

Consolidated Financial Statements

Pacgen Biopharmaceuticals Corporation

(a development stage enterprise)

(Expressed in Canadian dollars)

March 31, 2009 and 2008



AUDITORS' REPORT

To the Shareholders of
Pacgen Biopharmaceuticals Corporation

We have audited the consolidated balance sheets of **Pacgen Biopharmaceuticals Corporation** (a development stage enterprise) (the "Company") as at March 31, 2009 and 2008, and the consolidated statements of operations and comprehensive loss and cash flows for each of the years in the two year period ended March 31, 2009 and for the period from April 23, 2004 (inception) to March 31, 2009, and the consolidated statements of shareholders' equity for years ended March 31, 2009 and 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at March 31, 2009 and 2008 and the consolidated results of its operations and its cash flows for the years then ended, and for the period from April 23, 2004 (inception) to March 31, 2009 in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Vancouver, Canada,
July 10, 2009.

Chartered Accountants

Pacgen Biopharmaceuticals Corporation**(a development stage enterprise)**

Incorporated under the Business Corporation Act (British Columbia)

CONSOLIDATED BALANCE SHEETS
[See Note 1 – Nature of Operations and Going Concern]

(expressed in Canadian dollars)

	March 31, 2009	March 31, 2008
	\$	\$
ASSETS		
Current		
Cash and cash equivalents <i>[note 7]</i>	308,871	1,438,691
Amounts receivable	15,155	12,800
Prepaid expenses and other	515,619	469,307
Total current assets	839,645	1,920,798
Deferred acquisition costs	3,775	—
Property and equipment <i>[note 8]</i>	67,874	101,236
Intangible assets <i>[note 9]</i>	765,229	1,002,203
Total assets	1,676,523	3,024,237
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	911,688	1,378,733
Other payable <i>[note 10]</i>	625,423	—
Convertible debentures <i>[note 11]</i>	318,831	—
Current portion of deferred leasehold inducement	6,916	6,916
	1,862,858	1,385,649
Convertible debentures <i>[note 11]</i>	213,000	—
Deferred leasehold inducement	3,459	10,375
Total liabilities	2,079,317	1,396,024
Commitments and contingencies <i>[notes 13 and 14]</i>		
Shareholders' equity (deficit)		
Share capital <i>[note 12]</i>		
Issued and outstanding:		
Common shares <i>[note 12(a)]</i>	13,012,118	13,012,118
Preferred shares <i>[note 12(b)]</i>	—	—
Contributed surplus <i>[notes 11 and 12(e)]</i>	1,415,409	1,163,776
Deficit	(14,830,321)	(12,547,681)
Total shareholders' equity (deficit)	(402,794)	1,628,213
Total liabilities and shareholders' equity	1,676,523	3,024,237

See accompanying notes

On behalf of the Board:

/s/ Telvin Ju
Director/s/ Kevin McGarry
Director

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

**CONSOLIDATED STATEMENTS OF OPERATIONS AND
COMPREHENSIVE LOSS**

(expressed in Canadian dollars)

	Year ended March 31, 2009 \$	Year ended March 31, 2008 \$	Cumulative from Inception to March 31, 2009 \$
EXPENSES			
Research and development <i>[note 6]</i>	1,451,884	3,480,523	7,782,314
Research and development expense recovery <i>[notes 6 and 10]</i>	(865,287)	—	(865,287)
	586,597	3,480,523	6,917,027
General and administration	1,052,414	1,901,567	6,079,382
Stock based compensation <i>[note 12(e)]</i>	160,687	346,348	1,087,860
Amortization	263,816	269,245	797,319
	2,063,514	5,997,683	14,881,588
OTHER			
Interest and other income	39,123	94,838	263,929
Loss on disposal of property and equipment	(6,520)	(9,089)	(15,609)
Foreign exchange losses	(251,729)	(147,778)	(435,053)
	(219,126)	(62,029)	(186,733)
Loss before income taxes	(2,282,640)	(6,059,712)	(15,068,321)
Future income tax recovery <i>[note 15]</i>	—	85,000	238,000
Net loss and comprehensive loss for the period	(2,282,640)	(5,974,712)	(14,830,321)
Basic and diluted loss per common share	(0.06)	(0.19)	
Weighted average number of common shares outstanding	35,144,693	30,711,416	

