

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013

(UNAUDITED)

DIAMEDICA INC.

Condensed Consolidated Interim Statements of Financial Position

Amounts in Canadian Dollars

(Unaudited)

	Note	As at September 30, 2013 $	As at December 31, 2012 $
ASSETS			
Current			
Cash and cash equivalents		**1,098,643**	2,327,650
Amounts receivable	4	**25,235**	20,405
Prepaid expenses		**104,018**	103,726
Total current assets		**1,227,896**	2,451,781
Property and equipment	5	**19,683**	6,560
Intangible assets	6	**283,910**	1,368,969
Total non-current assets		**303,593**	1,375,529
Total assets		**1,531,489**	3,827,310
LIABILITIES			
Current			
Accounts payable and accrued liabilities	7	**993,202**	1,574,253
Total liabilities		**993,202**	1,574,253
EQUITY			
Share capital	8	**33,693,763**	30,119,600
Warrants	8	**886,524**	277,000
Contributed surplus	8	**3,998,202**	3,488,991
Deficit		**(38,040,202)**	(31,632,534)
Total equity		**538,287**	2,253,057
Total liabilities and equity		**1,531,489**	3,827,310

Going concern (note 2(b))

Approved by the Board and authorized for issue on November 28, 2013:

(signed) Dawson Reimer, Director (signed) Thomas Wellner, Director

See accompanying notes to the condensed consolidated interim financial statements

DIAMEDICA INC.

Condensed Consolidated Interim Statements of Loss and Comprehensive Loss

Amounts in Canadian Dollars

(Unaudited)

	Note	**Three Months Ended September 30, 2013** **$**	Three Months Ended September 30, 2012 $	**Nine Months Ended September 30, 2013** **$**	Nine Months Ended September 30, 2012 $
EXPENSES					
Research and development	10,11	**1,204,034**	2,252,916	**5,655,611**	5,964,284
General and administrative	10,11	**148,860**	298,329	**762,483**	1,006,332
		1,352,894	2,551,245	**6,418,094**	6,970,616
Finance income	12	**(4,738)**	(14,005)	**(17,430)**	(35,558)
Finance costs	12	**9,642**	442	**7,004**	24,113
		4,904	(13,563)	**(10,426)**	(11,445)
Net loss and comprehensive loss for the period		**1,357,798**	2,537,682	**6,407,668**	6,959,171
Basic and diluted loss per common share		**(0.02)**	(0.05)	**(0.12)**	(0.14)

See accompanying notes to the condensed consolidated interim financial statements

DIAMEDICA INC.

Condensed Consolidated Interim Statements of Changes in Equity

Amounts in Canadian Dollars
(Unaudited)

	Share capital		Warrants		Contributed		
	Number	Amount	Number	Amount	surplus	Deficit	Total
	#	$	#	$	$	$	$
	(note 8)		(note 8)	(note 8)			
Balance, December 31, 2012	50,534,443	30,119,600	1,055,600	277,000	3,488,991	(31,632,534)	2,253,057
Net loss and comprehensive loss for the period	-	-	-	-	-	(6,407,668)	(6,407,668)
Transactions with owners of the Company, recognized directly in equity							
Units issued, net of issue costs	5,111,175	3,466,456	2,555,587	482,671	-	-	3,949,127
Compensation warrants issued	-	-	357,782	71,556	-	-	71,556
Shares issued on exercise of stock options	71,042	79,562	-	-	(33,312)	-	46,250
Warrant repricing	-	-	-	60,000	(60,000)	-	-
Shares issued on exercise of warrants	24,025	28,145	(24,025)	(4,703)	-	-	23,442
Share-based compensation	-	-	-	-	602,523	-	602,523
Total transactions with owners of the Company	5,206,242	3,574,163	2,889,344	609,524	509,211	-	4,692,898
Balance, September 30, 2013	55,740,685	33,693,763	3,944,944	886,524	3,998,202	(38,040,202)	538,287

