
# Management Discussion and Analysis of Financial Condition and Results of Operations

## Fiscal 2012 –Third Quarter
## for the three and nine month periods ended January 31, 2012

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## Overview

The following management discussion and analysis (MD&A) is a review of the financial condition and results of operations of Critical Outcome Technologies Inc. (COTI or the Company) for the quarter ended January 31, 2012, and has been prepared with all information available up to and including March 28, 2012. This MD&A is intended to assist in understanding the dynamics of the Company's business and the key factors underlying its financial results.

The unaudited condensed interim financial statements (interim financial statements) have been prepared in accordance with International Accounting Standard (IAS) 34, Interim Financial Reporting and with International Financial Reporting Standards (IFRS) 1, First-time Adoption of IFRS. By their nature, the interim financial statements do not conform in all respects with disclosures for annual financial statements and should be read in conjunction with the Company's audited financial statements for the year ended April 30, 2011, prepared in accordance with Canadian Generally Accepted Accounting Principles (CGAAP). The Company adopted IFRS effective May 1, 2011. While the Company's annual financial statements for the year ended April 30, 2011 have been audited in accordance with CGAAP, they were not audited in accordance with IFRS. Further discussion related to the impact of the transition to IFRS is noted as appropriate in this MD&A.

All dollar amounts are expressed in Canadian dollars. Historic quarterly interim reports, the Company's Annual Information Form (AIF) and annual audited financial statements as well as additional supplementary information concerning the Company can be found on SEDAR at www.sedar.com.

## Forward-looking Statements

This MD&A contains certain statements based upon forward-looking information (forward-looking statements or FLS) concerning the Company's plans for its operations and other matters within the meaning of applicable Canadian provincial securities laws. FLS are necessarily based on estimates and assumptions that are inherently subject to significant business, economic and competitive uncertainties and contingencies. All statements that address activities, events or developments that the Company believes, expects or anticipates will or may occur in the future are FLS. FLS are subject to a variety of risks and uncertainties that may cause the actual events or results of the Company to differ materially from those discussed in the FLS, and even if such actual events or results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on, the Company.

Any statements that express or involve discussion with respect to predictions, expectations, beliefs, plans, projections, objectives, or assumptions of future events or performance (often, but not always, using words or phrases such as "expects" or "does not expect", "is expected", "anticipates" or "does not anticipate", "plans", "estimates" or "intends", or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved) are not statements of historical fact and may be FLS. The major FLS included in this MD&A are set out in Table 1.

*Table 1: Forward-looking Statements*

| MD&A Section Heading | Nature of Forward-looking Information Disclosed |
|---|---|
| Our Business | • Intends to license its targeted molecules<br>• Plans for further testing of COTI-2 leading to an IND filing and readiness for a Phase 1 clinical trial<br>• Plans for future application of the CHEMSAS® technology on a collaboration basis<br>• The Company's commercialization strategy for collaborations |
| Liquidity and Capital Resources | • Expectations of future expenditures on patents and computer software<br>• Plans for future research and development projects and additional financing |
| Financial and Operational Progress and Outlook | • Scientific experiments for COTI-2 progressing to optimize the licensing value of the drug candidate<br>• *In vitro* testing progressing for the AML program<br>• Seeking partners to develop and market the HIV-1 integrase program for co-development |
| Industry and Economic Factors Affecting Performance | • The expected continuation of losses until a revenue transaction is secured<br>• Plans to negotiate future licensing agreements<br>• Plans to raise additional financing through different venues and mechanisms available to the Company |
| Changes in Accounting Policies Including Initial Adoption | • The adoption of new accounting standards issued by the Accounting Standards Board particularly those related to Financial Instruments |

The basis for the FLS is management's current expectations, estimates, projections and assumptions. By their nature, they are not guarantees of future performance as they involve significant risks and uncertainties.

The main assumptions used by management to develop the forward-looking information include the following:

- An ability to obtain sufficient financing to support working capital requirements and fund further research and development initiatives over the long term
- An ability to further develop the CHEMSAS® technology for internal and collaborative purposes
- A continuation of favourable preclinical test results from the COTI-2 program and an ability to meet the requirements for regulatory approval
- Obtaining patent protection for the Company's compounds and other intellectual property
- An ability to attract and retain skilled and experienced personnel and to maintain relationships with third party clinical research organizations

Management of COTI considers the assumptions on which the FLS are based to be reasonable. However, management cautions the reader that because of the many risk factors as set out in the Company's AIF, including those specifically described below which are of particular importance to the assumptions above, actual results could differ materially from those expressed or implied in the FLS. These assumptions may prove to be wrong, and as such, undue reliance should not be placed on any individual FLS.

The main risk factors that will influence the Company's ability to realize on its FLS include:

- The ability to raise sufficient financing for continuing operations and development including maintaining the Company's workforce
- The ability to establish customer relationships leading to licensing agreements for the Company's compounds
- The ability to generate customer demand for outputs from the CHEMSAS® technology
- The ability to continue favourable preclinical test results from the Company's lead oncology compound, COTI-2
- The ability to meet future regulatory requirements to commercialize compounds, in particular COTI-2
- The ability to obtain patent protection for the Company's compounds

The forward-looking information is provided as of the date of this MD&A and the Company does not undertake any obligation to publicly update or revise any forward-looking information, whether because of new information, future events, or otherwise, except as required by securities laws.