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

CONSOLIDATED STATEMENTS OF CASH FLOWS

(expressed in Canadian dollars)

	Year ended March 31, 2009 \$	Year ended March 31, 2008 \$	Cumulative from Inception to March 31, 2009 \$
OPERATING ACTIVITIES			
Loss for the period	(2,282,640)	(5,974,712)	(14,830,321)
Add items not affecting cash:			
Accretion of convertible debentures	8,277	—	8,277
Amortization	263,816	269,245	797,319
Deferred leasehold inducement	(6,916)	(1,153)	(8,069)
Future income tax recovery	—	(85,000)	(238,000)
Loss on disposal of property and equipment	—	9,089	9,089
Stock based compensation	160,687	346,348	1,087,860
Unrealized foreign exchange loss	214,934	87,936	302,870
Write-off of assets	6,520	5,548	29,887
	(1,635,322)	(5,342,699)	(12,841,088)
Changes in non-cash working capital items relating to operations:			
Amounts receivable	(2,355)	119,260	128,340
Prepaid expenses and other	48,428	384,386	(526,634)
Accounts payable and accrued liabilities	(788,951)	138,134	563,789
Other payable	637,655	—	637,655
Cash used in operating activities	(1,740,545)	(4,700,919)	(12,037,938)
INVESTING ACTIVITIES			
Acquisition of IL Therapeutics Inc.	—	—	1,237,089
Deferred acquisition costs	(3,775)	—	(3,775)
Proceeds from disposal of property and equipment	—	5,775	5,775
Purchase of property and equipment	—	(19,485)	(179,202)
Purchase of intangible assets	—	—	(59,743)
Leasehold inducement	—	18,444	18,444
Cash provided by (used in) investing activities	(3,775)	4,734	1,018,588
FINANCING ACTIVITIES			
Issuance of common shares for cash, net of share issuance costs	—	747,510	8,887,292
Issuance of preferred shares for cash, net of share issuance costs	—	—	1,131,593
Issuance of convertible debentures for cash	614,500	—	614,500
Advance from related party	—	—	694,836
Cash provided by financing activities	614,500	747,510	11,328,221
Increase (decrease) in cash and cash equivalents	(1,129,820)	(3,948,675)	308,871
Cash and cash equivalents, beginning of period	1,438,691	5,387,366	—
Cash and cash equivalents, end of period	308,871	1,438,691	308,871
Other supplemental cash flow information			
Preferred shares issued for technology [note 9(b)]	—	—	918,876
Common shares issued for technology [note 9(b)]	—	—	1,561,124
Preferred shares issued to agent as compensation	—	—	52,544
Common shares issued to agent as compensation [note 12(a)(i)]	—	21,546	151,546
Common shares issued to settle related party advance	—	—	718,836

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(expressed in Canadian dollars)

	Common Shares		Preferred Shares		Contributed	Deficit	Total
	Number	Amount	Number	Amount	Surplus		
		\$		\$	\$		
Balance, March 31, 2007	30,521,960	12,286,556	—	—	795,480	(6,572,969)	6,509,067
Issued for cash pursuant to a private placement [note 12(a)(i)]	4,515,003	747,510	—	—	—	—	747,510
Value of share purchase warrant pursuant to a private placement [note 12(a)(i)]	—	(2,535)	—	—	2,535	—	—
Compensation to private placement agent	107,730	(19,413)	—	—	19,413	—	—
Stock based compensation [note 12(e)]	—	—	—	—	346,348	—	346,348
Net loss for the period	—	—	—	—	—	(5,974,712)	(5,974,712)
Balance, March 31, 2008	35,144,693	13,012,118	—	—	1,163,776	(12,547,681)	1,628,213
Equity component of a private placement of convertible debentures [note 11]	—	—	—	—	90,946	—	90,946
Stock based compensation [note 12(e)]	—	—	—	—	160,687	—	160,687
Net loss for the period	—	—	—	—	—	(2,282,640)	(2,282,640)
Balance, March 31, 2009	35,144,693	13,012,118	—	—	1,415,409	(14,830,321)	(402,794)

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN

Pacgen Biopharmaceuticals Corporation (the "Company") was incorporated under the Business Corporations Act (British Columbia) on April 23, 2004. The Company is a life science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II, proof of concept efficacy in human. The Company identifies innovative therapeutic drug candidates globally, and develops these drug candidates in accordance to the US Food and Drug Administration regulatory standards to feed the product development pipelines of the pharmaceuticals industry.

