REPLICEL LIFE SCIENCES INC.

INDEPENDENT AUDITOR'S REPORT AND CONSOLIDATED FINANCIAL STATEMENTS

For the year-ended December 31, 2012

(<u>Stated in Canadian Dollars</u>)

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Independent Auditor's Report

To the shareholders of RepliCel Life Sciences Inc.

We have audited the accompanying consolidated financial statements of RepliCel Life Sciences Inc., which comprise the consolidated statement of financial position as at December 31, 2012 and December 31, 2011 and the consolidated statements of comprehensive loss, cash flows, and changes in equity for the years ended December 31, 2012, 2011 and 2010, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by IASB, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting and Oversight Board (United States). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of RepliCel Life Sciences Inc. as at December 31, 2012 and December 31, 2011 and its financial performance and its cash flows for the years ended December 31, 2012, 2011 and 2010 in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 2a in the accompanying financial statements which indicates the Company has incurred operating losses since inception, which raises substantial doubt about the Company's ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of these uncertainties.

"BDO Canada LLP"

Chartered Accountants
Vancouver, British Columbia

April 18, 2013

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Financial Position
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

	Notes		December 31, 2012		December 31, 2011
Assets					
Current assets					
Cash and cash equivalents		**$**	**384,286**	$	565,143
Sales taxes recoverable			**47,713**		27,045
Prepaid expenses and deposits			**51,894**		20,644
			483,893		612,832
Non-current assets					
Equipment	7		**21,595**		18,587
Total assets		**$**	**505,488**	$	631,419
Liabilities					
Current liabilities					
Accounts payable and accrued liabilities	9	**$**	**416,125**	$	229,969
			416,125		229,969
Non-current liabilities					
Warrants denominated in a foreign currency	8g		**68,205**		-
Total liabilities			**484,330**		229,969
Shareholders' equity					
Common shares	8		**8,319,082**		6,266,739
Share subscriptions	8		**24,851**		-
Contributed surplus	8		**1,910,621**		1,004,932
Accumulated deficit			**(10,233,396)**		(6,870,221)
Total shareholders' equity			**21,158**		401,450
Total liabilities and shareholders' equity		**$**	**505,488**	$	631,419

The accompanying notes form an integral part of these consolidated financial statements.

Approved on behalf of the Board:

/s/ "David Hall"	*/s/ "Peter Jensen"*
Director	Director

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Comprehensive Loss
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

		December 31, 2012		December 31, 2011		December 31, 2010
Clinical expenses						
Clinical trial costs (Note 9)	$	**638,734**	$	637,649	$	367,763
Research expenses						
Consulting fees (Note 9)		**329,909**		292,207		132,100
Intellectual property costs		**96,432**		89,552		50,386
General and administrative expenses						
Accounting and audit fees		**73,015**		120,357		81,456
Depreciation (Note 7)		**6,082**		7,592		6,940
Consulting fees (Note 9)		**123,200**		185,959		198,196
Insurance		**54,591**		48,006		30,472
Legal fees (Note 9)		**95,383**		118,950		116,954
Listing expense		**-**		-		85,000
Marketing and investor relations		**639,997**		334,709		57,353
Office		**198,377**		170,975		53,259
Salaries (Note 9)		**656,803**		623,027		109,830
Stock-based compensation (Notes 6 and 8)		**1,381,589**		947,272		1,176,900
Transfer agent and filing fees		**54,755**		26,973		24,851
Travel and promotion		**125,102**		130,098		51,065
Loss before other items		**4,473,969**		3,733,326		2,542,525
Other items:						
Change in fair value of warrants denominated in a foreign currency (Note 8g)		**(1,116,445)**		-		-
Foreign exchange loss (gain)		**5,651**		(39,386)		-
Loss on disposal of equipment		**-**		19,499		-
Total comprehensive loss	$	**3,363,175**	$	3,713,439		2,542,525
Total comprehensive loss attributable to non-controlling interest	$	**-**	$	219,479		
Total comprehensive loss attributable to owners' of the parent		**3,363,175**		3,493,960		2,542,525
Basic and diluted loss per share	$	**(0.08)**	$	(0.10)		(0.12)
Weighted average shares outstanding		**42,680,615**		34,942,240		21,567,675

The accompanying notes form an integral part of these consolidated financial statements.

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Cash Flows
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

		December 31, 2012		December 31, 2011		December 31, 2010
Operating activities						
Comprehensive loss	$	**(3,363,175)**	$	(3,713,439)	$	(2,542,525)
Add items not involving cash:						
Depreciation		**6,082**		7,591		6,940
Loss on disposal of equipment		**-**		19,499		-
Stock-based compensation		**1,381,589**		947,272		1,176,900
Change in fair value of warrants		**(1,116,445)**		-		-
Listing expense		**-**		-		85,000
Changes in non-cash working capital balances:						
Sales taxes recoverable		**(20,668)**		13,832		(21,558)
Prepaid expenses and deposits		**(31,250)**		2,948		11,120
Accounts payable and accrued liabilities		**186,156**		(393,326)		389,822
Net cash used in operating activities		**(2,957,711)**		(3,115,623)		(894,301)
Investing activities						
Purchase of Equipment		**(9,090)**		(12,929)		(20,449)
Cash acquired on acquisition of RepliCel		**-**		-		1,109,664
Net cash provided by (used in) investing activities		**(9,090)**		(12,929)		1089,215
Financing activities						
Gross proceeds on issuance of common shares		**2,796,740**		2,482,170		412,500
Issuance of preferred shares		**-**		-		204
Finder's fee		**(35,647)**		-		-
Proceeds of share subscriptions		**24,851**		-		-
Net cash provided by financing activities		**2,785,944**		2,482,170		412,704
Increase (decrease) in cash and cash equivalents during the year		**(180,857)**		(646,382)		607,618
Cash and cash equivalents , beginning of the year		**565,143**		1,211,525		603,907
Cash and cash equivalents , end of the year	$	**384,286**	$	565,143	$	1,211,525

Non-cash transactions (Note 14)

The accompanying notes form an integral part of these consolidated financial statements.

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Changes in Equity
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

	Attributable to the Owners' of the Parent									
	Common Stock			Series B Preferred Shares		Series C Preferred Shares		Contributed	Accumulated	
	Shares	Amount	Share Subscriptions	Shares	Amount	Shares	Amount	Surplus	Deficit	**Total**
Balance, January 1, 2012	43,150,008	$ 6,266,739	$ -	-	$ -	-	$ -	$ 1,004,932	$ (6,870,221)	**$ 401,450**
Shares issued for cash at USD $1.50 – Note 8b	1,875,046	2,761,093	-	-	-	-	-	-	-	**2,761,093**
Warrants denominated in a foreign currency – Note 8g	-	(963,100)	-	-	-	-	-	-	-	**(963,100)**
Escrow Release – Note 8f	-	254,350	-	-	-	-	-	-	-	**254,350**
Stock based compensation – Note 8e	-		-	-	-	-	-	905,689	-	**905,689**
Share subscriptions	-	-	24,851	-	-	-	-	-	-	**24,851**
Net loss for the year	-	-	-	-	-	-	-	-	**(3,363,175)**	**(3,363,175)**
Balance, December 31, 2012	45,025,054	$ 8,319,082	$ 24,851	-	$ -	-	$ -	$ 1,910,621	$ (10,233,396)	**$ 21,158**

The accompanying notes form an integral part of these consolidated financial statements.

