

**Med BioGene Inc.**

(a development stage company)

Consolidated Financial Statements

**December 31, 2014 and 2013**

(Expressed in US dollars)

## INDEPENDENT AUDITORS' REPORT

### To the Shareholders of Med BioGene Inc.,

We have audited the accompanying consolidated financial statements of Med BioGene Inc. and its subsidiary which comprise the consolidated statements of financial position as at December 31, 2014 and 2013, and the consolidated statements of comprehensive loss, cash flows and changes in equity for the years then ended, 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 the International Accounting Standards Board, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' 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. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free of 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 overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained 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 Med BioGene Inc. and its subsidiary as at December 31, 2014 and 2013 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

### Emphasis of Matter

Without modifying our opinion, we draw attention to Note 1 in the financial statements which indicates that the Company has limited working capital, limited sources of revenue, and is dependent upon its ability to secure new sources of financing. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern.

*De Visser Gray LLP*

**CHARTERED ACCOUNTANTS**

Vancouver, Canada  
April 29, 2015

# Med BioGene Inc.

(a development stage company)

## Consolidated Statements of Financial Position

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(expressed in US dollars)

	<b>December 31, 2014</b>	<b>December 31, 2013</b>
<b>ASSETS</b>		
<b>Current assets</b>		
Cash	\$ 144,306	\$ 181,507
Receivables (Note 5)	6,494	2,348
Total assets	<u>\$ 150,800</u>	<u>\$ 183,855</u>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	\$ 62,380	\$ 61,469
Due to related parties (Note 7)	126,717	9,762
Total liabilities	<u>189,097</u>	<u>71,231</u>
<b>EQUITY (DEFICIENCY)</b>		
Common shares (Note 6)	8,783,198	8,603,874
Equity reserves (Note 6)	4,620,151	4,620,151
Deficit accumulated during the development stage	(13,734,747)	(13,443,306)
Accumulated other comprehensive income	293,101	331,905
Total equity (deficit)	<u>(38,297)</u>	<u>112,624</u>
Total liabilities and equity (deficiency)	<u>\$ 150,800</u>	<u>\$ 183,855</u>

**Nature of operations and going concern** (Note 1)

**Commitments** (Note 10)

**Subsequent event** (Note 11)

**Approved by the Board of Directors on April 29, 2015**

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*"Dr. Iain Weir-Jones"*

Director

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*"Dr. Terence Friedlander"*

Director

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

# Med BioGene Inc.

(a development stage company)

## Consolidated Statements of Comprehensive Loss

For the years ended Decemebr 31, 2014 and 2013

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(expressed in US dollars)

	<u>2014</u>	<u>2013</u>
<b>Expenses</b>		
General and administrative	\$ 291,441	\$ 759,288
<b>Loss for the year</b>	(291,441)	(759,288)
<b>Other comprehensive loss</b>		
Items that can be reclassified subsequently to income:		
Cumulative translation adjustment	(38,804)	(6,240)
<b>Comprehensive loss for the year</b>	\$ (330,245)	\$ (765,528)
<b>Basic and diluted loss per share</b>	\$ (0.00)	\$ (0.01)
<b>Weighted average number of common shares</b>	80,947,811	79,027,817

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

# Med BioGene Inc.

(a development stage company)

## Consolidated Statements of Cash Flows

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

	<u>2014</u>	<u>2013</u>
<b>Cash flows from operating activities</b>		
Loss for the year	\$ (291,441)	\$ (759,288)
Items not affecting cash:		
Foreign exchange gain	(39,124)	(4,923)
Share-based payments	-	357,705
Changes in non-cash working capital items:		
Accounts payable and accrued liabilities	911	(23,208)
Due to related parties	116,955	(31,946)
Receivables	(4,146)	63,366
Net cash used in operating activities	<u>(216,845)</u>	<u>(398,294)</u>
<b>Cash flows from financing activities</b>		
Exercise of warrants	-	225,792
Proceeds from private placement	179,324	-
Net cash provided by financing activities	<u>179,324</u>	<u>225,792</u>
Effect of exchange rate changes on cash	<u>320</u>	<u>(1,317)</u>
<b>Change in cash</b>	<u>(37,201)</u>	<u>(173,819)</u>
<b>Cash – beginning of year</b>	<u>181,507</u>	<u>355,326</u>
<b>Cash – end of year</b>	<u>\$ 144,306</u>	<u>\$ 181,507</u>

**Supplemental disclosure with respect to cash flows** (Note 8)

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

# Med BioGene Inc.

(a development stage company)