These financial statements have been prepared in accordance with generally accepted accounting principles applicable to a going concern, which assumes that the Company will be able to meet its obligations and continue its operations for its next fiscal year. Realization values may be substantially different from the carrying values as shown and these financial statements do not give effect to adjustments that would be necessary to the carrying values and classifications of assets and liabilities should the Company be unable to continue as a going concern. As of March 31, 2009, the Company has not generated any revenue from its operations and has accumulated a deficit of \$14,830,321 (March 31, 2008 - \$12,547,681). Therefore, the Company is considered to be in the development stage. The Company has a working capital deficiency of \$1,023,213 as of March 31, 2009 which is not sufficient to sustain operations over the next year and the Company may be unable to continue realizing its assets and discharge its obligations in the normal course, all of which casts substantial doubt about the Company's ability to continue as a going concern. While the Company has been successful in securing financings in the past, there is no assurance that it will be able to do so in the future. Accordingly, these financial statements do not give effect to adjustments, if any, that would be necessary should the Company be unable to continue as a going concern. If the going concern assumption was not used then the adjustments required to report the Company's assets and liabilities on a liquidation basis could be material to these financial statements.

The recent global financial market downturn has led to an overall tightening in the credit markets and a substantial reduction in capital available to companies in the development stage. Smaller life science technology companies which are generally viewed as higher risk investments have been significantly affected. The Company undertook a comprehensive review of its product development programs, operations and projected cash requirements with the view of conserving cost and deferring cash outflows. As a result, the Company implemented a cost management program, ceased research and development activities and focused its operations in business development to secure collaborative partners for its drug candidates. The Company undertook a number of financing initiatives including a small bridge financing and negotiation with its major vendors for defer payments.

Pacgen Biopharmaceuticals Corporation
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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

1. NATURE OF OPERATIONS AND GOING CONCERN (cont'd.)

On January 30, 2009, the Company announced that it intended to offer, through one or more tranches of closings of a non-brokered private placement, convertible debentures in an aggregate principal amount of up to approximately \$610,000 (the "Offering"). The Company closed this Offering in two tranches in February 2009 and March 2009 for an aggregate principal amount of \$614,500, as described in *note 11*. In February 2009, the Company terminated all of its employees except for certain key personnel who have agreed to provide services as consultants and be compensated through stock options.

On March 6, 2009, the Company finalized its negotiation with a vendor to settle its outstanding account of approximately US\$1.3 million (\$1.65 million). The Company received a credit note and recovered approximately US\$604,000 (\$747,000) of research and development expenditures from this vendor. For the remaining balance of US\$708,000 (\$893,000), the Company made an initial payment of US\$128,000 (\$157,000) and agreed to pay the balance of US\$580,000 (\$731,000) by installments, as described in *note 10*. Management has been in constant communication with this vendor to keep them apprised of the Company's developments.

The Company has also reviewed strategic alternatives to leverage its technology portfolio and to enhance its ability to raise capital. As part of these efforts, the Company signed a share purchase agreement with the shareholders of Xphase Pharmaceuticals Inc. ("Xphase") in June 2009, as described in *note 18*. Xphase, a privately held pharmaceutical company, has the right to acquire the exclusive global rights, excluding China, of AF-05, a novel anti-anxiety drug candidate currently in Phase I clinical trial in China. Xphase also provides consulting and project management services to assist small to medium pharmaceutical and biotechnology companies globally.

Pursuant to the share purchase agreement, the Company agreed to issue 3 million common shares of the Company to Xphase shareholders in exchange for 100% ownership of Xphase as well as management services of Xphase principals. Upon the achievement of certain pre-defined business development milestones, Xphase shareholders will be entitled to an additional 3.5 million common shares of the Company. Following the acquisition of Xphase, the Company has positioned itself to become a global life science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II human proof of concept.

The Company is currently seeking additional funding to finance its operations and obligations. Management is considering all possible financing alternatives, including equity financing, debt financing, joint-venture, corporate collaboration and licensing arrangement.

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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and are presented in Canadian dollars. The following is a summary of significant accounting policies used in the preparation of these consolidated financial statements.