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Changes in Equity
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

	Attributable to the Owners' of the Parent										Attributable To Non-Controlling Interest	Total
	Common Stock			Series B Preferred Shares		Series C Preferred Shares		Contributed Surplus	Accumulated Deficit	Total		
	Shares	Amount	Share Subscriptions	Shares	Amount	Shares	Amount					
Balance, January 1, 2011	27,053,960	$ 3,344,320	$ -	5,577,580	$ -	7,577,580	$ 204	$ 235,705	$ (3,219,782)	**$ 360,447**	**$ 325,000**	**$ 685,447**
Net loss for the year	-	-	-	-	-	-	-	-	(3,493,960)	**(3,493,960)**	**(219,479)**	**(3,713,439)**
Private placement – Note 8b	2,651,200	2,482,170	-	-	-	-	-	-	-	**2,482,170**	**-**	**2,482,170**
Increase in non-controlling interest attributable to issuance of shares for cash to parent – Note 6	-	-	-	-	-	-	-	-	(505,345)	**(505,345)**	**505,345**	**-**
Exchange of shares – Note 6	10,844,846	262,000	-	5,422,420	-	5,422,420	-	-	348,866	**610,866**	**(610,866)**	**-**
Cancellation of shares – Note 6	2,600,002	204	-	(11,000,000)	-	(13,000,000)	(204)	-	-	**-**	**-**	**-**
Escrow release – Note 8f	-	178,045	-	-	-	-	-	-	-	**178,045**	**-**	**178,045**
Stock based compensation – Note 8e	-	-	-	-	-	-	-	769,227	-	**769,227**	**-**	**767,227**
Balance, December 31, 2011	43,150,008	$ 6,266,739	$ -	-	$ -	-	$ -	$ 1,004,932	$ (6,870,221)	**$ 401,450**	**$ -**	**$ 401,450**

The accompanying notes form an integral part of these consolidated financial statements.

REPLICEL LIFE SCIENCES INC.
Consolidated Statement of Changes in Equity
For the year-ended December 31, 2012
(Stated in Canadian Dollars)

	Attributable to the Owners' of the Parent										**Attributable To Non-Controlling Interest**	
	Common Stock			Series B Preferred Shares		Series C Preferred Shares						
	Shares	Amount	Share Subscriptions	Shares	Amount	Shares	Amount	Contributed Surplus	Accumulated Deficit	**Total**		**Total**
Balance, January 1, 2010	9,154,800	$ 1,154,800	$ 17,500	-	$ -	-	$ -	$ -	$ (615,257)	**$ 557,043**	$ -	**$ 557,043**
Net loss for the year	-	-	-	-	-	-	-	-	(2,542,525)	**(2,542,525)**	**-**	**(2,542,525)**
Shares issued for cash at $1.00 – Note 8b	430,000	430,000	(30,000)	-	-	-	-	-	-	**400,000**	**-**	**400,000**
Cash received for shares issued in 2009 at $1.00	-	-	12,500	-	-	-	-	-	-	**12,500**	**-**	**12,500**
Recapitalization transactions												
Pursuant to the acquisition of TrichoScience – Note 6	(9,584,800)	-	-	-	-	-	-	-	-	**-**	**-**	**-**
Exchange of shares – Note 6	22,653,960	818,325	-	5,577,580	-	5,577,580	-	-	(62,000)	**756,325**	**325,000**	**1,081,325**
Acquisition of 583885 – Note 6	4,400,000	941,195	-	-	-	-	-	-	-	**941,195**	**-**	**941,195**
Preferred shares issued for cash at US$0.0001 – Note 6	-	-	-	-	-	2,000,000	204	-	-	**204**	**-**	**204**
Stock based compensation – Note 8e	-	-	-	-	-	-	-	235,705	-	**235,705**	**-**	**235,705**
Balance, December 31, 2010	27,053,960	$ 3,344,320	$ -	5,577,580	$ -	7,577,580	$ 204	$ 235,705	$ (3,219,782)	**$ 360,447**	**$ 325,000**	**$ 685,447**

The accompanying notes form an integral part of these consolidated financial statements.

1. Corporate Information

RepliCel Life Sciences Inc. ("the Company" or "RepliCel") was incorporated under the Ontario Business Corporations Act on April 24, 1967. The Company's reporting jurisdiction is British Columbia. Its common shares are listed for trading in the United States on the OTCBB, trading under the symbol REPCF and in Canada on the CNSX, trading under the symbol RP.

RepliCel is in the business of developing and patenting a new hair follicle cell replication technology that has the potential to become the world's first autologous cellular treatment for hair loss in men and women. Our cellular replication and implantation technology is designed to grow new hair follicles in patients suffering from androgenetic alopecia. The procedure is also designed to rejuvenate damaged, miniaturized hair follicles in balding scalp skin.

The address of the Company's corporate office and principal place of business is Suite 2020 – 401 West Georgia Street, Vancouver, BC, V6B 5A1.

2. Basis of Presentation

The financial statements of the Company for the year-ended December 31, 2012, 2011 and 2010 have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

The financial statements are presented in Canadian dollars, which is also the Company's functional currency, unless otherwise indicated.

The financial statements were authorized for issue by the Board of Directors on April 18, 2013.

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment of complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 3.

Certain comparative figures have been reclassified to conform to the current year's presentation to better reflect and classify the results of operations.

a) Going Concern of Operations

These consolidated financial statements have been prepared on a going concern basis, which assumes that the Company will continue to realize its assets and discharge its obligations and commitments in the normal course of operations. At December 31, 2012, the Company is in the research stage, and has accumulated losses of $10,233,396 since its inception and expects to incur further losses in the development of its business, and requires additional funding to continue its research and development activities, which casts substantial doubt about the Company's ability to continue as a going concern.

The Company's ability to continue as a going concern is dependent upon its ability to generate future profitable operations and/or to obtain the necessary financing to meet its obligations and repay its liabilities arising from normal business operations when they come due. Management has a plan in place to address this concern and intends to obtain additional funds by equity financing to the extent there is a shortfall from operations. While the Company is continuing its best efforts to achieve the above plans, there is no assurance that any such activity will generate funds for operations.

If the going concern assumptions were not appropriate for these consolidated financial statements, then adjustments would be necessary to the carrying value of assets and liabilities, the reported net loss and the financial position classifications used.

(Stated in Canadian Dollars)

2. Basis of Presentation – *Continued*

b) Principles of Consolidation

These consolidated financial statements comprise the financial statements of the Company and its subsidiary as at December 31, 2012 and 2011, and the results of its subsidiary for the years ended December 31, 2012, 2011 and 2010.

Details of controlled entities are as follows:

	Country of Incorporation	Percentage Owned December 31, 2012	Percentage Owned December 31, 2011	Percentage Owned December 31, 2010
TrichoScience Innovations Inc.	Canada	100%	100%	55.4%
583885 BC Ltd. [i]	Canada	- %	- %	100%

[i.] 583885 BC Ltd. was dissolved on July 29, 2011.

Where the company has the power, either directly or indirectly, to govern the financial and operating policies of another entity or business so as to obtain benefits from its activities, it is classified as a subsidiary. The consolidated financial statements present the results of the company and its subsidiary ("the Group") as if they formed a single entity. Intercompany transactions and balances between group companies are therefore eliminated in full.

The consolidated financial statements incorporate the results of business combinations using the acquisition method. In the statement of financial position, the acquiree's identifiable assets, liabilities and contingent liabilities are initially recognised at their fair values at the acquisition date. The results of acquired operations are included in the consolidated statement of comprehensive income from the date on which control is obtained. They are deconsolidated from the date control ceases. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

Reverse take-overs that do not meet the definition of a business are accounted for as asset acquisitions using the requirements of IFRS 2 – share-based payments.

c) Derivative liabilities

Derivative instruments, including embedded derivatives, are measured at fair value with any changes in the fair values of derivative instruments being recognized in profit and loss. The disclosure of the Company's financial instruments is further described in Note 8(g).

3. Critical Accounting Estimates and Judgements

RepliCel Life Sciences Inc. makes estimates and assumptions about the future that affect the reported amounts of assets and liabilities. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions.

The effect of a change in an accounting estimate is recognized prospectively by including it in comprehensive income in the period of the change, if the change affects that period only, or in the period of the change and future periods, if the change affects both.

