period	208	29	237	(94)	143
Property and equipment and intangible assets	293	22	315	(116)	199
Other tax assets	36	(3)	33	58	91
	5,993	(327)	5,666	(1,430)	4,236
Deferred tax liabilities:					
Scientific Research & Experimental Development ("SRED") investment tax credits	42	130	172	(120)	52
Long-term debt	–	–	–	4	4
	42	130	172	(116)	56
Net deferred tax asset	5,951		5,494		4,180
Valuation allowance	4,779	(250)	4,529	(1,416)	3,113
Net deferred tax assets	\$ 1,172		\$ 965		\$ 1,067
Deferred tax (recovery) expense*		\$ (208)		\$ 102	

* Certain columns will not total due to rounding

The Company reviews all available evidence to evaluate the recoverability of deferred tax assets. This includes a review of the Company's cumulative losses in recent years, the carryforward period related to the tax losses, and the tax planning strategies available to the Company. The Company has unused tax loss carryforwards in the United States of approximately 3.1 million United States dollars, which expire between 2027 and 2031, and are available to reduce taxable income in future years. The Company has unused tax loss carryforwards in Switzerland of approximately 32.5 million Swiss Francs, which are available to reduce taxable income in future years which expire between 2014 and 2018. The benefit of these losses has not been recorded in these interim consolidated financial statements. They have been fully offset by a valuation allowance.

9. INTANGIBLE ASSETS

	Patents	Computer software	Registered trademarks	Total intangible assets
Cost				
Cost as at April 1, 2010	\$ 1,593	\$ 578	\$ 231	\$ 2,402
Additions – internally developed	197	–	49	246
Additions – acquired separately	–	73	–	73
Disposals	(25)	(292)	(57)	(374)
Cost as at March 31, 2011	1,765	359	223	2,347
Additions – internally developed	13	–	9	22
Additions – acquired separately	–	9	–	9
Disposals	(10)	–	–	(10)
Cost as at June 30, 2011	1,768	368	232	2,368
Amortization and impairment losses				
Accumulated amortization as at April 1, 2010	668	361	75	1,104
Amortization for the year	84	133	23	240
Disposals	(2)	(288)	(14)	(304)
Accumulated amortization as at March 31, 2011	750	206	84	1,040
Amortization for the period	22	28	5	55
Disposals	(1)	–	–	(1)
Accumulated amortization as at June 30, 2011	771	234	89	1,094
Net book value				
As at April 1, 2010	\$ 925	\$ 217	\$ 156	\$ 1,298
As at March 31, 2011	\$ 1,015	\$ 153	\$ 139	\$ 1,307
As at June 30, 2011	\$ 997	\$ 134	\$ 143	\$ 1,274

10. PROPERTY AND EQUIPMENT

	Building	Lab equipment	Land under finance lease	Furniture and equipment	Computer hardware	Leasehold improvements	Total
Cost							
Cost as at April 1, 2010	\$ 10,105	\$ 1,529	\$ 2,426	\$ 985	\$ 513	\$ 355	\$ 15,913
Additions	43	48	–	114	48	2	255
Disposals	–	(139)	–	(167)	(137)	–	(443)
Cost as at March 31, 2011	10,148	1,438	2,426	932	424	357	15,725
Cost as at April 1, 2011	10,148	1,438	2,426	932	424	357	15,725
Additions	–	1	–	6	10	–	17
Disposals	–	–	–	(1)	–	–	(1)
Cost as at June 30, 2011	10,148	1,439	2,426	937	434	357	15,741
Accumulated Depreciation							
Accumulated Depreciation as at April 1, 2010	1,881	431	–	360	215	22	2,909
Depreciation for the period	350	234	–	192	132	36	944
Disposals	–	(103)	–	(139)	(111)	–	(353)
Accumulated Depreciation as at March 31, 2011	2,231	562	–	413	236	58	3,500
Accumulated Depreciation as at April 1, 2011	2,231	562	–	413	236	58	3,500
Depreciation for the period	92	54	–	45	27	9	227
Disposals	–	–	–	–	–	–	–
Accumulated Depreciation as at June 30, 2011	2,323	616	–	458	263	67	3,727
Net book value							
As at April 1, 2010	\$ 8,224	\$ 1,098	\$ 2,426	\$ 625	\$ 298	\$ 333	\$ 13,004
As at March 31, 2011	\$ 7,917	\$ 876	\$ 2,426	\$ 519	\$ 188	\$ 299	\$ 12,225
As at June 30, 2011	\$ 7,825	\$ 823	\$ 2,426	\$ 479	\$ 171	\$ 290	\$ 12,014

For the three months ended June 30, 2011, the Company recorded a loss on disposal of property and equipment of \$1 (three months ended June 30, 2010 – \$4) related to property and equipment no longer in use.

The Company has pledged land and building as collateral under the terms of the demand operating line of credit (note 12).

The Company leases a parcel of land under a finance lease agreement. The lease provides the Company with the option to purchase the land at a stated amount.

REVALUATION OF LAND UNDER FINANCE LEASE AND BUILDING

The Company's land under finance lease and building balances were assessed by an independent valuator for land and building as at April 1, 2010. The revaluation of the land under finance lease and building values was determined using a combination of direct comparisons with other similar properties and the cost approach method of valuation. This revaluation has been used as the deemed cost for land under finance lease and building under the transitional provision of IFRS 1.

11. ACCOUNTS PAYABLE AND ACCRUALS

	June 30 2011	March 31 2011	April 1 2010
Trade payables	\$ 4,625	\$ 4,862	\$ 6,383
Accrued liabilities	2,038	2,181	2,208
Employee and payroll liabilities	1,418	755	766
Other accrued liabilities	135	24	61
	\$ 8,216	\$ 7,822	\$ 9,418

Trade payables are non-interest bearing and are normally settled on 60-day terms. Accrued liabilities, employee and payroll liabilities, and other accruals are non-interest bearing and have no fixed term.

