

MANAGEMENT'S DISCUSSION AND ANALYSIS

for the three and six months ended September 30, 2011

The following Management's Discussion and Analysis ("MD&A") for Afexa Life Sciences Inc. ("Afexa" or the "Company") was prepared as of November 11, 2011 to assist readers in understanding our consolidated financial performance for the three and six months ended September 30, 2011. This MD&A should be read in conjunction with the accompanying unaudited interim consolidated financial statements for the three and six months ended September 30, 2011 and the notes contained therein. In addition, this MD&A should be read in conjunction with the MD&A and audited consolidated financial statements for the year ended March 31, 2011.

International Financial Reporting Standards ("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 is reporting using IFRS as issued by the International Accounting Standards Board ("IASB") for our condensed consolidated interim financial statements ("consolidated financial statements") ended September 30, 2011 and the comparative periods. Details of the more significant accounting differences can be found in the "Changes in Accounting Policies Including Transition to IFRS" section of this and our June 30, 2011 first quarter MD&A, as well as in our unaudited interim consolidated financial statements ended June 30, 2011 and September 30, 2011.

The policies applied are based on IFRS issued and outstanding as of November 11, 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.

This MD&A contains forward-looking statements. Please see the section "Advisory Regarding Forward-looking Statements" for a discussion of the risks, uncertainties and assumptions used to develop our forward-looking statements.

These accounting principles require us to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. We believe these estimates and assumptions are reasonable based on the information available at the time that these estimates and assumptions are made. These estimates and assumptions have been discussed with the Audit Committee of the Board of Directors of Afexa. Actual results may differ under different assumptions and conditions.

Additional information on Afexa, including our most recently filed Annual Information Form dated June 24, 2011, MD&A and audited financial statements, are available on the System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com.

Our Business

We are a life sciences and technology company founded in 1992 and headquartered in Edmonton, Alberta, Canada. We have 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, our scientists are able to precisely identify 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. Our lead commercial product, COLD-FX®, is approved to help reduce the frequency, duration, and severity of cold and flu symptoms by

strengthening the immune system. COLD-FX continues to be the number one selling cold and flu remedy in Canada (source: The Nielsen Company MarketTrack National all channel dollar sales for the categories of Cold Remedies and Supplements and Products ("Point of Sale Data"), 52 weeks ended September 24, 2011). We recently licensed and launched COLDSORE-FX[®] in Canada.

Significant Events and Overall Performance

On October 18, 2011, Valeant Pharmaceutical International, Inc. ("Valeant") announced that they acquired approximately 73.8% of Afexa's common shares and were extending their offer to purchase the remaining outstanding common shares of Afexa. Pursuant to a support agreement between Afexa and Valeant, the majority of the directors of Afexa as well as the interim CEO were replaced with Valeant appointees. On October 27, 2011, Valeant announced that they acquired additional shares for a total share ownership of approximately 81.6% of Afexa's common shares. Afexa is now preparing for a special meeting of its shareholders to be held on December 12, 2011 that will propose an acquisition transaction be accepted. This will result in the privatization of Afexa effective in December 2011 and the remaining shareholders of Afexa being paid for their Afexa shares in December 2011.

During the quarter ended September 30, 2011, we achieved revenue of \$15.0 million, reflecting a 21.9% decrease over the same three-month period in 2010. For the six-month period ended September 30, 2011 revenue of \$19.6 million was achieved which is \$1.4 million or 6.6% lower than the \$21.0 million achieved in the same period ending September 30, 2010. The reduced revenue is primarily due to a reduction of orders from one significant customer and the prevalence of relatively low incidences of flu at the beginning of this year's cold and flu season.

Margins for the quarter ended September 30, 2011 improved to 74.3% from 73.5% achieved in the same quarter of the previous year due to improved inventory management and logistics. Operating expenses increased to \$10.9 million in the quarter compared to \$7.4 million in the same quarter last year, primarily due to the incurrence of legal, advisory, employee retention, and acceleration and revaluation of share-based payments related to takeover bids that the Company received during this period. A net loss of \$0.2 million was incurred in the quarter ended September 30, 2011 as compared to a \$4.8 million net income in the prior year's corresponding quarter. The lower net income is due to the lower sales and higher expenses.