3. Critical Accounting Estimates and Judgements – *Continued*

Information about critical judgments in applying accounting policies that have the most significant risk of causing material adjustment to the amounts reported in these financial statements are discussed below:

Share Based Payments and Derivatives Liabilities related to Equities

The Company measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield and making assumptions about them. The assumptions and models used for estimating the fair value for share-based payment transactions are disclosed in Note 8 (e.

Similar methodology to the share-based payments is used to determine the fair value of derivative liabilities related to warrants denominated in U.S. dollars. The assumptions and models used for estimating the fair value for derivative liabilities are disclosed in Note 8(g).

Income Taxes

Significant judgment is required in determining the provision for income taxes. There are many transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Company recognizes liabilities and contingencies for anticipated tax audit issues based on the Company's current understanding of the tax law. For matters where it is probable that an adjustment will be made, the Company records its best estimate of the tax liability including the related interest and penalties in the current tax provision. Management believes they have adequately provided for the probable outcome of these matters; however, the final outcome may result in a materially different outcome than the amount included in the tax liabilities.

In addition, the Company will recognize deferred tax assets relating to tax losses carried forward to the extent there are sufficient taxable temporary differences relating to the same taxation authority and the same taxable entity against which the unused tax losses can be utilized. However, utilization of the tax losses also depends on the ability of the taxable entity to satisfy certain tests at the time the losses are recouped.

4. Summary of Significant Accounting Policies

The accounting policies set out below have been applied consistently to all years presented in these consolidated financial statements

a) Cash and cash equivalents

Cash and cash equivalents include cash on hand and guarantee investment certificates with financial instructions and other short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and subject to an insignificant risk of change in value.

b) Equipment

Recognition and Measurement

On initial recognition, equipment is valued at cost, being the purchase price and directly attributable cost of acquisition or construction required to bring the asset to the location and condition necessary to be capable of operating in the manner

4. Summary of Significant Accounting Policies – *Continued*

b) Equipment – *Continued*

intended by the Company, including appropriate borrowing costs and the estimated present value of any future unavoidable costs of dismantling and removing items. The corresponding liability is recognized within provisions.

Equipment is subsequently measured at cost less accumulated depreciation, less any accumulated impairment losses.

When parts of an item of equipment have different useful lives, they are accounted for as separate items (major components) of equipment.

Major Maintenance and Repairs

Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit or loss during the financial period in which they are incurred.

Gains and Losses

Gains and losses on disposal of an item of equipment are determined by comparing the proceeds from disposal with the carrying amount, and are recognized net within other income in profit or loss.

Depreciation

Depreciation and amortization rates applicable to each category of equipment are as follows:

Furniture and equipment	20%
Computer equipment	30%

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate Depreciation is taken at half the annual rate in the year of acquisition.

c) Impairment of Non-Financial Assets

Other non-financial assets are subject to impairment tests whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Where the carrying value of an asset exceeds its recoverable amounts, which is the higher of value in use and fair value less costs to sell, the asset is written down accordingly.

Where it is not possible to estimate the recoverable amount of an individual asset, the impairment test is carried out on the asset's cash-generating unit, which is the lowest group of assets in which the asset belongs for which there are separately identifiable cash inflows that are largely independent of the cash inflows from other assets. The Company has one cash-generating unit for which impairment testing is performed.

An impairment loss is charged to the profit or loss, except to the extent they reverse gains previously recognized in other comprehensive loss/income.

4. Summary of Significant Accounting Policies – *Continued*

d) Basic and Diluted Loss per Share

Basic loss per share is calculated by dividing the net loss by the weighted average number of common shares outstanding for the relevant period.

Diluted earnings/loss per common share is computed by dividing the net income or loss applicable to common shares by the sum of the weighted average number of common shares issued and outstanding and all additional common shares that would have been outstanding, if potentially dilutive instruments were converted.

The number of shares potentially issuable at December 31, 2012 that were not included in the computation of loss per share totaled 7,475,046 (2011: 5,035,000; 2010: 4,035,000) consisting of 3,650,000 (2011: 2,835,000; 2010:1,485,000) outstanding stock options and warrants, and 1,700,000 (2011: 2,200,000; 2010: 2,550,000) contingently issuable common shares held in escrow to be released upon the occurrence of certain milestones (Note 8(f)) and 2,125,046 warrants (2011: Nil; 2010: Nil).

e) Income Taxes

Income tax expense comprises of current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that it relates to a business combination or items recognized directly in equity or in other comprehensive loss/income.

Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income or loss for the current year and any adjustment to income taxes payable in respect of previous years. Current income taxes are determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date.

Deferred tax assets and liabilities are recognised where the carrying amount of an asset or liability in the consolidated statement of financial position differs from its tax base, except for differences arising on:

- the initial recognition of goodwill;
- the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting or taxable profit; and
- investments in subsidiaries and jointly controlled entities where the Group is able to control the timing of the reversal of the difference and it is probable that the difference will not reverse in the foreseeable future.

Recognition of deferred tax assets is restricted to those instances where it is probable that taxable profit will be available against which the difference can be utilised.

The amount of the asset or liability is determined using tax rates that have been enacted or substantively enacted by the reporting date and are expected to apply when the deferred tax liabilities/(assets) are settled/(recovered).

Deferred tax assets and liabilities are offset when the Group has a legally enforceable right to offset current tax assets and liabilities and the deferred tax assets and liabilities relate to taxes levied by the same tax authority on either:

- the same taxable group company; or
- different group entities which intend either to settle current tax assets and liabilities on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax assets or liabilities are expected to be settled or recovered.

4. Summary of Significant Accounting Policies – *Continued*

f) Intangible Assets

Externally acquired intangible assets

Externally acquired intangible assets are initially recognised at cost and subsequently amortised on a straight-line basis over their useful economic lives.

In-process research and development programmes acquired in combinations are recognised as an asset even if subsequent expenditure is written off because the criteria specified in the policy for development costs below are not met.

Internally generated intangible assets (development costs)

Expenditure on internally developed products is capitalised if it can be demonstrated that:

- it is technically feasible to develop the product for it to be sold;
- adequate resources are available to complete the development;
- there is an intention to complete and sell the product;
- the Group is able to sell the product;
- sale of the product will generate future economic benefits; and
- expenditure on the project can be measured reliably.

Capitalised development costs are amortised over the periods the Group expects to benefit from selling the products developed.

Development expenditure not satisfying the above criteria and expenditure on the research phase of internal projects are recognised in the consolidated statement of comprehensive income as incurred.

The Company expenses research costs until such time FDA approval is obtained.

g) Foreign Currency Translation

Foreign currency accounts are presented in Canadian dollars, which is also the functional currency.

At the transaction date, each asset, liability, revenue and expense denominated in a foreign currency is translated into Canadian dollars by the use of the exchange rate in effect at that date. At the year-end date, unsettled monetary assets and liabilities are translated into Canadian dollars by using the exchange rate in effect at the year-end date and the related translation differences are recognized in net income.

Non-monetary assets and liabilities that are measured at historical cost are translated into Canadian dollars by using the exchange rate in effect at the date of the initial transaction and are not subsequently restated. Non-monetary assets and liabilities that are measured at fair value or a re-valued amount are translated into Canadian dollars by using the exchange rate in effect at the date the value is determined and the related translation differences are recognized in net income or other comprehensive loss consistent with where the gain or loss on the underlying non-monetary asset or liability has been recognized.

4. Summary of Significant Accounting Policies – *Continued*

h) Share-based Payments

The Company adopted a stock option plan during the year ended December 31, 2010 (Note 8(c)). In addition, certain of the Company's founders have entered into option agreements with consultants and employees of the Company.

Employees (including senior executives) of the Company receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments (equity-settled transactions).

Equity-settled transactions

The cost of equity-settled transactions is recognized, together with a corresponding increase in contributed surplus in equity, over the period in which the performance and/or service conditions are fulfilled. The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The income statement expense or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period and is recognized as stock based compensation expense (Note 8(c)).