[a] Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, IL Therapeutics Inc. incorporated in Canada under the Canada Business Corporations Act. The consolidated financial statements for fiscal year ended March 31, 2008 also include accounts of Pacgen Biopharmaceuticals Corporation (Taiwan Branch) ("Pacgen Taiwan") which was wound up in March 2008. All significant inter-company balances and transactions have been eliminated on consolidation.

[b] Use of estimates

The preparation of these consolidated financial statements, in conformity with Canadian generally accepted accounting principles, requires management to make estimates and assumptions that affect the amounts recorded in the consolidated financial statements. Significant areas requiring the use of estimates relate to the assessment for impairment and useful lives of intangible assets, determination of share value in transactions where shares are issued as a consideration, accrued liabilities and determination of fair value of stock-based compensation. The reported amounts and note disclosures are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned course of actions. Actual results may differ from those estimates.

[c] Foreign currency translation

The Company follows the temporal method of accounting for the translation of foreign currency amounts into Canadian dollars. Under this method, monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars using the exchange rate in effect on the balance sheet date. All other assets and liabilities are translated at the exchange rates in effect on the transaction dates. Revenue and expense items are translated at the average exchange rates prevailing during the period except for amortization which is translated using historical rates. Foreign exchange gains and losses, both realized and unrealized, are included in the determination of the loss for the period.

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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

[d] Cash and cash equivalents

The Company considers all highly liquid financial instruments with a maturity of 90 days or less when purchased to be cash equivalents. Cash equivalents are carried at cost, which approximate their market values. Interest earned is recognized in operations. At March 31, 2009 and 2008, cash and cash equivalents consisted of cash on deposit with banks, as well as subscription amounts received in trust accounts following closing of a financing.

[e] Property and equipment

Property and equipment are recorded at cost less accumulated amortization. Amortization is provided based on the estimated useful lives of the property and equipment using the following methods and annual rates:

Computer equipment	30% declining balance
Computer software	2 years straight-line
Leasehold improvement	Term of lease
Office furniture and equipment	20% declining balance

[f] Intangible assets

Intangible assets of the Company include technology licenses and rights acquired from third parties. Technology licenses and rights are initially recorded at the fair value based on consideration paid and are amortized on a straight-line basis over the estimated useful life of the underlying technologies of 5 to 10 years. The Company reviews the estimated useful lives and carrying values of its technology licenses and rights as part of its periodic assessment for impairment of long-lived assets. No impairment adjustment has been recorded to date.

The amount shown for technology licenses and rights do not necessarily reflect present or future value and the ultimate amount recoverable will be dependent upon the successful development and commercialization of products based on these underlying technologies.

[g] Impairment of long-lived assets

Property and equipment, and intangible assets with finite life are reviewed for potential impairment whenever events or changes in circumstances indicating that the carrying value of these assets may not be recoverable. If the estimated net recoverable value, calculated based on the estimated undiscounted future cash flow, is less than the carrying value of the underlying long-lived assets, then the carrying value is written down to its fair value, based on the related estimated discounted future cash flow. No impairment adjustment has been recorded to date.

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**NOTES TO CONSOLIDATED
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(expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

[h] Convertible debentures

The Company's convertible debentures are segregated into their debt and equity components at the date of issuance, in accordance with the substance of the contractual agreements. The debt component of the instruments is classified as a liability, and recorded at the present value of the Company's obligations to make future interest payments and settle the redemption value of the instruments. The carrying value of the debt component is accreted to the original face value of the instruments, over the term of the convertible debentures, using the effective interest rate method. The value of the conversion option makes up the equity component of the instruments. The conversion option is recorded using the residual method. Transaction costs associated with convertible debentures financing are expensed in the period in which they are incurred.

[i] Deferred leasehold inducement

Deferred leasehold inducement, which is comprised of a tenant improvement allowance, is being amortized to reduce rent expense on a straight-line basis over the initial term of lease as a reduction on rent expense.

[j] Research and development costs

Research costs, including costs for new patents and patent applications, are expensed in the period in which they are incurred. Development costs are expensed in the period in which they are incurred unless such development costs meet the criteria under Canadian generally accepted accounting principles for deferral and amortization. No development cost has been deferred to date.

Contract research and development expenses, including fees paid to contract research organizations, investigators and other vendors who conduct certain product development activities on behalf of the Company, are recognized in a period based on estimates of the work performed using an accrual basis of accounting. These estimates are based on patient enrolment, services provided and goods delivered, contractual terms and experience with similar contracts. The Company monitors these factors to the extent possible and adjust the estimates accordingly.