Summary of consolidated financial results				
(in thousands except for per share amounts)	Three months ended September 30		Six months ended September 30	
	2011	2010	2011	2010
Revenue	\$15,022	\$19,232	\$19,596	\$20,990
Net (loss) income	(158)	4,777	(3,295)	667
(Loss) earnings per share - basic and diluted	(0.00)	0.05	(0.03)	0.01
Cash used in operating activities	2,509	1,068	(3,615)	7,647
			As at	As at
			September 30, 2011	March 31, 2011
Total assets			39,315	36,236
Total long-term debt and obligations under capital lease			872	843
Shareholders' equity			23,358	25,591

Results of Operations for the Three and Six Months Ended September 30, 2011

Revenue

During the three months ended September 30, 2011, our revenue decreased by 21.9% to \$15.0 million from revenue of \$19.2 million reported in the same three-month period of 2010. The reduced revenue is primarily due to a reduction of orders from one significant customer. This customer changed a seasonal promotion program that has been held in recent years and therefore did not order the volume of product that this program historically required. Management also believe that relatively low incidences of flu, as reported by SDI Health LLC in their Canada National Report on Flu/Cold/Respiratory Illness Activity Notification (“FAN”) Report, has negatively impacted the volume of product that our retail customers are ordering.

On a year-to-date basis, revenue for the six months ended September 30, 2011 of \$19.6 million was \$1.4 million below the revenue achieved in the same six-month period of 2010 due to the reduced revenue achieved in the most recently completed quarter as discussed above.

Gross Margin

Gross margin for the three and six months ended September 30, 2011 was \$11.2 million (74.3%) and \$14.1 million (71.7%), respectively, as compared to \$14.1 million (73.5%) and \$14.9 million (71.2%), for the corresponding periods in 2010. The lower gross margin in the current quarter and six months ended September 30, 2011 are due to lower revenue. Margin as a percentage of revenue has increased due to improvements to our inventory management processes to achieve lower production costs and reduce obsolescence related inventory write-downs.

General and Administration

General and administration costs increased by \$3.4 million to \$6.2 million during the quarter ended September 30, 2011 from \$2.8 million reported in the same period of the previous year. The increase is primarily due to the incurrence of legal, strategic and financial advisory, and employee retention costs, as well as the acceleration of share-based expenses related to takeover bids and the search for alternative investors during this period.

On a six-month basis, general and administration costs increased by \$3.7 million to \$8.8 million from the same six-month period in 2010. The increase can be attributed to the costs incurred in the second quarter of this year related to the takeover bids and the search for alternative investors.

Sales and Marketing

Sales and marketing expenses increased to \$3.1 million during the three-month period ended September 30, 2011 from \$3.0 million in the corresponding period ended September 30, 2010 primarily due to the acceleration of share-based payments related to takeover bids that the Company received during this period. Sales and marketing expenses increased to \$5.9 million during the six-month period ended September 30, 2011 compared to \$5.3 million in the corresponding period last year. This increase is due to the costs related to the takeover bids but also from first quarter costs related to the launch of COLDSORE-FX and an increase in the purchase of market data.

Research and Development

Research and development costs decreased by \$0.1 million to \$1.5 million during the three months ended September 30, 2011 from \$1.6 million in the previous year. The decrease is due to rescheduling of various research and development activities. On a year-to-date basis, research and development costs also decreased to \$3.1 million from \$3.3 million and this decrease is a result of rescheduling of a number of research and development activities.

Partially offsetting research and development costs in the six-month period ended September 30, 2011 were \$0.3 million (six months ended September 30, 2010 - \$0.2 million) of Scientific Research and Experimental development ("SRED") investment tax credits.

Finance Costs

In the second quarter ended September 30, 2010, we paid out our mortgage and, other than an obligation under a finance lease, we no longer have long-term debt. Interest incurred in the current quarter of \$64 thousand and in the six months ended September 30, 2011 of \$96 thousand is primarily due to this obligation under finance lease, bank charges, and for the utilization of a line of credit.