No expense is recognized for awards that do not ultimately vest, except for equity-settled transactions where vesting is conditional upon a market or non-vesting condition, which are treated as vesting irrespective of whether or not the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

Where the terms of an equity-settled transaction award are modified, the minimum expense recognized is the expense as if the terms had not been modified, if the original terms of the award are met. An additional expense is recognized for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. This includes any award where non-vesting conditions within the control of either the entity or the employee are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph. All cancellations of equity-settled transaction awards are treated equally. No expense is recognized for awards that do not ultimately vest.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of diluted earnings per share.

Cash-settled transactions

The cost of cash-settled transactions is measured initially at fair value at the grant date using a binomial model. This fair value is expensed over the period until the vesting date with recognition of a corresponding liability. The liability is remeasured to fair value at each reporting date up to and including the settlement date, with changes in fair value recognized as employee benefits expense.

i) Leased assets

Where substantially all of the risks and rewards incidental to ownership of a leased asset have been transferred to the Group (a "finance lease"), the asset is treated as if it had been purchased outright. The amount initially recognised as an asset is the lower of the fair value of the leased property and the present value of the minimum lease payments payable over the term of the lease. The corresponding lease commitment is shown as a liability. Lease payments are analysed

4. Summary of Significant Accounting Policies – *Continued*

i) Leased assets – *Continued*

between capital and interest. The interest element is charged to the consolidated statement of comprehensive income over the period of the lease and is calculated so that it represents a constant proportion of the lease liability. The capital element reduces the balance owed to the lessor.

Where substantially all of the risks and rewards incidental to ownership are not transferred to the Group (an "operating lease"), the total rentals payable under the lease are charged to the consolidated statement of comprehensive income on a straight-line basis over the lease term. The aggregate benefit of lease incentives is recognised as a reduction of the rental expense over the lease term on a straight-line basis.

j) Events After the Financial Position Date

Events after the financial position date that provide additional information about the Company's position at the financial position date (adjusting event) are reflected in the consolidated financial statements. Events after the financial position date that are not adjusting events, if any, are disclosed when material to the consolidated financial statements.

k) Financial Instruments

The Company classifies its financial instruments in the following categories: at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale and financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition.

Financial assets are classified at fair value through profit or loss when they are either held for trading for the purpose of short-term profit taking, derivatives not held for hedging purposes, or when they are designated as such to avoid an accounting mismatch or to enable performance evaluation where a group of financial assets is managed by key management personnel on a fair value basis in accordance with a documented risk management or investment strategy. Such assets are subsequently measured at fair value with changes in carrying value being included in profit or loss.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are subsequently measured at amortized cost. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets.

Held-to-maturity investments are non-derivative financial assets that have fixed maturities and fixed or determinable payments, and it is the Company's intention to hold these investments to maturity. They are subsequently measured at amortized cost. Held-to-maturity investments are included in non-current assets, except for those which are expected to mature within 12 months after the end of the reporting period.

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or are not suitable to be classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments and are subsequently measured at fair value. These are included in current assets. Unrealized gains and losses are recognized in other comprehensive income, except for impairment losses and foreign exchange gains and losses.

Non-derivative financial liabilities (excluding financial guarantees) are subsequently measured at amortized cost. Regular purchases and sales of financial assets are recognized on the trade-date – the date on which the Company commits to purchase the asset.

4. Summary of Significant Accounting Policies – *Continued*

k) Financial Instruments – *Continued*

Financial assets are derecognized when the rights to receive cash flows from the underlying instruments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

At each reporting date, the Company assesses whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a significant and prolonged decline in the value of the instrument is considered to determine whether an impairment has arisen.

As of December 31, 2012, the Company has derivative liabilities of $68,205 (2011: $Nil) in warrants denominated in a foreign currency.

IFRS 7 fair value measurement hierarchy

IFRS 7 requires certain disclosures which require the classification of financial assets and financial liabilities measured at fair value using a fair value hierarchy that reflects the significance of the inputs used in making the fair value measurement (see note 4). The fair value hierarchy has the following levels:

(a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
(b) inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2); and
(c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).

The level in the fair value hierarchy within which the financial asset or financial liability is categorised is determined on the basis of the lowest level input that is significant to the fair value measurement. Financial assets and financial liabilities are classified in their entirety into only one of the three levels.

Impairment of Financial Assets

At each reporting date, the Company assesses whether there is objective evidence that a financial asset carried at amortized cost is impaired. If such evidence exists, the impairment loss is the difference between the amortized costs of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account. Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

l) Share Capital

Financial instruments issued by the Group are classified as equity only to the extent that they do not meet the definition of a financial liability or financial asset.

The Group's ordinary shares are classified as equity instruments. During the year ended December 31, 2012 the Company did not have any Class B preferred shares or Class C convertible preferred shares outstanding. During the year ended December 31, 2011 the Company also had Class B preferred shares and Class C convertible preferred shares outstanding which are also classified as equity instruments.

5. Accounting Standards, Amendments and Interpretations Not Yet Effective

Certain pronouncements were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting periods beginning after January 1, 2013 or later periods. The following new standards, amendments and interpretations, which have not been early adopted in these consolidated financial statements, will or may have an effect on the Company's future results and financial position:

- IFRS 9 Financial Instruments

  IFRS 9 Financial Instruments is part of the IASB's wider project to replace IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The standard is effective for annual periods beginning on or after January 1, 2015. The Company is in the process of evaluating the impact of the new standard.

- IFRS 10 Consolidated Financial Statements

  IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. This standard is applicable for annual periods beginning on or after January 1, 2013. The adoption of this standard is not expected to have material impact on the consolidated financial statements.

- IFRS 13 Fair Value Measurement

  IFRS 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRS. The requirements, which are largely aligned between IFRS and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRS or US GAAP. The standard is effective for annual periods beginning on or after January 1, 2013. The adoption of this standard is not expected to have material impact on the Company's financial statements.

- Amendment to IAS 1 Presentation of Financial Statements

  The amendments to IAS 1 revise the presentation of other comprehensive income (OCI). Separate subtotals are required for items which may subsequently be recycled through profit or loss and items that will not be recycled through profit or loss. The standard is effective for annual periods beginning on or after July 1, 2012. The Company has determined that there is no material impact as a result of these amendments on the presentation of the income statement.

- Amendment to IAS 32 Financial Instruments: Presentations

  The amendments to IAS 32 pertained to the application guidance on the offsetting of financial assets and financial liabilities, focused on four main areas: the meaning of 'currently has a legally enforceable right of set-off', the application of simultaneous realization and settlement, the offsetting of collateral amounts and the unit of account for applying the offsetting requirements. The standard is effective for annual periods beginning on or after January 1, 2014. The Company is in the process of evaluating the impact that the adoptions of this standard may have on its financial statements.

(Stated in Canadian Dollars)

5. Accounting Standards, Amendments and Interpretations Not Yet Effective – *Continued*

- Amendment to IFRS 7, Financial Instruments: Disclosure

  Amended standard IFRS 7 Financial Instruments: Disclosures outlines the disclosures required when initially applying IFRS 9 Financial Instruments. The standard is effective for annual periods beginning on or after January 1, 2015. The Company is in the process of evaluating the impact that the adoptions of this standard may have on its financial statements.

There are no other IFRS or IFRIC Interpretations that are not yet effective that would be expected to have a material impact on the Company.