Amounts advanced to third parties in connection with planned future research and development activities are deferred as prepaid expenses and are expensed as research and development costs based on work performed during the period.

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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

[k] Future income taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income taxes are recognized for the future income tax consequences attributable to differences between carrying values of assets and liabilities and their respective income tax bases. Future income tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, measured using substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future income tax assets, net of a valuation allowance, are recorded in the financial statements if realization is considered more likely than not.

[l] Investment tax credits

The Company recognizes tax credits for qualifying research and development costs when there is reasonable assurance of realization of such credits. The Company accounts for investment credits relating to research and development expenses as a reduction of such expenses and those relating to capital expenditures as reduction of the cost of the assets acquired. No investment tax credits have been recorded in these financial statements as there is no reasonable assurance of realization.

[m] Stock-based compensation

The Company grants stock options to employees, directors, and consultants pursuant to a stock option plan described in *note 12(e)*. The Company uses the fair value method to account for all stock-based awards granted, modified or settled, and the Black-Scholes option pricing model to determine the fair value of stock options granted. As such, a compensation expense is recorded based on the estimated fair value of options with a corresponding credit to contributed surplus. Any consideration received on the exercise of stock options is credited to share capital.

The fair value of stock-based awards to employees and directors is measured on the date of grant and amortized over the vesting period. The fair value of stock-based awards to consultants is measured at the performance commitment date or the date that the service is delivered.

[n] Loss per common share

Basic loss per common share is computed using the weighted average number of common shares outstanding during the period. Diluted loss per common share is equivalent to the basic loss per common share as the effect of outstanding warrants and options disclosed in *note 12* are anti-dilutive for all periods presented.

Pacgen Biopharmaceuticals Corporation
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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

3. CHANGES IN ACCOUNTING POLICIES

[a] General Standards of Financial Statement Presentations

In May 2007, the Canadian Accounting Standards Board (the "AcSB") amended CICA Handbook Section 1400, "*General Standards of Financial Statement Presentation*", to change the guidance related to management's responsibility to assess the ability of the entity to continue as a going concern.

The main features of the changes are as follows:

- (i) management is required to make an assessment of an entity's ability to continue as a going concern;
- (ii) in making its assessment, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the balance sheet date;
- (iii) financial statements must be prepared on a going concern basis unless management either intends to liquidate the entity, to cease trading or cease operations, or has no realistic alternative but to do so;
- (iv) disclosure is required of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern; and
- (v) when financial statements are not prepared on a going concern basis, that fact should be disclosed, together with the basis on which the financial statements are prepared and the reason the entity is not regarded as a going concern.

This section became effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. The Company adopted these standards commencing April 1, 2008. The new disclosure requirements pertaining to this section are contained in *note 1* of these consolidated financial statements.

[b] Capital Disclosures

The AcSB issued Section 1535, "*Capital Disclosures*". This section establishes standards for disclosing information about an entity's capital and how it is managed in order that a user of the financial statements may evaluate the entity's objectives, policies and processes for managing capital. This section became effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. The Company adopted these standards commencing April 1, 2008. The adoption of these new standards did not have a material impact on the Company's consolidated financial statements. The new disclosure requirements pertaining to this section are contained in *note 4* of these consolidated financial statements.

Pacgen Biopharmaceuticals Corporation
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**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2009 and 2008

(expressed in Canadian dollars)

3. CHANGES IN ACCOUNTING POLICIES (cont'd.)

[c] Financial Instruments – Disclosure and Presentation

The AcSB issued two new sections in relation to financial instruments: Section 3862, “*Financial Instruments – Disclosure*” and Section 3863, “*Financial Instruments – Presentation*”. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how these risks are managed. The new presentation standard carries forward the former presentation requirements. Both sections became effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007. The Company adopted these standards commencing April 1, 2008. The adoption of these new standards did not have a material impact on the Company’s consolidated financial statements. The new disclosure requirements pertaining to these sections are contained in *note 5* of these consolidated financial statements.

[d] New Accounting Pronouncements

In February 2008, the AcSB confirmed that Canadian GAAP for public companies will be converged with International Financial Reporting Standards (“IFRS”) for accounting periods commencing on or after January 1, 2011. IFRS uses a conceptual framework similar to Canadian GAAP, but there are some significant differences on recognition, measurement and disclosures. The Company continues to monitor and assess the impact of convergence of Canadian GAAP and IFRS.