12. LONG-TERM DEBT AND OTHER CREDIT FACILITIES

LONG-TERM DEBT

	April 1, 2010
Term mortgage with interest at the bank's prime lending rate plus 1.25%.	\$ 5,146
Financing loan bearing interest at 7.39%.	108
	5,254
Less: financing charge	16
	5,238
Less: current portion	710
	\$ 4,528

The term mortgage and the financing loan were fully repaid as at March 31, 2011 and as such, no balance was owing at March 31, 2011 and June 30, 2011.

DEMAND OPERATING LINE OF CREDIT

Afexa has a credit facility agreement that consists of a demand operating line of credit of \$15,000, with interest at the bank's prime lending rate plus 0.75%. The portion of the line of credit that is available to Afexa is based on: (i) 65% of the Edmonton, Alberta head office and research centre's appraised value to a maximum limit of \$6,750 (maximum limit to be reduced annually based on an amortization period of 15 years), (ii) 75% of accounts receivable aged less than 90 days, and (iii) 50% of finished goods inventory to a maximum limit of \$4,125. The credit facility is collateralized by a General Security Agreement constituting a first ranking security interest in all personal property of the Company and a demand collateral mortgage constituting a first fixed charge on the Company's head office and research facility.

13. OBLIGATIONS UNDER FINANCE LEASE

Future lease liabilities are as follows:

	June 30 2011	March 31 2011	April 1 2010
Land under finance lease at an imputed interest rate of 6.75%.	\$ 1,155	\$ 1,155	\$ 1,155
Less: imputed interest charges	297	312	366
	858	843	789
Less: current portion	–	–	–
Long-term portion of obligations under finance lease	\$ 858	\$ 843	\$ 789

The land under finance lease is utilized for the Company's head office and research centre. The Company has an option to purchase the land under finance lease on or before November 30, 2015 for \$1,155. The Company intends to exercise this option.

14. CUSTOMER DEPOSITS

The Company has received customer deposits totaling \$1,621 (March 31, 2011 – \$1,628 and April 1, 2010 – \$2,094) for product shipped with risk of return. When the risk for the product shipped with the possibility of return is substantially eliminated, the revenue from the product shipment will be recognized and the liability for the customer deposit eliminated. If the product is returned and cash payment has been made, the customer is entitled to a refund of the deposit. There is no certainty on the amount of deposits that will be recognized as revenue, or may require refund.

15. PROVISIONS

Changes to the Company's provisions are as follows:

	Legal provisions	Other provisions	Total
Balance as at April 1, 2010	\$ 69	\$ 44	\$ 113
Arising during the year	64	–	64
Utilized	(18)	(6)	(24)
Release of unused amounts	(50)	(38)	(88)
Balance as at March 31, 2011	\$ 65	\$ –	\$ 65
Utilized	(23)	–	(23)
Release of unused amounts	(4)	–	(4)
Balance as at June 30, 2011	\$ 38	\$ –	\$ 38

As at June 30, 2011, the Company was involved in a legal claim in the normal course of operations. Management has reviewed the claim and believes the ultimate resolution of the legal claim will not have a material adverse effect on the Company's financial position. Although the ultimate amount of the litigation provision is uncertain, the accrued amount of this obligation is based on management's best estimate of the amount required to settle. Management anticipates this legal claim will be resolved within the next fiscal year.

Other provisions consist of an estimated sales tax liability with uncertain timing and amounts. This provision was settled and was no longer required by March 31, 2011.

16. SHARE CAPITAL

(a)

Authorized:

Unlimited number of voting common shares with no par value.

Unlimited number of preferred shares with no par value, voting rights to be determined prior to first issue.

Issued and outstanding:

	Number of shares	Share capital
Voting common shares:		
Balance, April 1, 2010	104,504,670	\$ 23,011
Share repurchase under normal course issuer bid	(1,309,618)	(288)
Exercise of options	7,500	4
Balance, March 31, 2011	103,202,552	22,727
Share repurchase under normal course issuer bid	(30,626)	(7)
Balance, June 30, 2011	103,171,926	\$ 22,720

On October 14, 2009, the Company received approval from the Toronto Stock Exchange ("TSX") to renew its normal course issuer bid ("NCIB") to repurchase its common shares from the market. Effective October 18, 2010, the Company again renewed its NCIB with the TSX. Under the renewed NCIB, the Company may acquire up to 5,212,941 common shares, until the renewed NCIB expires on October 17, 2011.

During the three months ended June 30, 2011, 30,626 common shares were repurchased (three months ended June 30, 2010 – nil) pursuant to the NCIB at a total cost of \$12 or \$0.38 per common share. All common shares repurchased were cancelled, resulting in a reduction in share capital of \$7 and a reduction in contributed surplus of \$5 representing the consideration in excess of stated capital.

(b) Share option plan

The Company has an incentive share option plan for certain employees, contractors, officers and directors. Options issued under the plan vest over a period which generally extends between four and five years and are settled on an equity basis. Options vest annually in proportion to the number of vesting periods, based on the anniversary date of the options granted. The total number of common shares reserved for issuance under the share option plan shall not exceed 22,170,442. As at June 30, 2011, 5,926,286 (March 31, 2011 – 5,582,036) common shares remain reserved for issuance under the share option plan.