6. Reverse Takeover Transaction

On December 22, 2010, RepliCel closed a Share Exchange Agreement with TrichoScience Innovations Inc. ("TrichoScience") and with certain accepting shareholders of TrichoScience, whereby RepliCel (formerly Newcastle Resources Ltd.) acquired 50.7% (4,860,000) of the issued and outstanding shares of TrichoScience in exchange for 11,155,165 common shares (at an exchange ratio of 2.2958), 5,577,580 Class B preferred shares and 5,577,580 Class C convertible preferred shares of RepliCel (the "Acquisition"). Also at closing, RepliCel acquired an additional 1,000,000 common shares of TrichoScience for $1,000,000 ("Investment One"), thereby increasing RepliCel's ownership in TrichoScience to 55.4% at December 31, 2010, resulting in 63% of the voting rights in RepliCel being held by former TrichoScience shareholders.

TrichoScience was incorporated under the Canada Business Corporations Act on September 7, 2006 and is currently in the research and development stage and therefore has not yet realized any revenues from its planned operations. .

As the former shareholders of TrichoScience controlled 63% of the issued voting shares of RepliCel after the closing of the transaction, the transaction was accounted for as TrichoScience being the continuing entity and the resulting consolidated financial statements are presented as a continuation of TrichoScience. At the date the share exchange was completed the common stock of RepliCel became 22,653,960 common shares, comprising of 11,155,165 common shares issued to participating shareholders of TrichoScience and 11,498,795 common shares held by existing RepliCel shareholders (total common shares 22,653,960). During the year ended December 31, 2011 the remaining TrichoScience shareholders tendered 4,724,800 TrichoScience shares in exchange for 10,844,846 common shares of RepliCel.

As TrichoScience is deemed to be the acquirer for accounting purposes, its assets and liabilities are included in the consolidated balance sheets for the continuing entity at their historical carrying values. The Company's assets and liabilities at the date of the transaction are also included in the consolidated balance sheets at their historical carrying values.

RepliCel is not considered a business as defined by IFRS. As a result, at the date of the acquisition, the transaction was accounted for as a share based payment transaction under IFRS 2 Share Based Payments whereby TrichoScience is deemed to have issued shares in exchange for the net assets of RepliCel together with the listing status of RepliCel.

The net identifiable assets of RepliCel at the date of the acquisition were as follows:

Cash	$ 1,109,664
Sales taxes recoverable	19,319
Prepaid expenses	13,392
Accounts payable and accrued liabilities	(146,050)
Net assets acquired	$ 996,325

6. Reverse Takeover Transaction – *Continued*

The Company recognized $85,000 as listing expense during the year ended December 31, 2010, being the difference between the fair value of the share based payment of $1,081,325 and the net identifiable assets received. The fair value of the share based payment was determined with reference to the fair market value of Newcastle, (now RepliCel) shares that would have been received by the shareholders of TrichoScience had 100% of the shares been exchanged. The fair value of each Newcastle, (now RepliCel) share was determined with reference to the price at which the shares had been sold in arms' length transaction prior to the acquisition.

At closing, the TrichoScience shareholders who received shares of RepliCel in connection with the closing deposited the common shares with a trustee pursuant to the terms of a pooling agreement between RepliCel and the trustee. The common shares are subject to a timed release schedule under which 15% of the shares will be released on the first day of each of the fiscal quarters occurring after the first anniversary of the closing.

Non-Controlling Interest

At closing, certain shareholders of TrichoScience did not exchange their shares for shares of RepliCel (the "Non-Accepting Shareholders") and, as such, are treated as a non-controlling interest in the consolidated financial statements. In a reverse acquisition, the non-controlling interest reflects the non-controlling shareholders' proportionate interest in the pre-combination carrying amounts of the legal acquiree's net assets. The non-controlling interest at December 22, 2010 was 44.6% and the Company recorded a non-controlling interest of $325,000, representing the non-controlling interest of the net book value of the net assets of TrichoScience, with a $62,000 increase in accumulated deficit reflecting the Company's proportionate increase in ownership in TrichoScience.

During the year ended December 31, 2011, RepliCel purchased 2,050,000 newly issued common shares of TrichoScience for $2,050,000 ("Investment Two"). As a result, the non-controlling interest increased by $505,345 representing the non-controlling interests' proportionate share in Investment Two.

During the year ended December 31, 2011, the remaining 4,724,800 shares of TrichoScience were tendered for exchange by the Non-Accepting Shareholders in exchange for 10,844,848 common shares with an ascribed fair value of $262,000, 5,422,420 Series B Preferred Shares and 5,422,420 Series C Preferred Shares of the Company. As a result the non-controlling interest was eliminated and the Company recorded an adjustment of $348,866 into deficit attributable to the Owners' of the Parent, representing a decrease in the non-controlling interest of the net book value of the net assets of TrichoScience..

At December 31, 2011, 100% percent of the non-accepting shareholders had tendered their shares in exchange for RepliCel shares. As a result of achieving Investment One and Investment Two, TrichoScience is now 100% owned subsidiary of RepliCel. As a result, the Class B preferred shares were extinguished for no consideration. There is no non-controlling interest at December 31, 2012 (December 31, 2011: $nil; December 31, 2010: $325,000).

Class B and C Preferred Shares

Pursuant to the Share Exchange Agreement, Class B and C preferred shares were created and issued. No amount of the value assigned to share capital issued with the Share Exchange Agreement was allocated to the Class B preferred shares or the Class C convertible preferred shares due to these shares having assessed nominal value of $204 at the time of closing. The Class B preferred shares have been extinguished, as the Company has achieved the following milestones during the year ended December 31, 2011:

6. Reverse Takeover Transaction – *Continued*

Class B and C Preferred Shares *– Continued*

- RepliCel purchased common shares of TrichoScience in aggregate amount of not less than $3,000,000 and RepliCel raised the proceeds to make these investments by selling its shares at not less than $1 per share (completed); and

- RepliCel acquired at least 90% of the issued and outstanding common shares of TrichoScience (completed).

Each Class C convertible preferred share is voting and convertible into ½ of one common share of RepliCel upon approval by the United States Food and Drug Administration of the commercial sale of TrichoScience's hair cell replication technology in the United States. Other than transfers of Class C Shares amongst original shareholders of TrichoScience Innovations Inc., the Class C convertible preferred shares cannot be sold, transferred or otherwise disposed of without the consent of the Company's directors.

During the year-ended December 31, 2011, 13,000,000 of the Company's Class C preferred shares (each, a "Class C Share"), being all the issued and outstanding Class C Shares, were converted, on a 5:1 ratio, into 2,600,002 common shares of the Company (each, a "Common Share") by the holders thereof. All of the Common Shares issued on conversion of the Class C Shares have been deposited with a trustee pursuant to the terms of pooling agreements between RepliCel, the trustee and the respective shareholders. The Common Shares are subject to a timed release schedule under which 15% of the shares will be released on the first day of each of the fiscal quarters beginning January 1, 2013.

583885 B.C. Ltd.

Concurrent with the reverse acquisition, RepliCel also acquired all of the issued and outstanding common shares of 583885 B.C. Ltd. ("583885") in exchange for 4,400,000 common shares of RepliCel. 583885 did not have any assets or liabilities at the date of acquisition and was a private company controlled by RepliCel's incoming Chief Executive Officer ("CEO"). 3,400,000 shares of RepliCel controlled by the Company's CEO were deposited with an escrow agent pursuant to the terms of an escrow agreement between RepliCel and the escrow agent. These shares are released upon satisfaction of certain performance conditions as set out in the escrow agreement and each release of shares from escrow will be considered a compensatory award. The Compensatory award is recorded as an expense at the fair value of the consideration given based on the price of RepliCel's common shares on the acquisition date. This amount was determined to be US$0.50 per share, based on the price of the shares being offered in the private placement that closed concurrent with the share exchange to arm's length parties at a price of US$0.50.

During the year-ended December 31, 2012, the performance condition with respect to 500,000 shares (Year ended December 31, 2011: 350,000 shares, Year ended December 31, 2010: 850,000 shares, being the completion of Investment Two described above) had been achieved, and $254,350 representing the fair value of the shares released from escrow was recorded as stock-based compensation (year-ended December 31, 2011: $178,045; year ended December 31, 2010: $432,295). Compensation expense relating to the transaction date fair value of the remaining 1,700,000 common shares will be recognized in the period the respective performance condition is probable and amortized over the period the performance condition is met.