Income Taxes

During the quarter, we recognized income tax expense of \$0.4 million as compared to \$1.9 million in the corresponding quarter last year. The lower income tax expense is due to lower net income before tax. A significant portion of the income tax expense in the current quarter is due to the non-deductibility of share-based expenses related to the accelerated vesting and revaluation of share options triggered by events related to the takeover bids described earlier. In addition, expensing of deferred and restricted share units was recognized in the quarter based on an increased market price of the Company's common shares. During the six months ended September 30, 2011, we recognized an income tax recovery of \$0.6 million as compared to an income tax expense of \$0.4 million in the six months ended September 30, 2010. The income tax recovery for the current six-month period is relatively low as a percentage of the pre-tax loss due to the non-deductibility of share-based payments described above and due to a decrease in tax reserves related to revenue allowances.

Net Earnings

We incurred a net loss of \$0.2 million during the three-month period ended September 30, 2011 compared to net earnings of \$4.8 million reported in the same period ended September 30, 2010. The decrease in earnings is due to lower revenue in the current quarter and increased expenses related to takeover bids. These costs included the incurrence of additional share-based payments of \$2.3 million as compared to \$0.3 million in the corresponding period of last year due to events that triggered the accelerated vesting of options. Also reducing net income is additional expensing of deferred and restricted share units due to an increase in the share price of the Company's common shares from the end of prior quarter. Under IFRS, the share-based payments have been allocated to the respective operating expense categories contained in the Company's Interim Consolidated Statement of (Loss) Income. On a year-to-date basis, a net loss of \$3.3 million has been incurred compared to net income of \$0.7 million in the six months ended September 30, 2010. The decrease in net income is due to lower revenue and the higher expenses related to the costs associated with the takeover bids.

Quarterly information								
(in thousands except for per share amounts)								
	For quarters ended							
	September 30 2011 IFRS	June 30 2011 IFRS	March 31 2011 IFRS	December 31 2010 IFRS	September 30 2010 IFRS	June 30 2010 IFRS	March 31 2010 Canadian GAAP	December 31 2009 Canadian GAAP
Revenue	\$15,022	\$4,574	\$6,084	\$12,691	\$19,232	\$1,758	\$4,827	\$29,547
Net earnings (loss)	(158)	(3,137)	(2,548)	1,055	4,777	(4,110)	(4,027)	6,816
Earnings (loss) per common share - basic and diluted	(0.00)	(0.03)	(0.03)	0.01	0.05	(0.04)	(0.04)	0.06

Most of our revenue is from the sale of COLD-FX. Sales of this product exhibit a seasonal pattern tied to the frequency and severity of colds and flu, as well as other factors including weather. This affects the volume and timing of sales. The quarter ended September 30 corresponds to the time that most of our major customers commence stocking up on cold and flu products in anticipation of demand in the late fall and winter months when, historically, the incidence of colds and flu rises. Further orders are made for restocking of product once the cold and flu season commences, which typically corresponds to our quarter ended December 31. Our quarter ended March 31 corresponds to the time that the incidence of colds and flu are on the decline. The quarter ended June 30 is historically the quarter with the lowest revenue as the incidence of colds and flu is typically at its lowest.

We believe that in the quarter ended December 31, 2009, public awareness of flu increased with a higher incidence of flu and the associated World Health Organization announcement, and media coverage thereon, of H1N1, a pandemic strain of the flu. Revenue and net earnings increased in this quarter as compared to the corresponding prior year's quarter because of an increase in demand for COLD-FX during this period. In the quarters ended March 31, 2010 and June 30, 2010, concerns over H1N1 declined and retailers were well stocked with cold and flu products. Fewer incidents of flu resulted in lower retailer sale volumes of cold and flu products and as a result, restocking orders for COLD-FX were relatively low in these periods. During the quarter ended September 30, 2010, revenue again increased as retail customers began stocking up on cold and flu products prior to the fall and winter cold and flu season. During the quarter ended December 31, 2010, revenue was lower than normal for this time of year as retailers entered the quarter well stocked with COLD-FX and the incidence of cold and flu was lower than in the same quarter last year. In the quarters ended March 31, 2011 and June 30, 2011, revenue declined from the prior quarters ended September 30, 2010 and December 31, 2010 as these quarters are outside of or at the end of the cold and flu season and retailers managed down their product inventory levels. Revenue for the quarter ended September 30, 2011 increased from the prior two quarters as the Company was entering the current year's cold and flu season.