In February 2008, the CICA issued Section 3064, “*Goodwill and Intangible Assets*”, which replaces Section 3062, “*Goodwill and Other Intangible Assets*” and Section 3450, “*Research and Development Costs*”. Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The new section will be applicable to the Company’s consolidated financial statements for its fiscal year beginning April 1, 2009. The Company is currently evaluating the impact of the adoption of this new section on its consolidated financial statements.

In January 2009, the CICA issued Section 1601 “*Consolidations*” and Section 1602 “*Non-controlling Interests*”. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are applicable to interim and annual financial statements of the Company beginning on January 1, 2011. The Company is in the process of evaluating the impact of these standards.

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**NOTES TO CONSOLIDATED
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(expressed in Canadian dollars)

3. CHANGES IN ACCOUNTING POLICIES (cont'd.)

[d] New Accounting Pronouncements (cont'd.)

In January 2009, the CICA issued Section 1582 "*Business Combinations*" replacing Section 1581 "*Business Combinations*". The new section improves the relevance, reliability and comparability of the information that a reporting entity provides in its financial statements about a business combination and its effects. The section is applicable to the annual and interim financial statements of the Company beginning on or January 1, 2011, with early adoption permitted. The Company is in the process of evaluating the impact of this standard.

In January 2009, the CICA issued EIC 173 "*Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*". This guidance requires that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This guidance is applicable to the Company's 2009 fiscal year with retrospective application without restatement of prior periods. The Company is in the process of evaluating the impact of this new guidance.

4. CAPITAL DISCLOSURE

The Company's objectives when managing capital are to ensure its ability to continue as a going concern in order to pursue the development of its drug candidates and the ultimate sale or out-license of these drug candidates to pharmaceutical companies. The Company attempts to maximize return to shareholders by minimizing shareholder dilution and, when possible, utilizing non-dilutive funding arrangements, such as interest income and collaborative partnership arrangements.

The Company includes convertible debentures and equity comprised of issued share capital, contributed surplus and deficit in the definition of capital. Other than the recent issuance of convertible debentures, the Company has financed its capital requirements primarily through share issuances since inception.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and risk characteristics of the underlying assets. The Company may issue new shares or raise debt. The Company is not subject to any externally imposed capital requirements and the overall strategy with respect to capital management remains unchanged from the year ended March 31, 2008.

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**NOTES TO CONSOLIDATED
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5. FINANCIAL INSTRUMENTS AND RISK

The Company's financial instruments consist of cash and cash equivalents, amounts receivable, accounts payable and accrued liabilities, other payable and convertible debentures. The fair value of these instruments approximates their carrying amount due to their immediate or short-term maturity. Other payable and convertible debentures were recorded at fair value on the date of issuance. The Company has classified its financial instruments as follows:

Financial Instrument	Classification	Measurement
Cash and cash equivalents	Held for trading	Fair value
Amounts receivable	Loans and receivables	Amortized cost using the effective interest method
Accounts payable and accrued liabilities	Other financial liabilities	Amortized cost using the effective interest method
Other payable	Other financial liabilities	Amortized cost using the effective interest method
Convertible debentures	Other financial liabilities	Amortized cost using the effective interest method

The Company did not have any held-to-maturity or available-for-sale financial instruments, nor did it acquire or hold any derivative products during the years ended March 31, 2009 and 2008.

The Company's financial instruments are exposed to certain financial risks, including credit risk, interest rate risk, currency risk and liquidity risk:

[a] Credit risk

Credit risk is the risk of a financial loss to the Company if counterparty to a financial instrument fails to meet its contractual obligations, and arises principally of cash and cash equivalents. The Company has investment policies to mitigate against the deterioration of principal, to enhance the Company's ability to meet its liquidity needs and to optimize yields within those parameters. These investment policies limit the investing of excess funds to liquid term deposits with banks and government guaranteed securities with maturities of two years or less.

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5. FINANCIAL INSTRUMENTS (cont'd.)