At December 31, 2012, there were 1,700,000 common shares held in escrow (December 31, 2011: 2,200,000 common shares; December 31, 2010: 2,550,000 common shares).

The other 1,000,000 common shares issued were not subject to escrow provisions and thus were fully vested, non-forfeitable at the date of issuance. Stock based compensation of $Nil (representing the fair value of the shares issued) was recognized for these shares during the year ended December 31, 2012 (December 31, 2011: Nil; December 31, 2010:$508,800).

(Stated in Canadian Dollars)

7. Equipment

	Furniture and Equipment	Computer Equipment	Total
Cost:			
At December 31, 2011	$ 6,995	$ 19,704	**$ 26,699**
Additions	7,254	1,836	**9,090**
Disposals	-	-	**-**
At December 31, 2012	14,249	21,540	**35,789**
Depreciation:			
At December 31, 2011	1,868	6,244	**8,112**
Charge for the year	2,201	3,881	**6,082**
Elimination on disposal	-	-	**-**
At December 31, 2012	4,069	10,125	**14,194**
Net book value at December 31, 2012	$ 10,180	$ 11,415	**$ 21,595**

	Furniture and Equipment	Computer Equipment	Total
Cost:			
At December 31, 2010	$ 25,880	$ 16,258	**$ 42,138**
Additions	-	12,929	**12,929**
Disposals	(18,885)	(9,483)	**(28,368)**
At December 31, 2011	6,995	19,704	**26,699**
Depreciation:			
At December 31, 2010	5,311	4,079	**9,390**
Charge for the year	1,882	5,710	**7,592**
Elimination on disposal	(5,325)	(3,545)	**(8,870)**
At December 31, 2011	1,868	6,244	**8,112**
Net book value at December 31, 2011	$ 5,127	$ 13,460	**$ 18,587**

8. Share Capital

a) Authorized:

Unlimited common shares without par value
Unlimited Class A non-voting, convertible, redeemable, non-cumulative 6% preferred shares without par value

b) Issued and Outstanding:

During the year-ended December 31, 2012:

(i) The Company completed a private placement of 1,875,046 units at US$1.50 per unit for proceeds of $2,796,740 (US$2,812,569). A finder's fee of $35,647 (US$36,000) was paid in cash in connection with the private placement. Each unit issued consists of one common share of the Company and one common share purchase warrant. Each warrant entitles the holder to purchase an additional common share at US$2.50 per share for a period of 24 months from the closing of the Financing. As the share purchase warrants are denominated in a currency other than the Company's functional currency, the fair value of the share purchase warrants is recognized as a derivative liability. The fair value on issuance was determined to be $963,100. These warrants have been included in the share warrant data presented in Note 8g.

During the year-ended December 31, 2011:

(i) The Company completed a private placement of 2,550,000 common shares at US$1.00 per share for proceeds of $2,482,170 (US$2,550,000). A finder's fee of 101,200 common shares was issued in connection with the private placement with a fair value of $98,164 (US$101,200).

(ii) The Company acquired 4,724,800 common shares of TrichoScience pursuant to the Non-Accepting Shareholders tendering their shares in exchange for 10,844,848 common shares, 5,422,420 Class B preferred shares and 5,422,420 Class C preferred shares in RepliCel. (Note 6).

During the year-ended December 31, 2010:

(i) The Company issued 430,000 common shares at a price of $1.00 per share, of which $30,000 had been received during the year ended December 31, 2009.

(ii) The Company completed the RTO transaction as described in Note 6.

c) Stock Option Plans:

(i) Under various Founders' Stock Option Agreements, certain founders of TrichoScience granted stock options to acquire TrichoScience shares to employees and consultants of TrichoScience. These founders' options are exercisable at $1 per share with 1/3 vesting one year from the date of grant and the remaining 2/3 vesting on a monthly basis over between 24-month and 36-month periods expiring after six to seven years. Pursuant to the Share Exchange Agreement, the Founders Stock Option Agreements were converted into rights to receive the number of Founders' RepliCel shares acquired by conversion of the founders TrichoScience shares under the Share Exchange Agreement. All other terms remained the same. This modification of stock options resulted in no incremental value and therefore no additional stock based compensation expense was recognized for the modification.

(Stated in Canadian Dollars)

8. Share Capital – *Continued*

c) Stock Option Plans – *Continued*

(ii) On December 22, 2010, the Company approved a Company Stock Option Plan whereby the Company may grant directors, officers, employees and consultants' stock options. The maximum number of shares reserved for issue under the plan cannot exceed 10% of the outstanding common shares of the Company as at the date of the grant. The stock options can be exercisable for a maximum of 7 years from the grant date and with various vesting terms.

d) Fair value of Company Options Issued from January 1, 2010 to December 31, 2012

On June 21, 2012 under the Company Stock Option Plan, 300,000 options were granted to consultants of the Company. The options vest over a period of three years and are exercisable at US$1.10 per share until June 21, 2017.

On April 18, 2012 under the Company Stock Option Plan, 790,000 options were granted to employees and consultants of the Company. The options vest over a period of three years and are exercisable at US$1.50 per share until April 18, 2019. During the year-ended December 31, 2012, 75,000 of these options were forfeited.

On January 3, 2012 under the Company Stock Option Plan, 100,000 options were granted to a consultant of the Company. The options are exercisable at US$2.35 per share and expire on January 3, 2019. The options vest according to specific milestones.

On March 11, 2011, under the Company Stock Option Plan, 1,350,000 options were granted to the directors, officers and consultants of the Company. The options are exercisable at US$1.00 per share and expire on March 11, 2018. The options vest over a three year period.

During the year ended December 31, 2010, under the Company Stock Option Plan 1,485,000 options were granted to the directors, officers and consultants of the Company. The options are exercisable at US$0.50 per share and expire July 13, 2017. The options fully vested during the year ended December 31, 2011. During the year-ended December 31, 2012, 300,000 of these options were cancelled.

The weighted-average grant date fair value of options granted was estimated using the following weighted average assumptions:

Grant Date	Number of Options Outstanding	Risk-free interest rate	Weighted-average expected life	Expected volatility	Expected dividends	Expected forfeiture rate	Fair value
December 22, 2010	1,185,000	2.66%	7 years	81%	Nil	0%	0.17
March 11, 2011	1,350,000	2.88%	7 years	81%	Nil	0%	0.72
January 3, 2012	100,000	1.71%	7 years	81%	Nil	0%	1.01
April 18, 2012	715,000	1.74%	7 years	89%	Nil	0%	1.15
June 21, 2012	300,000	1.26%	5 years	89%	Nil	0%	0.78

The volatility assumption is based on the pattern and level of historical volatility of a sample of entities in the life sciences industry for the first seven years in which the shares of those entities were publicly traded.

(Stated in Canadian Dollars)

8. Share Capital – *Continued*

d) Fair value of Options Issued from January 1, 2011 to December 31, 2012 – *Continued*

Options Issued to Employees

The fair value at grant date is determined using a Black-Scholes option pricing model that takes into account the exercise price, the term of the option, the impact of dilution, the share price at grant date and expected price volatility of the underlying share, the expected dividend yield, the expected forfeiture rate and the risk free interest rate for the term of the option.