Consolidated Statements of Changes in Equity

For the years ended December 31, 2014 and 2013

(expressed in US dollars)

	Number of shares	Common shares	Equity reserves	Accumulated other comprehensive income	Deficit accumulated during the development stage	Total equity (deficiency)
<b>Balance - December 31, 2012</b>	<b>77,607,833</b>	<b>\$ 8,370,351</b>	<b>\$ 4,270,177</b>	<b>\$ 338,145</b>	<b>\$ (12,684,018)</b>	<b>\$ 294,655</b>
Exercise of warrants	2,318,000	233,523	(7,731)	-	-	225,792
Other comprehensive loss for the year - Cumulative translation adjustment	-	-	-	(6,240)	-	(6,240)
Share-based payments	-	-	357,705	-	-	357,705
Loss for the year	-	-	-	-	(759,288)	(759,288)
<b>Balance - December 31, 2013</b>	<b>79,925,833</b>	<b>\$ 8,603,874</b>	<b>\$ 4,620,151</b>	<b>\$ 331,905</b>	<b>\$ (13,443,306)</b>	<b>\$ 112,624</b>
Private placement	4,000,000	179,324	-	-	-	179,324
Other comprehensive loss for the year - Cumulative translation adjustment	-	-	-	(38,804)	-	(38,804)
Loss for the year	-	-	-	-	(291,441)	(291,441)
<b>Balance - December 31, 2014</b>	<b>83,925,833</b>	<b>\$ 8,783,198</b>	<b>\$ 4,620,151</b>	<b>\$ 293,101</b>	<b>\$ (13,734,747)</b>	<b>\$ (38,297)</b>

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

# Med BioGene Inc.

(a development stage company)

Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## 1 Nature of operations and going concern

### Nature of operations

Med BioGene Inc. (the “Company”), incorporated on April 28, 2006 under the Laws of British Columbia, is based in Vancouver, British Columbia. The Company’s head office and registered office address is 598 East Kent Avenue South, Vancouver, BC, V5X 4V6. The Company is listed on the TSX Venture Exchange (“TSX-V”) under the symbol “MBI”.

The Company is a life science company focused on the development and commercialization of genomic-based clinical laboratory diagnostic tests for cancer. The Company’s first test under development is GeneFx Lung (formerly known as LungExpress Dx), a test for early-stage non-small-cell lung cancer that improves upon staging for identifying those patients who, following surgical removal of their tumor, are at a higher and lower risk of mortality to assist in selecting patients who may benefit from adjuvant chemotherapy. The Company is considered to be in the development stage as all of its efforts have been devoted to research and development, raising capital, recruitment of personnel and long-term planning to commercialize the Company’s products. The Company has not generated income from operations and depends on equity financing to support its operations.

On April 15, 2011, the Company closed a commercialization, license and research reimbursement agreement (as amended, the “Commercialization Agreement”) with Helomics (formerly “Precision Therapeutics Inc.”). The agreement provides Helomics with the exclusive global rights to develop and commercialize GeneFx Lung. Under the terms of the Commercialization Agreement, Helomics paid to the Company, within 120 days of closing, license fees and research cost reimbursements aggregating \$2,292,589 (received during the year ended December 31, 2011), half of which is creditable against future royalties that may be owed to the Company by Helomics. In addition, the Company is eligible to receive from Helomics up to \$1.0 million in the following milestone payments, all of which are creditable against future royalties that may be owed to the Company by Helomics: following the commercial launch of GeneFx Lung, amounts totaling \$500,000 and, following the achievement of \$5 million in net revenues from GeneFx Lung, amounts totaling \$500,000. The Company will receive royalty payments based on a percentage in the high single digits of Helomics’s future net revenues associated with the commercialization of GeneFx Lung or any other products incorporating the Company’s technology. Helomics is responsible for all future costs associated with the development and commercialization of GeneFx Lung and the Company is obligated to pay to the University Health Network (“UHN”) royalties of a percentage in the high teens of the actual amounts received by the Company pursuant to the sublicensing of technology licensed by the Company from UHN (paid \$222,816 during the year ended December 31, 2011). Following the closing of the Commercialization Agreement, the Company moved from a development-stage, research and development-oriented organization, to one that is focused on managing the license and rights to GeneFx Lung granted to Helomics under the Commercialization Agreement.