## The Company

COTI is a London, Ontario based company resulting from the amalgamation on October 13, 2006 of Aviator Petroleum Corp. (Aviator), a public company listed on the TSX Venture Exchange (TSXV), and Critical Outcome Technologies Inc., a private company under the provisions of the *Business Corporations Act* (Ontario). The amalgamation constituted the qualifying transaction for Aviator pursuant to the policies of the TSXV. The amalgamated company adopted the name Critical Outcome Technologies Inc. and its common shares were listed and posted for trading on the TSXV under the symbol COT on October 30, 2006.

On November 27, 2007, the Company completed an acquisition of all the outstanding common shares in the capital of 3015402 Ontario Inc. operating as DDP Therapeutics (DDP), in which the Company had, up to the date of the acquisition, a 10% ownership interest. DDP was formed in early 2005 to develop a library of small cell lung cancer molecules discovered by the Company using its drug discovery technology.

On May 1, 2008, the Company amalgamated with this wholly owned subsidiary under the laws of the Province of Ontario.

## Our Business

COTI is a biotechnology company focused on applying its proprietary computer-based technology, CHEMSAS®, to identify, profile, optimize and select potential new drug candidates at the discovery stage of preclinical drug development and thereby reduce the timeline and cost of getting new drug therapies to market. The Company's long-term business model is to license its targeted molecules following synthesis and completion of confirmatory preclinical testing to the investigational new drug (IND) ready stage in order to address pipeline needs of pharmaceutical and biotechnology companies.

The Company is developing focused portfolios of novel, proprietary and optimized small molecules as potential drug candidates for specific therapeutic targets in diseases that have high morbidity and mortality rates and currently have either poor or no effective therapies. COTI has concentrated on developing drug candidates for the treatment of various cancers, human immunodeficiency virus (HIV), Alzheimer's disease and multiple sclerosis. Cancer types specifically targeted include small cell lung, adult myelogenous leukemia (AML), ovarian, endometrial, pancreatic, brain, breast and colon.

The Company is currently taking a particularly promising oncology molecule, COTI-2, forward through various preclinical tests to Phase 1 clinical trials as commercial validation of both the compounds viability as a clinical drug candidate and the underlying CHEMSAS® technology used to discover it. In this regard, COTI is currently focused on preparing for IND clinical trial submission based on the positive preclinical test results achieved for COTI-2, its lead cancer molecule, against a number of cancer indications. Current testing initiatives and planning would enable an IND filing in calendar 2012. Upon acceptance of an IND filing, COTI-2 would be available for licensing or co-development as a Phase 1 ready compound.

The Company also seeks to leverage CHEMSAS® to identify targeted lead candidates of commercial interest to pharmaceutical, biotechnology, research and academic organizations on a collaborative basis. The Company's preferred commercialization strategy for collaborations involves an upfront fee and a shared risk/reward revenue model delivered through a series of milestone payments based on preclinical and clinical test results. This service offering provides prospective customers with an efficient and cost effective approach for generating targeted discovery stage compounds while enhancing value to COTI and its shareholders from the underlying CHEMSAS® technology. This collaboration approach resulted in two engagements with multinational pharmaceutical companies in the past few years, one for a cancer target and the other for an HIV target.

## Financial Review of Operations

Revenues

Operating:

There were no operating revenues in the quarter ended January 31, 2012 (Q3-F'12) or in the quarter ended January 31, 2011 (Q3-F'11) or for the nine months ended January 31, 2012 (YTD-F'12) or for the nine months ended January 31, 2011 (YTD-F'11). The Company continued to

pursue a licensing agreement for its preclinical lead oncology compound, COTI-2, during Q3-F'12 with several interested parties but without reaching mutual agreement on contractual terms.

Non-operating:

Investment tax credit (ITC) income of $33,669 was recognized in the third quarter, relating to scientific research and development tax credits earned on eligible expenditures. There was no ITC income recognized in Q3-F'11 as the Company was following a policy of recognizing ITCs on a received basis at that time compared to the current accrual basis.

The Company earned $2,162 in interest income on its cash, cash equivalents and short-term investments in Q3-F'12 compared to $2,185 in Q3-F'11.

Operating Expenses

Operating expenses decreased from $635,959 in Q3-F'11 to $624,652 for Q3-F'12, a decrease of $11,307. One major item accounted for this comparable quarterly change as the recognition of investment tax credits increased from $0 in Q3-F'11 to $33,669 in Q3-F'12.

Operating expenses increased from $1,534,169 for YTD-F'11 to $1,931,522 for YTD-F'12, an increase of $397,353. This increase related primarily to $259,274 in higher stock-based compensation expense for YTD-F'12. This resulted primarily from a recovery of $110,509 in previously recognized stock-based compensation expense. Table 2 provides a breakdown of the components of stock-based compensation expense for Q3-F'12 and Q3-F'11 and YTD-F'12 and YTD-F'11 respectively.

*Table 2: Stock-Based Compensation Expense – Comparative Periods Ended January 31*

| | Q3-F'12 | Q3-F'11 | Change |
|---|---|---|---|
| Recognized on new option grants | $ - | $ - | $ - |
| Recognized on existing options | 75,411 | 71,069 | 4,342 |
| | $ 75,411 | $ 71,069 | $ 4,342 |

| | YTD-F'12 | YTD-F'11 | Change |
|---|---|---|---|
| Recognized on new option grants | $ 84,188 | $ 2,481 | $ 81,707 |
| Recognized on existing options | 98,122 | 122,791 | (24,669) |
| Re-measurement of consultant options | - | (91,728) | 91,728 |
| Reversal of unvested cancelled options | - | (110,509) | 110,509 |
| | $ 182,310 | $ (76,965) | $ 259,275 |

Quarterly research and product development (R&D) expenditures increased year over year due to the increased synthesis costs for the COTI-2 and AML projects, and increased *in vivo* and *in vitro* testing for COTI-2. Table 3 provides a breakdown of R&D costs by major expense types for the comparable three and nine month fiscal periods ended January 31 respectively.