The continuity of the Company's outstanding and exercisable options is as follows:

	3 months ended June 30, 2011		12 months ended March 31, 2011	
	Number of options outstanding	Weighted average exercise price	Number of options outstanding	Weighted average exercise price
Outstanding, beginning of period	7,105,914	\$ 0.60	5,658,684	\$ 0.78
Exercised	–	–	(7,500)	0.40
Granted	–	–	2,290,980	0.51
Expired, cancelled, and forfeited	(344,250)	0.51	(836,250)	1.54
Outstanding, end of period	6,761,664	\$ 0.61	7,105,914	\$ 0.60
Exercisable, end of period	2,136,921	\$ 0.67	2,143,171	\$ 0.66

The following table summarizes information about share options outstanding and exercisable as at June 30, 2011:

Exercise price	Number outstanding	Weighted average remaining term (in years)	Options vested	Options not vested
\$ 0.40	960,000	3.7	490,000	470,000
\$ 0.48	600,000	3.2	300,000	300,000
\$ 0.51	1,975,980	5.6	–	1,975,980
\$ 0.64	1,085,000	4.7	296,250	788,750
\$ 0.68	1,169,000	2.5	705,000	464,000
\$ 0.76	698,684	4.6	174,671	524,013
\$ 1.24	220,000	1.5	132,000	88,000
\$ 1.25	25,000	2.1	15,000	10,000
\$ 4.04	28,000	0.2	24,000	4,000
	6,761,664		2,136,921	4,624,743

During the three months ended June 30, 2011, \$116 (three months ended June 30, 2010 – \$149) was recognized as share-based payments related to options with a corresponding increase to contributed surplus.

No options were issued in the three months ended June 30, 2011. In the three months ended June 30, 2010, the actual weighted average fair value of options issued was \$0.27 per common share, as determined using the Black-Scholes option pricing model. The following weighted average assumptions were utilized to calculate the fair value:

	3 months ended June 30 2010
Total options granted	200,000
Weighted average exercise price	\$ 0.46
Risk-free interest rate	2.15%
Expected life	4 years
Vesting period	4 years
Expected annual volatility	79%
Expected dividend yield	–

(c) Deferred share units

	3 months ended June 30 2011	12 months ended March 31 2011
Balance, beginning of period	574,647	251,246
Issued	89,744	323,401
Outstanding and exercisable, end of period	664,391	574,647

During the three months ended June 30, 2011, the Company issued DSUs, with fair value of \$34 (three months ended June 30, 2010 – \$44), and recognized a recovery of share-based payments of \$35 (three months ended June 30, 2010 – \$33 expense), with a corresponding decrease to accounts payable and accruals. No DSUs were redeemed for the three months ended June 30, 2011. All outstanding DSUs are considered vested at the date of grant. As at June 30, 2011, \$252 (March 31, 2011 – \$287) was recorded in accounts payable and accruals related to the outstanding DSUs.

(d) Restricted share units

	3 months ended June 30 2011	12 months ended March 31 2011
Balance, beginning of period	1,535,439	743,421
Issued	–	792,018
Outstanding, end of period	1,535,439	1,535,439
Exercisable, end of period	–	–

During the three months ended June 30, 2011, the Company did not issue RSUs (three months ended June 30, 2010 – nil). For the three months ended June 30, 2011, the Company recognized a recovery of share-based payments of \$12 (three months ended June 30, 2010 – \$30), with a corresponding decrease to accounts payable and accruals or other long-term liabilities. As at June 30, 2011, the RSUs outstanding had a vesting period that extends between three months and three years. As at June 30, 2011, \$309 (March 31, 2011 – \$321) was recorded in accounts payable and accruals and other long-term liabilities related to the outstanding RSUs.

SUMMARY OF SHARE-BASED PAYMENTS

	3 months ended June 30 2011	3 months ended June 30 2010
Share options expense	\$ 116	\$ 149
Expense arising from DSUs granted	34	44
Effect of changes in the fair value of DSUs	(69)	(12)
Effect of changes in the fair value of RSUs	(12)	(30)
Total share-based payments expense	\$ 69	\$ 151

The total carrying amount of liabilities associated with share-based payments at June 30, 2011 is \$561 (March 31, 2011 – \$608), of which \$252 relates to the fair value of DSUs and RSUs that have already vested (March 31, 2011 – \$287).

17. CONTRIBUTED SURPLUS

	3 months ended June 30 2011	12 months ended March 31 2011
Balance, beginning of period	\$ 8,733	\$ 8,531
Share-based payment expense recognition of fair value of share options granted	116	605
Recognition of fair value of share options exercised	–	(2)
Consideration in excess of stated capital	(5)	(401)
Balance, end of period	\$ 8,844	\$ 8,733

18. LOSS PER SHARE

	June 30 2011	June 30 2010
Net loss and comprehensive loss (numerator for basic and diluted loss per share)	\$ (3,137)	\$ (4,110)
Weighted average number of common shares outstanding	103,198,513	104,504,670
Basic and diluted weighted average number of common shares outstanding	103,198,513	104,504,670
Loss per share – basic and diluted	\$ (0.03)	\$ (0.04)

For the three months ended June 30, 2011, 6,188,714 options (June 30, 2010 – 4,770,104) were excluded from the diluted earnings per share under the treasury method as the Company was not in an earnings position as at June 30, 2011.

19. EXPENSE BY FUNCTION

3 months ended June 30, 2011	Cost of goods sold	Sales and marketing	General and administration	Research and development	Other expenses
Employee costs	\$ 381	\$ 1,109	\$ 1,614	\$ 1,054	\$ –
Share-based payments	9	20	14	26	–
Depreciation	38	23	48	118	–
Amortization	4	8	6	37	–
Other costs	1,250	1,623	892	390	14
	\$ 1,682	\$ 2,783	\$ 2,574	\$ 1,625	\$ 14

3 months ended June 30, 2010	Cost of goods sold	Sales and marketing	General and administration	Research and development	Other expenses
Employee costs	\$ 331	\$ 897	\$ 1,310	\$ 894	\$ –
Share-based payments	7	34	77	33	–
Depreciation	52	24	71	150	–
Amortization	2	5	4	30	–
Other costs	559	1,354	872	536	6
	\$ 951	\$ 2,314	\$ 2,334	\$ 1,643	\$ 6

20. EMPLOYEE SAVINGS PLAN

The Company matches employee voluntary contributions to their Registered Retirement Savings Plans to a maximum of 3% of earnings for each employee. Contributions made by the Company during the three months ended June 30, 2011 were \$79 (three months ended June 30, 2010 – \$67).