To date, the Company has financed its cash requirements primarily from share issuances. The Company’s ability to realize the carrying value of its assets is dependent on successfully bringing its technologies to market and achieving future profitable operations, the outcome of which cannot be predicted at this time. If and until the Company can generate licensing revenues sufficient to finance its cash requirements, it will need to raise additional funds from debt or equity financing.

# Med BioGene Inc.

(a development stage company)

Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## Going concern

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) applicable to a going concern, which contemplates the realization of assets and the discharge of liabilities in the normal course of business. As discussed further below, there are material uncertainties that cast significant doubt on the validity of this assumption.

As at December 31, 2014, the Company has working capital deficiency of \$38,297 (2013 – working capital of \$112,624), shareholders’ deficiency of \$38,297 (2013 – shareholders’ equity of \$112,624), and accumulated losses of \$13,734,747 (2013 - \$13,443,306) since its inception and expects to incur further losses in the development of its business. During the year ended December 31, 2011, under the terms of the Commercialization Agreement, Helomics paid to the Company license fees and research reimbursement totaling \$2,292,589. Such amount paid by Helomics to the Company, not including research reimbursements allocated to such amount totaling over \$1 million, is subject to the Company’s obligation to pay to UHN royalties of a percentage in the high teens pursuant to the sublicensing of technology licensed by the Company from UHN (paid \$222,816 during the year ended December 31, 2011).

Management has assessed the Company’s ability to continue as a going concern. In order for the Company to maintain operations following the closing of the Commercialization Agreement, the Company will need to retain enough cash resources to allow it to maintain operations until expected licensing revenue from GeneFx Lung will be greater than the Company’s operational costs. The Company cannot, with certainty, estimate or know the timing and extent of receipt of licensing revenues from GeneFx Lung or the exact cash resources required by the Company to maintain operations until sufficient licensing revenues are received by the Company, if at all. Until the Company can generate licensing revenues sufficient to finance its cash requirements, if at all, it will need to raise additional external funds through the sale of equity or debt securities or the merger or sale of the Company. The sale of such additional equity and debt securities may result in substantial dilution to the Company’s shareholders or may not be available, if at all, in amounts or on terms acceptable to the Company. If additional capital is required and not obtained, the Company will be forced to cease operations.

If the going concern assumption is not appropriate, it may be necessary to adjust the carrying values of assets and liabilities, and the reported net losses and consolidated statement of financial position classifications used. Such adjustments could be material.

## 2 Summary of accounting policies

### Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments that have been measured at fair value.

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”), applicable to the preparation of financial statements.

The policies applied in these consolidated financial statements are based on IFRS issued and outstanding as of December 31, 2014.

# Med BioGene Inc.

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Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## **Principles of consolidation**

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary DTX Acquisition Company Inc. (incorporated in Alberta). All material intercompany transactions and balances have been eliminated upon consolidation.

## **Reporting currency and foreign currency translation**

The consolidated financial statements of the Company are based on a Canadian dollar functional currency and have been translated into the US dollar reporting currency as follows: assets and liabilities using the rate of exchange prevailing at the financial position date; shareholders' equity using the applicable historical rate; and revenue and expenses at the average rate of exchange for the respective periods. Translation gains and losses have been included as part of the cumulative translation adjustment, which is reported as a component of accumulated other comprehensive income. The Company uses the US dollar reporting currency due to its relations with the USA.

The Company translates non-Canadian dollar balances for operations into the functional currency as follows:

- (i) property and equipment using historical rates;
- (ii) other assets and liabilities using closing rates with translation gains and losses recorded in other income/expense; and
- (iii) income and expenses using average exchange rates, except for expenses that relate to non-monetary assets and liabilities measured at historical rates, which are translated using the same historical rate as associated non-monetary assets and liability.

Exchange gains and losses arising on translation are included in the consolidated statements of comprehensive loss under other comprehensive income (loss). The other comprehensive loss for the year ended December 31, 2014 was \$38,804 (2013 – \$6,240).

## **Use of estimates and judgments**

The preparation of the consolidated financial statements in conformity with IFRS requires management to make estimates, judgments and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

# Med BioGene Inc.

(a development stage company)

Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## (i) Critical accounting estimates

Critical accounting estimates are estimates and assumptions made by management that may result in a material adjustment to the carrying amount of assets and liabilities within the next financial year and are, but are not limited to, the following:

### *Share-based payments*

The fair value of stock options issued are subject to the limitation of the Black-Scholes option pricing model that incorporates market data and involves uncertainty in estimates used by management in the assumptions. Because the Black-Scholes option pricing model requires the input of highly subjective assumptions, including the volatility of share prices, changes in subjective input assumptions can materially affect the fair value estimate.