*Table 3: R&D Expenses – Comparative Periods Ended January 31*

| | Q3-F'12 | Q3-F'11 | Change |
|---|---|---|---|
| R&D testing, consulting and materials | $ 52,010 | $ 20,591 | $ 31,419 |
| Synthesis | 23,137 | 9,534 | 13,603 |
| | 75,147 | 30,125 | 45,023 |
| Labour including benefits | 79,763 | 86,863 | (7,100) |
| Other | 8,730 | 8,267 | 463 |
| | 163,640 | 125,255 | 38,385 |
| Stock-based compensation | - | - | - |
| Total | $ 163,640 | $ 125,255 | $ 38,385 |

| | YTD-F'12 | YTD-F'11 | Change |
|---|---|---|---|
| R&D testing, consulting and materials | $ 115,728 | $ 93,792 | $ 21,936 |
| Synthesis | 112,889 | 68,679 | 44,210 |
| | 228,617 | 162,471 | 66,146 |
| Labour including benefits | 239,430 | 279,029 | (39,599) |
| Other | 21,542 | 17,349 | 4,193 |
| | 489,589 | 458,849 | 30,739 |
| Stock-based compensation | 6,126 | - | 6,126 |
| Total | $ 495,715 | $ 458,849 | $ 36,865 |

R&D testing, consulting and materials increased $42,759 offset by $11,340 in government assistance for a net increase of $31,419 for Q3-F'12 compared to Q3-F'11 due to increases in the extent of *in vitro* and *in vivo* testing for COTI-2. Synthesis costs increased $34,603 offset by $21,000 in government assistance for a net increase of $13,603. These costs were focused on COTI-2's oral formulation and synthesis of the Company's acute myelogenous leukemia (AML) compounds.

R&D labour costs decreased year over year primarily related to the allocation of a portion of the Chief Scientific Officer's (CSO) salary costs to general and administrative (G&A) salary expense. The allocation was based on time commitments in his various roles as President, Chief Executive Officer (CEO) and CSO. The Company also recovered $10,375 in salary costs in Q3-F'12 from government assistance received for its AML project. There were no changes in R&D staff levels during the comparable periods.

Table 4 provides a breakdown of G&A costs by major expense types for the comparable three and nine month fiscal periods ended January 31 respectively.

*Table 4: G&A – Comparative Periods Ended January 31*

| | Q3-F'12 | Q3-F'11 | Change |
|---|---|---|---|
| Salaries and benefits | $ 93,046 | $ 94,213 | $ (1,167) |
| Amortization | 129,711 | 121,638 | 8,073 |
| Corporate governance | 7,773 | 9,639 | (1,866) |
| Promotion and travel | 4,625 | 6,229 | (1,604) |
| Professional fees | 94,250 | 70,373 | 23,877 |
| Rent | 9,346 | 9,346 | - |
| Insurance | 14,895 | 14,922 | (27) |
| Other | 7,658 | 40,919 | (33,261) |
| | 361,304 | 367,279 | (5,975) |
| Stock-based compensation | 74,411 | 71,069 | 3,342 |
| Total | $ 435,715 | $ 438,348 | $ (2,633) |

| | YTD-F'12 | YTD-F'11 | Change |
|---|---|---|---|
| Salaries and benefits | $ 302,987 | $ 291,629 | $ 11,358 |
| Amortization | 367,834 | 368,328 | (494) |
| Corporate governance | 56,016 | 71,022 | (15,006) |
| Promotion and travel | 21,542 | 15,833 | 5,709 |
| Professional fees | 313,987 | 205,045 | 108,942 |
| Rent | 28,038 | 28,593 | (555) |
| Insurance | 44,728 | 44,739 | (11) |
| Other | 24,651 | 53,987 | (29,336) |
| | 1,159,781 | 1,079,176 | 80,605 |
| Stock-based compensation | 173,613 | (76,966) | 250,579 |
| Total | $ 1,333,394 | $ 1,002,210 | $ 331,184 |

Q3-F'12 amortization costs increase by $8,073 as a result of the granting of the COTI-2 patent, which triggered the release of contingent consideration and an increase in the molecule value by $164,616.

Other professional fees increased in Q3-F'12 by $23,877 primarily due to consulting contracts related to the implementation of IFRS, financing and licensing.

Patent impairment of $34,406 was included in the Other line in Q3-F'11 as a result of the Company abandoning patent efforts on two series of HIV compounds and on one series of MS compounds. There was no impairment of patents recognized in Q3-F'12.

Table 5 provides a breakdown of sales and marketing costs (S&M) by major expense types for the comparable three and nine month periods ended January 31 respectively. S&M expenses decreased from $72,356 in Q3-F'11 to $58,966 in Q3-F'12 due to the timing of expenses for the BIO Europe convention. The expenses for fiscal 2012 were reported in Q2-F'12.