[b] Interest rate risk

Interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in the market interest rates. The Company is exposed to interest rate risk on its convertible debentures and other payables which bear floating interest rates. The Company estimates that one percent increase in the interest rate would increase the net loss and cash used in operations for the year ended March 31, 2009 by \$569. An opposite impact would have occurred to net loss and cash used in operations had interest rate decreased by one percent. Fluctuations in the market interest rates had limited impact on the Company's interest expense in the year ended March 31, 2009 given the timing of the issuance of convertible debentures in the fourth quarter. The Company had no exposure to interest rate fluctuations on liabilities in the preceding fiscal year. The Company does not use derivative instruments to reduce its exposure to interest rate risk.

The Company is also exposed to interest rate risk on its cash and cash equivalents that earn interest at market interest rates. Given the level of cash and cash equivalents held by the Company during the year ended March 31, 2009, fluctuations in the market interest rates had no significant impact on its interest income.

[c] Currency risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchanges rates. The Company operates primarily within Canada although a portion of its expenses are incurred in United States dollars ("US dollar"). The Company has not entered into foreign exchange derivative contracts. A significant change in the currency exchange rates between the Canadian dollar relative to the US dollar could have an effect on the Company's results of operations, financial position or cash flows.

As at March 31, 2009 and 2008, the Company had the following assets and liabilities denominated in US dollars:

	March 31, 2009 US\$	March 31, 2008 US\$
Cash and cash equivalents	14,802	8,818
Prepaid expenses	382,261	407,261
Accounts payable and accrued liabilities	413,679	1,200,023
Other payable	495,856	—
	1,306,598	1,616,102

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5. FINANCIAL INSTRUMENTS (cont'd.)

[c] Currency risk (cont'd)

Based on the above net exposures as at March 31, 2009, and assuming that all other variables remain constant, a 5% appreciation or deterioration of the Canadian dollar against the US dollar would result in a decrease or increase of \$32,319 (March 31, 2008 - \$35,455) in the Company's net loss and comprehensive loss.

[d] Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its obligations as they come due. The Company's exposure to liquidity risk is dependent on purchasing commitments and obligations and raising of funds to meet commitments and sustain operations. The Company manages liquidity risk by continuously monitoring its actual and forecasted working capital requirements, and actively managing its financing activities.

As of March 31, 2009, the Company had a working capital deficiency of \$1,023,213 (March 31, 2008 - \$535,149). The Company is currently seeking additional capital to meet its immediate obligations and to finance its operations. Management is considering all financing alternatives, including equity financing, debt financing, joint-venture, corporate collaboration and licensing arrangement.

6. RESEARCH AND DEVELOPMENT EXPENSES

Project	Year ended March 31, 2009 \$	Year ended March 31, 2008 \$	Cumulative from Inception to March 31, 2009 \$
PAC-113 [2005 – 2009]			
Expense	1,154,902	2,302,548	5,469,146
Recovery [note 10]	(865,287)	—	(865,287)
	289,615	2,302,548	4,603,859
PAC-G31P [2007 – 2009]	272,306	1,146,834	2,099,603
Other Projects	24,676	31,141	213,565
	586,597	3,480,523	6,917,027

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7. CASH AND CASH EQUIVALENTS

As at March 31, 2009, cash and cash equivalents include \$nil [2008 - \$900,000] of Canadian dollars term deposits with a weighted average interest rate of nil% [2008 - 3.84%], and \$250,000 [2008 - \$Nil] of subscription amounts received in trust accounts following the closing of a financing.

8. PROPERTY AND EQUIPMENT

	Cost	Accumulated Amortization	Net Book Value
	\$	\$	\$
March 31, 2009			
Computer equipment and software	46,304	33,080	13,224
Leasehold improvement	41,346	14,131	27,215
Office furniture and equipment	43,718	16,283	27,435
	131,368	63,494	67,874
March 31, 2008			
Computer equipment and software	55,280	25,450	29,830
Leasehold improvement	41,346	8,083	33,263
Office furniture and equipment	50,456	12,313	38,143
	147,082	45,846	101,236

During the year ended March 31, 2009, amortization was \$263,816 [2008 - \$269,245].

9. INTANGIBLE ASSETS

	March 31, 2009	March 31, 2008
	\$	\$
Technology, licenses and rights		
Cost	1,477,151	1,477,151
Accumulated amortization	711,922	474,948
	765,229	1,002,203

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9. INTANGIBLE ASSETS (cont'd.)