## (ii) Critical accounting judgments

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are, but are not limited to, the following:

### *Determination of functional currency*

In accordance with IAS 21 *The Effects of Changes in Foreign Exchange Rates*, management determined that the functional currency of the Company and its subsidiary is the Canadian dollar.

### *Going concern*

The determination that the Company will continue as a going concern for the next year.

## **Share-based payments**

The Company has an incentive stock option plan, which provides that the Board of Directors of the Company may from time to time, in its discretion, and in accordance with TSX-V requirements, grant to directors, officers, and consultants to the Company, non-transferable options to purchase common shares. Such options may be exercisable for a period of up to five years from the date of grant and are measured at the date of grant by reference to the fair value of the services received, or if the fair value of the received cannot be reasonably estimated, by using the Black-Scholes option pricing model. Vesting terms will be determined at the time of grant by the Board of Directors.

## **Warrants issued in equity financing transactions**

The Company engages in equity financing transactions to obtain the funds necessary to continue operations. These equity financing transactions may involve the issuance of common shares or units. Each unit typically comprises a certain number of common shares and a certain number of share purchase warrants ("Warrants"). Depending on the terms and conditions of each equity financing agreement, the Warrants are exercisable to acquire additional common shares at a price prior to expiry as stipulated by the agreement. Warrants that comprise a portion of units are assigned \$nil value and are not accounted for separately in share capital from the common shares that were concurrently issued. Warrants that are issued as payment for agency fees or other transactions costs are accounted for as share-based payments.

# Med BioGene Inc.

(a development stage company)

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For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## **Research, development and collaboration costs**

Research and development costs, which include clinical and regulatory activities, are expensed as incurred, net of related government contributions.

The Company enters into collaboration agreements and research subcontracting with various parties and records these costs as research and development expenses. It records accruals for estimated study costs, comprising work performed by its collaborators under contract terms. All clinical collaborators enter into agreements with the Company that specify work content and payment terms.

In addition to costs for research and development, under the UHN collaboration agreement, the Company will be required to make certain research funding payments, milestone payments and annual royalty payments based on sales of GeneFx Lung resulting from its commercial launch. At such time as the Company begins to generate revenue from the sale of GeneFx Lung, such payments to UHN will be recorded in cost of product revenues as a royalty payment.

From inception to December 31, 2014, the Company has incurred total research and development expenses of \$4,776,762 of which approximately 45% has been spent on GeneFx Lung. These expenses include costs incurred both to develop the GeneFx Lung assay and to carry out clinical validation studies to validate its multi-gene test. The remaining amount was expended primarily on the Company's earlier programs in cardiovascular disease and lymphoma on which work has been suspended.

## **Income taxes**

Income tax comprises current and deferred tax. Income tax is recognized in the consolidated statement of comprehensive loss except to the extent that it related to items recognized directly in equity, in which case the income tax is also recognized directly in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted, or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the consolidated statement of financial position date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except in the case of subsidiaries, where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are presented as non-current.

# Med BioGene Inc.

(a development stage company)

Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## Cash and cash equivalents

Cash and cash equivalents consist of cash on deposit and highly liquid short-term interest bearing securities with maturities at the date of purchase of three months or less. Cash and cash equivalents are held at a recognized Canadian financial institution. Interest earned is recognized in other income on the financial statements. As at December 31, 2014, cash and cash equivalents consists entirely of cash held in bank.

## Financial instruments

Financial assets and liabilities are recognized when the company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

- (i) Financial assets and liabilities at fair value through profit or loss: A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges.

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in net income/loss. Gains and losses arising from changes in fair value are presented in net income/loss within other gains and losses in the period in which they arise. Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond 12 months of the consolidated statement of financial position date, which is classified as non-current.

Cash and cash equivalents are included in fair value through profit or loss.

- (ii) Available-for-sale investments: Available-for-sale investments are non-derivatives that are either designated in this category or not classified in any of the other categories.

Available-for-sale investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from changes in fair value are recognized in other comprehensive income/loss. Available-for-sale investments are classified as non-current, unless the investment matures within 12 months, or management expects to dispose of them within 12 months.

Interest on available-for-sale investments, calculated using the effective interest method, is recognized in net income/loss as part of interest income. Dividends on available-for-sale equity instruments are recognized in net income/loss as part of other gains and losses when the Company's right to receive payment is established. When an available-for-sale investment is sold or impaired, the accumulated gains or losses are moved from accumulated other comprehensive income/loss to net income/loss and included in other gains and losses.

