

# **LORUS THERAPEUTICS INC.**

## **CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS and MANAGEMENT'S DISCUSSION AND ANALYSIS**

As at and for the three and nine month periods ended  
February 29, 2012

**Lorus Therapeutics Inc.**  
**Condensed Interim Consolidated Statements of Financial Position**  
(unaudited)

<i>(amounts in 000's of Canadian Dollars)</i>	<b>February 29, 2012</b>		May 31, 2011		June 1, 2010	
<b>ASSETS</b>						
<b>Current</b>						
Cash and cash equivalents (note 3 (d))	\$	<b>103</b>	\$	911	\$	667
Short-term investments (note 4)		-		-		247
Prepaid expenses and other assets		<b>337</b>		388		636
<b>Total Current Assets</b>		<b>440</b>		1,299		1,550
<b>Non-current</b>						
Equipment (note 5)		<b>66</b>		99		147
<b>Total Non-Current Assets</b>		<b>66</b>		99		147
<b>Total Assets</b>	\$	<b>506</b>	\$	1,398	\$	1,697
<b>LIABILITIES</b>						
<b>Current</b>						
Accounts payable	\$	<b>117</b>	\$	215	\$	387
Accrued liabilities		<b>1,160</b>		944		1,458
Promissory note payable (notes 7 and 13)		<b>300</b>		-		1,000
<b>Total Current Liabilities</b>		<b>1,577</b>		1,159		2,845
<b>SHAREHOLDERS' EQUITY</b>						
<b>Share capital (note 9)</b>						
Common shares		<b>170,001</b>		168,787		163,920
Stock options (note 10)		<b>496</b>		1,212		3,803
Contributed surplus		<b>19,933</b>		18,988		14,875
Warrants		<b>1,880</b>		1,032		1,039
Deficit		<b>(193,381)</b>		(189,780)		(184,785)
<b>Total Equity</b>		<b>(1,071)</b>		239		(1,148)
<b>Total Liabilities and Equity</b>	\$	<b>506</b>	\$	1,398	\$	1,697

*See accompanying notes to the consolidated interim financial statements (unaudited)*

*Basis of Presentation (note 2)*

*Subsequent Events (note 16)*

**Lorus Therapeutics Inc.**  
**Condensed Consolidated Interim Statements of Loss and Comprehensive Loss**  
(unaudited)

<i>(amounts in 000's of Canadian Dollars except for per common share data)</i>	<b>Three months ended Feb. 29, 2012</b>	<b>Three months ended Feb. 28, 2011</b>	<b>Nine months ended Feb. 29, 2012</b>	<b>Nine months ended Feb. 28, 2011</b>
<b>REVENUE</b>	\$ -	\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development (notes 6 and 12)	543	847	1,779	1,981
General and administrative (note 12)	479	701	1,825	1,875
<b>Operating expenses</b>	<b>1,022</b>	<b>1,548</b>	<b>3,604</b>	<b>3,856</b>
Finance expense (note 11)	3	-	3	71
Finance income	(2)	(6)	(6)	(10)
<b>Net financing expense (income)</b>	<b>1</b>	<b>(6)</b>	<b>(3)</b>	<b>61</b>
<b>Net loss and total comprehensive loss for the period</b>	<b>1,023</b>	<b>1,542</b>	<b>3,601</b>	<b>3,917</b>
<b>Basic and diluted loss per common share</b>	<b>\$ 0.05</b>	<b>\$ 0.10</b>	<b>\$ 0.18</b>	<b>\$ 0.32</b>
<b>Weighted average number of common shares (note 9(f)) outstanding used in the calculation of Basic and Diluted loss per common share</b>	<b>21,169</b>	<b>15,685</b>	<b>19,950</b>	<b>12,314</b>

*See accompanying notes to the consolidated interim financial statements (unaudited)*

**Lorus Therapeutics Inc.**  
**Condensed Interim Consolidated Statement of Changes in Equity**  
(unaudited)

<i>(amounts in 000's of Canadian Dollars)</i>	<b>Share Capital</b>	<b>Stock Options</b>	<b>Warrants</b>	<b>Contributed Surplus</b>	<b>Deficit</b>	<b>Total</b>
Balance, June 1, 2011	\$ 168,787	\$ 1,212	\$ 1,032	\$ 18,988	\$ (189,780)	\$ 239
Issuance of units (note 9(b))	1,214	-	609	-	-	1,823
Repricing of warrants (note 9(c))	-	-	239	(239)	-	-
Stock-based compensation (note 10)	-	468	-	-	-	468
Cancellation and forfeiture of stock options	-	(1,184)	-	1,184	-	-
Net loss	-	-	-	-	(3,601)	(3,601)
<b>Balance, February 29, 2012</b>	<b>\$ 170,001</b>	<b>\$ 496</b>	<b>\$ 1,880</b>	<b>\$ 19,933</b>	<b>\$ (193,381)</b>	<b>\$ (1,071)</b>
Balance June 1, 2010	163,920	3,803	1,039	14,875	(184,785)	(1,148)
Issuance of units (note 9(b))	4,867	-	1,032	-	-	5,899
Expiry of warrants (note 9 (c))	-	-	(417)	417	-	-
Stock based compensation (note 10)	-	283	-	-	-	283
Forfeiture of stock options	-	(3,071)	-	3,071	-	-
Net loss	-	-	-	-	(3,917)	(3,917)
<b>Balance, February 28, 2011</b>	<b>\$ 168,787</b>	<b>\$ 1,015</b>	<b>\$ 1,654</b>	<b>\$ 18,363</b>	<b>\$ (188,702)</b>	<b>\$ 1,117</b>

*See accompanying notes to the consolidated interim financial statements (unaudited)*

**Lorus Therapeutics Inc.**  
**Condensed Consolidated Interim Statements of Cash Flows**  
(unaudited)

<i>(amounts in 000's of Canadian Dollars)</i>	<b>Three months ended Feb. 29, 2012</b>	<b>Three months ended Feb. 28, 2011</b>	<b>Nine months ended Feb. 29, 2012</b>	<b>Nine months ended Feb. 28, 2011</b>
<b>Cash flows from operating activities:</b>				
Net loss for the period	\$ (1,023)	\$ (1,542)	\$ (3,601)	\$ (3,917)
Items not involving cash:				
Stock-based compensation	21	248	468	283
Depreciation of equipment	11	14	33	42
Finance expense	3	-	3	71
Change in non-cash operating working capital (note 11)	248	(396)	469	(1,372)
<b>Cash used in operating activities</b>	<b>(740)</b>	<b>(1,676)</b>	<b>(2,628)</b>	<b>(4,893)</b>
<b>Cash flows from financing activities:</b>				
Issuance of common shares and warrants, net of issuance costs (note 9)	-	1,641	1,823	5,899
Interest on promissory notes	(3)	-	(3)	(71)
<b>Cash (used in) provided by financing activities</b>	<b>(3)</b>	<b>1,641</b>	<b>1,820</b>	<b>5,828</b>
<b>Cash flows from investing activities:</b>				
Maturity of marketable securities and other investments	-	-	-	247
Additions to equipment	-	-	-	(4)
<b>Cash (used in) provided by investing activities</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>243</b>
<b>(Decrease) increase in cash and cash equivalents during the period</b>	<b>(743)</b>	<b>(35)</b>	<b>(808)</b>	<b>1,178</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>846</b>	<b>1,880</b>	<b>911</b>	<b>667</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 103</b>	<b>\$ 1,845</b>	<b>\$ 103</b>	<b>\$ 1,845</b>

*See accompanying notes to the interim consolidated financial statements (unaudited)*

## LORUS THERAPEUTICS INC.

### NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

#### 1. Reporting Entity

Lorus Therapeutics Inc. ("Lorus" or the "Company") is a biopharmaceutical company focused on the discovery, research and development of novel anticancer therapies with a high safety profile. Lorus has worked to establish a diverse anticancer product pipeline, with products in various stages of development ranging from discovery and pre-clinical to clinical stage development. The Company's shares are listed on the Toronto Stock Exchange. The head office, principal address and records of the Company are located at 2 Meridian Road, Toronto, Ontario, Canada, M9W 4Z7.

#### 2. Basis of presentation

##### (a) Statement of Compliance

These unaudited condensed consolidated interim financial statements of the Company and its subsidiary as at February 29, 2012 were prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board, and the Company has elected June 1, 2010 as the date of transition to IFRS (the "transition date"). As these financial statements represent the Company's presentation of its results and financial position under IFRS, they were prepared in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting* and IFRS 1, *First-time Adoption of IFRS* ("IFRS 1"). These unaudited condensed consolidated interim financial statements have been prepared in accordance with the accounting policies the Company expects to adopt in its consolidated financial statements as at and for the year ending May 31, 2012. The accounting policies applied in these unaudited condensed consolidated interim financial statements are based on the IFRS standards and International Financial Reporting Interpretations Committee ("IFRIC") interpretations issued and outstanding as of April 12, 2012, the date the Board of Directors approved the unaudited condensed consolidated interim financial statements. Any subsequent changes to IFRS that are given effect in the Company's annual consolidated financial statements for the year ending May 31, 2012 could result in restatement of these unaudited condensed consolidated interim financial statements, including the transition adjustments recognized on change-over to IFRS. The policies set out below were consistently applied to all periods presented unless otherwise noted below.

The Company's consolidated financial statements were previously prepared in accordance with Canadian Generally Accepted Accounting Principles ("Canadian GAAP"). Canadian GAAP differs in some areas from IFRS. Certain information and footnote disclosures which are considered material to the understanding of the Company's unaudited condensed consolidated interim financial statements and which are normally included in annual financial statements prepared in accordance with IFRS are provided in the notes, along with reconciliations and descriptions of the effect of the transition from Canadian GAAP to IFRS on equity, profit or loss and the statements of financial position and cash flows.

As these are the Company's third set of condensed consolidated interim financial statements in accordance with IFRS, the Company's disclosures exceed the minimum requirements under IAS 34, *Interim Financial Reporting*. The Company has elected to exceed the minimum requirements in order to present the Company's accounting policies in accordance with IFRS and the additional disclosures required under IFRS, which also highlight the changes from the Company's 2011 annual consolidated financial statements prepared in accordance with Canadian GAAP. In future condensed interim financial statements, the Company may not provide the same amount of disclosure in the Company's consolidated condensed interim financial statements under IFRS as the reader will be able to rely on the annual consolidated financial statements, which will be prepared in accordance with IFRS.

The unaudited condensed consolidated interim financial statements of the Company were reviewed by the Audit Committee and approved and authorized for issue by the Board of Directors on April 12, 2012.

##### (b) Basis of measurement – Going concern

These unaudited condensed consolidated interim financial statements have been prepared in accordance with IFRS accounting principles applicable to a going concern using the historical cost basis except for held-for-trading financial assets which are measured at fair value.

**There is substantial doubt about the Company's ability to continue as a going concern because management has forecasted that the Company's current level of cash and cash equivalents will not be sufficient to execute its current planned expenditures for the next 12 months without further financing being obtained.** The Company is currently in discussion with several potential investors to provide additional funding. Management believes that it will complete one or more of these arrangements in sufficient time to continue to execute its planned expenditures without interruption. However, there can be no assurance that the capital will be available as necessary to meet these continuing expenditures, or if the capital is available, that it will be on terms acceptable to the Company. The issuance of common shares by the Company could result in significant dilution in the equity interest of existing shareholders. The Company is also considering alternatives to delay its research programs or further reduce expenditures until financing is available. **There can be no assurance that the Company will be able to obtain sufficient financing to meet future operational needs. As a result, there is a substantial doubt as to whether the Company will be able to continue as a going concern and realize its assets and pay its liabilities as they fall due.**

These unaudited condensed consolidated interim financial statements do not reflect the adjustments that would be necessary should the Company be unable to continue as a going concern and therefore be required to realize its assets and settle its

## LORUS THERAPEUTICS INC.

### NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)

Three and nine months ended February 29, 2012 and February 28, 2011

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liabilities and commitments in other than the normal course of business and at amounts different from those in the accompanying unaudited condensed consolidated interim financial statements. Such amounts could be material.

#### **(c) Functional and presentation currency**

The functional and presentation currency of the Company and its Canadian subsidiary NuChem Pharmaceuticals Inc. is the Canadian dollar ("C\$").

#### **(d) Significant accounting judgments, estimates and assumptions**

The preparation of these unaudited condensed consolidated interim financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities at the date of the unaudited condensed consolidated interim financial statements and reported amounts of revenues and expenses during the reporting period. Actual outcomes could differ from these estimates. The unaudited condensed consolidated interim financial statements include estimates, which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the condensed consolidated interim financial statements, and may require accounting adjustments based on future occurrences.

The estimates and underlying assumptions are reviewed on a regular basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

The key assumptions concerning the future, and other key sources of estimation uncertainty as of the date of the statement of financial position that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next fiscal year arise in connection with the use of the going concern assumption, determination of impairment of goodwill and equipment, the valuation of contingent liabilities, the valuation of tax accounts and the determination of development costs which qualify for capitalization. Significant estimates also take place in connection with the valuation of share-based compensation and share purchase warrants.

### **3. Significant accounting policies**

#### **(a) Basis of consolidation:**

##### *(i) Business combinations:*

As part of its transition to IFRS, the Company elected not to restate any business combinations that occurred prior to June 1, 2010.

##### *(ii) Subsidiary:*

The consolidated financial statements include the accounts of the Company and its 80% owned subsidiary, NuChem Pharmaceuticals Inc. ("NuChem"). A subsidiary is an entity over which the Company has control, being the power to govern the financial and operating policies of the investee entity so as to obtain benefits from its activities. Accounting policies of subsidiaries are consistent with our accounting policies. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

#### **(b) Foreign currency translation:**

Foreign currency transactions are translated into Canadian dollars at rates prevailing on the transaction dates. Monetary assets and liabilities are translated into Canadian dollars at the rates in effect on the balance sheets dates. Gains or losses resulting from these transactions are accounted for in the loss for the period in 'general and administrative expenses'.

#### **(c) Derecognition of financial assets and liabilities:**

A financial asset is derecognised when the right to receive cash flows from the asset have expired or when the Company has transferred its rights to receive cash flows from the asset.

A financial liability is derecognized when its contractual obligations are discharged, cancelled or expire.

#### **(d) Financial instruments:**

Financial assets are comprised of cash and cash equivalents and short-term investments. Financial assets are initially recorded at fair market value.

##### *Cash and cash equivalents:*

The Company considers unrestricted cash on hand and term deposits and guaranteed investment certificates held by Canadian Schedule A banks, with original maturities of three months or less as cash and cash equivalents.

Cash and cash equivalents are classified as held-for-trading investments and measured at fair value through loss or profit. By virtue of the nature of these assets, fair value is generally equal to cost plus accrued interest. Where applicable, any

**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

significant change in market value would result in a gain or loss being recognized in the consolidated statements of loss and comprehensive loss.

*Short-term investments:*

Short-term investments are liquid Canadian government or corporate instruments having original maturity dates greater than three months and less than one year and are classified as held-to-maturity investments, except where the Company does not intend to, or cannot reasonably expect to hold the investment to maturity in which case the investment is designated as held-for-trading. Held-to-maturity investments are measured at amortized cost using the effective interest rate method, while held-for-trading investments are measured at fair value and the resulting gain or loss is recognized in the consolidated statements of loss and comprehensive loss. As at February 29, 2012, the Company did not hold any held-to-maturity investments

Financial liabilities consist of the following:

*Accounts payable, accrued liabilities and promissory notes payable:*

Accounts payable and accrued liabilities and promissory notes payable are typically short-term in nature and classified as other financial liabilities. These liabilities are carried at amortized cost using the effective interest rate method.

*Equity:*

Common shares and warrants to purchase common shares are classified as equity. The warrants are classified as equity as they are settleable for a fixed amount of cash for a fixed number of shares.

Incremental costs directly attributable to the issue of common shares or warrants are recognized as a reduction from equity, net of any tax effects.

*Transaction costs:*

Transaction costs are expensed as incurred for financial instruments designated or classified as held for trading. Transaction costs for other financial instruments are recognized as part of the financial instruments, carrying value.

**(e) Equipment:**

Equipment is measured at cost less accumulated depreciation and accumulated impairment loss. Cost includes expenditures that are directly attributable to the acquisition of the asset. The Company records depreciation at rates that charge operations with the cost of the assets over their estimated useful lives on a straight-line basis as follows:

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Furniture and equipment	Over 3 to 5 years
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The assets' residual value, useful life and methods of depreciation are reviewed each reporting period and adjusted prospectively if appropriate.

**(f) Research and development:**

Expenditures on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, are recognized in profit or loss as incurred.

Development activities involve a plan or design for the production of new or substantially improved products or processes. Development expenditures are capitalized only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Company intends to and has sufficient resources to complete development and to use or sell the asset. The expenditures capitalized would include the cost of materials, direct labour, overhead costs that are directly attributable to preparing the asset for its intended use, and borrowing costs on qualifying assets. Other development expenditures which do not meet the criteria for capitalization are recognized in profit or loss as incurred.

Capitalized development costs are recognized at cost less accumulated amortization and accumulated impairment losses.

The Company has not capitalized any development costs to date.



## **LORUS THERAPEUTICS INC.**

### **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

*Three and nine months ended February 29, 2012 and February 28, 2011*

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#### **(g) Investment tax credits:**

Research and development investment tax credits, which are earned as a result of incurring qualifying research and development expenditures, are recorded as a reduction of the related expense or cost of the asset acquired when there is reasonable assurance that they will be realized.

The Company's claim for Scientific Research and Experimental Development ("SR&ED") deductions and related investment tax credits for income tax purposes are based on management's interpretation of the applicable legislation in the Income Tax Act (Canada). These amounts are subject to review and acceptance by the Canada Revenue Agency or the Ontario Ministry of Finance prior to collection.

#### **(h) Stock-based compensation:**

The Company has a stock-based compensation plan (the "Plan") available to officers, directors, employees and consultants with grants under the Plan approved by the Company's Board of Directors. Under the Plan, the exercise price of each option equals the closing trading price of the Company's stock on the day prior to the grant. Vesting is provided for at the discretion of the Board of Directors and the expiration of options is to be no greater than 10 years from the date of grant.

The Company uses the fair value based method of accounting for employee awards granted under the Plan. The Company calculates the fair value of each stock option grant using the Black-Scholes Option Pricing model at the grant date. The stock-based compensation cost of the options is recognized as stock-based compensation expense over the relevant vesting period of the stock options using an estimate of the number of options that will eventually vest. At the end of each reporting period, the Company revises its estimate of the number of equity instruments expect to vest. The impact of the revision of the original estimates, if any, is recognized in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the stock option equity account.

Stock options awarded to non-employees are accounted for at the fair value of the goods received or the services rendered. The fair value is measured at the date we obtain the goods or the date the counterparty renders the service. If the fair value of the goods or services cannot be reliably valued the fair value of the options granted will be used.

The Company has a deferred share unit plan that provides directors the option of receiving payment for their services in the form of share units rather than common shares or cash. Share units entitle the director to elect to receive, on termination of his or her services with the Company, an equivalent number of common shares, or the cash equivalent of the market value of the common shares at that future date. For units issued under this plan, the Company records an expense and a liability equal to the market value of the shares issued. The accumulated liability is adjusted for market fluctuations on a quarterly basis. As at February 29, 2012 there were no units issued under this plan (see note 16).

The Company has an alternate compensation plan ("ACP") that provides directors and senior management ("participants") with the option of receiving director's fees, salary, bonuses or other remuneration ("Remuneration") in common shares rather than cash. Under the plan, the participant receives an allotment from treasury of such number of shares as will be equivalent to the cash value of the Remuneration determined by dividing the Remuneration by the weighted average closing common share price for the five trading days prior to payment date (the "5-day VWAP"). The issue price of the shares is the 5-day VWAP. There are currently no shares allotted for issuance under this plan.

#### **(i) Loss per share:**

Basic loss per share is computed by dividing the net loss available to common shareholders by the weighted average number of shares outstanding during the reporting period. Diluted loss per share is computed similar to basic loss per share except that the weighted average shares outstanding is increased to include additional shares for the assumed exercise of stock options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire common stock at the average market price during the reporting periods. The inclusion of the Company's stock options and warrants in the computation of diluted loss per share has an anti-dilutive effect on the loss per share and therefore, they have been excluded from the calculation of diluted loss per share.

#### **(j) Income taxes:**

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. A deferred tax asset is recognized for unused tax

## LORUS THERAPEUTICS INC.

### NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)

Three and nine months ended February 29, 2012 and February 28, 2011

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losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized.

#### **(k) Impairment:**

##### Non-financial assets

The carrying amounts of the Company's non-financial assets including equipment are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In estimating value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit, or CGU").

The Company's corporate assets do not generate separate cash inflows. If there is an indication that a corporate asset may be impaired, then the recoverable amount is determined for the CGU to which the corporate asset belongs.

Impairment losses recognized in respect of a CGU are allocated to reduce the carrying amount to the extent the carrying amount of the asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of a CGU are allocated to reduce the carrying amount of the assets in a unit on a pro-rated basis. Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit and loss.

#### **(l) Provisions:**

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as a financial cost.

Employee entitlements to annual leave are recognized as the employee earns them. A provision, stated at current cost, is made for the estimated liability at the end of each reporting period.

The Company has recorded a provision as related to an indemnification as described in note 14.

#### **(m) Recent accounting pronouncements:**

##### *(i) IFRS 9 Financial Instruments*

In October 2010, the International Accounting Standard Board ("IASB") issued IFRS 9, *Financial Instruments* ("IFRS 9"), which replaces IAS 39, *Financial Instruments: Recognition and Measurement*, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows. This new standard is effective for the Company's condensed interim and annual consolidated financial statements commencing June 1, 2015. The Company is assessing the impact of this new standard on its consolidated financial statements.

##### *(ii) IFRS 10 Consolidated Financial Statements*

This amendment establishes a single control model that applies to all entities. These changes will require management to exercise significant judgment to determine which entities are controlled, and therefore are required to be consolidated by a parent, compared with the former requirements. The amendment becomes effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate any impact on its consolidated financial statements related to the adoption of this new standard.

##### *(iii) IFRS 11 Joint Arrangements*

This amendment replaces IAS 31 – *Interests in Joint Ventures* and SIC-13 *Jointly controlled entity – Non-monetary Contributions by Venturers* and addresses only two forms of joint arrangements (joint operations and joint ventures) where there is joint control and removes the option to account for jointly controlled entities using proportionate consolidation. The amendment becomes effective for annual periods beginning on or after January 1, 2013. The Company does not anticipate any impact on its consolidated financial statements related to the adoption of this new standard.

##### *(iv) IFRS 13 Fair Value Measurement*

## **LORUS THERAPEUTICS INC.**

### **NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

*Three and nine months ended February 29, 2012 and February 28, 2011*

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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. 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 is assessing the impact of this new standard on its consolidated financial statements.

#### **4. Capital disclosures**

The Company's objectives when managing capital are to:

- Maintain its ability to continue as a going concern in order to provide returns to shareholders and benefits to other stakeholders;
- Maintain a flexible capital structure which optimizes the cost of capital at acceptable risk;
- Ensure sufficient cash resources to fund its research and development activity, to pursue partnership and collaboration opportunities and to maintain ongoing operations.

The capital structure of the Company consists of cash and cash equivalents and equity comprised of share capital, share purchase warrants, stock options, contributed surplus and deficit. The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share issuances, acquiring or disposing of assets, adjusting the amount of cash balances or by undertaking other activities as deemed appropriate under the specific circumstances.

Pursuant to the commitment letter (described in note 7) provided by Mr. Abramson, the Company has issued a grid promissory note to Mr. Abramson that will allow Lorus to borrow funds up to \$1.8 million. The funds may be borrowed at a rate of up to \$300,000 per month, incur interest at a rate of 10% per year and are due and payable on November 28, 2012.

The Company is not subject to externally imposed capital requirements.

While the Company's overall strategy with respect to capital risk management remains unchanged from the year ended May 31, 2011, the Company has forecasted that its current capital resources are not sufficient to carry out its research and development plans and operations for more than the next twelve months and continues to investigate various alternatives to obtain sufficient capital to continue its operations (note 2a).

#### **Cash and cash equivalents**

Cash and cash equivalents consists of cash of \$103 thousand and funds deposited into High Interest Savings Accounts totaling \$nil (May 31, 2011 – \$758 thousand and June 1, 2010 – nil). The current interest rate earned on these deposits is nil (May 31, 2011 – 1.2%, June 1, 2010 – nil)

#### **Short-term investment (relating to June 1, 2010)**

An investment consisting of a principle protected deposit note totaling \$247 thousand at June 1, 2010, was designated as held-for-trading investments, and was classified as short-term investments on the consolidated balance sheets. This investment was carried at fair value. There were no short-term investments held by the Company at May 31, 2011 or February 29, 2012.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)***Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

**5. Equipment:**

February 29, 2012	Cost	Accumulated depreciation	Net book value
Furniture and equipment	\$ 2,914	\$ 2,848	\$ 66

May 31, 2011	Cost	Accumulated depreciation	Net book value
Furniture and equipment	\$ 2,914	\$ 2,815	\$ 99

June 1, 2010	Cost	Accumulated depreciation	Net book value
Furniture and equipment	\$ 2,907	\$ 2,760	\$ 147

**6. Research and development programs:**

The Company has product candidates in three classes of anticancer therapies:

- small molecule therapies based on anti-angiogenic, anti-proliferative and anti-metastatic agents;
- RNA-targeted (antisense and siRNA) therapies, based on synthetic segments of DNA or RNA designed to bind to the messenger RNA that is responsible for the production of proteins over-expressed in cancer cells; and
- immunotherapy, based on macrophage-stimulating biological response modifiers.

**(a) Small Molecule Program:**

The Company has small molecule drug screening technologies and preclinical scientific expertise, which it is using to create a drug candidate pipeline. The Company's proprietary group of small molecule compounds includes lead drug LOR-253 which entered into a Phase I clinical trial in January of 2011 and LOR-500 which is in the pre-clinical stage of development.

**(b) RNA-Targeted Therapies:**

The Company's lead RNA-targeted drug candidate is LOR-2040. The Company has reported Phase II clinical results, completed to the end-of-stage assessment time point, of LOR-2040 in combination with cytarabine in relapsed and refractory acute myeloid leukemia ("AML") patient population. Based on these data, the Company is seeking a partnership or collaboration for future development.

**(c) Immunotherapy:**

The Company's immunotherapy product candidates are Virulizin® and Interleukin-17E ("IL-17E"). IL-17E is a protein-based therapeutic that the Company is seeking a partnership or collaboration for future development.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

Research and development expenditures by product class are as follows:

	Three months ended		Nine months ended	
	Feb 29, 2012	Feb 28, 2011	Feb 29, 2012	Feb 28, 2011
Small molecules	\$ 524	\$ 540	\$ 1,622	\$ 1,344
RNA-Targeted Therapies	—	220	—	508
Immunotherapy	—	—	—	—
<b>Total</b>	<b>\$ 524</b>	<b>\$ 760</b>	<b>\$ 1,622</b>	<b>\$ 1,852</b>

**7. Promissory notes payable**

Pursuant to the commitment letter (described in note 9(b)) provided by Mr. Abramson, the Company has issued a grid promissory note to Mr. Abramson that allows Lorus to borrow funds up to \$1.8 million. The funds may be borrowed at a rate of up to \$300 thousand per month, incur interest at a rate of 10% per year and are due and payable in full on November 28, 2012. The promissory note is subject to certain covenants which, if breached, could result in the promissory note becoming payable on demand. The covenants include:

- failure to pay any or all interest payable when due;
- ceasing or threaten to cease to carry on the business currently being carried on by Lorus or a substantial portion thereof or makes or agrees to make an assignment, disposition or conveyance;
- Lorus is an insolvent person or commits or threatens to commit any act of bankruptcy;
- Lorus proceeds or takes steps towards the dissolution, liquidation or winding up of the Company.

Lorus is not aware of any breach in these covenants and has not received notice of any breach of these covenants by Mr. Abramson,

As at February 29, 2012 the Company has drawn \$300,000 on this promissory note (see note 16).

In April 2010, the Company entered into a loan agreement with a company related to Mr. Abramson to borrow \$1 million. The loan amount, which was received on April 14, 2010, was unsecured, evidenced by a promissory note and bore interest at the annual rate of 10%. The principal and interest amount were due in six months and later extended a further three months. The principal amount was repaid in November 2010.

**8. Financial instruments****(a) Financial instruments**

The Company has classified its financial instruments as follows:

	As at February 29, 2012	As at May 31, 2011	As at June 1, 2010
<b>Financial assets</b>			
Cash and cash equivalents, consisting of guaranteed investment certificates, held for trading, measured at fair value through loss or profit	\$ 103	\$ 911	\$ 667
Short-term investments, held-for-trading, recorded at fair value through loss or profit	—	—	247
<b>Financial liabilities</b>			
Accounts payable, measured at amortized cost	117	215	387
Accrued liabilities, measured at amortized cost	1,160	944	1,458
Promissory note payable, measured at amortized cost	300	—	1,000

**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

*Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

At February 29, 2012, there are no significant differences between the carrying values of these amounts and their estimated market values due to their short-term nature.

**(b) Financial risk management**

The Company has exposure to credit risk, liquidity risk and market risk. The Company's Board of Directors has the overall responsibility for the oversight of these risks and reviews the Company's policies on an ongoing basis to ensure that these risks are appropriately managed.

**(i) Credit risk**

Credit risk is the risk of financial loss to the Company if a customer, partner or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's cash and cash equivalents. The carrying amount of the financial assets represents the maximum credit exposure.

The Company manages credit risk for its cash and cash equivalents by maintaining minimum standards of R1-low or A-low investments and the Company invests only in highly rated Canadian corporations with debt securities that are traded on active markets and are capable of prompt liquidation.

**(ii) Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. To the extent that the Company does not believe it has sufficient liquidity to meet its current obligations, the Board considers securing additional funds through equity, debt or partnering transactions. The Company manages its liquidity risk by continuously monitoring forecasts and actual cash flows. Refer to note 2(b) for further discussion on the Company's ability to continue as a going concern.

**(iii) Market risk**

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates and equity prices will affect the Company's income or the value of its financial instruments.

The Company is subject to interest rate risk on its cash and cash equivalents and short-term investments. The Company does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates relative to interest rates on the investments, owing to the relative short-term nature of the investments. The Company does not have any material interest bearing liabilities subject to interest rate fluctuations.

Financial instruments potentially exposing the Company to foreign exchange risk consist principally of accounts payable and accrued liabilities. The Company holds minimal amounts of U.S. dollar denominated cash, purchasing on an as needed basis to cover U.S. dollar denominated payments. At February 29, 2012, U.S. dollar denominated accounts payable and accrued liabilities amounted to \$238 thousand (February 28, 2011 - \$260 thousand). Assuming all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the U.S. dollar would result in an increase or decrease in loss for the year and comprehensive loss of \$24 thousand (February 28, 2011 - \$26 thousand). The Company does not have any forward exchange contracts to hedge this risk.

The Company does not invest in equity instruments of other corporations.

**(c) Capital management**

The Company's primary objective when managing capital is to ensure that it has sufficient cash resources to fund its development and commercialization activities and to maintain its ongoing operations. To secure the additional capital necessary to pursue these plans, the Company may attempt to raise additional funds through the issuance of equity or by securing strategic partners.

The Company includes cash and cash equivalents and short-term deposits in the definition of capital.

The Company is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital management strategy during the three months ended February 29, 2012.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**9. Share capital**

The Company is authorized to issue an unlimited number of common shares.

**(a) Continuity of common shares and warrants**

<i>(amounts in 000's)</i>	Common Shares		Warrants	
	Number	Amount	Number	Amount
<b>Balance at June 1, 2010</b>	<b>9,933</b>	<b>\$ 163,920</b>	<b>1,326</b>	<b>\$ 1,039</b>
Expiry of warrants (c)	—	—	(571)	(417)
Issuance of units (b)	4,170	3,226	4,170	1,032
Issuance of common shares (b)	1,582	1,641	—	—
<b>Balance at February 28, 2011</b>	<b>15,685</b>	<b>168,787</b>	<b>4,925</b>	<b>1,654</b>
Expiry of warrants (c)	—	—	(755)	(622)
<b>Balance at May 31, 2011</b>	<b>15,685</b>	<b>168,787</b>	<b>4,170</b>	<b>1,032</b>
Issuance of units (b)	5,484	1,214	5,678	609
Warrant repricing (c)	—	—	—	239
<b>Balance at February 29, 2012</b>	<b>21,169</b>	<b>\$ 170,001</b>	<b>9,848</b>	<b>\$ 1,880</b>

**(b) Equity issuances***August 2011 Unit Offering*

On July 22, 2011, the Company filed a final short-form prospectus in connection with a best efforts offering (the "Offering") of a minimum of 5,000,000 units of the Company (the "Units") at a price of \$0.40 per Unit for gross proceeds of \$2,000,000 and a maximum of 10,000,000 Units for gross proceeds of \$4,000,000. Each Unit consisted of one common share of Lorus (a "Common Share") and one common share purchase warrant of Lorus (a "Warrant"). Each Warrant entitles the holder to purchase one Common Share for five years after the closing of the Offering at an exercise price of \$0.45 per Common Share (the "Exercise Price"). If on any date (the "Accelerated Exercise Date") the 10-day volume weighted average trading price of the Common Shares on the Toronto Stock Exchange equals or exceeds 200% of the Exercise Price, then upon the Company sending the holders of Warrants written notice of such Accelerated Exercise Date and issuing a news release announcing such Accelerated Exercise Date, the Warrants shall only be exercisable for a period of 30 days following the date on which such written notice is sent to holders of Warrants.

In connection with the Offering, Herbert Abramson, a director of the Company, entered into an irrevocable commitment letter on June 20, 2011, and amended July 11, 2011, to purchase, directly or indirectly, common shares and common share purchase warrants (or as may otherwise be agreed) in the capital of Lorus (collectively the "Securities") having an aggregate subscription price equal to the difference (the "Commitment Amount"), if any, between (a) the sum of (i) the gross proceeds realized by Lorus in the Offering and (ii) the gross proceeds received by Lorus in respect of all financings completed by Lorus from the date of the final short-form prospectus to November 30, 2011 and (b) \$4.0 million.

The Offering closed on August 15, 2011 for total gross proceeds of \$2.2 million. In connection with the Offering, Lorus has issued 5.484 million Common Shares and 5.678 million Warrants including the broker warrants.

Mr. Abramson purchased 2.4 million Units as part of the Offering.

The total costs associated with the transaction were approximately \$395 thousand which included the \$25 thousand which represented the fair value of the brokers' services provided as part of the Offering. Each such broker warrant is exercisable for one Unit at a price of \$0.40 per Unit for a period of 24 months following the closing of the Offering. The Company has allocated the net proceeds of the Offering to the common shares and the common share purchase warrants based on their estimated relative fair values. Based on relative fair values, \$1.2 million of the net proceeds were allocated to the common shares and \$609 thousand to the common share purchase warrants.

*December 2010 Private Placement:*

On December 1, 2010, pursuant to a private placement, the Company issued 1.6 million common shares in exchange for gross cash consideration of \$1.66 million. The total costs associated with the transaction were approximately \$20 thousand. Mr. Herbert Abramson, a director of the Company, subscribed for 1,410,000 common shares, representing approximately 89% of the total number of common shares issued through the private placement. No commission was paid in connection with the private placement.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)***Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

*November 2010 Rights Offering:*

On August 27, 2010 the Company announced a proposed rights offering as described below including a \$4 million standby purchase agreement from a director of the Company, Mr. Herbert Abramson. Mr. Abramson also provided the Company with interim financing by way of three \$500 thousand monthly loans, advanced on August 11, 2010, September 13, 2010 and October 5, 2010. The loans were unsecured, had a six-month term (or the earlier of the closing of the rights issue) and bore interest at the annual rate of 10%. All three notes were repaid upon the close of the rights offering described below.

On September 27, 2010, Lorus filed a final short-form prospectus in each of the provinces of Canada in connection with a distribution to its shareholders in eligible jurisdictions outside the United States of rights exercisable for units of the Company (the "Rights Offering"). Under the Rights Offering, holders of common shares of the Company as of October 12, 2010, the record date, received one right for each common share held as of the record date. Each two rights entitled the holder thereof to purchase a unit of the Company at a price of \$1.11 per unit. Each unit consisted of one common share of the Company and one warrant to purchase an additional common share of the Company at a price of \$1.33 until May 2012.

A total of 4.2 million units of the Company at a price of \$1.11 per unit were issued in connection with the Rights Offering. As a result of the Rights Offering, Lorus issued 4.2 million common shares and 4.2 million common share purchase warrants for net proceeds of \$4.2 million. In connection with the Rights Offering, the Company secured a standby purchase arrangement of \$4 million by Mr. Abramson, one of the Company's directors. Mr. Abramson agreed to make an investment such that the minimum gross proceeds of the proposed Rights Offering would be \$4 million. No fee was payable to Mr. Abramson for this commitment. In accordance with the terms of the standby purchase agreement, Mr. Abramson subscribed for 3.6 million of the 4.2 million units of the Rights Offering for \$4.0 million.

The total costs associated with the transaction were approximately \$370 thousand. The Company has allocated the net proceeds of the Rights Offering to the common shares and the common share purchase warrants based on their estimated relative fair values. Based on relative fair values, \$3.2 million of the net proceeds were allocated to the common shares and \$1.0 million to the common share purchase warrants.

**(c) Warrants**Repricing

On November 29, 2011 shareholders of the Company (excluding insiders who also held warrants) approved a resolution to amend the exercise price of certain outstanding warrants from \$1.33 to the 5 day volume weighted average trading price on the Toronto Stock Exchange five days prior to approval plus a 10% premium. The revised warrant exercise price is \$0.28. The Company calculated an increased value attributed to the warrants of \$239 thousand related to the amendment. This increase was calculated by taking the Black Scholes value of the warrants immediately before the amendment and immediately after the amendment. There are 4.2 million warrants which were amended and of those 3.6 million are held by Mr. Abramson, a director of the Company.

Expiry

The warrants issued on November 27, 2009 expired unexercised on May 27, 2011. This expiry resulted in a transfer of the amount attributed to the expired warrants of \$622 thousand to contributed surplus.

The warrants issued on August 7, 2008 expired unexercised on August 10, 2010. This expiry results in a transfer of the amount attributed to the expired warrants of \$417 thousand to contributed surplus.

**(d) Continuity of contributed surplus**

Contributed surplus is comprised of the cumulative grant date fair value of expired share purchase warrants and expired stock options as well as the cumulative amount of previously expensed and unexercised equity settled share-based payment transactions.

	<b>Nine months ended February 29, 2012</b>	Nine months ended February 28, 2011	Year ended May 31, 2011
Balance, Beginning of year	\$ 18,988	\$ 14,875	14,875
Expiry of warrants (c)	—	417	1,039
Warrant repricing (c)	(239)	—	—
Forfeiture and cancellation of stock options	1,184	3,071	3,074
Balance, end of period	\$ 19,933	\$ 18,363	18,988



**LORUS THERAPEUTICS INC.**
**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**
*Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

**(e) Continuity of stock options**

	Nine months ended February 29, 2012	Nine months ended February 28, 2011	Year ended May 31, 2011
Balance, Beginning of year	\$ 1,212	\$ 3,803	3,803
Stock option expense	468	283	483
Forfeiture and cancellation of stock options	(1,184)	(3,071)	(3,074)
Balance, end of period	\$ 496	\$ 1,015	1,212

**(f) Loss per share**

Loss per common share is calculated using the weighted average number of common shares outstanding for the three and nine month periods ending February 29, 2012 of 21.169 million (February 28, 2011 – 15.685 million) and 19.950 million (February 28, 2011 - 12.314 million) calculated as follows:

	Three months ended February 29/28		Nine months ended February 29/28	
	2012	2011	2012	2011
Issued common shares, beginning of period	21,168,697	14,103,030	15,684,697	9,933,454
Effect of rights offering (note 9(b))	—	—	—	1,853,160
Effect of unit offering (note 9(b))	—	—	4,265,333	—
Effect of private placement (note 9(b))	—	1,581,667	—	527,222
	21,168,697	15,684,697	19,950,030	12,313,836

The effect of any potential exercise of our stock options and warrants outstanding during the year has been excluded from the calculation of diluted loss per common share as it would be anti-dilutive.

**10. Stock options**
**(a) Stock options transactions for the period:**

	Nine months ended February 29, 2012		Nine months ended February 28, 2011		Year ended May 31, 2011	
	Options	Weighted average exercise price	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding, Beginning of year	1,185,578	\$ 1.58	672,901	\$ 6.60	672,901	\$ 6.60
Granted	1,215,000	0.22	791,800	1.05	1,049,700	1.01
Exercised	—	—	—	—	—	—
Cancelled	(1,082,402)	1.21	—	—	—	—
Forfeited/Expired	(29,341)	6.03	(486,434)	7.30	(537,023)	6.76
Outstanding, end of period	1,288,835	\$ 0.51	978,267	\$ 1.80	1,185,578	\$ 1.58

**(b) Stock options outstanding at February 29, 2012:**

Range of exercise prices	Options outstanding		Options exercisable	
	Options	Weighted average remaining contractual life (years)	Options	Weighted average exercise price
\$ 0.22 - \$ 2.00	1,215,000	9.8	732,500	\$ 0.22
\$ 2.00 - \$ 4.99	40,663	7.0	34,597	2.89
\$ 5.00 - \$18.00	33,172	4.3	33,172	8.40
	1,288,835	9.5	800,269	\$ 0.67

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**(c) Fair value assumptions**

The following assumptions were used in the Black-Scholes option-pricing model to determine the fair value of stock options granted during the following periods:

	<b>Nine months ended February 29, 2012</b>	Nine months ended February 28, 2011	Year ended May 31, 2011
Exercise price	\$ 0.215	\$ 1.05	\$ 0.89-1.05
Grant date share price	\$ 0.215	\$ 1.03	\$ 0.86-1.03
Risk free interest rate	1.5%	1.85%	1.50-1.85%
Expected dividend yield	—	—	0%
Expected volatility	123%	119%	117-119%
Expected life of options	5 years	5 years	5 years
Weighted average fair value of options granted in the period	\$ 0.18	\$ 0.87	\$ 0.83

Stock options granted by the Company during the nine months ended February 29, 2012 have various vesting schedules. Options granted to directors consisted of 90,000 options that vested 50% upon issuance and 50% one year later. Two directors received options that totaled 550,000 options which vested immediately. Options granted to the CEO of 275,000 vested 50% immediately and 25% on each of November 29, 2012 and November 29, 2013. Options granted to certain members of management totaled 300,000 and vested 50% upon certain performance criteria measured as of May 31, 2012 and 25% May 31, 2013 and 25% on May 31, 2014.

Stock options granted by the Company during the year ended May 31, 2011 had three types of vesting schedules. Options granted to directors consisted of 30,000 options that vested 50% upon issuance and 50% one year later. Options granted to the CEO of 784,200 vested 50% at May 31, 2011 and 25% May 31, 2012 and 25% May 31, 2013. Options granted to certain members of management totaled 235,500 and vested 50% upon certain performance criteria measured as of May 31, 2011 and 25% May 31, 2012 and 25% on May 31, 2013.

Refer to note 12 for a breakdown of stock option expense by function.

The Company has reserved up to 3,175,000 common shares for issuance relating to outstanding options, rights and other entitlements under the security based compensation plans of the Company as of February 29, 2012.

**11. Additional cash flow disclosures**

Net change in non-cash operating working capital is summarized as follows:

	<b>Three months ended February 29/28</b>		<b>Nine months ended February 29/28</b>	
	<b>2012</b>	2011	<b>2012</b>	2011
Prepaid expenses and other assets	129	233	51	358
Accounts payable	(239)	(242)	(98)	(158)
Accrued liabilities	58	(387)	216	(572)
Promissory note payable	300	—	300	(1,000)
	<b>248</b>	(396)	<b>469</b>	(1,372)

During the three and nine months ended February 29, 2012 the Company accrued \$3 thousand in interest expense on the \$300 thousand promissory note due to Mr. Abramson. The interest has been accrued at a rate of 10%. During the three and nine months ended February 28, 2011 the Company incurred \$nil and \$71 thousand respectively of interest on promissory notes to Mr. Abramson. During the year ended May 31, 2011, the Company paid \$71 thousand in cash interest on promissory notes from Mr. Abramson and Mr. Abramson's related company that were repaid in November 2010.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**12. Other expenses***Components of research and development expenses:*

	Three months ended		Nine months ended	
	February 29/28		February 29/28	
	2012	2011	2012	2011
Program costs (note 6)	524	760	1,622	1,852
Stock based compensation	11	78	132	100
Depreciation of equipment	8	9	25	29
	<b>543</b>	<b>847</b>	<b>1,779</b>	<b>1,981</b>

*Components of general and administrative expenses:*

	Three months ended		Nine months ended	
	February 29/28		February 29/28	
	2012	2011	2012	2011
General and administrative excluding salaries	303	294	960	1,106
Salaries	163	232	521	573
Stock based compensation	10	170	336	183
Depreciation of equipment	3	5	8	13
	<b>479</b>	<b>701</b>	<b>1,825</b>	<b>1,875</b>

**13. Related Party Transactions**

In October 2009, the Company entered into a loan agreement with a member of its Board of Directors, Mr. Abramson, to borrow \$1 million. The loan amount, which was received on October 6, 2009, was unsecured, evidenced by a promissory note and bears interest at the annual rate of 10%. The principal and interest were due in six months. The principal amount of \$1 million was applied to subscribe for Units as part of the November 27, 2009 private placement.

On August 27, 2010 the Company announced a proposed rights offering as described in note 9(b) including a \$4 million standby purchase agreement from a director of the Company, Mr. Herbert Abramson. Mr. Abramson also provided the Company with interim financing by way of three \$500 thousand monthly loans, advanced on August 11, 2010 (outstanding at August 31, 2010), September 13, 2010 and October 5, 2010. The loans were unsecured, had a six-month term (or the earlier of the closing of the rights issue) and bore interest at the annual rate of 10%. All three notes were repaid upon the close of the rights offering described in note 9(b).

These transactions were in the normal course of business and have been measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

See also notes 7 and 9 for additional related party transactions.

**14. Commitments, contingencies and guarantees.**

## (a) Operating lease commitments:

The Company has entered into operating leases for premises and equipment under which it is obligated to make minimum annual payments as described below:

	Less than 1 year	1-3 years	3-5 years	Total
<b>Operating leases</b>	150	25	7	182

The Company's current facility lease expires in March 2013.

## (b) Other contractual commitments:

The Company holds an exclusive world-wide license from the University of Manitoba (the "University") and Cancer Care Manitoba ("CCM") to certain patent rights to develop and sub-license certain oligonucleotide technologies. In consideration for the exclusive license of the patent rights, the University and CCM are entitled to an aggregate of 1.67% of the net sales received by the Company from the sale of products or processes derived from the patent rights and 1.67% of all monies

## LORUS THERAPEUTICS INC.

### NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

received by the Company from sub-licenses of the patent rights. Any and all improvements to any of the patent rights derived in whole or in part by the Company after the date of the license agreement, being June 20, 1997, are not included within the scope of the agreement and do not trigger any payment of royalties.

The Company has not yet earned any revenue from the products covered under this agreement and, therefore, has not paid any royalties thereunder and cannot reasonably predict the timing and amount of any future payment. The Company does not expect to make any royalty payments under this agreement in fiscal years ended May 31, 2012 or 2013, and cannot reasonably predict when such royalties will become payable, if at all.

The Company has entered into various contracts with service providers with respect to the LOR-253 phase I clinical trial. These contracts could result in future payment commitments of approximately \$860 thousand. Of this amount \$360 thousand has been accrued or paid at February 29, 2012 (May 31, 2011 - \$248 thousand). The payments will be based on services performed and amounts maybe higher or lower based on actual services performed.

(c) Guarantees:

The Company entered into various contracts, whereby contractors perform certain services for the Company. The Company indemnifies the contractors against costs, charges and expenses in respect of legal actions or proceedings against the contractors in their capacity of servicing the Company. The maximum amounts payable from these guarantees cannot be reasonably estimated. Historically, the Company has not made significant payments related to these guarantees.

The Company indemnifies its directors and officers against any and all claims or losses reasonably incurred in the performance of their service to the Company to the extent permitted by law. The Company has acquired and maintains liability insurance for its directors and officers. The fair value of this indemnification is not determinable.

(d) Indemnification on arrangement:

On July 10, 2007, Lorus completed a plan of arrangement and corporate reorganization whereby the assets and liabilities of Lorus were transferred from one corporate entity ("Old Lorus") into a new corporate entity which continued to operate as Lorus Therapeutics Inc. Under the arrangement, the Company agreed to indemnify Old Lorus and its directors, officers and employees from and against all damages, losses, expenses (including fines and penalties), other third party costs and legal expenses, to which any of them may be subject arising out of any matter occurring:

- (i) prior to, at or after the effective time of the arrangement ("Effective Time") and directly or indirectly relating to any of the assets of Old Lorus transferred to the Company pursuant to the arrangement (including losses for income, sales, excise and other taxes arising in connection with the transfer of any such asset) or conduct of the business prior to the Effective Time;
- (ii) prior to, at or after the Effective Time as a result of any and all interests, rights, liabilities and other matters relating to the assets transferred by Old Lorus to the Company pursuant to the arrangement; and
- (iii) prior to or at the Effective Time and directly or indirectly relating to, with certain exceptions, any of the activities of Old Lorus or the arrangement.

The Company recorded a liability of \$100 thousand, which it believes to be a reasonable estimate of the fair value of the obligation for the indemnifications provided as at February 29, 2012. There have been no claims on this indemnification to date.

## 15. Explanation of transition to International Financial Reporting Standards

As stated in Note 2, these are the Company's third condensed consolidated interim financial statements prepared in accordance with IAS34.

The accounting policies disclosed in Note 3 have been applied in preparing our consolidated financial statements as at and for the three and nine months ended February 29, 2012, the comparative information presented as at and for the three and nine months ended February 28, 2011 and the year ended May 31, 2011 and in the preparation of our opening IFRS balance sheet at June 1, 2010 (our date of transition) and the statement of financial position as at May 31, 2011.

IFRS 1 requires first time adopters to retrospectively apply all effective IFRSs as of the reporting date. However, it also provides for certain optional exemptions and certain mandatory exceptions for the first time IFRS adopters. Details of the Company's initial elections of IFRS 1 exemptions are described below.

In preparing our opening balance sheet, we have adjusted amounts reported previously in our consolidated financial statements prepared in accordance with Canadian GAAP. An explanation of how the transition from Canadian GAAP to IFRS has affected our financial position, financial performance and cash flows is set out in the following tables and notes that accompany the tables.

**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

*Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

***Initial elections upon adoption of IFRS***

Under IFRS 1 the following applicable exemption applied to the Company's conversion from Canadian GAAP to IFRS.

- (i) **Share Based Payments:** The Company elected not to apply IFRS 2 to equity instruments that vested before the date of transition to IFRS.
- (ii) **Business combinations:** The Company applied the business combinations exemption to not apply IFRS 3, *Business Combinations*, retrospectively to past business combinations. Accordingly, we have not restated business combinations that took place prior to the Transition Date. In addition, and as a condition under IFRS 1 for applying this exemption, goodwill relating to business combinations that occurred prior to the Transition Date was tested for impairment as described in note 15 (b)(i).

**LORUS THERAPEUTICS INC.**  
**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**Reconciliation of financial position and shareholders' equity**

	Notes	June 1, 2010			May 31, 2011		
		Canadian GAAP	Effect of transition to IFRS	IFRS	Canadian GAAP	Effect of transition to IFRS	IFRS
<b>Current</b>							
Cash and cash equivalents		\$ 667	\$ -	\$ 667	911	-	911
Short-term investments		247	-	247	-	-	-
Prepaid expenses and other assets		636	-	636	388	-	388
<b>Total Current Assets</b>		<b>1,550</b>	<b>-</b>	<b>1,550</b>	<b>1,299</b>	<b>-</b>	<b>1,299</b>
<b>Non-Current</b>							
Equipment		147	-	147	99	-	99
Goodwill	(b) (i)	606	(606)	-	606	(606)	-
<b>Total Non-Current Assets</b>		<b>753</b>	<b>(606)</b>	<b>147</b>	<b>705</b>	<b>(606)</b>	<b>99</b>
<b>Total Assets</b>		<b>2,303</b>	<b>(606)</b>	<b>1,697</b>	<b>2,004</b>	<b>(606)</b>	<b>1,398</b>
<b>LIABILITIES</b>							
<b>Current</b>							
Accounts payable		387	-	387	215	-	215
Accrued liabilities		1,458	-	1,458	944	-	944
Promissory note payable		1,000	-	1,000	-	-	-
<b>Total Current Liabilities</b>		<b>2,845</b>	<b>-</b>	<b>2,845</b>	<b>1,159</b>	<b>-</b>	<b>1,159</b>
<b>SHAREHOLDERS' EQUITY</b>							
<b>Share capital</b>							
Common shares		163,920	-	163,920	168,787	-	168,787
Stock options	(b) (ii)	3,704	99	3,803	1,156	56	1,212
Contributed surplus		14,875	-	14,875	18,988	-	18,988
Warrants		1,039	-	1,039	1,032	-	1,032
Deficit	(b) (i) (ii)	(184,080)	(705)	(184,785)	(189,118)	(662)	(189,780)
<b>Total Equity</b>		<b>(542)</b>	<b>(606)</b>	<b>(1,148)</b>	<b>845</b>	<b>(606)</b>	<b>239</b>
<b>Total Equity and Liabilities</b>		<b>2,303</b>	<b>(606)</b>	<b>1,697</b>	<b>2,004</b>	<b>(606)</b>	<b>1,398</b>

**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**Reconciliation of financial position and shareholders' equity (continued)**

	Notes	February 28, 2011		
		Canadian GAAP	Effect of transition to IFRS	IFRS
<b>Current</b>				
Cash and cash equivalents		\$ 1,845	\$ -	1,845
Prepaid expenses and other assets		278	-	278
<b>Total Current Assets</b>		<b>2,123</b>	<b>-</b>	<b>2,123</b>
<b>Non-Current</b>				
Equipment		110	-	110
Goodwill	(b) (i)	606	(606)	-
<b>Total Non-Current Assets</b>		<b>716</b>	<b>(606)</b>	<b>110</b>
<b>Total Assets</b>		<b>2,839</b>	<b>(606)</b>	<b>2,233</b>
<b>LIABILITIES</b>				
<b>Current</b>				
Accounts payable		229	-	229
Accrued liabilities		887	-	887
<b>Total Current Liabilities</b>		<b>1,116</b>	<b>-</b>	<b>1,116</b>
<b>SHAREHOLDERS' EQUITY</b>				
<b>Share capital</b>				
Common shares		168,787	-	168,787
Stock options	(b) (ii)	1,000	15	1,015
Contributed surplus		18,363	-	18,363
Warrants		1,654	-	1,654
Deficit	(b) (i) (ii)	(188,081)	(621)	(188,702)
<b>Total Equity</b>		<b>1,723</b>	<b>(606)</b>	<b>1,117</b>
<b>Total Equity and Liabilities</b>		<b>2,839</b>	<b>(606)</b>	<b>2,233</b>

**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**Reconciliation of consolidated statement of loss and comprehensive loss  
for the three months ended February 28, 2011**

	Note	Canadian GAAP	Effect of transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	760	87	847
General and administrative	b (ii)	527	174	701
Stock-based compensation	b (ii)	287	(287)	-
Depreciation of equipment	b (ii)	13	(13)	-
<b>Operating expenses</b>		<u>1,587</u>	<u>(39)</u>	<u>1,548</u>
<b>(Loss) from operations</b>		<u>(1,587)</u>	<u>39</u>	<u>(1,548)</u>
Finance expense		-	-	-
Finance income		6	-	6
Net Financing expense (income)		<u>(6)</u>	<u>-</u>	<u>(6)</u>
<b>Net loss and other comprehensive loss for the period</b>		<u>\$ 1,581</u>	<u>\$ (39)</u>	<u>\$ 1,542</u>
<b>Basic and diluted loss per share</b>		<u>\$ 0.10</u>	<u>\$ 0.00</u>	<u>\$ 0.10</u>

**Adjustments to the Statement of Cash Flows for the three months ended February 28, 2011**

Consistent with the Company's accounting policy under IAS 7, *Statement of Cash Flows*, interest paid and received have been moved to the body of the *Statement of Cash Flows*, as an element of cash flows from investing activities or financing activities whereas it was previously disclosed as supplementary information. There are no material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

**Reconciliation of consolidated statement of loss and comprehensive loss  
for the nine months ended February 28, 2011**

	Note	Canadian GAAP	Effect of transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	1,852	129	1,981
General and administrative	b (ii)	1,680	195	1,875
Stock-based compensation	b (ii)	367	(367)	-
Depreciation of equipment	b (ii)	41	(41)	-
<b>Operating expenses</b>		<u>3,940</u>	<u>(84)</u>	<u>3,856</u>
<b>(Loss) from operations</b>		<u>(3,940)</u>	<u>84</u>	<u>(3,856)</u>
Finance expense		71	-	71
Finance income		(10)	-	(10)
Net Financing expense (income)		<u>61</u>	<u>-</u>	<u>61</u>
<b>Net loss and other comprehensive loss for the period</b>		<u>\$ 4,001</u>	<u>\$ (84)</u>	<u>\$ 3,917</u>
<b>Basic and diluted loss per share</b>		<u>\$ 0.32</u>	<u>-</u>	<u>0.32</u>



**LORUS THERAPEUTICS INC.**

**NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

**Reconciliation of consolidated statement of loss and comprehensive loss for the year ended May 31, 2011**

	Note	Effect of		
		Canadian GAAP	transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	2,298	220	2,518
General and administrative	b (ii)	2,101	319	2,420
Stock-based compensation	b (ii)	526	(526)	-
Depreciation of equipment	b (ii)	56	(56)	-
<b>Operating expenses</b>		<b>4,981</b>	<b>(43)</b>	<b>4,938</b>
<b>(Loss) from operations</b>		<b>(4,981)</b>	<b>43</b>	<b>(4,938)</b>
Interest expense		71	-	71
Interest income		(14)	-	(14)
Net financing expense (income)		57	-	57
<b>Net Loss and other comprehensive loss for the period</b>		<b>5,038</b>	<b>(43)</b>	<b>4,995</b>
<b>Basic and diluted loss per share</b>		<b>\$ 0.38</b>	<b>\$0.00</b>	<b>0.38</b>

**Adjustments to the Statement of Cash Flows for the year ended May 31, 2011**

Consistent with the Company's accounting policy under IAS 7, *Statement of Cash Flows*, interest paid and received have been moved to the body of the *Statement of Cash Flows*, as an element of cash flows from investing activities or financing activities whereas it was previously disclosed as supplementary information. There are no material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

**(a) Mandatory exceptions upon adoption of IFRS**

Estimates

In applying IFRS upon initial adoption, hindsight is not used to create or revise estimates. Estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS except where necessary to reflect any difference in accounting policy.

**(b) Impact on accounting policies upon adoption of IFRS**

The key areas where the Company has identified that accounting policies differ, or where accounting policy decisions were necessary that impacted the Company's consolidated interim financial statements, are discussed below.

(i) Goodwill:

Under Canadian GAAP, goodwill was reviewed for impairment annually and whenever events or circumstances indicated that the carrying amount of goodwill in a reporting unit exceeded its fair value. Goodwill impairment was calculated using a two-step process. The first step required an identification of impairment loss, if any, by comparing the carrying value of the reporting unit to the fair value, which in turn was determined based on the market capitalization of the Company. Under Canadian GAAP this test was performed at the reporting unit level which is defined as an operating segment or one level below. The Company only had one operating segment or component which is the development of anticancer product candidates. In the Company's case the first test always showed a higher fair value than carrying value and as such we were not required to proceed to step two, as no indicator of impairment existed.

Under IFRS, *IAS 36 Impairment of Assets* ("IAS 36"), there is no longer a two-step process; rather, the Company is required to make a formal estimate of the recoverable amount and the carrying amount of a cash generating unit ("CGU") that is subject to impairment testing. The recoverable amount under IAS 36 is the higher of fair value less costs to sell or value in use.

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)**

Three and nine months ended February 29, 2012 and February 28, 2011

(Tabular amounts are in 000's)

Impairment testing under IAS 36 is performed at the CGU level which is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other CGUs or groups of assets. For the Company, this requirement results in testing at a lower level than under Canadian GAAP. Based on our knowledge and historical transactions, the Company has identified three separate CGUs that represent each of our product platforms as they could have the ability to generate independent cash inflows. As the goodwill balance of \$606 thousand related to our acquisition of a private company in 1999, and the Antisense product platform contained therein, we have tested goodwill impairment on that CGU specifically for which the entire balance of goodwill has been allocated. There are no other assets subject to IAS 36 impairment testing in this CGU.

Under IAS 36, where the carrying value of a CGU subject to impairment testing is compared to the asset's value in use, any future cash flows expected to be provided by the CGU are discounted. The discounted cash flow model under IAS 36 indicates that only supportable evidence may be used in the calculations and should generally not use cash flows estimates beyond of a five-year period.

**Transition impact:** As a result of the application of IFRS, the Company recognized an impairment charge of the entire goodwill balance of \$606 thousand as of the Transition Date related to goodwill as the carrying amount of that CGU exceeded its recoverable amount which the Company has determined to be nil. The impact of the change in applying IFRS at the date of transition and as at May 31, 2011 is summarized as follows:

**Consolidated statement of financial position:**

	June 1, 2010	Feb 28, 2011	May 31, 2011
	\$	\$	\$
Decrease in goodwill	(606)	(606)	(606)
<b>Increase in deficit</b>	<b>606</b>	<b>606</b>	<b>606</b>

There was no impact to the consolidated statement of loss and comprehensive loss.

(ii) Share based payments:

IFRS 2, *Share-based Payments*, requires the fair value of each tranche of share options be amortized over its vesting period. Canadian GAAP allows for both the aforementioned method as well as the straight-line method of amortizing these costs. Under Canadian GAAP, forfeitures of share options can be accounted for at the time that they occur, whereas under IFRS, the number of share options that would ultimately vest is amortized over their respective vesting period.

Under Canadian GAAP, for share-based awards with graded vesting, the Company recognizes the fair value of the award (all tranches) on a straight-line basis over the underlying vesting period. In addition under Canadian GAAP the Company does not apply a forfeiture rate. The impact of applying the revised amortization method as well as applying an estimated forfeiture rate to the value of unvested options at the date of transition and as at May 31, 2011 is summarized as follows:

**Consolidated interim statement of loss and comprehensive loss:**

	Three months ended February 28, 2011	Nine months ended February 28, 2011	Year ended May 31, 2011
	\$	\$	\$
Decrease in share-based compensation	(39)	(84)	(43)

**LORUS THERAPEUTICS INC.****NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (Unaudited)***Three and nine months ended February 29, 2012 and February 28, 2011*

(Tabular amounts are in 000's)

**Consolidated statement of financial position:**

	<b>June 1, 2010</b>	<b>February 28, 2011</b>	<b>May 31, 2011</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>
Increase (Reduction) of Stock Option Equity Account	99	(84)	(43)
<b>Increase (Decrease) in deficit</b>	<b>99</b>	<b>(84)</b>	<b>(43)</b>

The Company will apply the requirements of estimating a forfeiture rate on stock options as prescribed under IFRS 2 and continue to amortize the fair value of each tranche of stock options over the related vesting period.

(iii) Estimates

In applying IFRS upon initial adoption, hindsight is not used to create or revise estimates. Estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS except where necessary to reflect any difference in accounting policies.

**16. Subsequent Events**

On March 12, 2012 the Company drew an additional \$300 thousand on the promissory note held by Mr. Abramson and described in note 7 above. The total outstanding on the promissory note following this advance is \$600 thousand with \$1.2 million available to be drawn under the terms of the facility.

On March 9, 2012 the Company issued 323,000 stock options at an exercise price of \$0.18 and 780,000 deferred share units with an issue price of \$0.18. These grants will be accounted for in the quarter ending May 31, 2012.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

April 12, 2012

## CAUTION REGARDING FORWARD-LOOKING STATEMENTS

*This management's discussion and analysis may contain forward-looking statements within the meaning of securities laws. Such statements include, but are not limited to, statements relating to:*

- *our ability to obtain the substantial capital required to fund research and operations;*
- *our plans to obtain partners to assist in the further development of our product candidates;*
- *our expectations with respect to existing and future corporate alliances and licensing transactions with third parties, and the receipt and timing of any payments to be made by us or to us in respect of such arrangements;*
- *our expectations regarding future financings;*
- *our plans to conduct clinical trials and pre-clinical programs;*
- *the length of clinical trials;*
- *the partnering potential of our products;*
- *our business strategy;*
- *our expectations regarding the progress and the successful and timely completion of the various stages of our drug discovery, pre-clinical and clinical studies and the regulatory approval process;*
- *our plans, objectives, expectations and intentions; and*
- *other statements including words such as "anticipate", "contemplate", "continue", "believe", "plan", "estimate", "expect", "intend", "will", "should", "may", and other similar expressions.*

*The forward-looking statements reflect our current views with respect to future events, are subject to risks and uncertainties, and are based upon a number of estimates and assumptions that, while considered reasonable by us, are inherently subject to significant business, economic, competitive, political and social uncertainties and contingencies. Many factors could cause our actual results, performance or achievements to be materially different from any future results, performance, or achievements that may be expressed or implied by such forward-looking statements, including, among others:*

- *our ability to continue to operate as a going concern;*
- *our ability to obtain the substantial capital required to fund research and operations;*
- *our lack of product revenues and history of operating losses;*
- *our early stage of development, particularly the inherent risks and uncertainties associated with (i) developing new drug candidates generally, (ii) demonstrating the safety and efficacy of these drug candidates in clinical studies in humans, and (iii) obtaining regulatory approval to commercialize these drug candidates;*
- *our ability to recruit patients for clinical trials;*
- *the progress of our clinical trials;*
- *our liability associated with the indemnification of in respect of the plan of arrangement and corporate reorganization completed on July 10, 2007;*
- *our ability to find and enter into agreements with potential partners;*
- *our drug candidates require time-consuming and costly preclinical and clinical testing and regulatory approvals before commercialization;*
- *clinical studies and regulatory approvals of our drug candidates are subject to delays, and may not be completed or granted on expected timetables, if at all, and such delays may increase our costs and could delay our ability to generate revenue;*
- *the regulatory approval process;*
- *our ability to attract and retain key personnel;*
- *our ability to obtain patent protection;*
- *our ability to protect our intellectual property rights and not infringe on the intellectual property rights of others;*
- *our ability to comply with applicable governmental regulations and standards;*
- *development or commercialization of similar products by our competitors, many of which are more established and have or have access to greater financial resources than us;*
- *commercialization limitations imposed by intellectual property rights owned or controlled by third parties;*
- *our business is subject to potential product liability and other claims;*
- *our ability to maintain adequate insurance at acceptable costs;*
- *further equity financing may substantially dilute the interests of our shareholders;*
- *changing market conditions; and*
- *other risks detailed from time-to-time in our on-going quarterly filings, annual information forms, annual reports and annual filings with Canadian securities regulators and the SEC, and those which are discussed under the heading "Risk Factors" in this document.*

Should one or more of these risks or uncertainties materialize, or should the assumptions set out in the section entitled "Risk Factors" underlying those forward-looking statements prove incorrect, actual results may vary materially from those described herein. These forward-looking statements are made as of the date of this management's discussion and analysis or, in the case of documents incorporated by reference herein, as of the date of such documents, and we do not intend, and do not assume any obligation, to update these forward-looking statements, except as required by law. We cannot assure you that such statements will prove to be accurate as actual results and future events could differ materially from those anticipated in such statements. Investors are cautioned that forward-looking statements are not guarantees of future performance and accordingly investors are cautioned not to put undue reliance on forward-looking statements due to the inherent uncertainty therein.

## LIQUIDITY AND CAPITAL RESOURCES

Since its inception, Lorus Therapeutics Inc. ("Lorus", the "Company", "we", "our", "us" and similar expressions) has financed its operations and technology acquisitions primarily from equity and debt financing, proceeds from the exercise of warrants and stock options, and interest income on funds held for future investment. We plan to continue our development programs from internal resources, as they are available.

There is substantial doubt about the Company's ability to continue as a going concern because management has forecasted that the Company's current level of cash and cash equivalents will not be sufficient to execute its current planned expenditures for the next 12 months without further investment. The Company is currently in discussion with several potential investors to provide additional funding. Management believes that it will complete one or more of these arrangements in sufficient time to continue to execute its planned expenditures without interruption. However, there can be no assurance that the capital will be available as necessary to meet these continuing expenditures, or if the capital is available, that it will be on terms acceptable to the Company. The issuance of common shares by the Company could result in substantial dilution in the equity interest of existing shareholders. The Company is also considering alternatives to delay its research programs until financing is available, amongst other cost savings measures. There can be no assurance that the Company will be able to obtain sufficient financing to meet future operational needs. As a result, there is a substantial doubt as to whether the Company will be able to continue as a going concern and realize its assets and pay its liabilities as they fall due.

The Management's Discussion and Analysis ("MD&A") does not reflect the adjustments that would be necessary should the Company be unable to continue as a going concern and therefore be required to realize its assets and liquidate its liabilities and commitments in other than the normal course of business and at amounts different from those in the accompanying unaudited condensed consolidated interim financial statements. Such amounts could be material.

This MD&A is prepared as of April 12, 2012. It contains certain forward-looking statements that involve known and unknown risks and uncertainties which are beyond the control of the Company. This MD&A should be read in conjunction with the unaudited condensed consolidated interim financial statements of the Company for the three months and nine months ended February 29, 2012 which are incorporated by reference herein and form an integral part of this MD&A.

## OVERVIEW

Lorus is a development stage life sciences company focused on the discovery, research and development of effective anticancer therapies with a high safety profile. Lorus has worked to establish a diverse anticancer product pipeline, with products in various stages of development ranging from pre-clinical to a completed Phase II clinical trial. A growing intellectual property portfolio supports our diverse product pipeline.

We believe that the future of cancer treatment and management lies in drugs that are effective, have minimal side effects, and therefore improve a patient's quality of life. Many drugs currently approved for the treatment and management of cancer are toxic with severe side effects, and we therefore believe that a product development plan based on effective and safe drugs could have broad applications in cancer treatment. Lorus' strategy is to continue the development of our product pipeline using several therapeutic approaches. Each therapeutic approach is dependent on different technologies, which we believe mitigates the development risks associated with a single technology platform. We evaluate the merits of each product throughout the clinical trial process and consider commercial viability as appropriate. The most advanced anticancer drugs in our pipeline, each of which flow from different platform technologies, are small molecules, immunotherapeutics and antisense.

Our business model is to take our product candidates through pre-clinical testing and into Phase I and Phase II clinical trials. It is our intention to then partner or co-develop these drug candidates after successful completion of Phase I or II clinical trials. Lorus will give careful consideration in the selection of partners that can best advance its drug candidates into a pivotal Phase III clinical trial and, upon successful results, commercialization. Our objective is to receive upfront and milestone payments as well as royalties from such partnerships, which will support continued development of our other product candidates.

Our success is dependent upon several factors, including, maintaining sufficient levels of funding through public and/or private financing, establishing the efficacy and safety of our products in clinical trials and securing strategic partnerships.

Our net loss for the three months ended February 29, 2012 was \$1.0 million (\$0.05 per share) compared to \$1.5 million (\$0.10 per share) in the same period in the prior year. The Company incurred a net loss of \$3.6 million (\$0.18 per share) for the nine months ended February 29, 2012 compared to \$3.9 million (\$0.32 per share) during the same period in the prior year.

The decrease in net loss in the three and nine month periods ended February 29, 2012 is due to lower general and administrative and research and development expenditures. In the three month period ended February 29, 2012 research and development costs were lower in the current period due to reduced program spending and general and administrative expenses were also lower in the current period due primarily to reduced stock based compensation expense due to option grants in November in the current year compared with December in the prior year. In the nine month period ended February 29, 2012 net loss was reduced due to lower research and development costs in the current year due to reduced program spending.

We utilized cash of \$740 thousand in our operating activities in three-month period ended February 29, 2012 compared with \$1.7 million during the same period in the prior year. For the nine months ended February 29, 2012 we utilized cash of \$2.6 million compared with \$4.9 million in the same period last year. The decrease in cash utilized in the three and nine months ended February

29, 2012 compared with the same periods in the prior year is due to lower spending in the current year as well as the advancement of promissory notes in the current year compared with repayment of outstanding promissory notes in the prior year.

At February 29, 2012, we had cash and cash equivalents of \$103 thousand compared to \$911 thousand at May 31, 2011. On November 28, 2011, the Company issued a grid promissory note to Mr. Abramson, a director of Lorus that allows Lorus to borrow funds of up to \$1.8 million. The funds may be borrowed at a rate of up to \$300 thousand per month, incur interest at a rate of 10% per year and are due and payable on November 28, 2012. At February 29, 2012 \$300 thousand had been drawn under the promissory note and subsequent to the quarter end on March 12, 2012 an additional \$300 thousand was drawn down for total balance owing of \$600 thousand and \$1.2 million available for use.

## RESULTS OF OPERATIONS

### Research and Development

Research and development expenses totaled \$543 thousand in the three-month period ended February 29, 2012 compared to \$847 thousand during the same period in the prior year and totaled \$1.8 million in the nine month period ended February 29, 2012 as compared to \$2.0 million in the same period in the prior year. Research and development expenses consisted of the following:

	Three months ended February 29/28		Nine months ended February 29/28	
	2012	2011	2012	2011
Program costs (see below)	524	760	1,622	1,852
Stock based compensation	11	78	132	100
Depreciation of equipment	8	9	25	29
	543	847	1,779	1,981

### Program costs by program:

	Three months ended		Nine months ended	
	Feb 29, 2012	Feb 28, 2011	Feb 29, 2012	Feb 28, 2011
Small molecules	\$ 524	\$ 540	\$ 1,622	\$ 1,344
RNA-Targeted Therapies	—	220	—	508
Immunotherapy	—	—	—	—
<b>Total</b>	<b>\$ 524</b>	<b>\$ 760</b>	<b>\$ 1,622</b>	<b>\$ 1,852</b>

The decrease in research and development costs during the three months ended February 29, 2012 compared with the prior year is due to decreased stock based compensation expense related to options granted in November in the current year and December in the prior year as well as lower program costs. After eliminating the effect of the non-cash stock based compensation expense, research and development expenses would be \$532 thousand in the three months ended February 29, 2012 compared with \$769 thousand in the same period in the prior year due to reduced program expenditures due primarily to no further spending on our RNA-targeted therapies and therefore lower personnel and development costs. In the prior year we incurred costs related to the development of a Phase III clinical trial protocol. Spending on our small molecule program is consistent year over year as the Phase I clinical trial was initiated in January 2011 and is still ongoing.

For the nine month period ended February 29, 2012 research and development spending decreased to \$1.8 million compared with \$2.0 million in the same period in the prior year. The decrease is attributable to a reduction in program spending to \$1.6 million compared with \$1.9 million in the same period in the prior year. The decrease from the prior year is due to no further spending on our RNA-targeted therapies, compared with \$508 thousand in the prior year. This reduction is offset by higher resources allocated to the development of our small molecule program, in particular the ongoing Phase I clinical trial for LOR-253 and the LOR-500 discovery program.

### General and Administrative

General and administrative expenses totaled \$479 thousand in the three-month period ended February 29, 2012 compared to \$701 thousand in same period in the prior year. For the nine month period ended February 29, 2012, general and administrative expenses were \$1.8 million compared with \$1.9 million in the same period in the prior year.

### Components of general and administrative expenses:

	Three months ended February 29/28		Nine months ended February 29/28	
	2012	2011	2012	2011
General and administrative excluding salaries	303	294	960	1,106
Salaries	163	232	521	573
Stock based compensation	10	170	336	183
Depreciation of equipment	3	5	8	13
	479	701	1,825	1,875

General and administrative expenses excluding salaries were consistent in the three months ended February 29, 2012 compared with the prior year. In the nine months ended February 29, 2012 general and administrative expenses excluding salaries were lower than the prior year due to financing fees incurred in the prior year related to a terminated financing. This was partially offset by higher audit related fees due to additional review work and the transition to IFRS in the current year. In the three and nine month periods ended February 29, 2012 salary costs compared with the prior year were lower due to a reduction in headcount in the current year.

Stock based compensation expense was lower in the three month periods ended February 29, 2012 compared with the same period in the prior year due to options issued in November in the current year compared with December in the prior year. As a result of immediate vesting of certain options the expense tends to be higher in the quarter the options are issued compared with subsequent quarters. Stock based compensation expense was higher in the nine month periods ended February 29, 2012 compared with the same period in the prior year due to certain one time grants in the current year and the cancellation of certain outstanding options (resulting in the acceleration of expense) which increased stock based compensation charges.

#### **Finance Expense**

Finance expense for the three months ended February 29, 2012 was \$3 thousand compared with \$nil for the three months ended February 28, 2011. For the nine months ended February 29, 2012 finance expense was \$3 thousand compared with \$71 thousand in the same period in the prior year. Finance expense incurred in the prior year relates to interest accrued at a rate of 10% on the related party promissory notes repaid in November 2010 described below. Interest expense incurred in the three and nine months ended February 29, 2012 relates to the \$300 thousand drawn on the \$1.8 million grid promissory note at a rate of 10% described below.

#### **Finance Income**

Finance income totaled \$2 thousand and \$6 thousand in the three and nine month periods ended February 29, 2012, respectively, compared to \$6 thousand and \$10 thousand in the same periods in the prior year. Finance income represents interest earned on our cash and cash equivalent balances.

#### **Net loss for the period**

Our net loss for the three months ended February 29, 2012 was \$1.0 million (\$0.05 per share) compared to \$1.5 million (\$0.10 per share) in the same period in the prior year. The Company incurred a net loss of \$3.6 million (\$0.18 per share) for the nine months ended February 29, 2012 compared to \$3.9 million (\$0.32 per share) during the same period in the prior year.

The decrease in research and development costs during the three months ended February 29, 2012 compared with the prior year is due to decreased stock based compensation expense related to options granted in November in the current year and December in the prior year as well as reduced program expenditures due primarily to no further spending on our RNA-Targeted Therapies. In the prior year we incurred costs related to the development of a Phase III clinical trial protocol. Spending on our small molecule program is consistent year over year as the Phase I clinical trial was initiated in January 2011 and is still ongoing. For the nine month period ended February 29, 2012 the decrease in research and development spending is attributable to a reduction in program spending due to no further spending on our RNA-targeted therapies. This reduction was offset by higher resources allocated to the development of our small molecule program and the LOR-253 Phase 1 clinical trial underway as well as the LOR-500 discovery program.

General and administrative stock based compensation expense was lower in the three month periods ended February 29, 2012 compared with the same period in the prior year due to options issued in November in the current year compared with December in the prior year. Due to immediate vesting of certain options the expense tends to be higher in the quarter the options are issued compared with subsequent quarters. General and administrative stock based compensation expense was higher in the nine month periods ended February 29, 2012 compared with the same period in the prior year due to certain one time grants in the current year and the cancellation of certain outstanding options (resulting in the acceleration of expense) which increased stock based compensation charges. In the nine months ended February 29, 2012 general and administrative expenses excluding salaries were lower due to financing fees incurred in the prior year related to a terminated financing offset by higher audit related fees due to additional review work and the transition to IFRS.

#### **PROMISSORY NOTES PAYABLE**

Pursuant to the commitment letter (described under 'Unit Financing') provided by Mr. Abramson, the Company has issued a grid promissory note to Mr. Abramson that allows Lorus to borrow funds up to \$1.8 million. The funds may be borrowed at a rate of up to \$300 thousand per month, incur interest at a rate of 10% per year and are due and payable in full on November 28, 2012. The promissory note is subject to certain covenants which, if breached, could result in the promissory note becoming payable on demand. The covenants include:

- failure to pay any or all interest payable when due;
- ceasing or threaten to cease to carry on the business currently being carried on by Lorus or a substantial portion thereof or makes or agrees to make an assignment, disposition or conveyance,;
- Lorus is an insolvent person or commits or threatens to commit any act of bankruptcy;
- Lorus proceeds or takes steps towards the dissolution, liquidation or winding up of the Company.

Lorus is not aware of any breach in these covenants and has not received notice of any breach of these covenants by Mr. Abramson,

At February 29, 2012 \$300 thousand has been drawn under the promissory note and subsequent to the quarter end on March 12, 2012 an additional \$300 thousand has been drawn down for a total balance owing of \$600 thousand and \$1.2 million available for use.

In April 2010, the Company entered into a loan agreement with a company related to Mr. Abramson to borrow \$1 million. The loan amount, which was received on April 14, 2010, was unsecured, evidenced by a promissory note and bore interest at the annual rate of 10%. The principal and interest amount were due in six months and later extended a further three months. The principal amount was repaid in November 2010.

## **WARRANT REPRICING**

On November 29, 2011 shareholders of the Company (excluding insiders who also held warrants) approved a resolution to amend the exercise price of certain outstanding warrants from \$1.33 to the 5 day volume weighted average trading price on the Toronto Stock Exchange five days prior to approval plus a 10% premium. The revised warrant exercise price is \$0.28. The Company calculated an increased value attributed to the warrants of \$239 thousand related to the amendment. This increase was calculated by taking the Black Scholes value of the warrants immediately before the amendment and immediately after the amendment. There are 4.2 million warrants which were amended and of those 3.6 million are held by Mr. Abramson, a director of the Company.

## **UNIT FINANCING**

### *August 2011*

On July 22, 2011, Lorus filed a final short-form prospectus in connection with a best efforts offering (the "Offering") of a minimum of 5,000,000 units of the Company (the "Units") at a price of \$0.40 per Unit for gross proceeds of \$2,000,000 and a maximum of 10,000,000 Units for gross proceeds of \$4,000,000. Each Unit consisted of one common share of Lorus (a "Common Share") and one common share purchase warrant of Lorus (a "Warrant"). Each Warrant entitles the holder to purchase one Common Share for five years after the closing of the Offering at an exercise price of \$0.45 per Common Share (the "Exercise Price"). If on any date (the "Accelerated Exercise Date") the 10-day volume weighted average trading price of the Common Shares on the Toronto Stock Exchange equals or exceeds 200% of the Exercise Price, then upon the Company sending the holders of Warrants written notice of such Accelerated Exercise Date and issuing a news release announcing such Accelerated Exercise Date, the Warrants shall only be exercisable for a period of 30 days following the date on which such written notice is sent to holders of Warrants.

In connection with the Offering, Herbert Abramson, a director of Lorus, entered into an irrevocable commitment letter on June 20, 2011, and amended July 11, 2011, to purchase, directly or indirectly, common shares and common share purchase warrants (or as may otherwise be agreed) in the capital of Lorus (collectively the "Securities") having an aggregate subscription price equal to the difference (the "Commitment Amount"), if any, between (a) the sum of (i) the gross proceeds realized by Lorus in the Offering and (ii) the gross proceeds received by Lorus in respect of all financings completed by Lorus from the date of the final short-form prospectus to November 30, 2011 and (b) \$4.0 million.

The Offering closed on August 15, 2011 for total gross proceeds of \$2.2 million. In connection with the Offering, Lorus has issued 5.5 million Common Shares and 5.5 million Warrants. Mr. Abramson purchased 2.4 million Units as part of the Offering.

The total costs associated with the transaction were approximately \$395 thousand which included the \$25 thousand which represented the fair value of the brokers' services provided as part of the Offering. Each broker warrant is exercisable for one Unit at a price of \$0.40 per Unit for a period of 24 months following the closing of the Offering. The Company has allocated the net proceeds of the Offering to the common shares and the common share purchase warrants based on their estimated relative fair values. Based on relative fair values, \$1.2 million of the net proceeds were allocated to the common shares and \$609 thousand to the common share purchase warrants.

## **PRIVATE PLACEMENT**

### *December 2010*

On December 1, 2010, pursuant to a private placement, the Company issued 1.6 million common shares in exchange for gross cash consideration of \$1.66 million. The total costs associated with the transaction were approximately \$20 thousand. Mr. Herbert Abramson, a director of the Corporation, subscribed for 1,410,000 common shares, representing approximately 89% of the total number of common shares issued through the private placement. No commission was paid in connection with the private placement.

## **RIGHTS OFFERING**

### *November 2010*

On August 27, 2010 the Company announced a proposed rights offering as described below including a \$4 million standby purchase agreement from a director of the Company, Mr. Herbert Abramson. Mr. Abramson also provided the Company with interim financing by way of three \$500 thousand monthly loans, advanced on August 11, 2010, September 13, 2010 and October 5, 2010. The loans were unsecured, had a six-month term (or the earlier of the closing of the rights issue) and bore interest at the annual rate of 10%. All three notes were repaid upon the close of the rights offering described below.

On September 27, 2010 Lorus filed a final short form prospectus in each of the provinces of Canada in connection with a distribution to its shareholders in eligible jurisdictions outside the United States of rights exercisable for units of the Company (the "Rights Offering").

Under the Rights Offering, holders of common shares of the Company as of October 12, 2010, the record date, received one right for each common share held as of the record date. Each two rights entitled the holder thereof to purchase a unit of the Company at a price of \$1.11 per unit. Each unit consisted of one common share of the Company and one warrant to purchase an additional common share of the Company at a price of \$1.33 until May 2012.



A total of 4.2 million units of the Company at a price of \$1.11 per unit were issued in connection with the Rights Offering. As a result of the Rights Offering Lorus issued 4.2 million common shares and 4.2 million common share purchase warrants for net proceeds of \$4.2 million.

In connection with the rights offering, the Company secured a standby purchase arrangement of \$4 million by Herbert Abramson, one of Lorus' directors. Mr. Abramson agreed to make an investment such that the minimum gross proceeds of the proposed rights offering would be \$4 million. No fee was payable to Mr. Abramson for this commitment. In accordance with the terms of the stand-by purchase agreement, Mr. Abramson subscribed for 3.6 million of the 4.2 million units of the offering for \$4.0 million.

The total costs associated with the transaction were approximately \$370 thousand. The Company has allocated the net proceeds of the Rights Offering to the common shares and the common share purchase warrants based on their relative fair values. Based on relative fair values, \$3.2 million of the net proceeds were allocated to the common shares and \$1.0 million to the common share purchase warrants.

#### RELATED PARTY TRANSACTIONS

In October 2009, the Company entered into a loan agreement with a member of its Board of Directors, Mr. Abramson, to borrow \$1 million. The loan amount, which was received on October 6, 2009, was unsecured, evidenced by a promissory note and bears interest at the annual rate of 10%. The principal and interest were due in six months. The principal amount of \$1 million was applied to subscribe for Units as part of the November 27, 2009 private placement.

On August 27, 2010 the Company announced a proposed rights offering as described in note 9(b) including a \$4 million standby purchase agreement from a director of the Company, Mr. Herbert Abramson. Mr. Abramson also provided the Company with interim financing by way of three \$500 thousand monthly loans, advanced on August 11, 2010 (outstanding at August 31, 2010), September 13, 2010 and October 5, 2010. The loans were unsecured, had a six-month term (or the earlier of the closing of the rights issue) and bore interest at the annual rate of 10%. All three notes were repaid upon the close of the rights offering described under 'Rights Offering' above.

These transactions were in the normal course of business and have been measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

See also 'Promissory Notes Payable', 'Unit Financing', 'Rights Offering' and 'Private Placement' for additional related party transactions and details.

#### WARRANT EXPIRY

The warrants issued on November 27, 2009 expired unexercised on May 27, 2011. This expiry resulted in a transfer of the value attributed to the expired warrants of \$622 thousand to contributed surplus.

The warrants issued on August 7, 2008 expired unexercised on August 10, 2010. This expiry results in a transfer of the value attributed to the expired warrants of \$417 thousand to contributed surplus.

#### QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

The selected financial information provided below is derived from the Company's unaudited quarterly financial statements for each of the last eight quarters.

Research and development expenditures have been consistent over the past eight quarters with increased activity in the quarter ended February 28, 2011 resulting from the initiation of the Phase I clinical trial for LOR-253 and associated activities.

The increased general and administrative costs in the quarter ended November 30, 2011 is due to one time stock option grants and cancellations during the quarter which resulted in higher than normal options expense. The increase in general and administrative costs for the quarter ended May 31, 2010 is due to the write off of \$569 thousand in costs associated with a terminated financing initiative. Increased expense in the quarter February 28, 2011 was due to one time stock option expense related to a large tranche of options with partially immediate vesting.

Cash used in operating activities fluctuates significantly due primarily to increases and decreases in the accounts payables, accrued liabilities and promissory notes payable balances.

	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
<i>(Amounts in 000's except for per common share data)</i>	Feb 29, 2012	Nov 30, 2011	Aug 31, 2011	May 31, 2011	Feb 28, 2011	Nov. 30, 2010	Aug. 31, 2010	May 31, 2010
	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	CGAAP
Revenue	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Research and development expense	543	648	588	536	847	621	514	601
General and administrative expense	479	811	535	545	701	556	618	1,173
Net (loss)	(1,023)	(1,457)	(1,121)	(1,077)	(1,542)	(1,220)	(1,156)	(1,820)

Basic and diluted

net (loss) per share	\$(0.05)	\$(0.07)	\$(0.06)	\$(0.07)	\$ (0.10)	\$ (0.11)	\$ (0.12)	\$ (0.18)
Cash used in operating activities	\$(740)	\$(811)	\$(1,077)	\$(934)	\$(1,676)	\$(2,560)	\$ (661)	\$(271)

## CASH POSITION AND OUTLOOK

At February 29, 2012, we had cash and cash equivalents of \$103 thousand compared to \$911 thousand at May 31, 2011. In addition, pursuant to the commitment letter (described under 'Unit Financing') provided by Mr. Abramson, the Company has issued a grid promissory note to Mr. Abramson that will allow Lorus to borrow funds up to \$1.8 million. The funds may be borrowed at a rate of up to \$300 thousand per month, incur interest at a rate of 10% per year and are due and payable on November 28, 2012. As at February 29, 2012 the Company had drawn \$300 thousand on this grid promissory note with \$1.5 million available for future use. Subsequent to the quarter end, on March 9, 2012, the Company drew down an additional \$300 thousand leaving \$1.2 million available for use as at April 12, 2012. The Company invests in highly rated and liquid debt instruments. Investment decisions are made in accordance with an established investment policy administered by senior management and overseen by the board of directors. Working capital (representing primarily cash, cash equivalents and other current assets less current liabilities) at February 29, 2012 was negative \$1.1 million. The Company has the ability to draw down the promissory note discussed above to pay its liabilities as they come due (see 'Subsequent Events' section below).

As discussed above, management has forecasted that the Company's current level of cash and cash equivalents will not be sufficient to execute its current planned expenditures for the next twelve months without further investment. The Company is currently investigating various alternatives to obtain sufficient capital to continue its operations and has implemented a series of strategies to reduce research, development and overhead expenditures until such time as it can obtain additional capital to fund its operations.

If we are able to secure additional financing, we intend to use these resources to fund our existing drug development programs and develop new programs from our portfolio of preclinical research technologies. The amounts actually expended for research and drug development activities and the timing of such expenditures will depend on many factors, including the ability of the Company to raise additional capital, the progress of the Company's research and drug development programs, the results of preclinical and clinical trials, the timing of regulatory submissions and approvals, the impact of any internally developed, licensed or acquired technologies, our ability to find suitable partnership agreements to assist financially with future development, the impact from technological advances, determinations as to the commercial potential of the Company's compounds and the timing and development status of competitive products.

We do not expect to generate positive cash flow from operations in the next several years due to additional research and development costs, including costs related to drug discovery, preclinical testing, clinical trials, manufacturing costs and operating expenses associated with supporting these activities. Negative cash flow will continue until such time, if ever, that we receive regulatory approval to commercialize any of our products under development and/or royalty or milestone revenue from any such products exceeds expenses.

Until one of our drug candidates receives regulatory approval and is successfully licensed or commercialized, Lorus will continue to incur operating losses. The magnitude of these operating losses will be largely affected by the timing and scope of future research and development, clinical trials and the Company's ability to raise additional working capital and/or establish effective partnerships to share the costs of development and clinical trials.

### Contractual Obligations and Off-Balance Sheet Financing

#### (a) Operating lease commitments:

The Company has entered into operating leases for premises and equipment under which it is obligated to make minimum annual payments as described below:

	Less than 1 year	1-3 years	3-5 years	Total
Operating leases	150	25	7	182

The Company's current facility lease expires in March 2013.

#### (b) Other contractual commitments:

The Company holds an exclusive world-wide license from the University of Manitoba (the "University") and Cancer Care Manitoba ("CCM") to certain patent rights to develop and sub-license certain oligonucleotide technologies. In consideration for the exclusive license of the patent rights, the University and CCM are entitled to an aggregate of 1.67% of the net sales received by the Company from the sale of products or processes derived from the patent rights and 1.67% of all monies received by the Company from sub-licenses of the patent rights. Any and all improvements to any of the patent rights derived in whole or in part by the Company after the date of the license agreement, being June 20, 1997, are not included within the scope of the agreement and do not trigger any payment of royalties.

The Company has not yet earned any revenue from the products covered under this agreement and, therefore, has not paid any royalties thereunder and cannot reasonably predict the timing and amount of any future payment. The Company does not expect to make any royalty payments under this agreement in fiscal years ended May 31, 2012 or 2013, and cannot reasonably predict when such royalties will become payable, if at all.

The Company has entered into various contracts with service providers with respect to the LOR-253 phase I clinical trial. These contracts could result in future payment commitments of approximately \$860 thousand. Of this amount \$360 thousand has been accrued or paid at February 29, 2012 (May 31, 2011 - \$248 thousand). The payments will be based on services performed and amounts may be higher or lower based on actual services performed.

(c) Guarantees:

The Company entered into various contracts, whereby contractors perform certain services for the Company. The Company indemnifies the contractors against costs, charges and expenses in respect of legal actions or proceedings against the contractors in their capacity of servicing the Company. The maximum amounts payable from these guarantees cannot be reasonably estimated. Historically, the Company has not made significant payments related to these guarantees.

The Company indemnifies its directors and officers against any and all claims or losses reasonably incurred in the performance of their service to the Company to the extent permitted by law. The Company has acquired and maintains liability insurance for its directors and officers. The fair value of this indemnification is not determinable.

(d) Indemnification on Arrangement:

On July 10, 2007, Lorus completed a plan of arrangement and corporate reorganization whereby the assets and liabilities of Lorus were transferred from one corporate entity ("Old Lorus") into a new corporate entity which continued to operate as Lorus Therapeutics Inc. Under the arrangement, the Company agreed to indemnify Old Lorus and its directors, officers and employees from and against all damages, losses, expenses (including fines and penalties), other third party costs and legal expenses, to which any of them may be subject arising out of any matter occurring:

- (i) prior to, at or after the effective time of the arrangement ("Effective Time") and directly or indirectly relating to any of the assets of Old Lorus transferred to the Company pursuant to the arrangement (including losses for income, sales, excise and other taxes arising in connection with the transfer of any such asset) or conduct of the business prior to the Effective Time;
- (ii) prior to, at or after the Effective Time as a result of any and all interests, rights, liabilities and other matters relating to the assets transferred by Old Lorus to the Company pursuant to the arrangement; and
- (iii) prior to or at the Effective Time and directly or indirectly relating to, with certain exceptions, any of the activities of Old Lorus or the arrangement.

The Company recorded a liability of \$100 thousand, which it believes to be a reasonable estimate of the fair value of the obligation for the indemnifications provided as at February 29, 2012. There have been no claims on this indemnification to date.

As of February 29, 2012 the Company has not entered into any off-balance sheet arrangements.

## **CAPITAL RISK MANAGEMENT**

The Company's objectives when managing capital are to:

- Maintain its ability to continue as a going concern in order to provide returns to shareholders and benefits to other stakeholders;
- Maintain a flexible capital structure which optimizes the cost of capital at acceptable risk;
- Ensure sufficient cash resources to fund its research and development activity, to pursue partnership and collaboration opportunities and to maintain ongoing operations.

The capital structure of the Company consists of cash and cash equivalents and equity comprised of share capital, share purchase warrants, stock options, contributed surplus and deficit. The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share issuances, acquiring or disposing of assets, adjusting the amount of cash balances or by undertaking other activities as deemed appropriate under the specific circumstances.

Pursuant to the commitment letter (described under 'Unit Financing') provided by Mr. Abramson, the Company has issued a grid promissory note to Mr. Abramson that will allow Lorus to borrow funds up to \$1.8 million and as of April 12, 2012 \$600 thousand has been drawn on this facility leaving \$1.2 million available for future use. The funds may be borrowed at a rate of up to \$300 thousand per month, incur interest at a rate of 10% per year and are due and payable on November 28, 2012.

The Company is not subject to externally imposed capital requirements.

While the Company's overall strategy with respect to capital risk management remains unchanged from the year ended May 31, 2011, the Company has forecasted that its current capital resources are not sufficient to carry out its research and development plans and operations for more than the next twelve months and continues to investigate various alternatives to obtain sufficient capital to continue its operations.

## **RISK FACTORS**

Before making an investment decision with respect to our common shares, you should carefully consider the following risk factors, in addition to the other information included or incorporated by reference into this report. The risks set out below are not the only risks we face. If any of the following risks should be realized, our business, financial condition, prospects or results of operations would likely

suffer. In that case, the trading price of our common shares could decline and you may lose all or part of the money you paid to buy our common shares.

**Please refer to our MD&A for the year ended May 31, 2011 for a complete discussion of risks and uncertainties.**

- We are at an early stage of development. Significant additional investment will be necessary to complete the development of any of our products.
- Our ability to continue as a going concern.
- We need to raise additional capital. The cash and cash equivalents on hand are not sufficient to execute our operating strategies for the next twelve months and we may not be able to raise sufficient funds to continue operations.
- Further equity financings may substantially dilute the interests of our shareholders.
- We have a history of operating losses. We expect to incur net losses and we may never achieve or maintain profitability.
- We may be unable to obtain partnerships for one or more of our product candidates which could curtail future development and negatively impact our share price.
- There is no assurance that an active trading market in our common shares will be sustained.
- Clinical trials are long, expensive and uncertain processes and Health Canada or the FDA may ultimately not approve any of our product candidates. We may never develop any commercial drugs or other products that generate revenues.
- We have indemnified Old Lorus and its directors, officers and employees in respect of the Arrangement.
- As a result of intense competition and technological change in the pharmaceutical industry, the marketplace may not accept our products or product candidates, and we may not be able to compete successfully against other companies in our industry and achieve profitability.
- We may be unable to obtain patents to protect our technologies from other companies with competitive products, and patents of other companies could prevent us from manufacturing, developing or marketing our products.
- Our products and product candidates may infringe the intellectual property rights of others, which could increase our costs.
- Our share price has been and may continue to be volatile and an investment in our common shares could suffer a decline in value.
- Future sales of our common shares by us or by our existing shareholders could cause our share price to fall.

## FINANCIAL INSTRUMENTS

### (a) Financial instruments

The Company has classified its financial instruments as follows:

	As at February 29, 2012	As at May 31, 2011	As at June 1, 2010
<b>Financial assets</b>			
Cash and cash equivalents, consisting of guaranteed investment certificates, held for trading, measured at fair value through loss or profit	\$ 103	\$ 911	\$ 667
Short-term investments, held-for-trading, recorded at fair value through loss or profit	—	—	247
<b>Financial liabilities</b>			
Accounts payable, measured at amortized cost	117	215	387
Accrued liabilities, measured at amortized cost	1,160	944	1,458
Promissory note payable, measured at amortized cost	300	—	1,000

At February 29, 2012, there are no significant differences between the carrying values of these amounts and their estimated market values due to their short-term nature.

### (b) Financial risk management

The Company has exposure to credit risk, liquidity risk and market risk. The Company's Board of Directors has the overall responsibility for the oversight of these risks and reviews the Company's policies on an ongoing basis to ensure that these risks are appropriately managed.

#### (i) Credit risk

Credit risk is the risk of financial loss to the Company if a customer, partner or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's cash and cash equivalents. The carrying amount of the financial assets represents the maximum credit exposure.

The Company manages credit risk for its cash and cash equivalents by maintaining minimum standards of R1-low or A-low investments and the Company invests only in highly rated Canadian corporations with debt securities that are traded on active markets and are capable of prompt liquidation.

#### **(ii) Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. To the extent that the Company does not believe it has sufficient liquidity to meet its current obligations, the Board considers securing additional funds through equity, debt or partnering transactions. The Company manages its liquidity risk by continuously monitoring forecasts and actual cash flows. Refer to note 2(b) of the third quarter interim financial statements for further discussion on the Company's ability to continue as a going concern.

#### **(iii) Market risk**

Market risk is the risk that changes in market prices, such as interest rates, foreign exchange rates and equity prices will affect the Company's income or the value of its financial instruments.

The Company is subject to interest rate risk on its cash and cash equivalents and short-term investments. The Company does not believe that the results of operations or cash flows would be affected to any significant degree by a sudden change in market interest rates relative to interest rates on the investments, owing to the relative short-term nature of the investments. The Company does not have any material interest bearing liabilities subject to interest rate fluctuations.

Financial instruments potentially exposing the Company to foreign exchange risk consist principally of accounts payable and accrued liabilities. The Company holds minimal amounts of U.S. dollar denominated cash, purchasing on an as needed basis to cover U.S. dollar denominated payments. At February 29, 2012, U.S. dollar denominated accounts payable and accrued liabilities amounted to \$238 thousand (February 28, 2011 - \$260 thousand). Assuming all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the U.S. dollar would result in an increase or decrease in loss for the year and comprehensive loss of \$24 thousand (February 28, 2011 - \$26 thousand). The Company does not have any forward exchange contracts to hedge this risk.

The Company does not invest in equity instruments of other corporations.

#### **(c) Capital management**

The Company's primary objective when managing capital is to ensure that it has sufficient cash resources to fund its development and commercialization activities and to maintain its ongoing operations. To secure the additional capital necessary to pursue these plans, the Company may attempt to raise additional funds through the issuance of equity or by securing strategic partners.

The Company includes cash and cash equivalents and short-term deposits in the definition of capital.

The Company is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital management strategy during the three months ended February 29, 2012.

### **TRANSITION TO IFRS**

On June 1, 2011, the Company adopted International Financial Reporting Standards ("IFRS") for financial reporting purposes, with a transition date of June 1, 2010, from the previous standard of Canadian Generally Accepted Accounting Principles ("GAAP"). As is required for all Canadian public companies, Q1 2012 was the first interim reporting period under IFRS. The process to completion was intensive and taxing on the resources of a small finance team at Lorus, but was successfully completed on schedule. While there was no material impact to financial results from the transition, readers of the unaudited consolidated interim financial statements for Q1 and subsequently Q2 and Q3 2012 the reader will note the significant differences in the IFRS reporting requirements. Readers are encouraged to pay particular attention to Note 15 of those financial statements for a comprehensive discussion of the financial impact of the transition to IFRS.

The accounting policies disclosed in Note 3 to the interim financial statements have been applied in preparing our consolidated financial statements as at and for the three and nine months ended February 29, 2012, the comparative information presented as at and for the three and nine months ended February 28, 2011 and the year ended May 31, 2011 and in the preparation of our opening IFRS balance sheet at June 1, 2010 (our date of transition) and the statement of financial position as at May 31, 2011.

IFRS 1 requires first time adopters to retrospectively apply all effective IFRSs as of the reporting date. However, it also provides for certain optional exemptions and certain mandatory exceptions for the first time IFRS adopters. Details of the Company's initial elections of IFRS 1 exemptions are described below.

In preparing our opening balance sheet, we have adjusted amounts reported previously in our consolidated financial statements prepared in accordance with Canadian GAAP. An explanation of how the transition from Canadian GAAP to IFRS has affected our financial position, financial performance and cash flows is set out in the following tables and notes that accompany the tables.

#### **Initial elections upon adoption of IFRS**

Under IFRS 1 the following applicable exemption applied to the Company's conversion from Canadian GAAP to IFRS.

- (i) Share Based Payments:** The Company elected not to apply IFRS 2 to equity instruments that vested before the date of transition to IFRS.

(ii) **Business combinations:** The Company applied the business combinations exemption to not apply IFRS 3, *Business Combinations*, retrospectively to past business combinations. Accordingly, we have not restated business combinations that took place prior to the Transition Date. In addition, and as a condition under IFRS 1 for applying this exemption, goodwill relating to business combinations that occurred prior to the Transition Date was tested for impairment as described in note 15 (b)(i) to the interim financial statements.

## Reconciliation of financial position and shareholders' equity

	Notes	June 1, 2010			May 31, 2011		
		Canadian GAAP	Effect of transition to		Canadian GAAP	Effect of transition to	
			IFRS	IFRS		IFRS	IFRS
<b>Current</b>							
Cash and cash equivalents		\$ 667	\$ -	\$ 667	911	-	911
Short-term investments		247	-	247	-	-	-
Prepaid expenses and other assets		636	-	636	388	-	388
<b>Total Current Assets</b>		<b>1,550</b>	<b>-</b>	<b>1,550</b>	<b>1,299</b>	<b>-</b>	<b>1,299</b>
<b>Non-Current</b>							
Equipment		147	-	147	99	-	99
Goodwill	(b) (i)	606	(606)	-	606	(606)	-
<b>Total Non-Current Assets</b>		<b>753</b>	<b>(606)</b>	<b>147</b>	<b>705</b>	<b>(606)</b>	<b>99</b>
<b>Total Assets</b>		<b>2,303</b>	<b>(606)</b>	<b>1,697</b>	<b>2,004</b>	<b>(606)</b>	<b>1,398</b>
<b>LIABILITIES</b>							
<b>Current</b>							
Accounts payable		387	-	387	215	-	215
Accrued liabilities		1,458	-	1,458	944	-	944
Promissory note payable		1,000	-	1,000	-	-	-
<b>Total Current Liabilities</b>		<b>2,845</b>	<b>-</b>	<b>2,845</b>	<b>1,159</b>	<b>-</b>	<b>1,159</b>
<b>SHAREHOLDERS' EQUITY</b>							
<b>Share capital</b>							
Common shares		163,920	-	163,920	168,787	-	168,787
Stock options	(b) (ii)	3,704	99	3,803	1,156	56	1,212
Contributed surplus		14,875	-	14,875	18,988	-	18,988
Warrants		1,039	-	1,039	1,032	-	1,032
Deficit	(b) (i) (ii)	(184,080)	(705)	(184,785)	(189,118)	(662)	(189,780)
<b>Total Equity</b>		<b>(542)</b>	<b>(606)</b>	<b>(1,148)</b>	<b>845</b>	<b>(606)</b>	<b>239</b>
<b>Total Equity and Liabilities</b>		<b>2,303</b>	<b>(606)</b>	<b>1,697</b>	<b>2,004</b>	<b>(606)</b>	<b>1,398</b>

**Reconciliation of financial position and shareholders' equity (continued)**

		February 28, 2011		
		Canadian	Effect of	
Notes		GAAP	transition to	IFRS
			IFRS	
<b>Current</b>				
	Cash and cash equivalents	\$ 1,845	\$ -	1,845
	Prepaid expenses and other assets	278	-	278
	<b>Total Current Assets</b>	<b>2,123</b>	<b>-</b>	<b>2,123</b>
<b>Non-Current</b>				
	Equipment	110	-	110
	Goodwill	606	(606)	-
	<b>Total Non-Current Assets</b>	<b>716</b>	<b>(606)</b>	<b>110</b>
	<b>Total Assets</b>	<b>2,839</b>	<b>(606)</b>	<b>2,233</b>
<b>LIABILITIES</b>				
<b>Current</b>				
	Accounts payable	229	-	229
	Accrued liabilities	887	-	887
	<b>Total Current Liabilities</b>	<b>1,116</b>	<b>-</b>	<b>1,116</b>
<b>SHAREHOLDERS' EQUITY</b>				
<b>Share capital</b>				
	Common shares	168,787	-	168,787
	Stock options	1,000	15	1,015
	Contributed surplus	18,363	-	18,363
	Warrants	1,654	-	1,654
	Deficit	(188,081)	(621)	(188,702)
	<b>Total Equity</b>	<b>1,723</b>	<b>(606)</b>	<b>1,117</b>
	<b>Total Equity and Liabilities</b>	<b>2,839</b>	<b>(606)</b>	<b>2,233</b>



**Reconciliation of consolidated statement of loss and comprehensive loss  
for the three months ended February 28, 2011**

	Note	Effect of		
		Canadian GAAP	transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	760	87	847
General and administrative	b (ii)	527	174	701
Stock-based compensation	b (ii)	287	(287)	-
Depreciation of equipment	b (ii)	13	(13)	-
<b>Operating expenses</b>		<u>1,587</u>	<u>(39)</u>	<u>1,548</u>
<b>(Loss) from operations</b>		<u>(1,587)</u>	<u>39</u>	<u>(1,548)</u>
Finance expense		-	-	-
Finance income		6	-	6
Net Financing expense (income)		<u>(6)</u>	<u>-</u>	<u>(6)</u>
<b>Net loss and other comprehensive loss for the period</b>		<u>\$ 1,581</u>	<u>\$ (39)</u>	<u>\$ 1,542</u>
<b>Basic and diluted loss per share</b>		<u>\$ 0.10</u>	<u>\$ 0.00</u>	<u>\$ 0.10</u>

**Adjustments to the Statement of Cash Flows for the three months ended February 28, 2011**

Consistent with the Company's accounting policy under IAS 7, *Statement of Cash Flows*, interest paid and received have been moved to the body of the *Statement of Cash Flows*, as an element of cash flows from investing activities or financing activities whereas it was previously disclosed as supplementary information. There are no material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

**Reconciliation of consolidated statement of loss and comprehensive loss  
for the nine months ended February 28, 2011**

	Note	Effect of		
		Canadian GAAP	transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	1,852	129	1,981
General and administrative	b (ii)	1,680	195	1,875
Stock-based compensation	b (ii)	367	(367)	-
Depreciation of equipment	b (ii)	41	(41)	-
<b>Operating expenses</b>		<u>3,940</u>	<u>(84)</u>	<u>3,856</u>
<b>(Loss) from operations</b>		<u>(3,940)</u>	<u>84</u>	<u>(3,856)</u>
Finance expense		71	-	71
Finance income		<u>(10)</u>	<u>-</u>	<u>(10)</u>
Net Financing expense (income)		<u>61</u>	<u>-</u>	<u>61</u>
<b>Net loss and other comprehensive loss for the period</b>		<u>\$ 4,001</u>	<u>\$ (84)</u>	<u>\$ 3,917</u>
<b>Basic and diluted loss per share</b>		<u>\$ 0.32</u>	<u>\$ 0.00</u>	<u>0.32</u>

**Reconciliation of consolidated statement of loss and comprehensive loss  
for the year ended May 31, 2011**

	Note	Effect of		
		Canadian GAAP	transition to IFRS	IFRS
<b>REVENUE</b>		\$ -	\$ -	\$ -
<b>EXPENSES</b>				
Research and development	b (ii)	2,298	220	2,518
General and administrative	b (ii)	2,101	319	2,420
Stock-based compensation	b (ii)	526	(526)	-
Depreciation of equipment	b (ii)	56	(56)	-
<b>Operating expenses</b>		<u>4,981</u>	<u>(43)</u>	<u>4,938</u>
<b>(Loss) from operations</b>		<u>(4,981)</u>	<u>43</u>	<u>(4,938)</u>
Interest expense		71	-	71
Interest income		(14)	-	(14)
Net financing expense (income)		57	-	57
<b>Net Loss and other comprehensive loss for the period</b>		<u><b>5,038</b></u>	<u><b>(43)</b></u>	<u><b>4,995</b></u>
<b>Basic and diluted loss per share</b>		<u><b>\$ 0.38</b></u>	<u><b>\$0.00</b></u>	<u><b>0.38</b></u>

**Adjustments to the Statement of Cash Flows for the year ended May 31, 2011**

Consistent with the Company's accounting policy under IAS 7, *Statement of Cash Flows*, interest paid and received have been moved to the body of the *Statement of Cash Flows*, as an element of cash flows from investing activities or financing activities whereas it was previously disclosed as supplementary information. There are no material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

**(a) Mandatory exceptions upon adoption of IFRS**

Estimates

In applying IFRS upon initial adoption, hindsight is not used to create or revise estimates. Estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS except where necessary to reflect any difference in accounting policy.

**(b) Impact on accounting policies upon adoption of IFRS**

The key areas where the Company has identified that accounting policies differ, or where accounting policy decisions were necessary that impacted the Company's consolidated interim financial statements, are discussed below.

(i) Goodwill:

Under Canadian GAAP, goodwill was reviewed for impairment annually and whenever events or circumstances indicated that the carrying amount of goodwill in a reporting unit exceeded its fair value. Goodwill impairment was calculated using a two-step process. The first step required an identification of impairment loss, if any, by comparing the carrying value of the reporting unit to the fair value, which in turn was determined based on the market capitalization of the Company. Under Canadian GAAP this test was performed at the reporting unit level which is defined as an operating segment or one level below. The Company only had one operating segment or component which is the development of anticancer product candidates. In the Company's case the first test always showed a higher fair value than carrying value and as such we were not required to proceed to step two, as no indicator of impairment existed.

Under IFRS, *IAS 36 Impairment of Assets* ("IAS 36"), there is no longer a two-step process; rather, the Company is required to make a formal estimate of the recoverable amount and the carrying amount of a cash generating unit ("CGU") that is subject to impairment testing. The recoverable amount under IAS 36 is the higher of fair value less costs to sell or value in use.

Impairment testing under IAS 36 is performed at the CGU level which is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other CGUs or groups of assets. For the Company, this requirement results in testing at a lower level than under Canadian GAAP. Based on our knowledge and historical transactions, the Company has identified three separate CGUs that represent each of our product

platforms as they could have the ability to generate independent cash inflows. As the goodwill balance of \$606 thousand related to our acquisition of a private company in 1999, and the Antisense product platform contained therein, we have tested goodwill impairment on that CGU specifically for which the entire balance of goodwill has been allocated. There are no other assets subject to IAS 36 impairment testing in this CGU.

Under IAS 36, where the accounting value of a CGU subject to impairment testing is compared to the asset's value in use, any future cash flows expected to be provided by the CGU are discounted. The discounted cash flow model under IAS 36 indicates that only supportable evidence may be used in the calculations and should generally not use cash flows estimates beyond of a five-year period.

**Transition impact:** As a result of the application of IFRS, the Company recognized an impairment charge of the entire goodwill balance of \$606 thousand as of the Transition Date related to goodwill as the carrying amount of that CGU exceeded its recoverable amount which the Company has determined to be nil. The impact of the change in applying IFRS at the date of transition and as at May 31, 2011 is summarized as follows:

**Consolidated statement of financial position:**

	June 1, 2010	Feb 28, 2011	May 31, 2011
	\$	\$	\$
Decrease in goodwill	(606)	(606)	(606)
<b>Increase in deficit</b>	<b>606</b>	<b>606</b>	<b>606</b>

There was no impact to the consolidated statement of loss and comprehensive loss.

(ii) Share based payments:

IFRS 2, *Share-based Payments*, requires the fair value of each tranche of share options be amortized over its vesting period. Canadian GAAP allows for both the aforementioned method as well as the straight-line method of amortizing these costs. Under Canadian GAAP, forfeitures of share options can be accounted for at the time that they occur, whereas under IFRS, the number of share options that would ultimately vest is amortized over their respective vesting period.

Under Canadian GAAP, for share-based awards with graded vesting, the Company recognizes the fair value of the award (all tranches) on a straight-line basis over the underlying vesting period. In addition under Canadian GAAP the Company does not apply a forfeiture rate. The impact of applying the revised amortization method as well as applying an estimated forfeiture rate to the value of unvested options at the date of transition and as at May 31, 2011 is summarized as follows:

**Consolidated interim statement of loss and comprehensive loss:**

	Three months ended February 28, 2011	Nine months ended February 28, 2011	Year ended May 31, 2011
	\$	\$	\$
Decrease in share-based compensation	(39)	(84)	(43)

**Consolidated statement of financial position:**

	June 1, 2010	Feb 28, 2011	May 31, 2011
	\$	\$	\$
Increase (Reduction) of Stock Option Equity Account	99	(84)	(43)
<b>Increase (Decrease) in deficit</b>	<b>99</b>	<b>(84)</b>	<b>(43)</b>

The Company will apply the requirements of estimating a forfeiture rate on stock options as prescribed under IFRS 2 and continue to amortize the fair value of each tranche of stock options over the related vesting period.

(iii) Estimates

In applying IFRS upon initial adoption, hindsight is not used to create or revise estimates. Estimates previously made by the Company under Canadian GAAP were not revised for application of IFRS except where necessary to reflect any difference in accounting policies.

## **DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING**

There were no changes in our internal control over financial reporting during the quarter ended February 29, 2012 that materially affected or are reasonably likely to materially affect, internal control over financial reporting.

## **UPDATED SHARE INFORMATION**

As at April 12, 2012, the Company had 21.2 million common shares issued and outstanding and common share purchase warrants convertible into 9.8 million common shares. In addition, the Company had issued and outstanding 1.6 million stock options to purchase an equal number of common shares.

## **SUBSEQUENT EVENTS**

On March 12, 2012 the Company drew an additional \$300 thousand on the promissory note held by Mr. Abramson and described under 'Promissory Notes Payable' above. The total outstanding on the promissory note following this advance is \$600 thousand with \$1.2 million available to be drawn under the terms of the facility.

On March 9, 2012 the Company issued 323,000 stock options at an exercise price of \$0.18 and 780,000 deferred share units with an issue price of \$0.18. These grants will be accounted for in the quarter ending May 31, 2012.

## **ADDITIONAL INFORMATION**

Additional information relating to Lorus, including Lorus' 2011 annual information form and other disclosure documents, is available on SEDAR at [www.sedar.com](http://www.sedar.com).