21. GOVERNMENT GRANTS

During the three months ended June 30, 2011, the Company recorded the benefit of investment tax credits of \$164 (three months ended June 30, 2010 – \$76) as a reduction in research and development expenses.

The Company also recorded a reduction of research and development expense related to government assistance in connection with research activities of \$43 (three months ended June 30, 2010 – \$52).

22. NET FINANCE COSTS

	3 months ended June 30 2011	3 months ended June 30 2010
Interest on the demand operating line of credit	\$ 2	\$ –
Interest on financing lease	15	13
Interest on long-term debt	–	54
Other interest and bank charges	15	13
Total finance cost	\$ 32	\$ 80
Interest earned on cash balances	\$ 3	\$ 17
Total finance income	3	17
Net finance costs	\$ 29	\$ 63

23. RELATED PARTY TRANSACTIONS

KEY MANAGEMENT PERSONNEL COMPENSATION

Aggregate compensation to the directors and key management personnel of the Company during the period was as follows:

	3 months ended June 30 2011	3 months ended June 30 2010
Short-term employee benefits	\$ 581	\$ 484
Post-employment benefits	15	12
Share-based payment benefits	21	72
	\$ 617	\$ 572

Short-term employee benefits consist of salaries, bonuses, directors fees, and all other short-term monetary and non-monetary benefits. Share-based payment benefits consist of the fair value of share-option awards, DSUs, and RSUs expensed in the period. No long-term employee benefits or termination benefits were recognized in the three months ended June 30, 2011 or the three months ended June 30, 2010.

TRANSACTIONS WITH RELATED PARTIES

Included in general and administration expenses during the three months ended June 30, 2011, were management and consulting fees of \$nil (three months ended June 30, 2010 – \$32) incurred from a company controlled by a director of Afexa.

All transactions with related parties occurred in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

24. CAPITAL DISCLOSURES

The Company's objective in managing capital is to safeguard the Company's ability to continue as a going concern so that it can continue to develop and commercialize evidence-based natural health products to increase shareholder value. Capital is defined by the Company as shareholders' equity, long-term debt, and obligations under finance lease and is as follows:

	June 30 2011	March 31 2011	April 1 2010
Share Capital	\$ 22,720	\$ 22,727	\$ 23,011
Obligations under finance lease	858	843	789
Current portion of long-term debt	–	–	710
Long-term debt	–	–	4,528
Total capital	\$ 23,578	\$ 23,570	\$ 29,038

The Company has externally imposed capital requirements as governed through its demand operating line of credit. These requirements are to ensure the Company continues to operate in the normal course of business and to ensure the Company manages its debt relative to tangible net worth. These capital requirements are congruent with the Company's management of capital. The Company met all externally imposed capital requirements at the end of the period.

The Company monitors capital on the basis of the current ratio and debt to tangible net worth ratio which are both financial covenants of the credit facility agreement. The current ratio is calculated as current assets (as shown on the statement of financial position) over current liabilities (as shown on the statement of financial position) and is to be maintained above 1.25:1. As at June 30, 2011, this ratio has decreased to 1.74:1 from the March 31, 2011 ratio of 2.28:1. The decrease in this ratio from March 31, 2011 is largely due to the increase in current liabilities resulting from the Company utilizing the demand operating line of credit.

Debt to tangible net worth is calculated as total liabilities (as shown on the statement of financial position) over tangible net worth. Tangible net worth is defined as the sum of share capital, contributed surplus and deficit less intangible assets and deferred tax assets. This ratio is to be maintained below 2.00:1. As at June 30, 2011, this ratio was 0.68:1 (March 31, 2011 – 0.46:1). The increase in this ratio can also be attributed to the Company's utilization of its demand operating line of credit in the period.

25. FINANCIAL INSTRUMENTS

FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of financial instruments represents the amounts that would have been received from or paid to counterparties, calculated at the reporting date, to settle these instruments. Cash, trade and other receivables, trade and other payables are financial assets and liabilities that have short periods to maturity and therefore, have carrying values that approximate their estimated fair value.

MANAGEMENT OF RISKS ARISING FROM FINANCIAL INSTRUMENTS

The Company does not use financial derivatives. There has been no change with respect to the Company's overall risk exposure during the period ended June 30, 2011.

MARKET RISK

(a) Interest rate risk

The Company's mortgage was subject to interest rate cash flow risk as the required cash flow to service the debt will fluctuate as a result of the changing bank prime lending rate. The outstanding term mortgage with the lender was fully repaid during the year ended March 31, 2011. The Company entered into a credit facility agreement with a new bank that consists of a demand operating line of credit of \$15,000, with interest at the bank's prime lending rate plus 0.75% (note 12). A change in the interest rate would not materially affect the results of operations or cash flows as the Company entered into the demand operating line of credit late in the period.

(b) Foreign exchange risk

The Company is currently not exposed to significant foreign currency risk as the assets and liabilities denominated in foreign currencies are minimal.

CREDIT RISK

The maximum exposure to credit risk of the Company as at June 30, 2011 is the carrying value of its financial assets. The Company manages credit risk by maintaining bank accounts with reputable financial institutions and only investing in securities that are highly rated, traded in active markets and capable of prompt liquidation.

The Company's exposure to credit risk related to accounts receivable arises from the possibility that a customer does not fulfil its obligations. This is minimized through a customer base predominantly comprised of well established retailers and wholesalers, a program of credit evaluation of new customers and limits on the amount of credit extended as deemed necessary. The Company performs continuous evaluation of its accounts receivable and records an allowance for doubtful accounts. The failure of a large customer would have a significant effect on the Company (note 6).