*Table 5: S&M – Comparative Periods Ended January 31*

| | Q3-F'12 | Q3-F'11 | Change |
|---|---|---|---|
| Salaries and benefits | $ 49,772 | $ 48,648 | $ 1,124 |
| Marketing and travel | 8,261 | 22,830 | (14,569) |
| Other | 934 | 878 | 56 |
| | 58,966 | 72,356 | (13,390) |
| Stock-based compensation | - | - | - |
| Total | $ 58,966 | $ 72,356 | $ (13,390) |

| | YTD-F'12 | YTD-F'11 | Change |
|---|---|---|---|
| Salaries and benefits | $ 140,831 | $ 131,012 | $ 9,819 |
| Marketing and travel | 39,074 | 52,178 | (13,104) |
| Other | 3,381 | 6,934 | (3,553) |
| | 183,286 | 190,124 | (6,837) |
| Stock-based compensation | 2,571 | 5,230 | (2,659) |
| Total | $ 185,857 | $ 195,354 | $ (9,497) |

## Financial Results Summary by Quarter

Table 6 summarizes the financial results of COTI by quarter for the past two fiscal years and the most recent three quarters. The three quarters of FYE 2012 and the four quarters of FYE 2011 are restated in compliance with IFRS. The four quarters presented for FYE 2010 were prepared under the CGAAP framework required at that time and have not been adjusted to conform to IFRS.

*Table 6: Summary of Quarterly Financial Results*

| FYE 2012 | Q1 31-Jul | Q2 31-Oct | Q3 31-Jan | Q4 30-Apr | Year to Date |
|---|---|---|---|---|---|
| Revenue | $ - | $ - | $ - | | $ - |
| Loss | (642,257) | (648,530) | (619,550) | | (1,910,337) |
| Loss per common share | $ (0.01) | $ (0.01) | $ (0.01) | | $ (0.03) |

| FYE 2011 | Q1 31-Jul | Q2 31-Oct | Q3 31-Jan | Q4 30-Apr | Full Year |
|---|---|---|---|---|---|
| Revenue | $ - | $ - | $ - | $ - | $ - |
| Loss | (558,950) | (334,498) | (634,345) | (473,585) | (2,001,378) |
| Loss per common share | $ (0.01) | $ (0.01) | $ (0.01) | $ (0.01) | $ (0.04) |

| FYE 2010 | Q1 31-Jul | Q2 31-Oct | Q3 31-Jan | Q4 30-Apr | Full Year |
|---|---|---|---|---|---|
| Revenue | $ - | $ - | $ - | $ - | $ - |
| Loss | (979,089) | (976,678) | (773,217) | (831,326) | (3,560,310) |
| Loss per common share | $ (0.02) | $ (0.02) | $ (0.02) | $ (0.02) | $ (0.08) |

The majority of the variation by quarter across the years, and year over year, is explained by three expense categories as set out in Table 7.

*Table 7: Selected Quarterly Expense Categories*[1]

| FYE 2012 | Q1 31-Jul | Q2 31-Oct | Q3 31-Jan | Q4 30-Apr | Year to Date |
|---|---|---|---|---|---|
| General and administration | $ 374,143 | $ 424,333 | $ 361,304 | | $ 1,159,780 |
| Research and product development | 205,941 | 120,008 | 163,640 | | 489,589 |
| Investment tax credit recovery | (29,889) | (19,888) | (39,822) | | (89,599) |
| Stock-based compensation | 41,182 | 66,717 | 74,411 | | 182,310 |
| Total of expense categories | 591,377 | 591,171 | 559,533 | | 1,742,081 |
| Total expense for the quarter | $ 649,097 | $ 657,773 | $ 624,652 | | $ 1,931,522 |
| Expense categories as a % of total expense | 91.1% | 89.9% | 89.6% | 0.0% | 90.2% |

| FYE 2011 | Q1 31-Jul | Q2 31-Oct | Q3 31-Jan | Q4 30-Apr | Full Year |
|---|---|---|---|---|---|
| General and administration | $ 360,708 | $ 351,097 | $ 367,233 | $ 307,468 | $ 1,386,506 |
| Research and product development | 196,374 | 137,220 | 125,255 | 133,893 | 592,742 |
| Investment tax credit recovery | - | (122,244) | - | (72,185) | (194,429) |
| Stock-based compensation | (57,157) | (90,878) | 71,069 | 45,287 | (31,679) |
| Total of expense categories | 499,925 | 275,195 | 563,557 | 414,463 | 1,753,140 |
| Total expense for the quarter | $ 562,452 | $ 335,758 | $ 635,959 | $ 469,924 | $ 2,004,093 |
| Expense categories as a % of total expense | 88.9% | 82.0% | 88.6% | 88.2% | 87.5% |

(1) The presentation noted in this table does not conform to the IFRS functional presentation in the Company's interim financial statements. Stock-based compensation included in General and Administration, and Research and Product Development in the financial statements has been removed from the functional disclosure and shown separately in this table.

The variability in the second quarter trend noted in Table 7 is largely due to the impact of the recovery of $110,509 in Q2-F'11 for previously recognized stock-based compensation costs on the cancellation of options upon the resignation of the former CEO in June 2010. The year over year third quarter comparison is relatively consistent with an increase in R&D expense in Q3-F'12 being partially offset by the recognition of investment tax credits (ITCs) earned on such expenditures during the quarter. This reflects the change in recognition of ITCs to an earned basis that commenced in Q4-F'11 compared to when received, as had previously been the practice.

The remaining variability by quarter over the years is largely explained by variable spending in third party R&D testing and synthesis and the use of consultants. The balance of the remaining expense categories remained relatively consistent.

## Liquidity and Capital Resources

At the end of Q3-F'12, the Company had cash, cash equivalents and short-term investments of $597,738 compared to $2,094,917 cash, cash equivalents and short-term investments at the end of FYE 2011 reflecting a decrease of $1,497,179. Table 8 summarizes the changes in cash resources for the comparable nine-month periods ending January 31 for fiscal 2012 and 2011. The difference in the cash positions is a modest $11,814 as illustrated.