	Share capital		Warrants		Contributed		
	Number	Amount	Number	Amount	surplus	Deficit	Total
	#	$	#	$	$	$	$
Balance, December 31, 2011	46,960,943	24,391,827	3,415,500	726,309	2,602,214	(21,632,894)	6,087,456
Net loss and comprehensive loss for the period	-	-	-	-	-	(6,959,171)	(6,959,171)
Transactions with owners of the Company, recognized directly in equity							
Shares issued on exercise of warrants, net of issue costs	3,300,500	5,281,929	(2,244,900)	(424,824)	-	-	4,857,105
Shares issued on exercise of stock options	273,000	445,844	-	-	(164,444)	-	281,400
Warrants expired	-	-	(115,000)	(24,485)	24,485	-	-
Share-based compensation	-	-	-	-	799,055	-	799,055
Total transactions with owners of the Company	3,573,500	5,727,773	(2,359,900)	(449,309)	659,096	-	5,937,560
Balance, September 30, 2012	50,534,443	30,119,600	1,055,600	277,000	3,261,310	(28,592,065)	5,065,845

See accompanying notes to the condensed consolidated interim financial statements

DIAMEDICA INC.

Condensed Consolidated Interim Statements of Cash Flows

Amounts in Canadian Dollars
(Unaudited)

	Note	**Nine months ended September 30, 2013** $	Nine months ended September 30, 2012 $
OPERATING ACTIVITIES			
Net loss and comprehensive loss for the period		**(6,407,668)**	(6,959,171)
Adjustments for items not affecting cash			
Share-based compensation		**602,523**	799,055
Depreciation of property and equipment	5	**3,720**	2,222
Amortization of intangible assets	6	**1,174,416**	1,761,624
		(4,627,009)	(4,396,270)
Changes in non-cash working capital items			
Amounts receivable		**(4,830)**	31,530
Prepaid expenses		**(292)**	(46,582)
Accounts payable and accrued liabilities		**(581,051)**	435,084
Cash used in operating activities		**(5,213,182)**	(3,976,238)
FINANCING ACTIVITIES			
Units issued, net of cash issue costs	8	**4,020,683**	-
Issue of common shares on exercise of warrants	8	**23,442**	4,857,105
Issue of common shares on exercise of stock options	8	**46,250**	281,400
Cash provided by financing activities		**4,090,375**	5,138,505
INVESTING ACTIVITIES			
Acquisition of property and equipment	5	**(16,843)**	(1,315)
Acquisition of patents pending	6	**(89,357)**	(44,506)
Cash used in investing activities		**(106,200)**	(45,821)
Net increase (decrease) in cash and cash equivalents during the period		**(1,229,007)**	1,116,446
Cash and cash equivalents, beginning of the period		**2,327,650**	2,707,663
Cash and cash equivalents, end of period		**1,098,643**	3,824,109
Cash and cash equivalents are comprised of			
Cash in bank		**1,098,643**	3,824,109
Supplemental cash flow information			
Incentive warrants issued May 8, 2012 (Note 8)		**-**	277,000
Common share purchase warrants issued as agents consideration (Note 8)		**71,556**	-

See accompanying notes to the condensed consolidated interim financial statements

1. Corporate information

DiaMedica Inc. (the "Company" or "DiaMedica") is a development stage biopharmaceutical company engaged in the discovery and development of drugs for the treatment of diabetes and related diseases.

The Company is a listed company incorporated under the Corporations Act (Manitoba) and domiciled in Manitoba, Canada whose shares are publicly traded on the TSX Venture Exchange. The Company's registered office is at 1700 – 360 Main Street, Winnipeg, Manitoba R3C 3Z3.

2. Basis of presentation

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

These consolidated financial statements have been prepared in compliance with International Accounting Standard 34 ("IAS 34") Interim Financial Reporting. The notes presented in these consolidated financial statements include only significant events and transactions occurring since our last fiscal year end and are not fully inclusive of all matters required to be disclosed in our annual audited consolidated financial statements.

The policies applied in these consolidated financial statements are based on IFRS issued and in effect as of November 28, 2013, the date the Board of Directors approved the statements. Any subsequent changes to IFRS or their interpretation, that are given effect in the company's annual consolidated financial statements for the year ending December 31, 2013 could result in restatement of these interim consolidated financial statements.

(b) Basis of measurement and going concern

These consolidated financial statements have been prepared on the historical cost basis, except for held-for-trading financial assets which are measured at fair value.

These consolidated financial statements have been prepared using IFRS that are applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they come due. There is substantial doubt about the appropriateness of the use of the going concern assumption because the Company has experienced operating losses and cash outflows from operations since incorporation, the Company will require ongoing funding in order to continue its research and development activities, and it has not reached successful commercialization of its products.