LIQUIDITY RISK

The Company's exposure to liquidity risk is dependent on the sale of inventory, collection of accounts receivable, purchasing commitments, and obligations or raising of funds to meet commitments and sustain operations. The Company's liquidity objective is to maintain the capacity to fund assets and repay liabilities in a timely and cost-effective manner under adverse market conditions and unforeseen events. This capacity primarily derives from the Company's earnings and ability to issue debt and equity instruments as well as its ability to generate liquidity from its statement of financial position (convert assets, for example inventory, to cash).

The Company controls liquidity risk by managing working capital, cash flows and the availability of borrowing facilities. The Company's undiscounted contractual obligations, which include interest thereon, are as set out in the summary of contractual obligations (note 28). As at June 30, 2011, the Company has financial assets that are expected to generate sufficient cash inflows to meet cash outflows on financial liabilities.

26. CHANGE IN NON-CASH OPERATING WORKING CAPITAL

	3 months ended June 30 2011	3 months ended June 30 2010
Accounts receivable	\$ (305)	\$ 261
Inventory	(1,925)	(1,821)
Prepaid expenses and deposits	(535)	(461)
Income taxes receivable	(813)	(2,493)
Accounts payable and accruals	463	(673)
Provisions	(27)	15
Customer deposits	(7)	(368)
	\$ (3,149)	\$ (5,540)

27. SEGMENTED INFORMATION

The Company operates in one operating segment – biopharmaceutical products. Management assesses performance and makes resource decisions based on the consolidated results of operations of this operating segment. Substantially all of the operations of the Company are directly engaged in or support this operating segment. Other operations are not material and share many of the same economic and operating characteristics as biopharmaceutical products and, accordingly, they are included with biopharmaceutical products for purposes of segment reporting.

The Company derives significant revenue from certain customers. During the three months ended June 30, 2011 three Canadian customers (three months ended June 30, 2010 – three Canadian customers) accounted for \$3,056 or 67% (three months ended June 30, 2010 – \$1,034 or 59%) of the Company's consolidated revenue.

For the three months ended June 30, 2011 and three months ended June 30, 2010, substantially all of the Company's revenue was generated in Canada. All of the Company's property and equipment is located in Canada.

28. COMMITMENTS

OPERATING LEASE COMMITMENTS

	June 30 2011	March 31 2011	April 1 2010
Less than one year	\$ 186	\$ 193	\$ 202
Between one and five years	731	706	720
More than five years	726	775	973
	\$ 1,643	\$ 1,674	\$ 1,895

The Company has entered into agreements to lease premises in Toronto and Montreal, Canada. These leases expire at various dates up to February 29, 2020.

During the three months ended June 30, 2011 an amount of \$46 was recognized as an expense in profit or loss in respect of operating leases (June 30, 2010 – \$43).

OTHER COMMITMENTS

The Company has various sponsorship agreements and other commitments made in the normal course of business. As at June 30, 2011, the Company's contractual obligations, commitments, other than operating leases over the next five years and thereafter are as follows:

	June 30 2011	March 31 2011	April 1 2010
Less than one year	\$ 1,280	\$ 1,413	\$ 1,323
Between one and five years	88	144	510
More than five years	–	–	–
	\$ 1,368	\$ 1,557	\$ 1,833

In addition to the contractual obligations noted in the above table, the Company signed a commitment on May 26, 2010 to purchase a minimum of \$3,000 of inventory from a contract manufacturer organization ("CMO") over a three-year period to encourage the CMO to invest in specific equipment required to produce the Company's products. As at June 30, 2011, the remaining commitment to the CMO was \$2,730. On March 24, 2011, the Company also entered into an agreement with another CMO to develop a new product. If the Company proceeds in launching this product, the contractual terms provide for a commitment of \$1,210. As at June 30, 2011, the potential remaining commitment to the CMO was \$1,203.

The Company has financial assets that are expected to generate sufficient cash inflows to meet cash outflows on financial liabilities.

29. TRANSITION TO IFRS

For all periods up to and including March 31, 2011, the Company prepared its consolidated financial statements in accordance with Canadian GAAP. These unaudited interim consolidated financial statements for the three months ended June 30, 2011 are the first consolidated financial statements that comply with IFRS.

Accordingly, the Company has prepared interim consolidated financial statements that comply with IFRS applicable for periods beginning on or after April 1, 2011, as described in the Company's accounting policies (note 2). The Company prepared its opening statement of financial position as at April 1, 2010, its date of transition to IFRS. The principal adjustments made by the Company in restating its Canadian GAAP statements of financial position as at April 1, 2010, the previously published Canadian GAAP consolidated financial statements for the year ended March 31, 2011 and for the three months ended June 30, 2010 are explained within this note.

In preparing these interim consolidated financial statements in accordance with IFRS 1, the Company has applied the mandatory exceptions and certain of the optional exemptions from full retrospective application of IFRS.

ELECTED EXEMPTIONS FROM FULL RETROSPECTIVE APPLICATION

In preparing these interim consolidated financial statements, the Company has applied the following optional exemptions from full retrospective application of IFRS provided under IFRS 1 – *First-time Adoption of International Financial Reporting Standards*:

- **Cumulative translation differences**

The Company has elected to set cumulative translation differences arising from translation of its foreign subsidiaries into the Canadian dollar, to be \$nil at April 1, 2010.

- **Share-based payments**

The Company has elected not to retrospectively apply IFRS 2 – *Share-Based Payments* to its equity instruments granted on or before November 7, 2002, or granted after November 7, 2002 that vested before April 1, 2010.

For its cash-settled share-based payment transactions, or deferred share units and restricted share units, the Company has elected not to retrospectively apply IFRS 2 to any liabilities settled before April 1, 2010.

- **Fair value as deemed cost**

The Company has elected to measure its land under finance lease and building at their respective fair values as at April 1, 2010 and use those amounts as the assets' deemed cost at that date. For all other property and equipment assets, the Company continues to use the historical cost model.