Significant Current and Subsequent Events

On October 18, 2011, Afexa was advised by 1625907 Alberta Ltd. (the "Offeror"), a wholly-owned subsidiary of Valeant Pharmaceuticals, Inc. ("Valeant"), that 80,929,921 common shares ("Common Shares") of Afexa were deposited to the Offeror's offer (the "Valeant Offer") dated October 3, 2011 to acquire all of the issued and outstanding Common Shares and that all such Common Shares have been taken up and will be paid for in accordance with the terms of the Valeant Offer. The Common Shares taken up under the Valeant Offer represent approximately 73.8% of the issued and outstanding Common Shares (on a fully-diluted basis).

On October 27, 2011, Afexa was advised that 8,523,517 Common Shares were deposited to the Valeant Offer and that all such Common Shares have been taken up and were paid for in accordance with the terms of the Valeant Offer. Together with the Common Shares previously

taken up on October 17, 2011, the Common Shares taken up under the Valeant Offer represent approximately 81.6% of the issued and outstanding Common Shares (on a fully-diluted basis).

Afexa's shareholders who tendered to the Valeant Offer received \$0.85 per share in cash which was paid to Afexa's shareholders in accordance with the terms of the Valeant Offer.

Valeant also announced that the votes attached to the Common Shares held by the Offeror are sufficient to approve a subsequent acquisition transaction which will result in the privatization of Afexa and the remaining shareholders of Afexa receiving \$0.85 per Common Share.

The Offeror has advised Afexa that the Valeant Offer will not be further extended and that it will vote its Common Shares in favour of the approval of the subsequent acquisition transaction at the December 12, 2011 special meeting of Afexa shareholders. Following the approval of the subsequent acquisition, Afexa's Common Shares will be delisted from the Toronto Stock Exchange and application will be made to the relevant securities regulatory authorities for Afexa to cease to be a reporting issuer. Afexa has filed a notice on SEDAR for the special shareholder meeting to be held on December 12, 2011.

Liquidity and Capital Resources

Our main source of capital during the period ended September 30, 2011 was our cash on hand provided from operating activities in prior periods and utilization of our operating line of credit. The primary use of our cash was the funding of operating activities. In addition to our net loss, we used cash on hand to fund the seasonal production build-up of our inventory and receivables for the fall cold and flu season. We also used \$0.1 million in cash on hand to finance capital expenditures for the six-month period ended September 30, 2011.

Our working capital and capital expenditure requirements depend upon numerous factors including, but not limited to, the success and timing of the introduction of new products or entry into new markets, consumer demand, risk of sales returns, timing of market development programs, and long-term focus on product research and development activities. We believe that future cash generated from operating activities and the availability of our operating line of credit (see "Aggregate Contractual Obligations and Off-balance Sheet Financing") will be sufficient to fund both our future working capital needs and research and development activities beyond the next twelve months (see "Advisory Regarding Forward-looking Statements").

Selected cash flow and capitalization data				
(in thousands)	Three months ended		Six months ended	
	2011	September 30 2010	2011	September 30 2010
Cash provided by (used in) operating activities	2,509	1,068	(3,615)	(7,647)
			As at	As at
			September 30, 2011	March 31, 2011
Net demand operating line of credit and cash			(\$22)	\$3,691
Long-term debt and obligations under capital lease			872	843

Cash

At September 30, 2011, we had \$201 thousand of cash on hand and utilized \$223 thousand of a \$15 million demand operating line of credit. This compares to \$3.7 million in cash and no utilization of our operating line at March 31, 2011. During the quarter, we used cash on hand and the operating line to fund our operations, build up inventory and receivable levels for the cold and flu season, and purchase a limited amount of tangible and intangible long term assets.