The Company does not have any financial assets classified as available-for-sale investments.

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## Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

- (iii) Loans and receivables: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of trade receivables and are included in current assets due to their short-term nature. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

The Company does not have financial assets classified as loans and receivables.

- (iv) Financial liabilities: Financial liabilities are non-derivatives and are recognized initially at fair value, net of transaction costs incurred, and are subsequently stated at amortized cost. Any difference between the amounts originally received, net of transaction costs, and the redemption value is recognized in the consolidated statement of comprehensive loss over the period to maturity using the effective interest method.

Accounts payable and due to related parties are included in financial liabilities.

### **Impairment of non-financial assets**

Property and equipment and intangible assets are tested for impairment at the end of each reporting period or when events or changes in circumstances indicate that the carrying amount may not be recoverable. Long-lived assets that are not amortized are subject to an annual impairment test. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units or CGUs). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds the recoverable amount.

Goodwill is reviewed for impairment annually or at any time if an indicator of impairment exists.

Goodwill acquired through a business combination is allocated to each CGU, or group of CGUs, that are expected to benefit from the related business combination. A group of CGUs represents the lowest level within the entity at which the goodwill is monitored for internal management purposes, which is not higher than an operating segment.

The Company evaluates impairment losses, other than goodwill impairment, for potential reversals when events or circumstances warrant such consideration.

### **Patent costs**

The costs incurred in establishing and maintaining patents for intellectual property developed internally are expensed in the period incurred.

### **Investment tax credits**

Investment tax credits can be used to reduce taxable income in future taxation years. Investment tax credits are recorded when the qualifying expenditures have been incurred and if it is reasonably assured that the tax credits will be realized. Investment tax credits are earned when expenditures are made on qualifying research and development; such expenditures are subject to audit by the Canada Revenue Agency. As management

# Med BioGene Inc.

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Notes to the Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

believes there is sufficient uncertainty regarding the utilization of deferred tax assets, no deferred tax assets have been recognized.

## **Government contribution agreements**

Contributions under government agreements relate to funding of eligible research and development expenditures for defined programs. Amounts received or receivable are included as a contribution in determining the loss for the year as a reduction of the expenses to which they relate.

## **Earnings per share**

Basic earnings per share ("EPS") is calculated by dividing the net income (loss) for the period attributable to equity owners of the Company by the weighted average number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. The Company's potentially dilutive common shares comprise outstanding stock options and warrants.

In determining diluted loss per share for the years ended December 31, 2014 and 2013, the Company has not increased the weighted average number of shares outstanding to include warrants and stock options as those instruments are considered anti-dilutive for purposes of calculating loss per share.

## **Revenue recognition**

The Company entered into the Commercialization Agreement with Helomics where the terms of the agreement provide for payments for license fees and research reimbursements (Note 1). Revenues are recorded when licensing payments are received in accordance with the terms of the agreement and are recognized on that basis in the consolidated financial statements.

## **Change in accounting policies**

The Company adopted the following accounting policies effective January 1, 2014:

Amendments to IAS 32 *Financial Instruments: Presentation* provides for amendments relating to offsetting financial assets and financial liabilities. The Company has adopted this policy and it does not have significant effect on the consolidated financial statements.

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For the years ended December 31, 2014 and 2013

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(expressed in US dollars)

## Accounting standards issued but not yet applied

The Company has reviewed new and revised accounting pronouncements that have been issued but are not yet effective. The Company has not early adopted any of these standards and is currently evaluating the impact, if any, that these standards might have on its consolidated financial statements.

Accounting standards issued with the effective date to be finalized:

*IAS 1 Presentation of Financial Statements* – In December 2014, the IAS issued an amendment to address perceived impediments to preparers exercising their judgment in presenting their financial reports. The changes clarify that materiality considerations apply to all parts of the financial statements and the aggregation and disaggregation of line items within the financial statements.

*IFRS 11 Joint Arrangements* – In May 2014, the IASB issued an amendment to clarify the accounting for acquisitions of an interest in a joint operation when the operation constitutes a business.

*IFRS 15 Revenue from Contracts with Customers* – IFRS 15 was issued in May 2014 and specifies how and when an entity will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers.

*IFRS 10 Consolidated Financial Statements* – In September 2014, amendments to IFRS 10 were issued to provide guidance on recognising gains and losses from the loss in control of a subsidiary in the parent's profit or loss.

*IFRS 9 Financial Instruments* – IFRS 9 replaces the current standard IAS 39 *Financial Instruments: Recognition and Measurement*, replacing the current classification and measurement criteria for financial assets and liabilities with only two classification categories: amortized cost and fair value.

## 3 Capital disclosure

The Company considers share capital and equity reserves as capital. The Company's objectives when managing its capital structure are to provide sufficient capital to advance the commercialization of its products, meet the Company's obligations as they come due, and provide for the potential acquisition of additional intellectual property rights related to products within the Company's strategic plans.

The Company's officers and senior management take full responsibility for managing the Company's capital and do so through quarterly meetings and regular review of financial information. The Company's Board of Directors is responsible for overseeing this process.

The Company monitors its capital structure and may make adjustments to it in light of changes in the Company's operating performance, changes in economic conditions and the risk characteristics of the underlying assets. When adjustments to the capital structure are considered appropriate, such changes may include the issuance of new shares, issuance of new debt, or re-purchasing of shares for cancellation.

The Company is not subject to externally imposed capital requirements and there has been no change with respect to the overall capital risk management strategy during the year ended December 31, 2014. The method used by the Company to manage its capital has been the issuance of new share capital. Management does not foresee any changes to this in 2015, however this cannot be assured (see Note 1 – Going concern).

# Med BioGene Inc.

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Notes to the Consolidated Financial Statements

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(expressed in US dollars)

## 4 Financial instruments and financial risk management

The Company is exposed to certain financial risks, including credit risk, liquidity risk and market risk.

### Credit risk

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 and arises principally from the Company's cash and cash equivalents and government contribution receivable. At present, the Company invests its excess cash in guaranteed certificates from Canadian chartered banks and will only consider investment of excess cash in highly rated government and corporate debt securities. The Company has established guidelines, including diversification, credit ratings and maturities, to ensure safety and liquidity of its cash.

These guidelines are periodically reviewed by the Company's audit committee and modified to reflect changes in market conditions.

### Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. To the extent that the Company does not believe it has sufficient liquidity to meet its current obligations, the Board of Directors considers securing additional funds through issuances of equity and debt or partnering transactions. The Board of Directors approves the Company's annual operating and capital budgets as well as any material transactions outside the ordinary course of business. Management regularly reviews these budgets and maintains short-term cash flow forecasts. At December 31, 2014, the Company's current liabilities including accounts payable and due to related parties were \$189,097 (2013 - \$71,231). Further information relating to liquidity risk is set out in Note 1.

### Market risk

Market risk is the risk that changes in foreign exchange rates, interest rates and equity prices will affect the Company's future cash flows or valuation of its financial instruments. The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. Foreign currency risk is limited to the portion of the Company's business transactions denominated in currencies other than the Canadian dollar, primarily expenses for consulting, research and development work incurred in US dollars. The Company believes that the results of operations and cash flows would be affected by a sudden change in foreign exchange rates, but would not impair or enhance its ability to pay its US dollar denominated obligations. The Company does not currently view its exposure to US dollars as a significant risk due to the limited volume of transactions it conducts in this currency.

The Company is subject to interest rate risk on its cash and cash equivalents and believes that the results of operations, financial position and cash flows would not be significantly affected by a sudden change in market interest rates relative to the investment interest rates due to the short-term nature of the investments. Excess cash is invested in highly rated investment securities at fixed interest rates with varying terms to maturity but generally with maturities of three months or less from the date of purchase.

As at December 31, 2014, the Company had no cash equivalents. The Company does not invest in equity instruments of other corporations.

Changes in the Company's share price could impact its ability to raise additional capital.

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(a development stage company)

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### Fair value hierarchy

Financial instruments recognized at fair value on the consolidated statements of financial position must be classified into one of the three following fair value hierarchy levels:

Level 1 – measurement based on quoted prices (unadjusted) observed in active markets for identical assets and liabilities;

Level 2 – measurement based on inputs other than quoted prices included in Level 1, that are observable for the asset and liability;

Level 3 – measurement based on inputs that are not observable (supported by little or no market activity) for the asset or liability.

The Company's financial instrument carrying amounts and fair values by levels per the fair value hierarchy are as follows:

	Fair Value Level	December 31, 2014	December 31, 2013
<b>Financial assets</b>			
Cash	1	\$ 144,306	\$ 181,507

### 5 Receivables

Receivables consist of the following:

	December 31, 2014	December 31, 2013
GST/HST receivable	\$ 6,494	\$ 2,074
Legal fees receivable	-	274
	\$ 6,494	\$ 2,348

### 6 Capital stock

a) Common shares

#### Authorized

Unlimited number of voting common shares, without par value.