- **Business combinations**

The Company will apply the business combinations exemption in IFRS 1 not to apply IFRS 3 – *Business Combinations* retrospectively to past business combinations. Accordingly, Afexa will not restate business combinations that took place prior to April 1, 2010.

In preparing these interim consolidated financial statements in accordance with IFRS 1, the Company has applied the following mandatory exemption from full retrospective application of IFRS:

- **Estimates**

The Company did not use hindsight to create or revise estimates previously made under Canadian GAAP. The Company's IFRS estimates as of April 1, 2010 are consistent with its Canadian GAAP estimates for the same date.

RECONCILIATION OF CANADIAN GAAP TO IFRS

In preparing its opening IFRS statement of financial position, the Company has adjusted the amounts reported previously in consolidated financial statements under Canadian GAAP. An explanation of the effect of transition from Canadian GAAP to IFRS on the Company's financial position and financial performance is set out in the following tables and accompanying notes to those tables. There are no differences between cash flows reported under Canadian GAAP to those reported under IFRS for the period ended June 30, 2010.

RECONCILIATION OF EQUITY AS REPORTED UNDER CANADIAN GAAP TO IFRS

	March 31 2011	June 30 2010	April 1 2010
Shareholders' equity, Canadian GAAP	\$ 24,794	\$ 21,865	\$ 25,795
IFRS adjustments			
Derecognition of intangible assets	(203)	(279)	(206)
Fair value of building and land under finance lease at deemed cost	634	542	512
Deferred tax adjustment from above noted items	366	410	398
Total adjustments	797	673	704
Shareholders' equity, IFRS	\$ 25,591	\$ 22,538	\$ 26,499

An explanation of the most significant differences between Canadian GAAP and IFRS that impacted opening shareholders' equity are described in further detail below.

RECONCILIATION OF FINANCIAL POSITION FROM CANADIAN GAAP TO IFRS AS AT APRIL 1, 2010

The following are reconciliations of the financial position previously presented under Canadian GAAP to financial position prepared under IFRS as at April 1, 2010 (date of transition).

As at April 1, 2010

Canadian GAAP accounts	Notes	Canadian GAAP balances	IFRS transitional adjustments	IFRS balances	IFRS accounts
Assets					Assets
Current					
Cash		\$ 17,685		\$ 17,685	Cash
Accounts receivable		998		998	Accounts receivable
Inventory		9,676		9,676	Inventory
Prepaid expenses and deposits		502		502	Prepaid expenses and deposits
Income taxes receivable		239		239	Income taxes receivable
Future income tax assets	(i)	738	(738)	–	
		29,838	(738)	29,100	
Intangible assets	(ii)	1,504	(206)	1,298	Intangible assets
Property and equipment	(iii)	12,492	512	13,004	Property and equipment
Inventory, non-current		243	–	243	Inventory, non-current
Future income tax assets	(i)(v)	–	1,067	1,067	Deferred tax asset
		\$ 44,077	\$ 635	\$ 44,712	
Liabilities					
Current					
Accounts payable and accruals	(vi)	\$ 9,531	\$ (113)	\$ 9,418	Accounts payable and accruals
	(vi)	–	\$ 113	113	Provisions
Current portion of long-term debt		710		710	Current portion of long-term debt
Customer deposits		2,094		2,094	Customer deposits
		12,335	–	12,335	
Obligations under capital lease		789		789	Obligations under finance lease
Other long-term liabilities		381		381	Other long-term liabilities
Future income tax liabilities	(i)	69	(69)	–	
Deferred revenue		180		180	Deferred revenue
Long-term debt		4,528		4,528	Long-term debt
		18,282	(69)	18,213	
Shareholders' Equity					
Share capital		23,011		23,011	Share capital
Contributed surplus	(iv)	8,260	271	8,531	Contributed surplus
Deficit	(ii)(iii)(iv)(v)	(5,476)	433	(5,043)	Deficit
		25,795	704	26,499	
		\$ 44,077	\$ 635	\$ 44,712	

RECONCILIATION OF FINANCIAL POSITION FROM CANADIAN GAAP TO IFRS AS AT MARCH 31, 2011

The following are reconciliations of the financial position previously presented under Canadian GAAP to financial position prepared under IFRS as at March 31, 2011:

As at March 31, 2011

Canadian GAAP accounts	Notes	Canadian GAAP balances	IFRS transitional adjustments	IFRS balances	IFRS accounts
Assets					Assets
Current					
Cash		\$ 3,691		\$ 3,691	Cash
Accounts receivable		768		768	Accounts receivable
Inventory		11,956		11,956	Inventory
Prepaid expenses and deposits		470		470	Prepaid expenses and deposits
Income taxes receivable		4,854		4,854	Income taxes receivable
Future income tax assets	(i)	538	(538)	–	
		22,277	(538)	21,739	
Intangible assets	(ii)	1,510	(203)	1,307	Intangible assets
Property and equipment	(iii)	11,591	634	12,225	Property and equipment
Future income tax assets	(i)(v)	61	904	965	Deferred tax asset
		\$ 35,439	\$ 797	\$ 36,236	
Liabilities					
Current					
Accounts payable and accruals	(vi)	\$7,887	\$(65)	\$7,822	Accounts payable and accruals
	(vi)	–	65	65	Provisions
Customer deposits		1,628		1,628	Customer deposits
		9,515	–	9,515	
Obligations under capital lease		843		843	Obligations under finance lease
Other long-term liabilities		287		287	Other long-term liabilities
		10,645	–	10,645	
Shareholders' Equity					
Share capital		22,727		22,727	Share capital
Contributed surplus	(iv)	8,371	362	8,733	Contributed surplus
Deficit	(ii)(iii)(iv)(v)	(6,304)	435	(5,869)	Deficit
		24,794	797	25,591	
		\$ 35,439	\$ 797	\$ 36,236	

IFRS adjustments

(i) Deferred tax assets and liabilities are classified as non-current under IAS 1. Under Canadian GAAP, deferred income tax relating to current assets or current liabilities were previously classified as current assets or liabilities. As at April 1, 2010, the current future income tax assets and non-current future income tax liabilities reported under Canadian GAAP of \$738 and \$69, respectively, have been reclassified as non-current deferred income taxes under IFRS. As at March 31, 2011, the current future income tax asset balance of \$538 has been reclassified to non-current deferred income taxes.