Options Issued to Non-Employees

Options issued to non-employees, are measured based on the fair value of the goods or services received, at the date of receiving those goods or services. If the fair value of the goods or services received cannot be estimated reliably, the options are measured by determining the fair value of the options granted, using a valuation model.

e) Stock-based Compensation

The Company recognized stock-based compensation of $1,381,589, of which $905,689 for the fair value of stock options granted under the Company Stock Option Plan and the Founders Stock Option Agreements, $254,350 for the release of escrow shares , and $221,500 for the fair value of warrants denominated in a foreign currency which were issued as compensation, in the statement of comprehensive loss for the year-ended December 31, 2012; (For the year-ended December 31, 2011- $769,227, $178,045 and $Nil, respectively; and for the year-ended December 31, 2010- $235,705, $432,395 and $Nil respectively). A summary of the status of the stock options outstanding under the Company Stock Option Plan for the year-ended December 31, 2012 is as follows:

	Number of Options		Weighted Average Exercise Price
Outstanding, January 1, 2012	2,835,000	$	US 0.74
Granted	1,190,000		US 1.47
Exercised	-		-
Forfeited	(300,000)		US 0.50
Cancelled	(75,000)		US 1.50
Outstanding, December 31, 2012	**3,650,000**		**US 0.98**
Exercisable, December 31, 2012	**2,113,750**		**US 0.77**
Outstanding, January 1, 2011	1,485,000	$	US 0.50
Granted	1,350,000		US 1.00
Exercised	-		-
Forfeited/Cancelled	-		-
Outstanding, December 31, 2011	2,835,000	$	US 0.74
Exercisable, December 31, 2011	1,822,500	$	US 0.59
Outstanding, January 1, 2010	-	$	-
Granted	1,485,000		US 0.50
Exercised	-		-
Forfeited/Cancelled	-		-
Outstanding, December 31, 2010	1,485,000		US 0.50
Exercisable, December 31, 2010	-	$	-

(Stated in Canadian Dollars)

8. Share Capital – *Continued*

e) Stock-based Compensation – *Continued*

The range of exercise prices for options outstanding under the Company Stock Option Plan as at December 31, 2012 is US$0.50 - US$2.35. The weighted average remaining contractual life for stock options under the Company Stock Option Plan as at December 31, 2012 is 5.16 years.

f) Escrow Shares

Pursuant to the Acquisition described in Note 6, at December 31, 2012:

i) 1,700,000 (December 31, 2011: 2,200,000; December 31, 2010: 2,550,000) common shares are held in escrow and are to be released upon the occurrence of certain milestones relating to the Company's hair cell replication technology. These shares have been excluded from the calculation of loss per share. During the year-ended December 31, 2012, 500,000 shares were released from escrow (December 31, 2011: 350,000; December 31, 2010: 850,000). The Company recognized a fair value of $254,350, (December 31, 2011: $178,045; December 31, 2010: $432,295) as stock based compensation expense in the statement of operations for the period. As at December 31, 2012, an accumulated 1,700,000 shares have been released from escrow (December 31, 2011: 1,200,000; December 31, 2010: 850,000).

ii) 14,499,156 (December 31, 2011: 25,600,013, December 31, 2010: 11,155,165) common shares are held in escrow under a pooling agreement and are subject to a timed release schedule under which:

a) 15% will be released on the first day of the Company's fiscal quarter beginning after the one year anniversary of the share exchange (the "First Quarter");
b) 15% will be released on the first day of each of the Company's next five fiscal quarters after the First Quarter;
c) the remaining 10% will be released on the first day of the ninth fiscal quarter after the First Quarter.

As the release of these shares is certain, they have been included in the calculation of loss per share. At December 31, 2012, 11,100,844 shares have been released from escrow (December 31, 2011: nil; December 31, 2010: nil).

g) Warrants denominated in a foreign currency

The continuity of the number of warrants denominated in another currency, each exercisable into one common share, is as follows:

	Warrants Outstanding		Weighted Average Exercise Price	Expiry
Outstanding, December 31, 2011	-	$	-	
February 29, 2012	66,304		US 2.50	March 1, 2014
March 29, 2012	876,042		US 2.50	March 29, 2014
April 18, 2012	502,667		US 2.50	April 18, 2014
April 20, 2012	430,033		US 2.50	April 20, 2014
May 17, 2012	250,000		US 2.00	May 17, 2016
Outstanding, December 31, 2012	2,125,046	$	US 2.44	

(Stated in Canadian Dollars)

8. Share Capital – *Continued*

g) Warrants denominated in a foreign currency – *Continued*

As the warrants are denominated in a currency other than the Company's functional currency, they meet the definition of a financial liability and accordingly are presented as such on the Company's consolidated statement of financial position and are fair valued at each reporting period. The fair value on issuance was determined to be $1,184,650, of which $221,550 was included in stock based compensation for the year-ended December 31, 2012 as warrants were initially issued as compensation and the remaining balance of $963,100 was debited against share capital. Assumptions applied by management were as follows: (1) risk-free rate of 1.10% – 1.35%; (2) dividend yield of nil; (3) an expected volatility of 89%; (4) an expected life of 24 - 48 months; (5) market price of US$1.50 and (6) an exercise price of US$2.00 – US$2.50.

The assumptions used to determine the fair value of $68,205 at December 31, 2012 were as follows: (1) risk-free rate of 1.14% – 1.21%; (2) dividend yield of nil; (3) an expected volatility of 89%; (4) an expected life of 14 – 41 months; (5) market price of US$0.46; and (6) an exercise price of US$2.00 – US$2.50.

The change in the fair value of the warrants for the year-ended December 31, 2012 was $1,116,445 (December 31, 2011 - $Nil; December 31, 2010 - $Nil) and was recorded in the consolidated statement of comprehensive loss.

	December 31, 2012	December 31, 2011	December 31, 2010
Warrants denominated in a foreign currency, opening balance	**$ -**	$ -	$ -
Fair value of warrants issued	**1,184,650**	-	-
Change in fair value of warrants	**(1,116,445)**	-	-
Warrants denominated in a foreign currency, closing balance	**$ 68,205**	$ -	$ -

Subsequent to December 31, 2012, the Company amended the exercise price of the warrants expiring March 1, 2014, March 29, 2014, April 18, 2014 and April 20, 2014 from US$2.50 to US$0.50 per share. The warrants entitle holders to purchase an aggregate of 1,875,046 common shares.

9. Related Party Transactions

Related party balances

The following amounts due to related parties are included in trade payables and accrued liabilities:

	December 31, 2012	December 31, 2011
Companies controlled by directors of the Company	**$ 31,318**	$ 10,000
Directors or officers of the Company	**21,015**	9,596
	$ 52,333	$ 19,596

These amounts are unsecured, non-interest bearing and have no fixed terms of repayment.

Related party transactions

The Company incurred the following transactions with companies that are controlled by directors and/or officers of the Company. The transactions were measured at the exchange amount which approximates fair value, being the amount established and agreed to by the parties.

(Stated in Canadian Dollars)

9. Related Party Transactions – *Continued*

Related party transactions – *Continued*

	December 31, 2012	December 31, 2011	December 31, 2010
Clinical trial costs	**$ 110,703**	$ 103,563	$ -
Research consulting fees	**163,543**	135,044	144,100
General and administrative consulting fees	**-**	45,750	116,475
Office	**-**	9,000	15,000
Legal fees	**-**	6,621	39,326
	$ 274,246	$ 299,977	$ 314,901

Key management compensation

Key management personnel are persons responsible for planning, directing and controlling the activities of an entity, and include executive directors, the Chief Executive Officer and the Chief Financial Officer.

	December 31, 2012	December 31, 2011	December 31, 2010
General and administrative – salaries	**$ 411,000**	$ 425,209	$ 30,000
Stock-based compensation	**161,565**	313,665	432,395
	$ 572,565	$ 738,874	$ 462,395

10. Income Taxes

a) Reconciliation of accounting and taxable income, for the years ended December 31 are as follows:

	2012	2011	2010
Net loss for the year before taxes	$ (3,363,175)	$ (3,713,439)	$ (2,542,525)
Combined federal and provincial income tax rate	25.0%	26.50%	31.00%
Expected income tax expense (recovery)	(841,000)	(984,000)	(788,000)
Increase (decrease) resulting from			
Income taxed at reduced rate	-	-	280,000
Non-deductible items	68,000	253,000	335,000
Tax adjustment from rate change and other	4,000	23,000	(158,000)
Change in unrecognized deferred tax assets	769,000	708,000	331,000
	$ -	$ -	$ -

Effective January 1, 2012, the Canadian Federal corporate tax rate decreased from 16.5% to 15% while the British Columbia provincial tax rate remained at 10%.