The Company's future operations are dependent upon its ability to generate product revenues, negotiate license agreements with partners, and secure additional funds. There can be no assurance that the Company will be successful in commercializing its products, entering into strategic agreements with partners, or raising additional capital on favourable terms or at all. There is also no certainty that these and other strategies will be sufficient to permit the Company to continue as a going concern. The Company believes it has sufficient resources available to support the Company's activities into the fourth quarter of 2013. The Company has advanced in seeking new funding from equity financings and/or licensing arrangements with development partners, however, there is no assurance that these funding initiatives will be successful.

These consolidated financial statements do not reflect adjustments in the carrying values of the Company's assets and liabilities, expenses, and the balance sheet classification used, that would be necessary if the going concern assumption was not appropriate. Such adjustments could be material.

(c) Functional and presentation currency

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

(d) Use of significant estimates and assumptions

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, revenue and expenses and the related disclosures of contingent assets and liabilities. Actual results could differ materially from these estimates and assumptions. We review our estimates and underlying assumptions on an ongoing basis. Revisions are recognized in the period in which the estimates are revised and may impact future periods.

We have applied significant judgments, estimates and assumptions to the measurement and timing of period of use of intangible assets, and to valuing our share-based compensation and warrants as follows:

Valuation of share-based compensation and warrants

Management measures the costs for share-based compensation and warrants using market-based option valuation techniques. Assumptions are made and estimates are used in applying the valuation techniques. These include estimating the future volatility of the share price, expected dividend yield, expected risk-free interest rate, future employee turnover rates, future exercise behaviours and corporate performance. Such estimates and assumptions are inherently uncertain. Changes in these assumptions affect the fair value estimates of share-based payments and warrants.

Measurement, period of use and potential impairment of intangible assets

Management reviews objective evidence each reporting period to assess whether there are indications of impairment of the intangible assets and make judgments about their period of use. These determinations and their individual assumptions require that management make a decision based on the best and most reliable information available at each reporting period.

3. Significant accounting policies

The Company's principal accounting policies were outlined in the Company's annual audited consolidated financial statements for the year ended December 31, 2012 and have been applied consistently to all periods presented in these consolidated financial statements, except as noted below. These statements should be read in conjunction with the annual audited consolidated financial statements for the year ended December 31, 2012.

New standards and interpretations adopted

IFRS 10 *Consolidated Financial Statements*

This amendment provides a single model to be applied in the control analysis for all investees. The amendments issued in June 2012 simplify the process of adopting IFRS 10 and provide additional relief from certain disclosures. The Company adopted IFRS 10, including the amendments issued in June 2012, in its financial statements for the annual period beginning on January 1, 2013. The adoption did not have a material impact on the financial statements.

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 and 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 IFRSs. The Company adopted IFRS 13 prospectively in its financial statements for the annual period beginning on January 1, 2013. The adoption did not have a material impact on the financial statements.

Annual Improvements to IFRSs 2009-2011 Cycle – various standards

In May 2012, the IASB published Annual Improvements to IFRSs – 2009-2011 Cycle as part of its annual improvements process to make non-urgent but necessary amendments to IFRS. These amendments are effective for annual periods beginning on or after January 1, 2013 with retrospective application. The Company adopted the amendments to the standards in its financial statements for the annual period beginning on January 1, 2013. The adoption did not have a material impact on the financial statements.

New standards and interpretations not yet effective

IFRS 9 *Financial Instruments: Classification and Measurement*

IFRS 9 (2010) reflects the first phase of the IASBs work on the replacement of IAS 39, Financial instruments: Recognition and Measurement and deals with the classification and measurement of financial assets and financial liabilities. This standard establishes two primary measurement categories for financial assets, amortized cost and fair value, and eliminates the existing categories of held to maturity, available for sale, and loans and receivables. The new classification will depend on the entity's business model and the contractual cash flow characteristics of the financial asset. The standard is effective for annual periods beginning on or after January 1, 2015. The Company intends to adopt IFRS 9 (2010) in its financial statements for the annual period beginning on January 1, 2015. The Company does not currently expect IFRS 9 (2010) to have a material impact on the financial statements. The classification and measurement of the Company's financial assets is not expected to change under IFRS 9 (2010) because of the nature of the Company's operations and the types of financial assets that it currently holds.