(ii) Afexa's websites were previously capitalized under Canadian GAAP and recorded as intangible assets. SIC 32 does not allow capitalization of Afexa's websites under IFRS. An amount of \$206 was derecognized as capitalized website costs as at the transition date and recorded to deficit. As at March 31, 2011, the total adjustment to intangible assets was \$203.

(iii) IFRS 1 allows the Company to use fair value as deemed cost in its opening statement of financial position to the difference between the fair value of these assets and the carrying value under Canadian GAAP. The change from April 1, 2010 to March 31, 2011 relates to the amortization on the fair value adjustment.

	April 1 2010	June 30 2010	March 31 2011
Land under finance lease			
Carrying value under Canadian GAAP	\$ 616	\$ 616	\$ 616
Fair value under IFRS	2,426	2,426	2,426
Increase in equity	\$ 1,810	\$ 1,810	\$ 1,810
Building			
Carrying value under Canadian GAAP	\$ 9,522	\$ 9,331	\$ 9,093
Fair value under IFRS	8,224	8,063	7,917
Decrease in equity	\$ (1,298)	\$ (1,268)	\$ (1,176)
Net increase in equity	\$ 512	\$ 542	\$ 634

(iv) Under Canadian GAAP, the Company calculated the fair value of share-based awards as one grant recognizing the fair value on a straight-line basis over the entire vesting period. As well, forfeitures of awards were recognized as they occurred. IFRS 2 requires that awards with multiple vesting dates are graded with each vesting period treated as a separate tranche. The fair value of each tranche is then calculated separately and is amortized over the vesting period of the respective tranches. Also, award forfeitures are estimated as part of share-based payments. The change in treatment of share-based awards has resulted in an increase of \$271 to contributed surplus at April 1, 2010. For the twelve months ended March 31, 2011, the contributed surplus balance increased by a total of \$362 over the Canadian GAAP balance.

(v) Upon transition to IFRS, the revaluation of the building and land and the derecognition of capitalized website costs caused a difference to the previously recorded deferred tax asset. This revaluation and derecognition resulted in a net deferred income tax adjustment of \$398 at the transition date under IFRS. The net deferred income tax adjustment at March 31, 2011 was \$366 related to the tax impact on the other IFRS adjustments.

(vi) IAS 1 requires provisions to be separately disclosed as a line item on the consolidated statements of financial position. As a result, the Company reclassified \$113 in legal and other provisions to be reclassified from accounts payable and accruals to provisions as at April 1, 2010. As at March 31, 2011, the amount reclassified to provisions from accounts payable and accruals was \$65.

RECONCILIATION OF NET LOSS AND COMPREHENSIVE LOSS AS REPORTED UNDER CANADIAN GAAP TO IFRS

Adjustments impacting comprehensive loss and deficit

	Notes	12 months ended March 31 2011	3 months ended June 30 2010
Net loss and comprehensive loss for the period, as reported under Canadian GAAP		\$ (828)	\$ (4,075)
IFRS adjustments			
Derecognition of intangible assets	(i)	3	(73)
Fair value of building and land under finance lease at deemed costs	(ii)	122	30
Share-based payment benefits	(iii)	(91)	(3)
Deferred tax adjustment from above noted items	(iv)	(31)	11
		3	(35)
Net loss and comprehensive loss for the period, as reported under IFRS		\$ (825)	\$ (4,110)

For details on the IFRS adjustments made, see explanations under *Restated statement of comprehensive loss and deficit*.

RESTATED STATEMENT OF COMPREHENSIVE LOSS AND DEFICIT

The following are reconciliations of the net loss and comprehensive loss previously presented under Canadian GAAP to net loss and comprehensive loss prepared under IFRS.

For the three months ended June 30, 2010

Canadian GAAP accounts	Notes	Canadian GAAP balances	IFRS transitional adjustments	IFRS balances	IFRS accounts
Revenue		\$ 1,758		\$ 1,758	Revenue
Cost of goods sold	(v)(vi)	988	(37)	951	Cost of goods sold
		770	37	807	
Operating expenses					Operating expenses
Sales and marketing	(i)(v)(vi)	2,093	221	2,314	Sales and marketing
General and administration	(v)(vi)	2,338	(4)	2,334	General and administration
Research and development	(v)(vi)	1,246	397	1,643	Research and development
Amortization	(i) (ii)(v)	383	(383)	–	
Stock-based compensation	(iii)(v)	148	(148)	–	
Loss (gain) on foreign exchange	(v)	(2)	8	6	Other expenses
		6,206	91	6,297	
Loss before other items and income taxes		(5,436)	(54)	(5,490)	Loss before finance items and income taxes
Other items					Finance items
Interest and bank charges		80		80	Finance costs
Interest income		(17)		(17)	Finance income
Impairment of intangible assets	(v)	4	(4)	–	
Other expense	(v)	4	(4)	–	
		71	(8)	63	
Loss before income taxes		(5,507)	(46)	(5,553)	Loss before income taxes
Income tax (recovery) expense					Income tax (recovery) expense
Current		(1,730)		(1,730)	Current
Future	(i) (ii)	298	(11)	287	Deferred
		(1,432)	(11)	(1,443)	
Net loss and comprehensive loss		\$ (4,075)	\$ (35)	\$ (4,110)	Net loss and comprehensive loss