(Stated in Canadian Dollars)

10. Income Taxes – *Continued*

b) The components of the deferred tax asset (liability) balances for the years ended December 31, are as follows:

	2012	2011
Deferred tax assets		
Non-capital losses	$ 1,854,000	$ 1,112,000
Equipment and other	90,000	63,000
Temporary differences relating to intellectual property costs	17,000	17,000
Unrecognized deferred tax assets	(1,961,000)	(1,192,000)
	$ -	$ -

Deferred tax assets in respect of losses and other temporary differences are recognized when it is more likely than not, that they will be recovered against profits in future periods. No deferred tax asset has been recognized as this criteria has not been met.

At December 31, 2012, the Company has non capital losses totalling approximately $7,415,100 that will expire beginning in 2026:

Year of Expiry	Amount
2026	$ 5,500
2027	16,200
2028	533,200
2029	1,169,400
2031	2,672,700
2032	3,018,100
	$ 7,415,100

11. Financial Instruments and Risk Management

As at December 31, 2012, the Company's financial instruments are comprised of cash, accounts payable and accrued liabilities, and warrants denominated in a foreign currency. The fair values of cash, accounts payable and accrued liabilities approximate their carrying value due to their short-term maturity.

The Company is exposed through its operations to the following financial risks:

- Currency risk
- Credit risk
- Liquidity risk
- Interest rate risk

In common with all other businesses, the Company is exposed to risks that arise from its use of financial instruments. This note describes the Company's objectives, policies and processes for managing those risks and the methods used to measure them. Further quantitative information in respect of these risks is presented throughout these financial statements.

11. Financial Instruments and Risk Management – *Continued*

There have been no substantive changes in the Company's exposure to financial instrument risks, its objectives, policies and processes for managing those risks or the methods used to measure them from previous periods unless otherwise stated in this note.

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company has an exposure to the European Euros as certain expenditures and commitments are denominated in European Euros and the Company is subject to fluctuations as a result of exchange rate variations to the extent that transactions are made in this currency. In addition, the Company holds a significant amount of cash in US dollars and is therefore exposed to exchange rate fluctuations on these cash balances. The Company does not hedge its foreign exchange risk. At December 31, 2012 the Company held cash balances of $371,930 (US$373,836) (December 31, 2011: $307,756 or US302,611; December 31, 2010: $nil). A 1% increase/decrease in the US dollars foreign exchange rate would have an impact of ±$3,719 (US$3,738) on the cash balance held at December 31, 2012.

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's credit risk is primarily attributable to its cash. The Company limits exposure to credit risk by maintaining its cash with large financial institutions. The Company's maximum exposure to credit risk is the carrying value of its financial assets.

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk through the management of its capital structure, more specifically, the issuance of new common shares, to ensure there is sufficient capital in order to meet short term business requirements, after taking into account the Company's holdings of cash and potential equity financing opportunities. The Company believes that these sources will be sufficient to cover the known short and long-term requirements at this time. There is no assurance that potential equity financing opportunities will be available to meet these obligations.

The following table sets out the contractual maturities (representing undiscounted contractual cash-flows) of financial liabilities as at December 31, 2012:

Year of expiry		Accounts payable and accrued liabilities		Total
Within 1 year	$	416,125	$	416,125

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. As the Company's cash is currently held in an interest bearing bank account, management considers the interest rate risk to be limited.

Classification of financial instruments

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

	Classification		**December 31, 2012**		December 31, 2011
Cash and cash equivalents	Loans and receivables	**$**	**384,286**	$	565,143
		$	**384,286**	$	565,143

(Stated in Canadian Dollars)

11. Financial Instruments and Risk Management – *Continued*

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

	Classification	December 31, 2012	December 31, 2011
Non-derivative financial liabilities:			
Accounts payable and accrued liabilities	Financial liabilities at amortized cost	**$ 416,125**	$ 229,969
Derivative financial liabilities:			
Warrants denominated in a foreign currency	Fair value through profit or loss	**68,205**	-
		$ 484,330	$ 229,969

12. Commitments

The Company has entered into an operating lease agreement for its office premises. The term of the lease is for three years with ending on October 31, 2015 and the annual commitments under the lease is as follows:

2013	2014	2015
$ 130,470	$ 133,200	$ 119,550

13. Capital Management

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern in order to pursue business opportunities. In order to facilitate the management of its capital requirements, the Company prepares periodic budgets that are updated as necessary. The Company manages its capital structure and makes adjustments to it to effectively support the Company's objectives. In order to pay for general administrative costs, the Company will use its existing working capital and raise additional amounts as needed. The Company will continue to advance its technology.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. The Company considers shareholders equity and working capital as components of its capital base. The Company can access or increase capital through the issuance of shares, and by sustaining cash reserves by reducing its capital and operational expenditure program. Management primarily funds the Company's expenditures by issuing share capital, rather than using capital sources that require fixed repayments of principal and/or interest. The Company is not subject to externally imposed capital requirements and does not have exposure to asset-backed commercial paper or similar products. The Company believes it will be able to raise additional equity capital as required, but recognizes the uncertainty attached thereto.

The Company's investment policy is to hold cash in interest bearing bank accounts, which pay comparable interest rates to highly liquid short-term interest bearing investments with maturities of one year or less and which can be liquidated at any time without penalties.

There has been no change in the Company's approach to capital management during the year-ended December 31, 2012.

14. Non-cash Transactions

Investing and financing activities that do not have a direct impact on current cash flows are excluded from the consolidated statements of cash flow. There were no non-cash transactions during the year-ended December 31, 2012.

During the year-ended December 31, 2011, the Company acquired 4,724,800 common shares of TrichoScience in exchange for 10,844,846 common shares, 5,422,420 Series B Preferred Shares and 5,422,420 Series C Preferred Shares of the Company, which was excluded from the condensed consolidated interim statement of cash flows for $262,000 (December 31 2010: $Nil). During the year-ended December 31, 2011, 13,000,000 of the Company's Class C preferred shares (each, a "Class C Share"), were converted, on a 5:1 ratio, into 2,600,000 common shares of the Company (each, a "Common Share") by the holders thereof.

During the year ended December 31, 2010, the following transactions were excluded from the consolidated statement of cash flows: The Company acquired 4,860,000 common shares of TrichoScience in exchange for 11,155,165 common shares, 5,577,580 Series B Preferred Shares and 5,577,580 Series C Preferred Shares of the company; and the Company acquired all of the issued and outstanding shares of 583885 in exchange for 4,440,000 common shares of the Company.

15. Segmental Reporting

The Company is organized into one business unit based on its hair cell replication technology and has one reportable operating segment.

16. Events after the Reporting Date

Subsequent to December 31, 2012, the Company amended the exercise price of the warrants expiring March 1, 2014, March 29, 2014, April 18, 2014 and April 20, 2014 from US$2.50 to US$0.50 per share. The Warrants entitle holders to purchase an aggregate of 1,875,046 common shares.

Subsequent to December 31, 2012, the Company completed a private placement of 1,643,555 units at a price of CAD$0.31 per unit for gross proceeds of $509,502, of which $24,851 was included in share subscriptions as at December 31, 2012. Each unit issued consists of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase an additional common share at CAD$0.50 per share for a period of 24 months from the closing of the financing.

Subsequent to December 31, 2012, the Company received a proposed assessment as a result of Canada Revenue Agency's audit of the Scientific Research & Experimental Development (SR&ED) Claim filed by TrichoScience for the period ending December 21, 2010. As a result of the assessment, TrichoScience will receive a refundable investment tax credit in the amount of $148,296.