*Table 8: Summary of Changes in Capital Resources* [(1)]

| | YTD Q3-F'12 | YTD Q3-F'11 |
|---|---|---|
| Increase (decrease) from: | | |
| Operating activities | $ (1,464,232) | $ (1,322,732) |
| Investing activities excluding changes in short-term investments | (51,637) | (44,520) |
| (Decrease) in capital resources before issuance of common shares and warrants | (1,515,869) | (1,367,252) |
| Proceeds from issuance of common shares and warrants | 11,445 | 32,848 |
| Interest received (paid) | 1,759 | (1,337) |
| (Decrease) increase in capital resources | (1,502,665) | (1,335,741) |
| Less: unrealized foreign exchange loss on capital resources | 5,486 | 83 |
| Capital resources - beginning of period | 2,094,917 | 1,945,376 |
| Capital resources - end of period | $ 597,738 | $ 609,552 |

(1) See Use of Non-GAAP Financial Measures

Investing activities in Q3-F'12 related to intangible asset expenditures for computer software and patents. Investment in such items will continue into the future as the Company relies heavily on computing technology to run its CHEMSAS® process, and investing in patents for the molecules identified from the process ensures that the licensing value of this intellectual property is protected.

In Q3-F'12, there were no options or warrants exercised.

The Company's working capital at Q3-F'12 was $553,100 compared to $1,953,490 at FYE 2011. Current assets continue to remain highly liquid, as there are no restrictions on the use of these assets. Cash equivalents are invested in instruments with maturities of three months or less. Short-term investments are held in a flexible guaranteed investment certificate, which became cashable without penalty after June 30, 2011. Current assets decreased to $828,516 at Q3-F'12 from $2,297,133 at FYE 2011 for a decrease of $1,468,617, primarily due to the decrease in cash and cash equivalents. Current liabilities decreased $68,227 to $275,416 at Q3-F'12 from $343,643 at FYE 2011 because of decreased project accruals and reduced trade payables related to professional fees.

The Company's exposure to fluctuations in the recoverability of its financial assets is limited as cash not required for current purposes is held in interest bearing cash accounts. Miscellaneous receivables are of high credit quality. The short periods to maturity of these instruments and their capacity for prompt liquidation result in future settlement amounts that are consistent with carrying values. Given the nature of the Company's financial liabilities, there is also limited risk that future settlement amounts will differ from carrying values. The Company does not have any derivative financial instruments, nor does it engage in hedging transactions, as risk exposure is limited.

The Company's long-term contractual obligations are summarized in Table 9. The last R&D contract commitment for $3,900 expires January 31, 2014.

*Table 9: Contractual Obligations*

| Obligation | Total | 2012 | 2013 |
|---|---|---|---|
| Premises rent [(1)] | $ 9,345 | $ 9,345 | $ - |
| Research and development contracts | 127,844 | 127,844 | - |
| Total contractual obligations | $ 137,189 | $ 137,189 | $ - |

[(1)] The premises lease agreement expired on May 31, 2009 and has been extended on a month-to-month basis with a 90-day notice period.

Subsequent to quarter end, on March 23, 2012, the Company completed the first tranche of a private placement and issued 3,125,000 units at $0.16 per unit for gross proceeds of $500,000. Each unit consisted of one common share and one common share purchase warrant with each warrant exercisable into one additional common share at a price of $0.30 until September 23, 2013. Cash costs of the private placement amounted to approximately $25,270. A total of 157,938 agent warrants exercisable into one additional common share at a price of $0.30 until September 23, 2013 were issued. The Company expects to complete the second tranche of the private placement in April 2012. This funding strengthens the Company's cash position and improves its liquidity. The funds raised in this placement will be used primarily to achieve the specific development milestones for the Company's lead preclinical oncology asset, COTI-2 previously announced by the Company as key value building milestones for the compound.

Future Plans Impact

The Company has formulated goals for the balance of fiscal 2012 and fiscal 2013 to advance the testing for COTI-2 in enhancing its attractiveness to potential licensees and to move the AML project and other projects forward as resources permit. The Company has discretion in many of its budgeted activities and plans to manage these activities in a manner to sustain operations until the necessary financing is available to meet its goals for COTI-2. The Company expects to continue its efforts to obtain financing over the next year to accomplish its goals.

## Off-Balance Sheet Arrangements

The Company has not historically utilized, nor is it currently utilizing any off-balance sheet instruments.

## Foreign Exchange Exposure

During Q3-F'12, the Company recorded a foreign exchange gain of $3,106 compared to a loss of $(113) in Q3-F'11. The gain recorded in Q3-F'12 reflects $5,486 in unrealized gains resulting from holding foreign currency balances at the quarter end compared to $83 in unrealized gains at Q3-F'11. The foreign currency exposure in Q3-F'12 was immaterial and unchanged from FYE 2011.

## Related Party Transactions

There were no related party transactions of a material nature that occurred during Q3-F'12. However, stock options expired during the quarter as follows:

a) On January 11, 2012, 260,000 vested options granted to directors expired unexercised.
b) On January 11, 2012, 455,000 vested options granted to employees expired unexercised.
c) On January 14, 2012, 50,000 vested options granted to an employee expired unexercised.

## Outstanding Share Information

Outstanding share information at the close of business on March 28, 2012 is set out in Table 10.

*Table 10: Outstanding Share Information*

| | Outstanding | Expiry Date |
|---|---|---|
| Common shares | | |
| Authorized - unlimited | | |
| Issued | 66,328,214 | |
| Fully diluted [1] | 88,100,480 | |
| Weighted average outstanding [2] | 62,907,034 | |
| Common share warrants | | |
| $0.30 compensation warrants | 385,500 | Sep 24/12 |
| $0.30 compensation warrants | 82,000 | Oct 6/12 |
| $0.30 compensation warrants | 40,000 | Oct 20/12 |
| $0.30 compensation warrants | 157,938 | Sep 23/13 |
| $0.55 warrants | 72,590 | Oct 27/11 |
| $0.55 warrants | 56,430 | Nov 27/11 |
| $0.30 warrants | 8,152,500 | Sep 24/12 |
| $0.30 warrants | 2,187,500 | Oct 6/12 |
| $0.30 warrants | 2,160,000 | Oct 20/12 |
| $0.30 warrants | 3,125,000 | Sep 23/13 |
| $0.37 warrants | 1,446,480 | Jan 31/13 |
| | 17,865,938 | |
| Common share stock options | | |
| $0.01 - $0.50 | 2,905,144 | Sep 9/14 - Oct 17/16 |
| $0.51 - $1.00 | 801,184 | Jan 11/12 - Mar 14/15 |
| $1.01 - $1.50 | 100,000 | Jul 15/13 |
| $1.51 - $2.00 | 100,000 | Oct 8/12 |
| | 3,906,328 | |

[1] Assumes conversion of all outstanding common share stock options and warrants.

[2] Weighted average shares outstanding calculated from May 1, 2011 to March 28, 2012

## Financial and Operational Progress & Outlook

### Financial Outlook for Q4-FYE 2012 and into FYE 2013

The Company continues to meet with prospective licensing partners and anticipates that it will be positioned to negotiate a licensing deal for COTI-2 in calendar 2012. As announced on April 12, 2011, the Company responded to scientific and business feedback from prospective licensing partners by initiating a series of three experiments to address risk reduction points common to these prospects. These experiments strengthen the scientific data package of COTI-2 making it more valuable to a potential partner through the reduction in the risk profile of the compound. Information from these scientific experiments is shared with prospective licensees as it becomes available. At October 31, 2011, the first of the three experiments was completed as discussed in the second quarter MD&A and as announced in a series of press releases dated June 26, August 16 and October 20, 2011. The second set of experiments that started in Q1-F'12 related to finding an optimal oral formulation continued to progress in Q3-F'12 with the identification of eight viable formulations as announced in January 2012 and discussed in more detail below. The last of the three experiments related to two species toxicity studies will commence in the second quarter of calendar 2012 based upon the selection of the optimal oral formulation from the candidates identified. The Company is focused on getting COTI-2 to a licensing agreement not only for the monetary benefit to its shareholders but the opportunity COTI-2 presents for further development in the clinic and ultimately for the benefit of oncology patients.

R&D expenditures have historically been conducted with contract research organizations in the most cost effective manner considering the opportunity for refundable ITCs in identifying least cost, best value suppliers, and this is anticipated to continue as the Company works to finalize its plans for the two species toxicity studies.

The Company's strategy to complement the development of COTI-2, and its ultimate licensing, by advancing other drug discovery projects along parallel tracks, continued during the quarter and is expected to continue for the balance of fiscal 2012 within the context of the Company's ability to finance such development. In this regard, the synthesis of compounds related to the Company's AML project was completed in January 2012. *In vitro* testing commenced in January 2012 and will continue during the fourth quarter of FYE 2012. Spending on the project, as previously announced, is partially offset through the recovery of approximately $100,000 from an NRC-IRAP funding commitment available for FYE 2012. To the end of Q3-F'12, the Company had recovered $29,115. This recovery will increase substantially in the fourth quarter, as synthesis was completed late in Q3-F'12 and as *in vitro* testing progresses on the compounds in Q4-F'12. The Company anticipates recovering the full amount of $100,000 by the Company's April 30, 2012 year end.

Expenditures on G&A and S&M activities for FYE 2012 are expected to remain consistent with those budgeted for the year with actual results for the first nine months being higher than budget by $35,974.

Expenditures on intangible assets and capital assets are trending below budget and are anticipated to be below the full year budget amount of approximately $150,000. This spending is primarily on the Company's patent portfolio and computer software.

Product Development Progress – Q3-F'12 and Future Outlook

The Company continued to make progress in developing its drug candidate pipeline during Q3-F'12 with primary focus on COTI-2, the Company's lead oncology compound, and the AML project. Because of limited financial resources, the Company has a number of drug compounds and programs whose further development remains on hold, the primary one of these being the HIV project. The Company is exploring a variety of ways to realize value on these compounds or further their development through co-development projects.

COTI-2

During the quarter, the Company continued development of COTI-2 by carrying out additional experiments and laboratory work in preparation for an IND clinical trial submission. A summary of key milestones in this development is set out below.

- Progress in developing an oral formulation candidate for COTI-2 continued during the quarter such that on February 1, 2012, the Company announced that it had successfully identified a small group of oral formulation candidates capable of being used in completing the two species toxicity testing for the COTI-2 clinical submission package and in the Phase 1 human clinical trial. The next step in the formulation project is to select the best candidate from the group based upon a number of criteria including ease of manufacturing, efficacy, and pharmacokinetic profile, including bioavailability. The final selection process will occur in Q4-F'12 once an optimal detection method is completed.

- Both Health Canada and the United States Food and Drug Administration require a validated detection method for measuring a drug's concentration in human plasma as part of the Phase 1 IND submission package. Based upon the functional detection method used for rodent species to date, the Company has done considerable work in developing the final detection method including the successful development of a radio-labeled COTI-2 isotope for use as an internal standard. Shortly after the quarter end, on February 8, 2012, the Company announced it had engaged Algorithme Pharma Inc. of Montreal, Canada, an internationally recognized contract research organization, to develop and validate the final method to be used for preclinical and Phase 1 studies for COTI-2. It is anticipated the development and validation of this process will take approximately six weeks to complete.

- The formulation work also produced a more detailed understanding of how COTI-2 is likely to behave in the body. Experiments from two rodent species demonstrated that orally administered COTI-2 is handled by the body in a complex but common way that produces sustained levels of COTI-2 in the blood for up to 48 hours after a single dose. This suggests that COTI-2 may be developed as an out-patient cancer therapy taken

daily or even on alternate days. A daily oral medication is usually considered optimal for home based patient administration because of the ease of patient compliance.

Acute Myelogenous Leukemia (AML)

Like many other cancers, AML is the result of multiple gene mutations that affect multiple cell signaling kinase pathways. With few exceptions, traditional therapies that target a single abnormal kinase have produced disappointing long-term results. On January 24, 2012, the Company announced it had completed synthesis of compounds from COTI's AML program and had initiated confirmatory preclinical tests. COTI's compounds target multiple kinases commonly mutated in AML and accordingly are believed to have a higher probability of success in improving outcomes for patients with AML. COTI's program has the potential to produce multiple drug candidates with differing activity profiles that can be used to treat acute leukemias with different gene mutation profiles.

Collaborations and Co-Development Projects

HIV-1 Integrase Co-development

As previously announced, the Company made a submission to a new initiative of the NRC-IRAP called the Canadian HIV Technology Development Program. In December 2011, the Company was advised that while its project proposal had strong scientific merit, concerns on the ability of the Company to take on more projects given its current financial capabilities, prevented the program administrator from approving a grant for 2012.

The Company has identified a number of parties with interest in the scientific program and continues to explore possible co-development opportunities.

Collaboration with a University Tech Transfer Office

During Q3-F'12, the Company made a proposal to provide its CHEMSAS® services to a university tech transfer office and research scientist in pursuit of lead candidates for organ transplant dysfunction. Funding for this research would result from a Canadian Institute of Health Research grant. A decision on the grant submission is expected in July 2012.

## Industry and Economic Risk Factors Affecting Performance

The biotechnology industry is regarded as high risk given the uncertain nature of developing drug candidates and limited access to capital. On the other hand, success in this industry can be highly rewarding. COTI operates in the discovery and preclinical stage of the drug development cycle. The realization of COTI's long-term potential is dependent upon the successful development and commercialization of molecules discovered using the Company's drug discovery technology either for its own account or in collaboration agreements for others, and in utilizing the technology to provide profiling and screening services on a fee for service basis. The major industry and economic risk factors affecting realization of this potential in Q3-F'12 remain substantially unchanged from the analysis discussed at length in the Company's AIF and the risks discussed in the FYE 2011 MD&A and Q1 and Q2-F'12 MD&As.

The three risk categories having the greatest affect on the Company during the quarter were:

1. the lack of product revenues;
2. securing licensing agreements; and,
3. access to capital.

Lack of Product Revenues

COTI has not recorded any revenues from the sale or license of any drug compounds or compound libraries during its first five years as a public company consistent with the most recent quarter, Q3-F'12. COTI has an accumulated deficit since its inception through to January 31, 2012 of $15,647,348. This deficit is expected to increase in the near term as COTI continues its product development efforts, develops relationships with prospective customers, and strives to obtain licensing and collaboration agreements. Operating losses are expected to be incurred until upfront licensing, milestone and royalty payments are sufficient to generate revenues to fund its continuing operations. COTI is unable to predict with any certainty when it will become profitable, or the extent of any future losses or profits.

Securing Adequate Licensing Agreements

The Company's ability to commercialize its products successfully will depend first, on meeting the scientific due diligence requirements of prospective customers and second, on its ability to negotiate satisfactory licensing terms with pharmaceutical or biotechnology organizations for preclinical compounds. While continued positive test results during fiscal 2012 generate positive feedback from potential licensees, these test outcomes have not translated into a contractual agreement to date. Licensing discussions during Q3-F'12 continued to find interest for early stage deals of novel compounds or classes of compounds. This reflects the macro events occurring within the pharmaceutical industry such as; the large number of blockbuster drugs that continue to come off patent protection and the need to find drugs to replace these lost revenues and the continued productivity challenges of pharmaceutical industry R&D spending in generating new compounds (*see Forbes – The Truly Staggering Cost of Inventing New Drugs, February 10, 2012*).

Access to Capital

The Company is seeking additional funds to continue to develop its R&D programs and to move its compounds more rapidly through development in calendar 2012 and 2013. These efforts were highlighted earlier in Liquidity and Capital Resources where the Company outlined the closing of the first tranche of a non-brokered private placement in late March 2012. If additional funding cannot be obtained, COTI may be required to delay, reduce, or eliminate one or more of its R&D programs or obtain funds through corporate partners or others who may require it to relinquish significant rights to its product candidates or obtain funds on less favourable terms than COTI would otherwise accept. COTI's success in obtaining future capital requirements will depend on many factors, such as establishing and maintaining investment industry relationships, collaborative partnering relationships, achieving a licensing agreement for COTI-2, and the general economic conditions and access to capital in the equity markets for

biotechnology companies. Despite the Company's financing efforts, there can be no assurance additional funding can be obtained.