For the year ended March 31, 2011

Canadian GAAP accounts	Notes	Canadian GAAP balances	IFRS transitional adjustments	IFRS balances	IFRS accounts
Revenue	(iv)	\$ 39,596	\$ 169	\$ 39,765	Revenue
Cost of goods sold	(v)(iv)	11,091	240	11,331	Cost of goods sold
		28,505	(71)	28,434	
Operating expenses					Operating expenses
Sales and marketing	(i)(v)(iv)	12,981	558	13,539	Sales and marketing
General and administration	(v)	9,206	862	10,068	General and administration
Research and development	(v)	4,859	752	5,611	Research and development
Amortization	(i) (ii)(v)	1,379	(1,379)	–	
Stock-based compensation	(iii)(v)	821	(821)	–	
Loss (gain) on foreign exchange	(v)	6	153	159	Other expenses
		29,252	125	29,377	
Loss before other items and income taxes		(747)	(196)	(943)	Loss before finance items and income taxes
Other items					Finance items
Interest and bank charges		289		289	Finance costs
Interest income		(58)		(58)	Finance income
Impairment of intangible assets	(v)	148	(148)	–	
Other expense	(v)	83	(83)	–	
		462	(231)	231	
Loss before income taxes		(1,209)	35	(1,174)	Loss before income taxes
Income tax (recovery) expense					Income tax (recovery) expense
Current		(451)		(451)	Current
Future	(i) (ii)	70	32	102	Deferred
		(381)	32	(349)	
Net loss and comprehensive loss		\$ (828)	\$ 3	\$ (825)	Net loss and comprehensive loss

(i) Afexa's websites were previously capitalized under Canadian GAAP and recorded as intangible assets. SIC 32 does not allow capitalization of Afexa's websites. An amount of \$146 in website additions were expensed in the twelve months ended March 31, 2011 (three months ended June 30, 2010 – \$88), \$71 was reversed for amortization taken under Canadian GAAP related to websites (three months ended June 30, 2010 – \$15), and \$78 was reversed from other expenses related to write-downs of websites (three months ended June 30, 2010 – \$nil).

(ii) The Company elected to measure land under finance lease and building, classified as property and equipment, at fair value as at April 1, 2010 and used that amount as deemed cost as at April 1, 2010. As a result of the decrease in the building's fair value, the Company's depreciation expense decreased by \$122 for the twelve months ended March 31, 2011 (three months ended June 30, 2010 – \$30).

(iii) Under Canadian GAAP, the Company calculated the fair value of share-based awards as one grant recognizing the fair value on a straight-line basis over the entire vesting period. As well, forfeitures of awards were recognized as they occurred. IFRS 2 requires that awards with multiple vesting dates are graded with each vesting period treated as a separate tranche. The fair value of each tranche is then calculated separately and is amortized over the vesting period of the respective tranches. Also, award forfeitures are estimated as part of share-based payments. The change in treatment of share-based awards has resulted in an increase of \$271 to contributed surplus at April 1, 2010. For the twelve months ended March 31, 2011, the contributed surplus balance increased by a total of \$362 over the Canadian GAAP balance.

(iv) When goods or services are rendered in exchange for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue under IAS 18. The revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents transferred. When the fair value of the goods or services received cannot be measured reliably, the revenue is measured at the fair value of the goods or services provided, adjusted by the amount of any cash or cash equivalents transferred. There was no such requirement under Canadian GAAP to recognize revenue when such an exchange occurred. As a result, for the twelve months ended March 31, 2011, the Company has recorded increased revenue of \$169, increased cost of goods sold of \$32, and additional sales and marketing expenses of \$137 for goods that were exchanged for services (three months ended June 30, 2010 – \$nil).

(v) Under Canadian GAAP, the Company presented revenue and expenses by function, with the exception of depreciation of property and equipment and amortization of intangible assets as well as share-based payments. Under IAS 1, the Company continues to group revenue and expenses by function. However, depreciation, amortization and share-based payments are no longer presented separately, but allocated based on function and included as part of cost of goods sold, sales and marketing, general and administration, and research and development expenses.

Additionally, gain or loss on foreign exchange, impairment of intangible assets and other expenses are now reported in aggregate as other expenses.

(vi) Certain expense items in the three months ended June 30, 2010 have been reclassified from the Canadian GAAP presentation to other expense lines within the consolidated statement of loss and comprehensive loss. The reclassification was made to better align the presentation of expenses in the three months ended June 30, 2010 to the annual consolidated statement of loss and comprehensive loss for the year ended March 31, 2011. The expense items affected were cost of goods sold, sales and marketing, general and administration, and research and development. There is no net impact to the net loss and comprehensive net loss for the period.

30. SUBSEQUENT EVENTS

On August 10, 2011, the Company was informed that Paladin Labs Inc. (“Paladin”) filed documents with the Canadian securities authorities formally commencing an unsolicited tender offer to acquire all of the outstanding common shares of the Company for either cash consideration of \$0.55 per common share or 0.013 of a Paladin share for each common share (“the Offer”). Paladin was a holder of approximately 14.9% of Afexa’s issued and outstanding common shares as at July 15, 2011. In response to the unsolicited offer; the Company issued a press release stating that “The Company’s Board of Directors believes the Paladin Offer significantly undervalues Afexa’s business.” The Board of Directors of Afexa have established a special committee of the Board to review the Offer and will issue a Directors’ Circular concerning the Paladin Offer.

On August 14, 2011, the Company adopted a new shareholder rights plan (the “New Rights Plan”). The New Rights Plan has been adopted to limit, to the extent possible, the ability of any investor to obtain effective control of Afexa through coercive and opportunistic methods without making a take-over bid offer to all shareholders of Afexa which a majority of shareholders find acceptable and otherwise to encourage fair treatment of shareholders in connection with any take-over bid offer for Afexa’s common shares.