Cash provided by (used in) operating activities

Cash provided by operating activities was \$2.5 million in the quarter compared with \$1.1 million in the same period in the prior year. Our lower net income in the current quarter resulted in less cash being generated; however this was offset by an increase in account payables (source of cash) as some of the costs related to the takeover bids were not paid by September 30, 2011. Cash used in operating activities in the six months ended September 30, 2011 was \$3.6 million compared with \$7.6 million used in the same period in the prior year. Lower net income in the current six-month period also resulted in less cash being generated; however, this was also offset by an increase in account payables.

Cash used in investing activities

Capital expenditures for the six months ended September 30, 2011 included purchases of property and equipment of \$48 thousand and additions to intangible assets of \$59 thousand. These expenditures were primarily laboratory equipment and computer hardware as well as for patent and trademark costs associated with new product development.

Cash used in financing activities

During the six months ended September 30, 2011, we issued share capital pursuant to option exercises of \$21 thousand and repurchased common shares under our Normal Course Issuer Bid ("NCIB") for \$12 thousand, resulting in net cash provided by financing activities of \$9 thousand. During the six months ended September 30, 2010, we repaid our mortgage in full and repurchased common shares under our NCIB resulting in net cash used in financing activities of \$5.3 million.

Normal Course Issuer Bid

On October 18, 2010, we renewed our NCIB with the Toronto Stock Exchange. Under the renewed NCIB, we may acquire up to 5,212,941 common shares, until the renewed NCIB expired on October 17, 2011.

During the three months ended June 30, 2011, we repurchased and cancelled 30,626 common shares pursuant to the NCIB at a total cost of \$12 thousand or \$0.38 per common share. No repurchases of shares were made in the three months ended September 30, 2011 or through to the expiry of the NCIB date of October 17, 2011. The NCIB was not renewed.

Aggregate contractual obligations and off-balance sheet financing

We have a demand operating line of credit of \$15.0 million with interest at the bank's prime lending rate plus 0.75%. The portion of the line of credit that is available to us is based on 65% of the appraised value of the Edmonton, Alberta head office and research centre to a maximum limit of \$6.8 million, 75% of accounts receivable aged less than 90 days, plus 50% of finished goods inventory to a maximum limit of \$4.1 million.

We also have an obligation under finance lease related to land which our Edmonton, Alberta head office and research facility is located on. The finance lease expires on November 15, 2015, and provides us an option to purchase the land on or before that time. We expect to exercise this

option on or before the expiration of the lease (see “Advisory Regarding Forward-looking Statements”).

In addition, we enter into operating and finance leases and purchasing agreements in the ordinary course of our business, including various agreements to provide financial assistance in research and development activities and clinical studies. To encourage a contract manufacturer organization (“CMO”) to invest in specific equipment required to produce our products, we signed on May 26, 2010 a commitment to purchase \$3.0 million of inventory from this CMO over a three-year period with \$2,426 remaining on this commitment. On March 24, 2011, we entered into an agreement with another CMO to develop a new product. If we proceed with launching this product, the contractual terms provide for a commitment of \$1.2 million. A consulting agreement for strategic and financial advisory services for a total of \$2.0 million was entered into during the current quarter with \$1.9 million remaining outstanding on the contract.

With the acquisition of the majority of Afexa’s Common Shares by Valeant, planned capital expenditures for the Company will be delayed and be re-evaluated based on the completion of integration plans with Valeant.

Related party transactions

No related party transactions occurred during the six months ended September 30, 2011. Included in general and administration expenses were management consulting fees of \$32 thousand for the three months ended September 30, 2010 incurred from a company controlled by a director of Afexa. These expenses occurred in the normal course of operations and were measured at their exchange amounts, which were established and agreed to as consideration by the related parties.

Outstanding shares and share options

We are authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at November 11, 2011, 109,606,840 common shares were outstanding (September 30, 2011 – 103,210,926 and March 31, 2011 - 103,202,552). No preferred shares were outstanding during or at the end of these periods. Certain of our employees, officers, contractors and directors have been granted options to purchase common shares under our share option plan. At November 11, 2011, there were no options outstanding (September 30, 2011 – 6,640,914 and March 31, 2011 – 7,105,914).