4. Amounts receivable

	September 30, 2013	December 31, 2012
	$	$
Other receivables	**2,445**	2,752
Taxes and tax credits receivable	**22,790**	17,653
	25,235	20,405

5. Property and equipment

	Computer and office equipment $
Cost	
Balance, December 31, 2011	18,521
Additions	3,762
Balance, December 31, 2012	22,283
Additions	16,843
Balance, September 30, 2013	**39,126**
Accumulated depreciation	
Balance, December 31, 2011	10,884
Depreciation	4,839
Balance, December 31, 2012	15,723
Depreciation	3,720
Balance, September 30, 2013	**19,443**
Net carrying amounts	
December 31, 2012	6,560
September 30, 2013	**19,683**

6. Intangible assets

	Acquired technology $	Patents $	Total $
Cost			
Balance, December 31, 2011	7,046,496	155,183	7,201,679
Additions	-	59,282	59,282
Balance, December 31, 2012	7,046,496	214,465	7,260,961
Additions	-	89,357	89,357
Balance, September 30, 2013	7,046,496	303,822	**7,350,318**
Accumulated amortization			
Balance, December 31, 2011	3,523,248	19,912	3,543,160
Amortization	2,348,832	-	2,348,832
Balance, December 31, 2012	5,872,080	19,912	5,891,992
Amortization	1,174,416	-	1,174,416
Balance, September 30, 2013	7,046,496	19,912	**7,066,408**
Net carrying amounts			
December 31, 2012	1,174,416	194,553	1,368,969
September 30, 2013	-	283,910	**283,910**

7. Accounts payable and accrued liabilities

	September 30, 2013 $	December 31, 2012 $
Trade and other payables	**328,267**	1,185,558
Accrued liabilities	**489,725**	329,658
Due to related parties	**175,210**	59,037
	993,202	1,574,253

8. Share capital

(a) Authorized

The Company has authorized share capital of an unlimited number of common voting shares.

Common shareholders are entitled to receive dividends as declared by the Company at its discretion and are entitled to one vote per share at the Company's annual general meeting.

In connection with the acquisition of Sanomune on June 30, 2010, 1,640,916 common shares were placed in escrow for a period of three years to be released in six semi-annual instalments. As at September 30, 2013, all common shares have been released from escrow.

(b) Common shares issued – for the nine months ended September 30, 2013

On March 22, 2013, the Company completed a prospectus offering of 5,111,175 units at a price of $0.90 per unit, for aggregate gross proceeds to the Company of $4,600,058 ($3,949,127 net of issuance costs). Each unit consisted of one common share and one half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one common share at a price of $1.10 at any time prior to expiry on March 22, 2016. The warrant expiry date can be accelerated at the option of the Company, in the event that the volume-weighted average trading price of the Company's common shares exceeds $1.60 per common share for any 10 consecutive trading days. In connection with the financing, the Company issued 357,782 compensation warrants. Each compensation warrant entitles the holder to acquire one common share at an exercise price of $0.90 prior to expiry on March 22, 2014.

The $0.90 unit issue price was allocated to common shares in the amount of $0.79 per common share and the unit warrants were allocated a price of $0.11 per half-warrant. The costs of the issue were allocated on a pro rata basis to the common shares and unit warrants. Accordingly, $3,466,456 was allocated to common shares and $482,671 to the unit warrants, net of issue costs. Assumptions used to determine the value of the unit warrants were: dividend yield 0%; risk-free interest rate 1.1%; expected volatility 69%; and average expected life of 36 months. Assumptions used to determine the value of the compensation warrants were: dividend yield 0%; risk-free interest rate 1.0%; expected volatility 63%, respectively; and average expected life of 12 months.

During the nine months ended September 30, 2013, 71,042 common shares were issued on the exercise of stock options for gross proceeds of $46,250 and 24,025 common shares were issued on the exercise of warrants for gross proceeds of $23,442.

Effective on July 9, 2013, the Company amended the exercise price of the 1,055,600 outstanding warrants that were issued in May 2012 in connection with an earlier exercise incentive program from an exercise price of $2.50 to an exercise price of $1.60.

Common shares issued – for the nine months ended September 30, 2012

During the nine months ended September 30, 2012, 273,000 common shares were issued on the exercise of stock options

for gross proceeds of $281,400.