On September 29, 2014, the Company issued 4,000,000 units at CAD\$ 0.05 per unit for gross proceeds of \$179,324 (CAD\$ 200,000) (the "Units"). Each Unit consists of one common share and one common share purchase warrant. Each whole common share purchase warrant will entitle the holder to purchase one common share at a price of \$0.10 for a period of 24 months. The securities issued pursuant to the private placement are subject to a four-month hold period from the date of closing.

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During the year ended December 31, 2013, the Company issued 2,318,000 common shares for proceeds of \$225,792 (CAD\$ 231,800) pursuant to the exercise of warrants.

### b) Stock options

On February 13, 2006, the Board of Directors of the Company adopted the Med BioGene Inc. 2006 Incentive Stock Option Plan (the "Plan"). At the annual and special meeting of the Company held on December 30, 2008, the shareholders approved the amendment of the Plan to increase the number of common shares in respect of which stock options may be granted thereunder to 8,250,000. At the annual and special meeting of the Company held on February 12, 2010, the shareholders of the Company approved the amendment to the Plan to increase the number of common shares in respect of which stock options may be granted thereunder to 14,474,000.

Stock options may be exercisable for a period of up to five years from the date of grant. Vesting terms are determined at the time of grant by the Board of Directors.

As at December 31, 2014, the following stock options were issued and outstanding:

Number of options outstanding and exercisable	Exercise price	Expiry date
250,000	0.11	March 18, 2015*
250,000	0.09	June 29, 2016
75,000	0.11	September 19, 2018
575,000		

*\*Subsequently expired unexercised*

The exercise prices of all stock options are denominated in Canadian dollars and are translated to US dollars at the December 31, 2014 exchange rate.

A summary of changes of stock options outstanding is as follows:

	Options	Weighted average exercise price
Outstanding - December 31, 2012	9,900,000	\$ 0.11
Granted	3,050,000	0.12
Expired/cancelled	(800,000)	0.16
Outstanding and exercisable - December 31, 2013	12,150,000	\$ 0.10
Expired	(1,900,000)	0.09
Forfeited	(9,675,000)	0.09
Outstanding and exercisable – December 31, 2014	575,000	\$ 0.10

During the year ended December 31, 2014, the Company granted no stock options (2013 – 3,050,000 stock options were granted with a fair value of \$357,705 which was expensed to operations).

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The following weighted average assumptions were used for the Black-Scholes option pricing model valuation of stock options granted:

	<u>2014</u>	<u>2013</u>
Risk-free interest rate	-	2.02%
Expected life of option	-	5 years
Expected dividend yield	-	0%
Expected stock price volatility	-	182.32%
Expected forfeiture rate	-	-

### c) Warrants

As at December 31, 2014, the following warrants were outstanding:

	<b>Number of warrants</b>	<b>Weighted average exercise warrants</b>
Balance - December 31, 2012	2,318,000	\$ 0.10
Exercised (Note 6(a))	(2,318,000)	0.10
Balance - December 31, 2013	-	
Issued (Note 6(a))	4,000,000	0.09
Balance - December 31, 2014	4,000,000	\$ 0.09

As at December 31, 2014, the weighted average remaining contractual life of outstanding warrants is 1.75 years.

The exercise prices of all share purchase warrants are denominated in Canadian dollars and are translated to US dollars at the December 31, 2014 exchange rate.

## 7 Related party transactions and balances

During the year ended December 31, 2014, the Company:

- (i) paid or accrued \$76,111 (2013 - \$121,388) for consulting fees to a company owned by a former director and officer of the Company;
- (ii) paid or accrued \$24,618 (2013 - \$35,937) for accounting fees to a firm where a former officer of the Company is partner;
- (iii) paid or accrued \$4,271 (2013 - \$nil) for accounting fees to a firm where a current director of the Company is partner;
- (iv) paid or accrued \$nil (2013 - \$13,368) for legal fees to a law firm where a former director is a former partner of which such fees were reimbursed from Helomics;
- (v) paid or accrued \$27,721 (2013 - \$42,375) for directors' fees to three former directors of the Company; and

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(vi) paid or accrued \$nil (2013 - \$4,886) for consulting fees to a former director of the Company.

Related party transactions are reflected as part of general and administrative expense. Amounts owing to these related parties (including former management and directors of the Company) as at December 31, 2014 were \$126,717 (December 31, 2013 - \$9,762). These amounts are non-interest bearing and due on demand.

Of the balance owed to related parties at December 31, 2014, \$114,324 (CAD\$ 132,626) (December 31, 2013 - \$nil) was owed to the Chief Executive Officer (“CEO”) for legal fees paid on behalf of the Company for corporate matters. The balance owed to the CEO was repaid subsequent to year end through the issuance of common shares of the Company (see also Note 11).

The share-based payments to directors and other key management personnel during the year ended December 31, 2014, was \$nil (2013 - \$348,909). Key management personnel include the Chief Executive Officer, Chief Financial Officer, and directors of the Company. Share-based payments are the fair value of the options granted to directors and other key management personnel.

### 8 Supplemental disclosure with respect to cash flows

There were no significant non-cash transactions for the year ended December 31, 2014.

The Company’s significant non-cash transactions during the year ended December 31, 2013 was as follows:

(a) reallocated a fair value of \$7,731 from warrant reserves to capital stock pursuant to the exercise of agent’s warrants.

### 9 Deferred income taxes

a) A reconciliation of income taxes at statutory rates with the reported taxes is as follows:

	2014	2013
Loss before income taxes	\$ (291,441)	\$ (759,288)
Expected tax recovery	\$ (75,775)	\$ (195,517)
Change in statutory rates	-	(1,005)
Non-deductible items	-	91,965
Changes in unrecognized deductible temporary differences	75,775	111,078
Other	-	(6,521)
Total	\$ -	\$ -

b) Deductible temporary differences, unused tax losses and unused tax credits for which no deferred tax assets/(liabilities) have been recognized are attributable to the following:

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	As at December 31,	
	2014	2013
Deferred tax assets		
Non-capital loss carry forwards	\$ 5,948,000	\$ 6,092,000
Research and development expenditure pool	1,862,000	2,031,000
Cumulative eligible capital expenditures	1,094,000	1,283,000
Investment tax credit	426,000	465,000
Share issuance costs	-	3,000
<b>Total</b>	<b>\$ 9,330,000</b>	<b>\$ 9,874,000</b>

There are no deferred tax assets/(liabilities) presented in the consolidated statement of financial position.

Tax attributes are subject to review and potential adjustments by tax authorities.

The Company has non-capital losses of approximately \$5,948,000 which may be carried forward and applied against taxable income in future years. These losses, if unutilized, will expire through to 2034. Subject to certain restrictions, the Company has further research and development expenditures totaling approximately \$1,862,000 available to reduce taxable income of future years and are not subject to expiry.

## 10 Commitments

On April 14, 2008, the Company entered into development agreements with UHN to provide the Company with exclusive world-wide rights to commercialize a prognostic test for early-stage non-small-cell lung cancer developed by UHN.

Effective February 24, 2009, the Company expanded its development agreement with UHN. The agreement expands the intellectual property licensed to the Company and amends the terms of the research collaboration between UHN and the Company. Under these agreements, the Company and UHN are collaborating in certain activities related to the development and validation of GeneFx Lung and associated data analysis and in the collection of patient specimens to be used in such activities. The research and development expense for this project incurred since inception is approximately \$718,237. The Company is obligated to provide UHN with up to \$878,663 in further milestone and development payments, along with royalties based on future net sales of the tests. Approximately 90% of the above contractual obligations to UHN are related to the launch and commercialization of GeneFx Lung, and if the Company is unsuccessful in its commercialization efforts, these amounts may never become obligations of the Company. On April 15, 2011, the Company closed the Commercialization Agreement with Helomics. Helomics is responsible for all future costs associated with the development and commercialization of GeneFx Lung and the Company is obligated to pay to UHN royalties of a percentage in the high teens of the actual amounts received by the Company pursuant to the sublicensing of technology licensed by the Company from UHN (see Note 1 – Nature of operations).

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## 11 Subsequent event

During the Board of Directors Meeting held on January 12, 2015, the company granted 1,200,000 stock options at a price of \$0.10 vesting immediately and expiring January 12, 2018.

On January 13, 2015, the Company entered into a debt settlement agreement with the Chief Executive Officer (“CEO”) and agreed to issue 2,652,520 common shares of the Company at a deemed price of \$0.04 (CAD\$ 0.05) per share, to settle payables of \$114,324 (CAD\$ 132,626) that were owed to the CEO at December 31, 2014 (see also Note 7). The common shares were issued on February 21, 2015.