Outlook

On October 27, 2011, Valeant owned approximately 81.6% of Afexa’s Common Shares. Afexa is now preparing for a special meeting of its shareholders to be held on December 12, 2011 that will propose that an acquisition transaction be accepted. This will result in the privatization of Afexa being effective in December 2011 and the remaining shareholders of Afexa being paid for their Afexa shares in December 2011. The Company’s strategic plans and initiatives are being re-evaluated and will be integrated with Valeant’s plans.

RISKS AND UNCERTAINTIES

Our business is subject to certain risks and uncertainties related to financial risks (including liquidity, interest rate, foreign exchange, credit and litigation risk); operational risks (including market, product, seasonality of demand, product development, material supply and reliance on third party risks); regulatory approvals, and health and safety risks. Further discussion regarding these and other risks can be found in our March 31, 2011 annual MD&A and our Annual Information Form dated June 24, 2011 available on the SEDAR website at www.sedar.com.

Prior to making any investment decision regarding Afexa, investors should carefully consider, among other things, the risks described within this MD&A and the business risks and factors set forth in our March 31, 2011 annual MD&A and Annual Information Form dated June 24, 2011. Other than, as discussed elsewhere in this MD&A, our business risks and factors for the three and six months ended September 30, 2011 are substantially the same as disclosed in our annual MD&A, and are incorporated by reference herein. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also adversely affect our business and operations.

DISCLOSURE CONTROLS AND PROCEDURES (“DC&P”) AND INTERNAL CONTROLS OVER FINANCIAL REPORTING (“ICFR”)

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in National Instrument 52-109 Certification of Disclosure in Issuers’ Annual and Interim Filings. We evaluate our DC&P and ICFR using the framework established in the Internal Control – Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Information Technology controls are evaluated using the Control Objectives for Information and Related Technology (COBIT[®]) framework.

There have been no changes in our internal control over financial reporting during the three months ended September 30, 2011, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Changes in internal control over financial reporting

Effective September 30, 2011, Mr. Jack Moffatt relinquished the role as Afexa Chief Executive Officer and Mr. William White was appointed Interim Chief Executive Officer effective October 1, 2011. Pursuant to a support agreement between Afexa and Valeant, the majority of the directors of Afexa as well as the Interim CEO were replaced with Valeant appointees after the close of the quarter. Mr. Thomas Schlader, President of Valeant Canada Limited was appointed Chief Executive Officer of Afexa on October 18, 2011.

Other than these changes in certifying officer oversight responsibility, there were no changes in internal control over financial reporting.

Limitations on the effectiveness of internal controls

Material misstatements due to error or fraud may not always be prevented or detected on a timely basis because of the inherent limitation of DC&P and ICFR, including the possibility of collusion or improper management override of controls. Inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. In addition, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Management will continue to monitor and improve internal controls as necessary and appropriate for the business. Further discussion regarding DC&P and ICFR can be found in our March 31, 2011 annual MD&A.

CRITICAL ACCOUNTING ESTIMATES

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 compensation.

On an ongoing basis, management reviews its estimates to ensure that these values appropriately reflect changes in our 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

We establish 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 us and/or our competitors;
- Analysis of retail sell-through;
- The effect of regulatory changes; and
- The estimated remaining shelf life of products.

Consistent with industry practice, we periodically offer promotional discounts or allowances to the existing customer base. Where products are sold into new markets or new products are launched, our 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 cash generating unit (“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 we are 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, we use 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

We depreciate property and equipment and amortize intangible assets over the estimated useful lives of the assets. We take into account expectations of the in-service period of these assets in determining these estimates. We assess 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 we determine that the useful life of an asset is different from the original assessment, changes to depreciation and amortization will be applied prospectively.

Accrued liabilities

We engage 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 our allocation of overhead. This allocation is based on estimated annual production levels. Production levels are substantially driven by current and future estimated demand for our products, as well as our 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.

Share-based compensation costs

We measure 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. We use 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 our 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, we estimate our 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

We are 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. We maintain provisions for uncertain tax positions that we believe appropriately reflect our 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. We review 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 taxation 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.