8. Share capital (continued)

On May 8, 2012, the Company completed an incentive program to encourage the early exercise of the $1.50 warrants that were previously issued in connection with DiaMedica's short form prospectus offering in July, 2011 (the "Original Warrants"). DiaMedica amended the terms of the Original Warrants to enable the holders thereof to receive a Unit in lieu of a common share of DiaMedica on the exercise of their Original Warrants prior to the May 8, 2012 expiry date. Each Unit consisted of one common share in the capital stock of DiaMedica and one-half of one warrant (each whole warrant, a "New Warrant"). Each New Warrant entitles the holder thereof to acquire a common share in DiaMedica at a price of $2.50 per share for 24 months following the date of issue of the Unit. On May 8, 2012, 2,111,200 common shares were issued on the exercise of $1.50 warrants for gross proceeds of $3,166,800 ($3,150,781 net of cash issue costs) under the incentive program, and accordingly, 1,055,600 New Warrants, with a total grant date fair value of $277,000, were issued with an exercise price of $2.50. Assumptions used in an option pricing model to determine the value of the New Warrants were: dividend yield 0%; risk-free interest rate 1.2%; expected volatility 74%; and expected life of 2 years.

In the event the volume-weighted average trading price of DiaMedica's common shares exceeds $3.00 per share for a period of 10 consecutive trading days, DiaMedica may, at its option, accelerate the New Warrant Expiry Date by delivery of notice to the holders of New Warrants and issuing a press release announcing such acceleration and, in such case, the New Warrant Expiry Date shall be deemed to be the 30th day following the later of: (i) the date on which the Warrant Acceleration Notice is sent to Warrant holders; and (ii) the date of issuance of the Warrant Acceleration Press Release.

On August 3, 2012, the ten-day volume-weighted average trading price of DiaMedica common shares exceeded $2.00 per common share and the Company provided notice to warrant holders that the expiry date of these warrants had been accelerated to September 7, 2012. In the third quarter, 1,189,300 warrants were exercised for gross proceeds of $1,706,324 and the remaining 115,000 warrants expired.

(c) Weighted average number of shares

The weighted average number of shares for the three and nine months ended September 30, 2013 was 55,723,868 and 54,157,827 (2012 - 49,830,510 and 48,373,898). The Company has not adjusted its weighted average number of shares outstanding for the purpose of calculating the diluted loss per share as any adjustment related to stock options, warrants or deferred share units would be anti-dilutive.

(d) Shareholder rights plan

The shareholders of the Company approved the adoption of a shareholder rights plan agreement (the "Plan") on September 22, 2011. The Plan is designed to provide adequate time for the Board of Directors and the shareholders to assess an unsolicited takeover bid for DiaMedica, to provide the Board of Directors with sufficient time to explore and develop alternatives for maximizing shareholder value if a takeover bid is made, and to provide shareholders with an equal opportunity to participate in a takeover bid and receive full and fair value for their Common Shares. The Plan will expire at the close of the Company's annual meeting of shareholders in 2014.

The rights issued under the Plan will initially attach to and trade with the Common Shares and no separate certificates will be issued unless an event triggering these rights occurs. The rights will become exercisable only when a person, including any party related to it, acquires or attempts to acquire 20 percent or more of the outstanding Common Shares without complying with the "Permitted Bid" provisions of the Plan or without approval of the Board of Directors. Should such an acquisition occur or be announced, each right would, upon exercise, entitle a rights holder, other than the acquiring person and related persons, to purchase Common Shares at a 50 percent discount to the market price at the time.

Under the Plan, a Permitted Bid is a bid made to all holders of the Common Shares and which is open for acceptance for not less than 60 days. If at the end of 60 days at least 50 percent of the outstanding Common Shares, other than those owned by the offeror and certain related parties have been tendered, the offeror may take up and pay for the Common Shares but must extend the bid for a further 10 days to allow other shareholders to tender. The issuance of Common Shares upon the exercise of the rights is subject to receipt of certain regulatory approvals.