## Use of Non-GAAP Financial Measures

Management has included a non-GAAP financial measure, Capital Resources, to supplement information contained in the MD&A. This non-GAAP measure does not have any standardized meaning prescribed under IFRS and therefore it may not be comparable to similar measures when presented by other issuers. Capital Resources is defined and calculated by the Company as cash, cash equivalents and short-term investments. This differs from IFRS disclosure where cash and cash equivalents are included in the Statement of Financial Position as cash and the Statement of Cash Flows is reconciled to this cash balance. Short-term investments are disclosed separately in the Statement of Financial Position and changes in short-term investments are disclosed separately in the Statement of Cash Flows in determining cash. The short-term investment is a guaranteed investment certificate encashable at any time up to its maturity date and with such high liquidity characteristics is a readily available source of capital. The use of Capital Resources and the inclusion of short-term investments in this measure sets out the Company's view on readily available cash, which Management believes provides more meaningful information with respect to the liquidity of the Company.

*Table 11: Reconciliation to Capital Resources*

| | January 31/12 | January 31/11 |
|---|---|---|
| Cash and cash equivalents | $ 494,688 | $ 609,552 |
| Short-term investments | 103,050 | - |
| Capital resources | $ 597,738 | $ 609,552 |

## Changes in Accounting Policies including Initial Adoption

First-time adoption of IFRS

The Company's unaudited interim consolidated financial statements have been prepared in accordance with IAS 34 and with IFRS 1. These unaudited interim financial statements do not include all of the information required for full annual financial statements. The impact of adopting IFRS is fully described in the notes to the financial statements. The impact upon adoption was not significant to the Company's financial statements and should not have any material affect going forward if comparing IFRS financial statements with the Company's financial statements under CGAAP prior to the adoption of IFRS.

Future Accounting Policy Changes

Certain pronouncements have been issued by the International Accounting Standards Board ("IASB") or International Financial Reporting Interpretation Committee that are mandatory for annual periods beginning after January 1, 2011 or later periods. Many of these updates are not applicable or are inconsequential to the Company and have been excluded from the discussion below. The remaining pronouncements are being assessed to determine their impact on the Company's results and financial position as follows:

(a) IFRS 7 Financial Instruments – Disclosures – Enhanced Derecognition Disclosure Requirements:

This amendment requires additional disclosure 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 Company's continuing involvement in those derecognized assets. The amendment becomes effective for annual periods beginning on or after July 1, 2011. This amendment affects disclosure only and has no impact on the Company's financial position or performance at this time as the Company has no assets under consideration for derecognition.

(b) IFRS 9 Financial Instruments – Classification and Measurement:

IFRS 9 reflects the first phase of the IASBs work on the replacement of International Accounting Standard 39, Financial Instruments: Recognition and Measurement, and deals with the classification and measurement of financial assets and financial liabilities. The Standard eliminates the existing IAS 39 categories of held to maturity, available-for-sale, and loans and receivables. This standard establishes two primary measurement categories for financial assets and liabilities, amortized cost and fair value.

Gains and losses on re-measurement of financial assets measured at fair value are recognized in profit or loss, except that for an investment in an equity instrument, which is not held-for-trading, IFRS 9 provides, on initial recognition, an irrevocable election to present all fair value changes from the investment in other comprehensive income (OCI). The election is available on an individual share-by-share basis. Amounts presented in OCI will not be reclassified to profit or loss at a later date.

For financial liabilities measured at fair value under the fair value option, changes in fair value attributable to changes in credit risk will be recognized in profit or loss. However, if this requirement creates or enlarges an accounting mismatch in profit or loss, the entire change in fair value will be recognized in profit or loss. Amounts presented in OCI will not be reclassified to profit or loss at a later date.

The standard is effective for annual periods beginning on or after January 1, 2013 and the Company intends to adopt IFRS 9 in its financial statements for the annual period beginning May 1, 2013. The Company does not expect IFRS 9 to have a material impact on its financial statements.

(c) IFRS 13 Fair Value Measurement:

In May 2011, the IASB published IFRS 13 Fair Value Measurement, which is effective prospectively for annual periods beginning on or after January 1, 2013. The disclosure requirements of IFRS 13 need not be applied in comparative information for periods before initial application. IFRS 13 replaces the fair value measurement guidance contained in individual

IFRSs with a single source of fair value measurement guidance. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date i.e. an exit price. The standard also establishes a framework for measuring fair value. It also sets out disclosure requirements for fair value measurements to provide information that enables financial statement users to assess the methods and inputs used to develop fair value measurements; and for recurring fair value measurements that use significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income. IFRS 13 explains 'how' to measure fair value when it is required or permitted by other IFRS. IFRS 13 does not introduce new requirements to measure assets or liabilities at fair value, nor does it eliminate the practical exceptions to fair value measurements that currently exist in certain standards. The Company intends to adopt IFRS 13 prospectively in its financial statements for the annual period beginning on May 1, 2013. The Company does not expect IFRS 13 to have a material impact on its financial statements.

(d) IAS 1 Presentation of Financial Statements

In June 2011, the IASB published amendments to IAS 1 Presentation of Financial Statements: Presentation of Items of Other Comprehensive Income, which are effective for annual periods beginning on or after July 1, 2012. These changes will apply retrospectively with early adoption permitted.

The amendments require that an entity present separately the items of OCI that are reclassified to profit or loss in the future from those that would never be reclassified to profit or loss. Consequently, an entity that presents items of OCI before related tax effects will also have to allocate the aggregated tax amount between these categories. The existing option to present the profit or loss and other comprehensive income in two statements has remained unchanged. The Company intends to adopt the amendments in its financial statements for the annual period beginning on May 1, 2013. The Company does not expect adoption to have a material impact on its financial statements.