CHANGES IN ACCOUNTING POLICIES INCLUDING TRANSITION TO IFRS

Transition to IFRS

During the fiscal year ended September 30, 2009, we commenced our process to transition to IFRS utilizing an implementation plan which encompassed, but was not limited to, evaluation of the IFRS standards, assessment of policy alternatives and elections, selection and application of accounting policies, integration and quantification of those policies into our business and financial statements and collection of all financial information necessary to produce IFRS compliant financial statements. Throughout this process, management established sufficient controls to ensure the accuracy, completeness and reliability of financial information and compliance with the new reporting standards. As part of this implementation plan, we also assessed and concluded that our information technology and data systems, internal control over financial reporting and disclosure controls and procedures, and business activities were minimally impacted by IFRS. Our conversion process is summarized in our March 31, 2011 annual MD&A under the Recent Accounting Pronouncements section.

The unaudited interim consolidated financial statements for the three and six months ended September 30, 2011 are the second presentation of our results and financial position in accordance with IFRS, the first being our first quarter results ended June 30, 2011. These statements are in compliance with IAS 34 – *Interim Financial Reporting*, and with IFRS 1 – *First Time Adoption of IFRS*. Subject to certain transition elections disclosed in the September 30, 2011 condensed consolidated interim financial statements, we have consistently applied the same accounting policies in our opening IFRS statement of financial position at April 1, 2010 and throughout all periods presented as if these policies have always been in effect.

Although the conceptual framework of IFRS is similar to that of Canadian GAAP, there are some significant differences on recognition, measurement, and disclosure. Our transitional elections, accounting policy choices, and their impact on the financial statements are described in full in note 14 of our September 30, 2011 consolidated financial statements.

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS

This MD&A contains certain forward-looking information and statements within the meaning of applicable securities laws. The use of any of the words “expect”, “anticipate”, “continue”, “estimate”, “objective”, “ongoing”, “may”, “will”, “would”, “project”, “could”, “should”, “contemplate”, “potential”, “depend”, “forecast”, “believe”, “plans”, “targets”, “intends” and similar expressions are intended to identify such forward-looking statements. These forward-looking statements reflect our beliefs and are based on information currently available to us. These statements require us to make assumptions that we believe are reasonable and are subject to inherent risks and uncertainties. Actual results and developments may differ materially from the results and developments discussed in the forward-looking statements as certain of these risks and uncertainties are beyond our control. The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon.

Examples of such forward-looking statements in this MD&A include, but are not limited to, our:

- *belief that we will have sufficient cash and operating line availability to fund both our working capital needs and research and development activities for the foreseeable future;*
- *expectations that the Company will exercise its option to purchase land which Afexa’s Edmonton, Alberta head office and research facility is located on; and*
- *plans that the Company will be privatized in December 2011 and the remaining shareholders of Afexa being paid for their Afexa shares in December 2011.*

Key Assumptions

Our forward-looking statements involve a number of significant assumptions. Key assumptions utilized in developing forward-looking statements related to our future growth expectations include:

- *customer pricing and related discounts and allowances remain comparable with historical levels;*
- *raw material and production costs remain comparable with historical experience;*
- *the incidence of colds and flu among the Canadian population will be at normal levels in fiscal 2012 and that retailers will replenish COLD-FX stock on a normalized basis.*

Risks

In addition to the risks outlined in the “Risks and Uncertainties” section of our MD&A, our forward-looking statements are subject to the following risks and uncertainties:

- *the incidence of illnesses in the general population;*
- *the impact of competition;*

- *consumer confidence and spending levels;*
- *general economic conditions;*
- *interest rates;*
- *unseasonable weather patterns;*
- *the cost and availability of capital;*
- *the cost and availability of grants/funding;*
- *product development;*
- *reliance on third parties;*
- *dependence on a small number of major customers;*
- *adequate cash position to mitigate potential tightening of credit terms;*
- *success and adequacy of our long-term strategic objectives; and*
- *risk that actual results may differ from management's assumptions and estimates.*

We believe the expectations and assumptions reflected in the forward-looking information and statements contained herein are reasonable. However, no assurance can be given that these expectations and assumptions are correct and that the results, performance or achievements expressed in, or implied by, forward-looking statements within this disclosure will occur, or if they do, whether any benefits may be derived from them. All forward-looking statements are expressly qualified in their entirety by this cautionary statement.

The forward-looking information and statements contained in this MD&A speak only as at the date of this MD&A, and we assume no obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws.