LED MEDICAL DIAGNOSTICS INC.

Management's Discussion and Analysis of
Financial Condition and Results of Operations

For the Three Months and Year ended December 31, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis has been prepared by management as of April 3, 2012 and should read in conjunction with the audited consolidated financial statements and related notes of LED Medical Diagnostics Inc. (the "Company" or "LED") as at and for the year ended December 31, 2011 (prepared in accordance with International Financial Reporting Standards or "IFRS") and with the audited consolidated financial statements and related notes thereto of the Company for the year ended December 31, 2010, which were prepared in accordance with Canadian generally accepted accounting principles. Comparative figures under IFRS as at the year ended December 31, 2010 are also provided. All amounts are presented in Canadian dollars unless otherwise noted. All referenced materials as well as additional disclosures are available at www.sedar.com.

DISCLAIMER FOR FORWARD-LOOKING STATEMENTS

The following Management's Discussion and Analysis contains statements which, to the extent that they are not recitations of historical fact, may constitute forward-looking information under applicable Canadian securities legislation. Such forward-looking statements or information includes financial and other projections as well as statements regarding the Corporation's future plans, objectives, performance, revenues, growth, profits, operating expenses or the Corporation's underlying assumptions and the Company's intention to expand its technology beyond dental applications. The words "may", "would", "could", "will", "likely", "expect", "anticipate", "intend", "plan", "forecast", "project", "estimate" and "believe" or other similar words and phrases may identify forward-looking statements or information. Persons reading this Management's Discussion and Analysis are cautioned that such statements or information are only predictions, and that the Corporation's actual future results or performance may be materially different. Factors that could cause actual events or results to differ materially from those suggested by these forward-looking statements include, but are not limited to: economic conditions; dilution; limited history of profits and operations; operational risk; distributor risks; working capital; potential conflicts of interest; speculative investment; volatility of stock price; intellectual property risks; disruptions in production; reliance on key personnel; seasonality; management's estimates; competitors; regulatory requirements; reliance on few suppliers; reliance on subcontractors; technological milestones; operating cost fluctuations; fluctuations in exchange rates; product liability and medical malpractice claims; access to credit; taxation; potential unknown liabilities; the need to develop, integrate and deploy software solutions to meet its customers' requirements; the possibility of development or deployment difficulties or delays; the dependence on its customers' satisfaction; the timing of entering into significant contracts; its customers' continued commitment to the deployment of the Corporation's solutions; the risks involved in developing integrated software solutions and integrating them with third-party products and services; the performance of the global economy and growth in software industry sales; market acceptance of the Corporation's products and services; customer and industry analyst perception of the Corporation and its technology vision and future prospects; the success of certain business combinations engaged in by the Corporation or by its competitors; possible disruptive effects of organizational or personnel changes; technological change, new products and standards; risks related to acquisitions and international expansion; reliance on large customers; concentration of sales; international operations and sales; management of growth and expansion; dependence upon key personnel and hiring; reliance on a limited number of suppliers; risks related to the Corporation's competition; the Corporation not adequately protecting its intellectual property; risks related to product defects and product liability; currency exchange rate risk; and including, but not limited to, other factors described in the Corporation's reports filed on SEDAR, including its financial statements and management's discussion and analysis for the year ended December 31, 2011. In drawing a conclusion or making a forecast or projection set out in the forward-looking information, the Corporation takes into account the following material factors and assumptions in addition to the above factors: the Corporation's ability to execute on its business plan; the acceptance of the Corporation's products and services by its customers; the timing of execution of outstanding or potential customer contracts by the Corporation; the sales opportunities available to the Corporation; the Corporation's subjective assessment of the likelihood of success of a sales lead or opportunity; the Corporation's historic ability to generate sales leads or opportunities; and that sales will be completed at or above the Corporation's estimated margins. This list is not exhaustive of the factors that may affect the Corporation's forward-looking information. These and other factors should be considered carefully and readers should not place undue reliance on such forward-looking information. All forward-looking statements made in this AIF are qualified by this cautionary statement and

there can be no assurance that actual results or developments anticipated by the Corporation will be realized. The Corporation disclaims any intention or obligation to update or revise forward-looking information, whether as a result of new information, future events or otherwise, except as required by law.

OVERVIEW

LED was incorporated under the BCBCA on July 17, 2002 as 651195 B.C. Ltd. and changed its name to LED Medical Diagnostics Inc. on August 20, 2003. LED's head office is located at 235 – 5589 Byrne Road, Burnaby, B.C. V5J 3J1. LED's registered and records office is located at 2500 – 700 West Georgia Street, Vancouver, B.C. V7Y 1B3. LED maintains a warehouse facility at 219 – 5589 Byrne Road, Burnaby, B.C. V5J 3J1. The Company is listed on the TSX Venture Exchange (TSX-V) under the trading symbol LMD.

LED has two wholly-owned operating subsidiaries, LED Dental (US) Ltd., which was incorporated under the laws of Washington State, and LED Dental Inc., which was incorporated under the BCBCA.

General Development of the Business

Headquartered in Burnaby, B.C., LED was founded in 2003 by current CEO and director Peter Whitehead. LED's first product, the VELscope®, is a first step towards LED's goal of becoming a global leader in developing advanced, affordable technology targeted to dental and medical healthcare providers for the detection, diagnosis, and treatment of disease.

Description of the Business

The VELscope tissue fluorescence visualization technology is backed by over $50 million in funding by the National Institutes of Health ("NIH") and other US and Canadian government and private organizations. The NIH, part of the U.S. Department of Health and Human Services, is the primary Federal agency for conducting and supporting medical research in the US. The technology for the VELscope system was developed by LED in partnership with the British Columbia Cancer Agency ("BCCA").

In 2006, VELscope received U.S. FDA and Health Canada clearances. The clearances were pertinent to the VELscope's use of tissue fluorescence visualization technology as a new standard of screening for mucosal abnormalities, potentially malignant tissue and cancerous disease, and for surgical margin delineation. VELscope is the only device on the market indicated for use to discover cancerous and precancerous lesions that might not be apparent to the naked eye, and for use to help determine appropriate surgical areas when excision is required.

The first-generation VELscope device was introduced in 2006. Since then, LED has sold over 6,000 devices, which have been used to conduct over 10 million oral soft tissue exams worldwide. Currently, VELscope fluorescence visualization technology is used to conduct more oral exams than any other adjunctive detection technology in the world.

Since its inception, LED has grown from a research and development, pre-commercial product development company, to its current status as a fast-growing sales and marketing-focused growth-stage company.

Pursuant to an agreement dated November 30, 2010, Henry Schein Dental became the exclusive distributor of the VELscope Vx Enhanced Oral Assessment system in North America. Henry Schein Dental is the U.S. dental business of Henry Schein, Inc. a world leader in the provision of healthcare products and services to office-based practitioners.

LED believes that the success of the VELscope to date, including a strong first quarter in 2011, has proven that LED is a strong research and development company. Since the VELscope was launched in 2006, LED has introduced first the VELscope Vantage, and, in 2011, the VELscope Vx. The VELscope Vx is portable, rechargeable, and significantly more affordable than previous models. Its increased functionality and lower production costs improve LED's prospects as it moves into other countries and other healthcare markets.

LED markets its products, in conjunction with its distribution partners, directly to dental practitioners. Such direct marketing includes direct mail/e-mail and advertising in industry journals, and personal visits. In most cases, direct marketing activities are oriented towards convincing dental practitioners to attend an education seminar or trade show event in which LED is a participant. LED has found that successful marketing of the VELscope requires marketing efforts geared towards education of

dental practitioners, focusing on the advantages of using the device as adjunctive diagnostic tool in the detection of oral diseases. In this regard, LED has arranged to host or actively attend over 125 dental industry trade shows and seminars in 2011. LED's educational seminars are often hosted by both company employees and key opinion leaders in the dental industry who are supportive of LED's products.

Products and Intellectual Property

The Company's primary product is the VELscope Vx released in early 2011 and is comprised of fluorescence technology aids in the early visualization of mucosal diseases and enhances effective oral mucosal examinations. The VELscope Vx is a handheld device that provides dentists and hygienists with an easy-to-use adjunctive mucosal examination system for the early detection of abnormal tissue. The patented VELscope technology platform was developed in collaboration with the BCCA and MD Anderson Cancer Center, with funding provided in part by the NIH. It is based on the direct visualization of tissue fluorescence and the changes in fluorescence that occur when abnormalities are present. The VELscope Vx handpiece emits a safe blue light into the oral cavity, which excites the tissue from the surface of the epithelium through to the basement membrane (where premalignant changes typically start) and into the stroma beneath, causing it to fluoresce. The clinician is then able to immediately view the different fluorescence responses to help differentiate between normal and abnormal tissue. In fact, VELscope Vx is the only non-invasive adjunctive device clinically proven to help discover occult oral disease.

VELscope Vx provides a more effective oral cancer screening protocol with immediate benefits for the patient, clinician and practice. When used as an adjunctive aid in combination with traditional oral cancer examination procedures, VELscope Vx facilitates the early discovery and visualization of mucosal abnormalities prior to surface exposure that may be, or may lead to oral cancer. In one or two minutes, with no rinses or stains required, a VELscope examination helps oral healthcare professionals assure their patients that the standard of care for oral mucosal screening has been utilized. Adding to the VELscope's value as an adjunctive device is its ability to aid in the visualization of a wide spectrum of oral trauma and disease. A recent study at the University of Washington demonstrated that the VELscope system is a powerful tool for the discovery of mucosal abnormalities such as viral, fungal and bacterial infections, inflammation from a variety of causes (including lichen planus and other lichenoid reactions), squamous papillomas and salivary gland tumours. VELscope Vx combines minimal per-patient costs with more effective oral mucosal examinations.

The technology used in the VELscope was jointly developed by scientists at the BCCA and LED founder Peter Whitehead. The VELscope technology integrates four concepts: light, sophisticated filtering, natural tissue fluorophores and human optical and neural physiology. Base patents on the technology were awarded in 2000 and fully acquired by LED in 2003. These patents are expected to be valid until at least 2017. Additional patents have been submitted and are pending. The technology platform is based on the direct visualization of tissue fluorescence and the changes in fluorescence that can result when abnormal tissue is present. This technology helps clinicians visualize abnormal oral tissue that is often not apparent under white light.

LED expects that expanding its proprietary visualization technology beyond dental applications will provide gynecologists, gastroenterologists, ear nose and throat specialists, dermatologists and family practitioners with cost-effective tools to aid in the detection of oral cancer and other oral mucosal abnormalities. LED has sought patent protection for its projects by filing one or more patent applications for each aspect of a device, system or method, that LED believes is both patentable and that justifies the costs of patent protection. LED intends to protect future developments in the same manner. LED maintains certain of its intellectual property as trade secrets. LED also has pursued and intends to pursue trademark, copyright and other intellectual property protection as it believes is warranted.

VELscope, VELscope Vantage, and the VELscope Vx technologies are composed of a light source, light guide, and viewing handpiece. The VELscope handpiece emits a safe, visible, blue light into the oral cavity, which excites mucosal tissue and causes it to fluoresce. When viewed through the VELscope handpiece, abnormal tissue typically appears as an irregular, dark area that stands out against the otherwise normal, green fluorescence pattern of surrounding healthy tissue. This difference in appearance allows clinicians to examine the oral cavity in real time and differentiate between healthy mucosa and areas of concern that may require further action. When used in combination with traditional oral mucosal examination procedures, VELscope facilitates the discovery and enhances the visualization of mucosal abnormalities. LED received FDA 510(k) clearance for these claims in April 2007. FDA 510(k) clearance is a premarket notification required for manufacturers of medical devices.

One of LED's most profound commitments is to help reduce the mortality of oral cancer. The services of LED and its partners are directed toward developing a professional outreach program with key university–based oral pathology, oral surgery, and oral medicine leaders worldwide to assist healthcare providers as the need arises. LED is positioned to facilitate the dissemination of

new findings that address early detection based on fluorescence and other technologies. Currently over 50% of US dental colleges own at least one VELscope.

LED launched the VELscope in 2006 with its current version, the VELscope Vx, launched in early 2011.

AMALGAMATION WITH SEARCHLIGHT

On February 24, 2011, and as accepted on November 21, 2011 by the TSX-V, the Company entered into a letter agreement (the "Agreement") with Searchlight Capital Corp. ("Searchlight"), a Capital Pool Company listed on the Exchange. The transaction resulted in the amalgamation of LED, its wholly-owned subsidiaries LED Dental Inc., LED Dental (US) Ltd., EMD Systems Ltd., Visiotech Diagnostics Inc. and Searchlight. On November 24, 2011, the Company began trading on the TSX Venture Exchange (trading symbol: LMD). The transaction was accounted for as an acquisition of Searchlight by LED. For purposes of this discussion, the "Company" is defined as the amalgamated entity.

SIGNIFICANT EVENTS FOR THE YEAR ENDED DECEMBER 31, 2011

Financial Events

- Revenue increase of 352% with approximately $7.1 million for the year ended December 31, 2011 over the same period in the prior year of approximately $1.6 million which is attributable to sales of the Company's new VELscope Vx product launched in early 2011.
- Operating expenses for the year ended December 31, 2011 increased by 39% to approximately $5.7 million from the same period in the prior year period of approximately $4.1 million which is due to increased sales and marketing costs to market the Company's new VELscope Vx product and administration expenses to transition to a public company entity in late 2011.
- EBITDA[1] of ($1.5) million for the year December 31, 2011 compared to EBITDA of ($3.7) million for the year ended December 31, 2010.
- The net loss for the year ended December 31, 2011 was approximately ($3.5) million compared to the net loss of approximately ($3.7) million for the year ended December 31, 2010. Net loss included $1.7 million of transaction costs as part of the amalgamation with Searchlight.
- Cash and cash equivalents increased to $992,360 as at December 31, 2011 from December 31, 2010 of $269,010.

Strategic Highlight

- The Company entered into a transaction with Searchlight Capital Corporate which transitioned it to a public company entity on the TSX-V (trading symbol: LMD) which commenced trading on November 24, 2011. As part of this transaction, the Company generated additional funds of approximately $1.1 million excluding related transaction costs.

Product and Customer Highlight

- The Company launched its new product, the VELscope Vx, during the first quarter of fiscal 2011.
- VELscope Vx oral cancer screening system has been approved for use by the dentists affiliated with Heartland Dental Care, which represents over 350 dental practices in 18 states.

FINANCIAL RESULTS FOR THE THREE MONTHS ENDED DECEMBER 31, 2011

The following analysis of the results of operations for the three months ended December 31, 2011 includes comparisons to the three months ended December 31, 2010.

[1] EBITDA or Earnings before Interest, Taxes, Depreciation and Amortization is a non-IFRS measure that does not have a standardized meaning and may not be comparable to a similar measure disclosed by other issuers. This measure does not have a comparable GAAP measure. EBITDA referenced here relates to operating loss and excludes amortization, depreciation, stock-based compensation and warrant expense.

Revenue

Revenues are derived from the sale of the Company's VELscope product and related consumable products which are disposal components for singular use of the VELscope product. LED launched the new version of its primary product, the VELscope Vx, in January of 2011. Revenue is expressed net of distributor volume rebates, price discounts and warrant expense on distributor warrants of approximately $410,000 in the three months ended December 31, 2011.

	Three months ended December 31, 2011	Three months ended December 31, 2010 (Restated)
Total revenue	**$2,004,767**	**$213,098**

As a result of launching its new VELsope Vx product in early 2011, LED had increased sales over the prior year with sales of approximately $2.1 million in the three months ended December 31, 2011 representing an increase of 841% over the same quarter in the previous year of $213,098. The increase in sales was due to improved market acceptance of the new product, an improved price point for the new product making it more attractive to a wider audience, and a significantly improved and enlarged sales and distribution network.

To date, the Company has had a significant portion of its revenue derived from sales to its distributor in North America. While the Company continues to focus its efforts on expanding to new markets, it is expected that in the near-term, revenue generation will continue to be concentrated from a small number of distributors. In each respective period, revenues from customers which amounted to 10% or more of the Company's revenues accounted for the following percentages of the Company's total revenues and is primarily attributable to its North American distributor:

	Three months ended December 31, 2011	Three months ended December 31, 2010
Revenue	$1,246,753	$ 5,347
Percentage of total revenue	**62%**	**3%**

The Company earned revenues attributed to the following geographical regions based on the location of the customer:

	Three months ended December 31, 2011	%	Three months ended December 31, 2010	%
North America	$1,962,528	98%	$157,989	74%
Rest of World	42,239	2%	55,109	26%
	$2,004,767	**100%**	**$213,098**	**100%**

For the three months ended December 31, 2011, the Company generated the majority of its revenue from the American and Canadian markets which is consistent with the prior periods.

Gross Margin[2]

The Company experienced gross margin for the following periods:

	Three months ended December 31, 2011	%	Three months ended December 31, 2010 (Restated)	%
Revenues	$ 2,004,767	100%	$ 213,098	100%
Cost of goods sold	996,318	50%	697,423	328%
Gross margin	**$ 1,008,449**	**50%**	**($ 484,325)**	**(227%)**

[2] Gross margin is a non-IFRS measure that does not have a standard meaning and may not be comparable to a similar measure disclosed by other issuers. Gross margin referenced here relates to revenues less cost of sales. This measure does not have a comparable IFRS measure and is used by the Company to manage and evaluate the operating performance of the Company.

LED had a higher percentage margin on sales for the three months ended December 31, 2011 due to a higher percentage of revenue from the sale of consumables at higher margin relative to its VELscope Vx device product than the three months ended December 31, 2011. Gross margin percentage is due to a variety of factors, most importantly being a complete redesign of the VELscope Vx product and the resulting production costs, and the accompanying sales and pricing strategy.

Operating Expenses

The Company reports its operating expenses by nature as follows:

	Three months ended December 31, 2011	**Three months ended December 31, 2010 (Restated)**
Depreciation of equipment	$ 14,123	$ 4,580
Amortization of intangible assets	6,561	6,561
Bad debt	-	29,319
Business development	216,513	231,661
Consulting fees	122,497	731,970
Insurance	32,750	18,258
Interest and bank charges	10,572	47,064
Office	20,389	56,834
Professional fees	282,211	142,276
Rental	26,947	21,541
Research and development, net of investment tax credits	(57,874)	(114,646)
Salaries and wages	677,345	238,584
Stock-based compensation	63,557	-
Telephone	7,960	14,521
Travel	121,350	62,167
Warranty	(13,007)	18,858
Total operating expenses	**$1,531,894**	**$1,509,548**
As a percentage of total revenue	**76%**	**708%**

Total operating expenses for the three months ended December, 2011 increased by 2% over the same period in the prior year which was due primarily to decreased consulting fees and business development costs offset by increased travel, professional fees and salaries and wages.

The Company maintains a direct sales force, with staff in the United States and Canada which supports the worldwide sales and marketing activities. Sales and marketing expense consists primarily of salaries and related personnel costs, sales commissions, consulting fees, trade show expenses, marketing collateral, advertising costs and facilities. The Company has a small research and development group primarily located in Canada. Research and development expenses relate primarily to salaries and related benefit costs, as well as a portion of the Company's overall facilities costs.

Administration expenses include executive and administrative staff, facilities, public company costs, insurance, corporate variable compensation accruals, accounting and legal fees as well as various general administrative costs.

EBITDA

EBITDA was ($276,941) for the three months ended December 31, 2011 compared to ($1,982,732) for the three months ended December 31, 2011.

	Three months ended December 31, 2011	Three months ended December 31, 2010 (Restated)
Operating loss	($ 523,445)	($ 1,993,873)
Add: Depreciation of equipment	14,123	4,580
Add: Amortization of intangible assets	6,561	6,561
Add: Stock-based compensation	63,557	-
Add: Warrants issued for distributor commitment	162,262	-
EBITDA	**($ 276,942)**	**($ 1,982,732)**

The increase in EBITDA was primarily due to increased revenues.

Net Loss and Comprehensive Loss

	Three months ended December 31, 2011	Three months ended December 31, 2010 (Restated)
Net Loss and Comprehensive Loss	**($ 2,376,887)**	**($ 2,003,742)**

Net loss and comprehensive loss for the three months ended December 31, 2011 was higher than the three months ended December 31, 2010 due to transaction costs of the Searchlight amalgamation of approximately $1.7 million offset by increased revenues.

SELECTED ANNUAL INFORMATION

The following selected annual information of the results of operations for the year ended December 31, 2011 includes comparisons to the years ended December 31, 2010 (information prepared under IFRS).

	Year ended December 31, 2011	Year ended December 31, 2010 (Restated)
Revenue	$ 7,126,641	$ 1,578,134
Net loss	($ 3,495,701)	($ 3,726,324)
Loss per share (basic and diluted)	($ 0.11)	($ 0.15)

As at	**December 31, 2011**	**December 31, 2010**
Total assets	$ 2,262,786	$ 1,369,621
Total long term financial liabilities	$ 10,140	$ 12,618

See Financial Results section below for discussion on Revenue and Net Loss for the year. The increase in total assets is primarily due to increase in cash of approximately $620,000, increase in accounts receivable of approximately $72,000, increase in inventory of approximately, $500,000 offset by decrease in investment tax credits recoverable of $350,000

FINANCIAL RESULTS FOR THE YEAR ENDED DECEMBER 31, 2011

The following analysis of the results of operations for the year ended December 31, 2011 includes comparisons to the year ended December 31, 2010.

Revenue

Revenue is expressed net of distributor volume rebates, price discounts and warrant expense on distributor warrants of approximately $1.5 million for the year ended December 31, 2011.

	Year ended December 31, 2011	Year ended December 31, 2010 (Restated)	Change
Total revenue	**$7,126,641**	**$1,578,134**	**352%**

The increase in revenue is attributable to the Company's launch of its new VELscope Vx product in early 2011.

In each respective period, revenues from customers which amounted to 10% or more of the Company's revenues accounted for the following percentages of the Company's total revenues and is primarily attributable to its North American distributor:

	Year ended December 31, 2011	Year ended December 31, 2010	Change
Revenue	$6,537,376	$105,799	6,079%
Percentage of total revenue	**92%**	**7%**	

The Company earned revenues attributed to the following geographical regions based on the location of the customer:

	Year ended December 31, 2011	%	Year ended December 31, 2010	%	Change
North America	$7,084,402	99%	$1,523,025	96%	365%
Rest of World	42,239	1%	55,109	4%	(23%)
Total revenue	**$7,126,641**	**100%**	**$1,578,134**	**100%**	**352%**

The Company continues to generate the majority of its revenue from North America.

Gross Margin

The Company experienced the following gross margin for year ended December 31, 2011 and 2010, respectively:

	Year ended December 31, 2011	%	Year ended December 31, 2010 (Restated)	%	Change
Revenues	$7,126,641	100%	$1,578,134	100%	352%
Cost of goods sold	3,210,792	45%	1,193,780	76%	169%
Gross margin	**$3,915,849**	**55%**	**$ 384,354**	**24%**	**919%**

The gross margin percentage for the year ended December 31, 2011 is higher than gross margin percentage over the same period in the prior year due to increased products sold due to the new VELscope Vx product introduced in early 2011.

Operating Expenses

The Company reports its operating expense by nature which increased during the year ended December, 2011 over the prior year by 39% as follows:

	Year ended December 31, 2011	Year ended December 31, 2010 (Restated)	Change
Depreciation of equipment	$ 42,794	$ 16,875	154%
Amortization of intangible assets	26,244	26,244	0%
Bad debt	-	51,943	(100%)
Business development	1,169,851	563,220	108%
Consulting fees	595,700	1,084,887	(45%)
Insurance	66,174	83,685	(21%)
Interest and bank charges	84,412	101,687	(17%)
Office	162,165	164,042	(1%)
Professional fees	527,521	348,275	51%
Rental	123,772	95,013	30%
Research and development, net of investment tax credits	23,112	289,956	(92%)
Salaries and wages	2,434,364	998,169	144%
Stock-based compensation	63,557	-	N/A
Telephone	55,290	52,659	5%
Travel	277,156	142,336	95%
Warranty	17,936	64,215	(72%)
Total operating expenses	**$5,670,048**	**$4,083,206**	**(39%)**
As a percentage of total revenue	**80%**	**269%**	

The increase in total operating expenses was due primarily to increased costs in salaries and wages and business development, consisting of increased sales employees for higher salary and commission, travel and entertainment, trade shows, marketing product collateral and other expenses to market the Company's new VELscope Vx product launched in early 2011 as well as administration costs to support the Company's transition to a public company entity in late 2011. Salary and wages increased as a result of the Company having more employees during the year ended December 31, 2011 compared to the prior year.

EBITDA

EBITDA was approximately ($1.5) million for the year ended December 31, 2011 compared to approximately ($3.7) million for year ended December 31, 2010. The improved EBITDA was due primarily to continued increased revenue during the year ended December 31, 2011.

	Year ended December 31, 2011	Year ended December 31, 2010 (Restated)
Operating loss	($ 1,754,199)	($ 3,698.852)
Add: Depreciation of equipment	42,794	16,875
Add: Amortization of intangible assets	26,244	26,244
Add: Stock-based compensation	63,557	-
Add: Warrants issued for distributor commitment	162,262	-
EBITDA	**($ 1,459,342)**	**($ 3,655,733)**

Net Loss and Comprehensive Loss

	Year ended December 31, 2011	Year ended December 31, 2010 (Restated)
Net loss and comprehensive loss	**($3,495,701)**	**($3,726,324)**

Net loss and comprehensive loss for the year ended December 31, 2011 was higher than the year ended December 31, 2011 due to transaction costs of the Searchlight amalgamation of approximately $1.7 million offset by higher revenue.

RESTATEMENT

The Company has restated its financial statements for the year ended December 31, 2010, in order to record:

a) An advance which was included in cost of goods sold at December 31, 2010;
b) Revenues recorded in fiscal 2010 but relate to the year ended December 31, 2011; and
c) Trades payable and accrued liabilities relating to the fiscal year 2010.

Consolidated statements of financial position	December 31, 2010 – As reported under IFRS	Adjustments	December 31, 2010 – As restated under IFRS
Receivables	$ 86,115	$ 145,488	$ 231,603
Prepayments	$ 50,848	$ 59,618	$ 110,466
Trades payable and accrued liabilities	$ 1,328,916	$ 132,734	$ 1,461,650
Share capital	$ 19,234,499	($ 13,151)	$ 19,221,348
Deficit	($ 21,787,642)	$ 85,523	($ 21,702,119)

Consolidated statements of operations and deficit and comprehensive loss	Three months ended December 31, 2010 – As reported under IFRS	Adjustments	Three months ended December 31, 2010 – As restated under IFRS
Sales	$ 67,610	$ 145,488	$ 213,098
Cost of goods sold	$ 756,941	($ 59,618)	$ 697,423
Professional fees	$ 22,693	$ 119,583	$ 142,276
Operating loss	($ 2,079,396)	$ 85,523	($ 1,993,873)
Net loss and comprehensive loss	($ 2,089,265)	$ 85,523	($ 2,003,742)

Consolidated statements of operations and deficit and comprehensive loss	Year ended December 31, 2010 – As reported under IFRS	Adjustments	Year ended December 31, 2010 – As restated under IFRS
Sales	$ 1,432,646	$ 145,488	$ 1,578,134
Cost of goods sold	$ 1,253,398	($ 59,618)	$ 1,193,780
Professional fees	$ 228,692	$ 119,583	$ 348,275
Operating loss	($ 3,784,375)	$ 85,523	($ 3,698,852)
Net loss and comprehensive loss	($ 3,811,847)	$ 85,523	($ 3,726,324)

LIQUIDITY AND CAPITAL RESOURCES

The Company finances its operations and capital expenditures through cash generated from operations and equity and debt financings. As at December 31, 2011, the Company had cash and cash equivalents totaling approximately $992,000 with working capital[3] of approximately $570,000 as compared to cash and cash equivalents of approximately $269,000 and working capital of approximately ($1.0 million) as at December 31, 2010.

[3] Working Capital is a non-IFRS measure that does not have a standardized meaning and may not be comparable to a similar measure disclosed by other issuers. This measure does not have a comparable IFRS measure. Working capital is defined as current assets less current liabilities. The Company believes that the inclusion of this no-IFRS measure financial measure provides investors with an alternative presentation useful to investors' understanding of the Company's core operating results and trends.

Three Months ended December 31, 2011

Cash provided by (used in):	Three months ended December 31, 2011	Three months ended December 31, 2010
Operating activities	($ 739,827)	($ 1,711,193)
Investing activities	252,293	(7,546)
Financing activities	1,260,483	1,622,740
Increase (decrease) in cash and cash equivalents	**$ 772,949**	**($ 95,999)**

Cash used in operating activities for all comparable periods was attributable to revenues earned offset by operating expenditures primarily consisting of sales and marketing costs to market the Company's new VELscope Vx product, and overall corporate administration activities.

The investing activities during the three months ended December 31, 2011 pertain to the Company purchasing equipment as well as cash received of approximately $265,000 as part of the Searchlight amalgamation. The investing activities during the three months ended December 31, 2010 pertain to the Company purchasing equipment

The financing activities during the three months ended December 31, 2011 relate primarily to the completion of the Searchlight amalgamation and subsequent financing offset by repayment of shareholder loans. The financing activities during the three months ended December 31, 2010 is attributable to funds received form shareholder loans during the period as well as private placement proceeds.

Year ended December 31, 2011

Cash provided by (used in):	Year ended December 31, 2011	Year ended December 31, 2010
Operating activities	($ 1,630,730)	($ 2,854,601)
Investing activities	212,730	(7,546)
Financing activities	2,141,350	2,737,740
Increase (decrease) in cash and cash equivalents	**$ 723,350**	**($ 124,407)**

As a result of continued investment in sales and marketing cost to market the new VELscope Vx product in 2011, the Company used cash in operations of approximately $1.6 million during the year ended December 31, 2011. This is compared to cash used in operations of approximately $2.9 million during the year ended December 31, 2010.

Cash provided by (used in) operating activities for all comparable periods was attributable to revenues earned offset by sales and marketing efforts related to the VELscope Vx product and other related product offerings, and overall corporate administration activities.

The investing activities during the year ended December 31, 2011 pertain to the Company purchasing equipment as well as cash received of approximately $265,000 as part of the Searchlight amalgamation. The investing activities during the year ended December 31, 2010 pertain to the Company purchasing equipment

During the year ended December 31, 2011, financing activities pertained to the completion of the Searchlight amalgamation and equity financings of approximately $2.8 million offset by repayments for shareholder loans obligations of approximately $639,000. During the year ended December 31, 2010, cash provided by investing activities due to equity financings of approximately $2.1 million and shareholder loans of $650,000.

STAFFING LEVELS

The following table summarizes the Company's headcount, by functional group:

	As at December 31, 2011	As at December 31, 2010
Sales and marketing	16	8
Research and development	2	1
Administration	6	4
Total	**24**	**13**

COMMITMENTS

The Company continues to have no bank debt, off-balance sheet financing arrangements or significant capital leases. The Company has leased facilities in Canada and the United States. Minimum lease payments as at December 31, 2011 are $93,048 for the year ending December 31, 2012.

GOVERNMMENT ASSISTANCE

Industry Canada

Investment tax credits recoverable represent amounts due from the Canada Revenue Agency in respect of the Company's expenditures on scientific research and experimental development. The Company is entitled to receive a refund of investment tax credit equal to 41.5% of qualifying expenditures. The amount recorded as investment tax credits recoverable represents management's estimate of the recoverable amount as at December 31, 2010.

Investment tax credits received are recorded under the cost reduction method in relation to the applicable cost. During the year ended December 31, 2010, investment tax credits recoverable of $350,000 were allocated as a reduction to research and development expenditures, and were receivable as at December 31, 2010. The Company received and additional $83,027 during the year ended December 31, 2011.

INTANGIBLE ASSETS IMPAIRMENT

Due to ongoing operating losses of the Company and current volatility and uncertainty of global financial markets, there is a possibility that the carrying values attributable to the Company's intangible assets may become impaired. At December 31, 2011 and 2010, management has tested the intellectual property and intangibles for recoverability and no events or changes in circumstances indicated that the carrying values may not be recoverable. Therefore, there is no impairment of these assets at December 31, 2011 or December 31, 2010. The recorded balance of intangible assets is $115,910 as at December 31, 2011. The remaining carrying value is the fair value of the estimated future cash flow stream associated with the assets.

OFF-BALANCE SHEET ARRANGEMENTS

None.

TRANSACTIONS WITH RELATED PARTIES

Transactions between the Company and its subsidiaries, which are related parties of the Company, have been eliminated on consolidation and are not disclosed in this note.

Related parties include key management, the Board of Directors, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.

In addition to the royalties accrued under the royalty agreement with the Company's CEO as well as loans received from shareholders, and related interest accrual,, during the year ended December 31, 2011 and 2010, the Company paid or accrued the following compensation expenses to key personnel of the Company:

	Year ended December 31, 2011	Year ended December 31, 2010
Short-term employee benefits*	$ 506,417	$ 288,564
Post employment benefits	$ Nil	$ Nil
Other long-term benefits	$ Nil	$ Nil
Termination benefits	$ Nil	$ 72,402
Share-based payments	$ Nil	$ Nil

(*) Included in short-term employee benefits are consulting fees paid to the former CEO and former CFO.

During the year ended December 31, 2011, and 2010, there were no options awarded to directors and key management under the Company's stock option plan.

PROPOSED TRANSACTIONS

None.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

These consolidated financial statements of the Company, approved by the Board of Directors on March 30, 2012, have been prepared in accordance with International Financial Reporting Standards ("IFRS") and their interpretations adopted by the International Accounting Standards Board ("IASB").

The Company previously prepared its financial statements in accordance with generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"). In 2010, the CICA handbook was revised to incorporate International Financial Reporting Standards, and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company has commenced reporting on this basis in these consolidated financial statements. In these financial statements, the term "Canadian GAAP" refers to Canadian GAAP before the adoption of IFRS.

These consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of financial statements, including IAS 34 and IFRS 1. Subject to certain transition elections disclosed in Note 21, these consolidated financial statements have been prepared using the historical cost basis and the Company has consistently applied the same accounting policies in its opening IFRS statement of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 21 discloses the impact of transition to IFRS on the Company's reported financial positions, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Company's consolidated financial statements for the year ended December 31, 2010.

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

The consolidated financial statements should be read in conjunction with the Company's Canadian GAAP annual financial statements for the year ended December 31, 2010.

Revenue Recognition

Revenue from product and service sales is recognized when the amount is fixed or determinable, title has transferred or initial services have been performed, and collection is reasonably assured.

Royalty revenue is recognized when the right to receive a royalty has been established and collection is reasonably assured.

Intangible Assets

Intangible assets acquired either individually or with a group of other assets are initially recognized or measured at cost. The cost of a group of intangible assets acquired in a transaction, including those acquired in a business combination that meet the specified criteria for recognition apart from goodwill, is allocated to the individual assets acquired based on their relative fair values.

Intangible assets with finite useful lives are amortized over their estimated useful lives. Amortization is calculated over their useful lives using the straight-line method and the following periods. The amortization methods and estimated useful lives of intangible assets are reviewed annually. Intangible assets are tested for impairment by comparing their carry values to the sum of the undiscounted cash flows expected to result from their use or eventual disposition. If not recoverable, the impairment charge is the difference between the carrying value and fair value.

Intangible assets, which consist of patents, intellectual property and related know-how, have finite lives and are measured at cost less accumulated amortization and accumulated impairment losses.

Intangible assets are being amortized using the straight line method over a 13 year period commencing in 2004.

Accounting standards issued but not yet effective

IFRS 9 Financial instruments ("IFRS 9")

IFRS 9 was issued by the IASB on November 12, 2009 and will replace IAS 39 Financial Instruments: Recognition and Measurement ("IAS 39"). The new standard replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value.

IFRS 9 also replaces the models for measuring equity instruments, and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where such equity instruments are measured at fair value through other comprehensive income, dividends are recognized in profit or loss to the extent not clearly representing a return of investment, are recognized in profit or loss; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income indefinitely.

Requirements for financial liabilities were added in October 2010 and they largely carried forward existing requirements in IAS 39, Financial Instruments – Recognition and Measurement, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss would generally be recorded in other comprehensive income.

This new standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

Recent pronouncements

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 10, Consolidated Financial Statements ("IFRS 10"), IFRS 11, Joint Arrangements ("IFRS 11"), IFRS 12, Disclosure of Interests in Other Entities ("IFRS 12"), IAS 27, Separate Financial Statements ("IAS 27"), IFRS 13, Fair Value Measurement ("IFRS 13") and amended IAS 28, Investments in Associates and Joint Ventures ("IAS 28"). Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its financial statements or whether to early adopt any of the new requirements.

The following is a brief summary of the new standards:

IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 Consolidation—Special Purpose Entities and parts of IAS 27 Consolidated and Separate Financial Statements.

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venture will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities—Non-monetary Contributions by Venturers.

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRSs. The new standard clarifies that fair value is 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. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.
In addition, there have been amendments to existing standards, including IAS 27 and IAS 28. IAS 27 addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 has been amended to include joint ventures in its scope and to address the changes in IFRS 10 – 13.

Accounting Standards

In fiscal 2011 the Company completed its International Financial Reporting Standards ("IFRS') conversion plan. Through assistance with respect to training and preparation of reconciliations of historical Canadian GAAP financial statements to IFRS, the Company believes that its accounting department has obtained sufficient understanding of IFRS for implementation purposes.

The Company's IFRS implementation project consisted of three primary phases which were completed in 2011 by a combination of in-house resources and external consultants:

- **Initial diagnostic phase** – Involved preparing a preliminary impact assessment to identify key areas that were impacted by the transition to IFRS. Each potential impact identified during this phase was ranked as having a high, moderate or low impact on the Company's reporting and the overall difficulty of the conversion effort. This phase was completed in fiscal 2010.

- **Impact analysis, evaluation and solution development phase** – Involved the selection of IFRS accounting policies by senior management and the review by the Audit Committee, the quantification of the impact of changes on the Company's existing accounting policies on the opening IFRS statement of financial position, and the development of IFRS financial statements. Management reviewed the transitional policy choices available under IFRS 1, *First-time Adoption of International Financial Reporting Standards*, and the impact of IFRS adoption was quantified in order to prepare an IFRS opening statement of financial position as at January 1, 2010. This phase was completed in the fiscal 2011.

- **Implementation and review phase** – Involved training key finance and other personnel and implementation of the required changes to information systems and business policies and procedures. The phase enabled the Company to collect the financial information necessary to prepare its first IFRS financial statements as at and for the three months ended March 31, 2011 and continue to report under IFRS on a go-forward basis during the remainder of fiscal 2011. This phase was completed in fiscal 2011.

IFRS Transition Plan

The Company established a comprehensive IFRS transition Plan and engaged third party consultants to assist with the planning and implementation of its transition to IFRS. The following summarizes the Company's results with respect to its IFRS plan:

Initial scoping and analysis of key areas for which accounting policies may be impacted by the transition to IFRS.	Complete.
Detailed evaluation of potential changes required to accounting policies, information systems and business processes, including the application of IFRS 1First Time Adoption of International Financial	Complete.

Reporting Standards.	
Final determination of changes to accounting policies and choices to be made with respect to first time adoption alternatives.	Complete.
Resolution of the accounting policy change implications on information technology, business processes and contractual arrangements.	Complete.
Quantification of the financial statement impact of changes in accounting policies.	Complete.
Management and employee education and training.	Complete.

As part of management's analysis of potential changes to significant accounting policies, the Company assessed what changes would be required to its accounting systems and business processes. The Company believes that the changes required were minimal and current systems and processes accommodate the necessary changes. The Company did not identify any contractual arrangements that were affected by changes to significant accounting policies.

The accounting and disclosure differences identified by the Company upon transition to IFRS are summarized below:

Impact on Financial Statement Presentation, Classification, and Disclosure

i) Financial Statement Presentation

The components of a complete set of IFRS financial statements are: consolidated statements of financial position (balance sheet), consolidated statements of operations and deficit, consolidated statements of comprehensive income (loss), consolidated statements of changes in equity, consolidated statements of cash flows, and notes including accounting policies. Under IFRS, the statement of financial position may be presented in ascending or descending order of liquidity. The income statement is classified by each expense classification– amortization, insurance, business development, etc. In addition, IFRS requires more detailed note disclosures than those required by Canadian GAAP.

Impact on the Company: *The Company reformatted its financial statements in compliance with IFRS and elected to retain its existing presentation, (i.e., descending order of liquidity).*

ii) Deferred taxes

IFRS: IAS 12 requires presentation of all deferred tax balances as non-current. **Canadian GAAP**: Current balances are presented separately.

Impact on the Company*: The Company is currently in a net deferred tax asset position with a full valuation allowance provision. As a result, there was no material impact upon the adoption of IAS 12.*

iii) Provisions

IFRS: A provision is a liability of uncertain timing or amount. Provisions are disclosed separately from liabilities and accrued liabilities and require additional disclosure. Provisions are also classified as current or non-current as appropriate (IAS 37 - Provisions and other liabilities). **Canadian GAAP:** Accounts payable, accrued liabilities and provisions may be and are disclosed by the Company on the statement of financial position as a single line item.

Impact on the Company: *There were not significant provisions requiring separate disclosure pursuant to IAS 37.*

IFRS-1 Transitional Policy Choices and Exceptions for Retrospective Application

IFRS-1 contains the following policy choices with respect to first-time adoption that were applicable to the Company:

ii) Equipment:

IFRS 1 provides a choice between measuring equipment at its fair value at the date of transition and using those amounts as deemed cost or using the historical cost basis under Canadian GAAP.

Impact on the Company: *The Company elected to use the historical cost carrying values for equipment as determined under Canadian GAAP for transitional purposes.*

<u>iii) Designation of previously recognized financial instruments</u>:

IFRS: IAS 39 restricts the circumstances in which the option to measure a financial instrument at fair value through profit or loss is available. **Canadian GAAP**: Contains no similar restriction.

Impact on the Company*: The Company believes that its historical classification of financial instruments under Canadian GAAP is consistent with the principles set out in IAS 39.*

Mandatorily Applicable Standards with Retrospective Application (i.e., Not Specifically Exempt Under IFRS - 1)

<u>i) Equipment - cost</u>

IFRS: IAS 16 contains more extensive guidance with respect to components within equipment. When an item of equipment comprises individual components for which different depreciation methods or rates are appropriate, each component is accounted for separately (component accounting). **Canadian GAAP**: Section 3061 essentially contains similar guidance but is less extensive.

Impact on the Company: *The Company has applied the straight line or declining balance amortization method to all of its assets that are used directly for operations. The Company believes that the "components" approach is primarily intended to apply to major inspection or overhaul cost that is embedded in the cost of an item of equipment. Given the Company's equipment consists primarily of computers and computer equipment, the Company identified no major inspection or overhaul cost with respect to its equipment. Accordingly, there was no material impact upon transition.*

<u>ii) Intangible assets – impairment</u>

IFRS: Under IAS 36 an asset is impaired if the recoverable amount is lower than the asset's carrying amount. Assets are evaluated either individually or grouped in a cash generating unit (CGU) for impairment-testing purposes. A CGU is the smallest group of assets that generates independent cash inflows and may be smaller than an asset group or a reporting unit under Canadian GAAP. Assets are tested, and any resulting impairment charges are measured using a one-step test that compares an asset or CGU's carrying value to its recoverable amount. **Canadian GAAP**: A two-step approach is used to measure impairment. In step 1, a recoverability test is performed by comparing the expected undiscounted future cash flows to be derived from the asset with its carrying amount. If the asset fails the recoverability test, step 2 is triggered, and the entity must record an impairment loss calculated as the excess of the asset's carrying amount over its fair value.

Impact on the Company*: The Company has concluded that there is no material difference between the carrying values of its intangible assets under IFRS and Canadian GAAP.*

<u>iii) Share based compensation</u>

IFRS: Under IFRS 2, graded vesting awards must be accounted for as though each installment is a separate award. IFRS does not provide for an election to treat the instruments as a pool and recognize the expense on a straight line basis. **Canadian GAAP**: Straight line basis is permissible under Canadian GAAP.

Impact on the Company: *The Company previously recognized share based compensation expense on a straight line basis under Canadian GAAP and therefore recorded transitional adjustments for options unvested at January 1, 2010 under IFRS. The Company has concluded that there is no material difference under IFRS and Canadian GAAP.*

<u>iv) Revenue recognition</u>

Revenue from product and service sales is recognized when the amount is fixed or determinable, title has transferred or initial services have been performed, and collection is reasonably assured.

Royalty revenue is recognized when the right to receive a royalty has been established and collection is reasonably assured.

Impact on the Company: *The Company has concluded that there is no material difference between its revenue recognition policies under IFRS and Canadian GAAP.*

vi) Functional currency

The Company uses the Canadian dollar as its functional currency. IAS 21 contains a more comprehensive framework for the determination of functional currency.

Impact on the Company: *The Company has concluded that the functional currency for the Company and its subsidiaries under both IFRS and Canadian GAAP is the Canadian dollar.*

Impact on Systems and Processes

The Company concluded that the adoption of IFRS did not have a pervasive impact on its systems and processes. The Company implemented certain minor changes to the general ledger account descriptions as well as the calculation methodologies previously used for certain specific financial statement areas such as asset impairment and share based compensation. As the accounting policies were selected, appropriate changes to ensure the integrity of internal control over financial reporting and disclosure controls and procedures were made.

FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board of Directors approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures. The type of risk exposure and the way in which such exposure is managed is provided as follows:

Classification of financial instruments

Financial assets included in the statement of financial position are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
Cash and cash equivalents			
Cash and cash equivalents	$ 992,360	$ 269,010	$ 393,417
Restricted cash	25,000	25,000	20,000
Loans and receivables:			
Receivables	303,800	231,603	408,676
Investment tax credits recoverable	-	350,000	261,522
	$ 1,321,160	**$ 875,613**	**$ 1,083,615**

Financial liabilities included in the statement of financial position are as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
Non-derivative financial liabilities:			
Trades payable	$ 1,029,909	$ 1,144,685	$ 641,226
Due to shareholders	104,544	689,491	-
Income taxes payable	-	10,713	10,510
Finance lease obligations	12,618	14,620	-
	$ 1,147,071	**$ 1,859,509**	**$ 651,736**

Fair value

The fair value of the Company's financial assets and liabilities approximates the carrying amount.

Financial instruments measured at fair value are classified into one of three levels in the fair value hierarchy according to the relative reliability of the inputs used to estimate the fair values. The three levels of the fair value hierarchy are:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

The carrying value of the Company's financial instruments are measured based on Level 1 input of the fair value hierarchy.

Credit Risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is exposed to credit risks arising from its cash holdings, receivables and investment tax credits recoverable. The Company manages credit risk by placing cash with major Canadian financial institutions. Receivables are due for completed sales and reimbursements and investment tax credits recoverable from the Government of Canada. Management believes that credit risk related to these amounts is low.

The Company monitors collectability of receivables on an on-going basis to determine credit risk. In order to mitigate credit risk, credit terms are only offered to the Company's exclusive distributor, a large multinational company. Other customers are required to pay in advance or by credit card, prior to shipping of the product. December 31, 2011, no accounts receivable are due beyond one year.

As at December 31, 2011, December 31, 2010 and January 1, 2010, the Company's exposure to credit risk for these financial instruments was as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
Cash and cash equivalents	$ 992,360	$ 269,010	$ 393,417
Restricted cash	25,000	25,000	20,000
Receivables	303,800	231,603	408,676
Investment tax credits recoverable	-	350,000	261,522
	$ 1,321,160	**$ 875,613**	**$ 1,083,615**

Receivables (related to trade accounts receivable) balances of $230,810 (December 31, 2010 - $224,543; January 1, 2010 - $359,523) were aged as follows as at December 31, 2011, December 31, 2010 and January 1, 2010. It does not include harmonized sales tax receivable of $72,990 as at December 31, 2011 (December 31, 2010 - $7,060; January 1, 2010 – $49,153).

Included in the balance as at December 31, 2011 was $154,629 which was related to the net accounts receivable balance of the Distributor. The Distributor's accounts receivable balance of $1,244,178 was netted against its accounts payable balance of $1,089,548.

	December 31, 2011	December 31, 2010	January 1, 2010
Current	$ 776	$ 177,683	$ 221,930
31-60 days	65,491	2,396	34,829
Over 60 days	164,543	44,4641	102,764
	$ 230,810	**$ 224,543**	**$ 359,523**

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company has a planning and budgeting process in place to help determine the funds required to support the Company's normal operating requirements on an ongoing basis. The Company ensures that there are sufficient funds to meet its short-term business requirements, taking into account its anticipated cash flows from operations and its holdings of cash and cash equivalents.

To manage liquidity risk, the Company reviews additional sources of capital to continue its operations and discharge its commitments as they become due. Historically, the Company's sole source of funding has been the issuance of equity securities for cash, primarily through private placements.

Trades payable were aged as follows as at December 31, 2011, December 31, 2010 and January 1, 2010 and does not include accrued liabilities of $377,220, warranty provision of $10,316 and state sales tax payable of $5,323 as at December 31, 2011 (December 31, 2010 - $284,794, $22,200 and $9,971 respectively; January 1, 2010 - $424,149, $9,185 and $19,873 respectively).

	December 31, 2011	December 31, 2010	January 1, 2010
Current	$ 296,326	$ 686,204	$ 241,953
31-60 days	119,583	84,677	125,563
Over 60 days	614,000	373,804	273,779
	$ 1,029,909	**$ 1,144,685**	**$ 641,295**

The following is an analysis of the contractual maturities of the Company's non-derivative financial liabilities as at December 31, 2011:

	Within one year	Between one and five years	More than five years
Trades payable	$ 1,029,909	$ -	$ -
Due to shareholders	104,544	-	-
Finance lease obligations	2,478	10,140	-
	$ 1,136,931	**$ 10,140**	**$ -**

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's functional currency is the Canadian dollar. Interest rate risk is limited to the portion of the Company's cash held in bank accounts that earn interest and interest paid on shareholder loans. Due to the limited and short term nature of these financial instruments, fluctuations in the interest rates will not have a significant impact on their fair value. As at December 31, 2011, the Company had not entered into any derivative contracts to manage this risk.

DISCLOSURE OF OUTSTANDING SHARE DATA

The Company is authorized to issue an unlimited number of common shares, without par value and an unlimited number preference shares without par value. As of April 3, 2012, the Company has 36,335,508 common shares outstanding and no preference shares outstanding.

The Company has instituted a rolling incentive stock option plan whereby shares reserved for issuance under the plan shall reflect 10% of the issued and outstanding common shares of the Company from time to time. As of April 3, 2012, the Company is entitled to grant incentive stock options for 3,633,550 common shares under the Company's stock option plan with a total of 330,000 options being issued and outstanding. The Company also has 8,971,968 warrants outstanding.

RISKS AND UNCERTAINTIES

An investment in the securities of the Company may be regarded as speculative due to the Company's stage of development. Risk factors relating to the Company could materially affect the Company's future results and could cause them to differ materially from those described in forward-looking statements relating to the Company. Prospective investors should carefully consider these risks.

The following are some of the risks that are associated with the Company's business and operations and should be carefully considered by any potential investor in the Company's shares:

History of Losses

The Company has a history of losses, and there can no assurance that the Company's losses will not continue in the future. As at December 31, 2011, the Company had an accumulated deficit of approximately $23.7 million. The Company's prospects must be considered in the context of its stage of development, the risks and uncertainties it faces, and the inability of the Company to accurately predict its operating results in the results of product development and sales and marketing initiatives. There can be no assurances that implementation of the Company's strategies will result in the Company becoming profitable.

Operational Risk

In the normal course of business, LED's operations continue to be influenced by a number of internal and external factors, and are exposed to risks and uncertainties, that can affect its business, financial condition and operating results. LED's activities are

subject to ongoing operational risks, including the performance of key suppliers, product performance, government and other industry regulations, all of which may affect its ability to meet its obligations. While management believes its innovation and technology make it a leader in the industry, revenue and results may be affected if products are not accepted in the market place, are not approved by regulatory authorities, or if products are not brought to market in a timely manner. LED is reliant on a small number of key employees, the loss of any one of whom could materially affect operating results and the ability to design and manufacture new products.

Distributor Risks

LED distributes its product in the North American market through an exclusive arrangement with one large distributor. In the event this distributor is unable or unwilling to promote and deliver the product to end customers, the Company's financial condition and operating results could be materially impacted. LED is seeking distribution partners in order to expand its business internationally. There can be no assurance the Company will be successful in finding such partners, nor that any such partners will be successful in managing the nuances of their markets to ensure the success of the Company's products in those markets.

Disruptions in Production

Factors that affect the production and sale of LED's products which could result in decreases in profitability include: (a) Acts of God; (b) the expiration or termination of leases, contracts, permits or licences; (c) sales price redeterminations; (d) future litigation; (e) work stoppages or other labour difficulties; (f) disputes with suppliers, distributors and subcontractors; (g) political risk with offshore suppliers; (h) reliance on suppliers with highly technical and not easily replaceable expertise; and (i) changes in the market and general economic conditions. Weather conditions, equipment replacement or repair and fires can have a significant impact on operating results.

Seasonality

Sales may have seasonal components which may result in significant variances in quarterly operating results and may also significantly increase working capital requirements.

Management's Estimates

Management's estimates may prove to be inaccurate due to unexpected changes in business or market conditions.

Regulatory Requirements

Regulatory requirements in international markets may require clinical or other studies that may restrict the ability or timing of LED to sell in these markets.

Reliance on Few Suppliers

The Company has a limited number of suppliers for the raw materials required for its products. A dispute with one of these suppliers, or adverse changes in the business of the suppliers may have a negative impact on the business, operating results and financial condition of the Company if it is unable to source comparable raw materials from alternate sources at competitive rates.

Reliance on Subcontractors

LED utilizes subcontractors who are responsible for its manufacturing requirements. If subcontractors manufacturing a material amount of products cease operations or are unable to come to terms on suitable arrangements with LED, LED's business and profitability may be adversely affected.

The Company May Not Realize the Benefits Currently Anticipated

As part of its strategy, the Company intends to continue its efforts to expand its existing customer base and products. A number of risks and uncertainties are associated with the development of new customers and products, including political, regulatory, design, sourcing, labour, operating, technical, and technological risks. There are also uncertainties relating to capital and other costs, and financing risks in developing new products. The failure to develop one or more of these initiatives successfully could have an adverse effect on the Company's financial position and results of operations.

Operating Cost Fluctuations

Although the Company believes it has consistently adopted conservative assumptions in its estimations, no assurances can be given that such assumptions will prove to be accurate, and, therefore, the operating costs of the Company may prove to be higher or lower than those estimated.

Fluctuations in Exchange Rates

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada and the United States. The Company's functional currency is the Canadian dollar. The Company has not hedged its exposure to currency fluctuations.

Assuming that all other variables remain constant, a 10% change in the value of the Canadian dollar against the US dollar would not materially affect the loss from operations.

Taxation

Canadian taxation authorities may challenge expense or tax credits claimed by LED including research and development expenses and related tax credits. If Canadian tax authorities successfully challenge such expenses or the correctness of tax credit claims, LED or the Resulting Company's operating results could be adversely affected. If Canadian taxation authorities reduce the tax credit either by reducing the rate of the grant or the eligibility of some research and development expenses in the future, LED or the Resulting Company's operating results will be adversely affected.

Worsened General Economic Conditions

The decline in the global economic environment in 2009 and the continuing economic instability in certain parts of the world resulted in increasing uncertainty regarding future revenue and customer commitments, both in terms of timing and magnitude for such future sales. If the global economic climate does not recover, the Company may not generate the sales activity required to support its operations resulting in requirement for additional restructurings and erosion of its existing capital resources which may hinder the future viability of the Company.

Additional Financing

The Company has a history of operating losses and uses cash raised in equity markets to partially fund working capital. If adequate funds are not available when required or on acceptable terms, the Company may be required to delay, scale back or terminate its product development activities and sales and marketing efforts, and may be unable to continue operations. There can be no assurance that the Company will be able to obtain the additional financial resources required to compete in its markets on favourable commercial terms or at all. Any equity offering may result in dilution to the ownership interests of shareholders and may result in dilution of the value of such interests. The availability, or lack thereof, of bank credit, additional supplier credit, or additional equity investment could adversely affect the Company's ability to meet its business objectives. Recent market events and conditions, including disruptions in the Canadian and international credit markets and other financial systems and the deterioration of the Canadian and global economic conditions, could, among other things, impede access to capital or increase the cost of capital, which would have an adverse effect on the Company's ability to fund its working capital and other capital requirements. The Company's access to additional capital may not be available on terms acceptable to the Company or at all.

Research and Development

If the Company fails to develop new products, incurs delays in developing new products, or if the product the Company develops are not successful, the Company's business could be harmed. Even if the Company does develop new products which are accepted by its target markets, the Company cannot assure that the revenue from these products will be sufficient to justify the Company's investment in research and development.

Stock Price Volatility

The market price for the common shares of the Company fluctuates significantly, and these fluctuations tend to be exaggerated if the trading volume is low. The market price of the common shares may rise or fall in response to announcements of

technological or competitive developments, acquisitions or strategic alliances by the Company or its competitors, the gain or loss by the Company of significant orders or broad market fluctuations.

Product Development and Technological Change

The market for the Company's products is characterized by rapidly changing technology, evolving industry standards and frequent new product introductions. To be successful, the Company will need to enhance existing products and to introduce new products and features in response to changing standards, customer requirements, and technological innovations by others. There can be no assurance that the Company will be successful in doing this in a timely manner or at all. There can be no assurance that products or technologies developed by others will not render the Company's products obsolete or non-competitive. There is no assurance that the Company will be able to successfully develop next generation operational products. Failure to do so may have an adverse effect on the business, operating results and financial condition of the Company.

Sales and Marketing and Strategic Alliances

If the Company is to become successful, it must continue to expand its sales and distribution channels and its marketing and technology alliances. There is no assurance the Company will be able to reach agreements with additional alliance or distribution partners on a timely basis or at all, or that these partners will devote sufficient resources to advancing the Company's interests. The Company's business, results of operation, financial condition and stock price may be materially adversely affected if any strategic partner discontinues its relationship with the Company for any reason. Additionally, the Company at times relies on the voluntary efforts of its strategic partners rather than compliance with contractual obligations, and there are at times no minimum performance requirements. Therefore, the Company cannot be certain that these relationships will be successful.

Dependence on a Small Number of Customers

The Company's revenue is dependent, in large part, on significant contracts from a limited number of customers. During the three and twelve months ended December 31, 2011, approximately 62% and 92% of the Company's consolidated revenue was attributable to its largest two customers. Management believes that revenue derived from current and future large customers will continue to represent a significant portion of total revenue. The inability to continue to secure and maintain a sufficient number of large contracts would have a material adverse effect on the business, financial condition, operating results and cash flows of the Company. Moreover, the success of the Company will depend in part upon its ability to obtain orders from new customers, as well as the financial condition and success of its customers and general economic conditions.

Intellectual Property Protection

The Company's ability to compete may be affected by its ability to protect its intellectual property. It relies primarily on a combination of copyright, trademark, patent and trade secret laws, confidentiality procedures and contractual provisions to protect its intellectual property. While the Company believes that its products and technologies are adequately protected against infringement, there can be no assurance of effective protection. Monitoring and identifying unauthorized use of the Company's technology is difficult, and the prohibitive cost of litigation may impair the Company's ability to prosecute any infringement. The commercial success of the Company will also depend upon its products not infringing any intellectual property rights of others and upon no claims for infringement being made against the Company. The Company believes that it is not infringing any intellectual property rights of third parties, but there can be no assurance that such infringement will not occur. An infringement claim against the Company by a third party, even if it is invalid, could have a material adverse effect on the Company because of the costs of defending against such a claim. LED may fail to protect or obtain protection of intellectual property. In addition, LED may be exposed to infringement, misappropriation or other claims by third parties which, if determined adversely, could result in LED paying significant damage awards. LED currently uses patents, trademarks and contractual arrangements with employees to protect its intellectual property rights. LED's existing and future patents could be challenged, invalidated, circumvented or rendered unenforceable. LED's pending patent applications may not result in issued patents, or if patents are issued, such patents may not provide meaningful protection again competitors or against competitive technology. Patents afford only limited protection, and the actions that LED take to protect intellectual property rights may not be adequate. In addition, the process of seeking patent and trademark protection can be time consuming and expensive and there can be no assurance that any future patent or trademark applications will be granted in respect of LED's technology or business.

Competition

Because of intense market competition, the Company may not succeed. Some of the Company's current and potential competitors have longer operating histories, stronger brand names and greater financial, technical, marketing and other resources than the Company. Current and potential competitors may also have existing relationships with many of the Company's prospective customers, and prospective OEM customers may be developing products for their own use that are comparable to the Company's products. In addition, the Company expects competition to persist and intensify in the future, which could adversely affect the Company's ability to increase sales. Competitors have and may in the future align themselves with one or more of several large distributors of dental products which may include exclusive marketing arrangements making a significant portion of the market unavailable to LED.

Potential Fluctuations in Quarterly Results

The Company's quarterly operating results may vary significantly depending on factors such as the timing of new product introductions and changes in pricing policies by the Company and its competitors, market acceptance of new and enhanced versions of the Company's products and the timing of significant orders. Because the Company's operating expenses are based on anticipated revenues and a high percentage of the Company's expenses are relatively fixed in the short term, variations in the timing of recognition of revenues can cause significant fluctuations in operating results from quarter to quarter and may result in unanticipated quarterly earnings shortfalls or losses. The market price of the Company's common shares may be highly volatile in response to such quarterly fluctuations.

Dependence on Key Personnel

The Company's future success depends largely on its ability to attract and retain talented employees. The Company's future results of operations will depend in part on the ability of its officers, management and other key employees to implement and expand operational, customer support and financial control systems and to expand, train and manage its employee base. The Company's future performance will also depend to a significant extent on its ability to identify, attract, train and retain highly skilled sales, technical, marketing and management personnel. If the Company were to lose the services of any key personnel, the Company may encounter difficulties finding qualified replacement personnel. LED's success is largely attributable to the leadership, contacts and efforts of LED's chief executive officer and senior management. If LED's chief executive officer or one or more of the members of the senior management cease working with the Company, and the Company is unable to engage suitable replacements on a timely and commercially viable basis, the business, operating results and financial condition of the Company may be adversely affected.

Acquisitions

The Company in the future may, acquire businesses, products or technologies that it believes complement or expand its existing business. Acquisitions of this type involve a number of risks, including the possibility that the operations of the acquired business will not be profitable or that the attention of the Company's management will be diverted from the day-to-day operation of its business. An unsuccessful acquisition could reduce the Company's margins or otherwise harm its financial condition. Any acquisition could result in a dilutive issuance of equity securities, the incurrence of debt and the loss of key employees. The Company cannot ensure that any acquisitions will be successfully completed or that, if one or more acquisitions are completed, the acquired businesses, products or technologies will generate sufficient revenues to offset the associated costs of the acquisitions or other adverse effects.

Product Liability and Medical Malpractice Claims

LED will be exposed to risks associated with product liability claims if the use of LED's products results in injury or property damage. Users and their patients of the VELscope may be injured as a result of malfunctions, defects or other causes. In addition, medical malpractice claims may be brought against LED. Because of LED's limited operating history, it is difficult to predict if product liability or medical malpractice claims will be brought in the future. LED carries what it believes to be adequate product liability insurance, but LED may not have adequate resources to satisfy a judgement if a successful claim is brought. The assertion of product liability or medical malpractice claims may also significantly damage LED's reputation.

Future Share Sales

If the Company's shareholders sell substantial amounts of the Company's common shares, the market price of the Company's common shares could decrease.

Management of Growth

The Corporation's future results of operations will depend in part on the ability of its officers and other key employees to implement and expand operational, customer support and financial control systems and to expand, train and manage its employee base. The Corporation's future performance will also depend to a significant extent on its ability to identify, attract, train and retain highly skilled sales, technical, marketing and management personnel.

INTERNAL CONTROL OVER FINANCIAL REPORTING AND DISCLOSURE CONTROLS

The Chief Executive Officer and Director of Finance have designed disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to them by others within the Company. The Chief Executive Officer and Director of Finance have also designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and preparation of the financial statements in accordance with Canadian generally accepted accounting principles.

The Chief Executive Officer and Director of Finance have evaluated the effectiveness of the Company's disclosure controls and procedures and assessed the design of the Company's internal controls over financial reporting. This evaluation identified no instances in which internal controls did not operate in an effective manner. Nonetheless, the Company has further strengthened its internal control processes to mitigate future potential material financial statement misstatements and other internal control violations. No additional changes were made in the Company's internal control over financial reporting during the three and nine months ended December 31, 2011 and the most recent interim period that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Because of the inherent limitations in a control system, any control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that it will prevent or detect all misstatements, due to error or fraud, from occurring in the financial statements. As the Company has a limited number of personnel, management has concluded that a weakness exists in the design of internal controls over financial reporting caused by a lack of adequate segregation of duties. This weakness has the potential to result in material misstatements in the Company's financial statements and should also be considered a weakness in its disclosure controls and procedures. Management has concluded that taking into account the present stage of the Company's development and the best interests of its shareholders, the Company does not have sufficient size and scale to warrant the hiring of additional personnel to correct this weakness at this time. To help mitigate the impact of this weakness and to ensure quality financial reporting, supervisory controls are exercised by management and the Audit Committee is vigilant in its' oversight.

The Chief Executive Officer and Director of Finance of the Company conducted an evaluation of the disclosure controls and procedures as required by Multilateral Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings" issued by the Canadian Securities Administrators. They concluded that as at September 30, 2011, the Company's disclosure controls and procedures were effective to provide reasonable assurance that material information regarding required disclosures was made known to them on a timely basis.