8. Share capital (continued)

(e) Deferred Share Units Plan

The shareholders of the Company approved the adoption of a deferred share units plan (the "DSU Plan") on September 22, 2011 reserving for issuance up to 2,000,000 common shares under the DSU Plan. The purpose of the DSU Plan is to provide an alternative form of compensation to satisfy directors' fees and annual and special bonuses payable to senior officers and Directors of the Corporation. No units were issued in the nine months ended September 30, 2013 (2012 – 47,435 units with a value of $80,640). A total of 74,556 units have been issued since inception of the DSU Plan. The DSU Plan is equity-settled and the fair value of units granted, which vest upon issuance, is included in share-based compensation expense.

(f) Stock option plan

The Company has a stock option plan which is administered by the Board of Directors of the Company with stock options granted to directors, management, employees and consultants as a form of compensation. 7,000,000 common shares were reserved for issuance under the plan. Options granted vest at various rates and have terms of up to 10 years.

Changes in the number of options outstanding during the nine months ended September 30 were as follows:

	2013		2012	
	Number of Options	Weighted average exercise price	Number of Options	Weighted average exercise price
Balance, beginning of period	4,327,500	$ 1.01	3,860,000	$ 0.87
Granted	848,000	1.07	720,000	1.70
Exercised	(71,042)	0.65	(273,000)	1.03
Forfeited	(111,458)	1.40	(96,500)	0.65
Expired/ cancelled	(50,000)	1.00	(208,000)	1.43
Balance, end of period	4,943,000	1.02	4,002,500	0.98
Options exercisable, end of period	3,385,458	0.92	2,212,914	0.83

The contributed surplus balance represents accumulated share-based compensation expenses and the fair value of warrants that have expired.

8. Share capital (continued)

The following table reflects stock options outstanding at September 30, 2013:

	Stock options outstanding			Stock options exercisable	
Range of exercise prices	Number outstanding	Weighted average remaining contractual life	Weighted average exercise price	Exercisable number	Weighted average exercise price
$0.42 - $0.50	447,500	1.8 years	$0.42	444,167	$0.42
$0.51 - $1.00	1,552,500	1.9 years	$0.69	1,443,126	$0.69
$1.01 - $1.50	2,148,000	7.6 years	$1.14	1,113,164	$1.15
$1.51 - $1.70	795,000	8.1 years	$1.69	385,001	$1.70
	4,943,000	5.3 years	$1.02	3,385,458	$0.92

Share-based compensation expense was determined based on the fair value of the options at the date of measurement using the Black-Scholes option pricing model with the following weighted average assumptions:

	September 30, 2013	September 30, 2012
Expected option life	3.8 years	3.2 years
Risk free interest rate	1.6%	1.2%
Dividend yield	nil	nil
Expected volatility	77%	91%

The Black-Scholes model used by the Company to calculate option values was developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differs from the Company's stock option awards. This model also requires highly subjective assumptions, including future stock price volatility and average option life, which greatly affect the calculated values. The risk-free interest rate is based on the yield of a Canadian Government bond with a remaining term equal to the expected term of the option. The volatility is based solely on historical volatility equal to the expected life of the option. The life of the options is estimated considering the vesting period at the grant date, the life of the option and the average length of time similar grants have remained outstanding in the past. The forfeiture rate is an estimate based on future expectations. The dividend yield is assumed to be nil since it is the present policy of the Company to retain all earnings to finance operations and future growth.

During the nine months ended September 30, 2013, the Company issued 848,000 (2012 – 720,000) stock options with a fair value of $512,172 (2012 – $725,620). The weighted average grant-date fair value of the stock options granted during the nine months ended September 30, 2013 was $0.60 (2012 - $1.01).

9. Income taxes

The Company recognized no income taxes in the statements of loss and comprehensive loss, as it has been incurring losses since inception, and it is not probable that future taxable profits will be available against which the accumulated tax losses can be utilized.

10. Research and development

Components of research and development expenses for the three months ended September 30 were as follows:

	2013	2012
	$	$
Research and development programs, excluding the below	**753,096**	1,316,036
Salaries, fees and short-term benefits	**319,880**	215,790
Share-based compensation	**150,494**	133,114
Depreciation of property and equipment	**1,202**	768
Amortization of intangible assets	**-**	587,208
Government assistance	**(20,638)**	-
Total	**1,204,034**	2,252,916

Components of research and development expenses for the nine months ended September 30 were as follows:

	2013	2012
	$	$
Research and development programs, excluding the below	**3,195,325**	3,145,521
Salaries, fees and short-term benefits	**970,947**	507,880
Share-based compensation	**352,479**	563,493
Depreciation of property and equipment	**3,720**	2,222
Amortization of intangible assets	**1,174,416**	1,761,624
Government assistance	**(41,276)**	(16,456)
Total	**5,655,611**	5,964,284

Quarterly research and development expenses may vary due to the timing of costs for manufacturing, initiating and completing pre-clinical and clinical trials, granting of stock options, and recognizing government assistance.

11. General and Administrative

Components of general and administrative expenses for the three months ended September 30 were as follows:

	2013	**2012**
	$	**$**
General and administrative, excluding the below	**82,567**	193,834
Salaries, fees and short-term benefits	**16,300**	29,774
Share-based compensation	**49,993**	74,721
Total	**148,860**	298,329

Components of general and administrative expenses for the nine months ended September 30 were as follows:

	2013	**2012**
	$	**$**
General and administrative, excluding the below	**410,046**	648,006
Salaries, fees and short-term benefits	**102,393**	122,764
Share-based compensation	**250,044**	235,562
Total	**762,483**	1,006,332

12. Finance income and finance costs

Finance income for the three months ended September 30 was as follows:

	2013	2012
	$	$
Interest income	**4,738**	12,611
Net foreign currency gain	**-**	1,394
Finance income	**4,738**	14,005

Finance income for the nine months ended September 30 was as follows:

	2013	2012
	$	$
Interest income	**13,967**	35,558
Net foreign currency gain	**3,463**	-
Finance income	**17,430**	35,558

Finance costs for the three months ended September 30 were as follows:

	2013	2012
	$	$
Bank charges	**1,231**	442
Net foreign currency loss	**8,411**	-
Finance costs	**9,642**	442

Finance costs for the nine months ended September 30 were as follows:

	2013	2012
	$	$
Bank charges	**7,004**	976
Net foreign currency loss	**-**	23,137
Finance costs	**7,004**	24,113

13. Commitments and contingencies

As at September 30, 2013 and in the normal course of business, the Company had obligations to make future payments, representing research and development contracts and other commitments that are known and committed in the amount of $2,305,000 over the next 12 months, $97,000 from 12 to 24 months, $44,000 from 24-36 months and $20,000 each year thereafter. The Company's largest commitment is a contract in the amount of approximately $2.5 million for the Phase I/II clinical trial of which $930,000 has been expensed to date.

The Company enters into research, development and license agreements in the ordinary course of business where the Company receives research services and rights to proprietary technologies. Milestone and royalty payments that may become due under various agreements are dependent on, among other factors, clinical trials, regulatory approvals and ultimately the successful development of a new drug, the outcome and timing of which is uncertain.

The Company periodically enters into research and license agreements with third parties that include indemnification provisions customary in the industry. These guarantees generally require the Company to compensate the other party for certain damages and costs incurred as a result of claims arising from research and development activities undertaken by or on behalf of the Company. In some cases, the maximum potential amount of future payments that could be required under these indemnification provisions could be unlimited. These indemnification provisions generally survive termination of the underlying agreement. The nature of the indemnification obligations prevents the Company from making a reasonable estimate of the maximum potential amount it could be required to pay. Historically, the Company has not made any indemnification payments under such agreements and no amount has been accrued in the accompanying consolidated financial statements with respect to these indemnification obligations.

14. Related parties

The key management personnel of the Company are the Directors, the President and Chief Executive Officer and the Vice Presidents.

Compensation for key management personnel of the Company for the three months ended September 30 was as follows:

	2013	2012
	$	$
Salaries, fees and short-term benefits	**217,857**	140,784
Share-based compensation	**168,435**	179,198
Total personnel expenses	**386,292**	319,982

Compensation for key management personnel of the Company for the nine months ended September 30 was as follows:

	2013	2012
	$	$
Salaries, fees and short-term benefits	**705,854**	454,753
Share-based compensation	**419,699**	577,567
Total personnel expenses	**1,125,553**	1,032,320

Executive officers and directors participate in the stock option plan and certain officers participate in the Company's health plan. Directors receive annual and meeting fees for their services. As at September 30, 2013, the key management personnel control approximately 2% of the voting shares of the Company.

Amounts due to related parties, including amounts due to key management personnel, at the year-end are unsecured, interest free and settlement occurs in cash. There have been no guarantees provided or received for any related party receivables or payables.