- [a] On February 1, 2005, the Company entered into a license agreement with Demegen, Inc. ("Demegen"), a third party, to acquire an exclusive world-wide license, with a right to sublicense, use, improve, develop and commercially exploit certain patented technologies for the treatment of human oral disease conditions (the "Demegen Sublicense"). In consideration for the Demegen Sublicense, the Company paid Demegen an initial license fee of US\$50,000.

The Company subsequently entered into an amendment agreement with Demegen, on January 2, 2006, to revise the royalty payment terms of the Demegen Sublicense. In exchange for a reduced percentage of royalties on net product sales and net sublicenses revenue, the Company issued to Demegen 800,000 common shares of the Company at a price of \$0.60 per share and 500,000 share purchase options with a fair value of \$30,000 with an exercise price of \$2.25 per share. These warrants expired unexercised on December 7, 2008.

The initial fees at the exchange amount of \$59,472, the fair value of the common shares issued of \$480,000 and the fair value of the share purchase options granted of \$30,000 had been capitalized as technology license and rights and amortized on a straight line basis over ten years. The net book value of the Demegen Sublicense as of March 31, 2009 was \$385,821 (March 31, 2008 - \$442,795).

- [b] On April 4, 2006, the Company completed the acquisition (the "ILT Acquisition") of all of the issued and outstanding shares of IL Therapeutics Inc. ("ILT") comprised of common shares and retractable investment shares. The ILT Acquisition provided the Company approximately \$1.5 million in working capital and certain technology relating to the prevention and treatment of severe inflammatory diseases characterized with neutrophil over-recruitment (the "PAC-G31P Technology"). The consideration for the ILT Acquisition comprised 1,250,000 preferred shares, 1,470,588 common shares and 1,250,000 common share purchase warrants of the Company, at an aggregate fair value of \$2,000,000. The ILT Acquisition was accounted for as an asset acquisition and the purchase price was allocated to ILT's identifiable assets and liabilities.

The share purchase price allocated to the acquired PAC-G31P Technology of \$907,409 had been capitalized as technology license and rights and amortized on a straight line basis over five years. The net book value of the acquired technology as of March 31, 2009 was \$379,408 (March 31, 2008 - \$559,408).

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10. OTHER PAYABLE

On March 6, 2009, the Company finalized its settlement arrangement with a vendor for its outstanding accounts of approximately US\$1.3 million (\$1.65 million). As part of this settlement, the Company received from this vendor a credit note of approximately US\$604,000 (\$747,000) as a research and development expense recovery in the year ended March 31, 2009. For the remaining balance of US\$708,000 (\$893,000), the Company made an initial payment of US\$128,000 (\$157,000) and agreed to pay the balance amount of US\$580,000 (\$731,000) by three minimum installments.

The minimum payments of US\$150,000 (\$189,000), US\$150,000 (\$189,000) and US\$280,000 (\$353,000) are due on July 15, 2009 [note 18], October 15, 2009 and December 30, 2009, respectively. Pursuant to the settlement agreement, should the Company successfully complete a transaction or multiple transactions which give rise to accumulated proceeds equal to or greater than US\$500,000 (approximately \$631,000), the Company is obligated to make the first payment immediately. The Company is entitled to earlier repayment by giving a 10 days notice.

Unless all minimum payments are made in accordance to the settlement agreement, the Company is obligated to pay interest at a rate of six percent above the average daily prime interest rate of a chartered bank on amounts due and outstanding from the respective due dates until paid [note 18]. All interest payments are due and payable in full on December 30, 2009.

11. CONVERTIBLE DEBENTURES

On January 30, 2009, the Company announced that it intended to offer, through one or more tranches of closings of a non-brokered private placement, convertible debentures in an aggregate principal amount of up to approximately \$610,000 (the "Offering"). The Company closed this Offering in two tranches in February 2009 and March 2009 for an aggregate principal amount of \$614,500.

Maturity Date	Principal Amount \$
February 3, 2010 ⁽¹⁾	364,500
April 14, 2010 ⁽²⁾	250,000
	614,500

⁽¹⁾ Include debentures of \$243,000 held by director or officer of the Company (the "Insiders").

⁽²⁾ The second tranche of the Offering was closed on March 30, 2009 with final completion on April 14, 2009.

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11. CONVERTIBLE DEBENTURES (cont'd.)

The convertible debentures will bear interest from the date of issuance at a rate of prime plus 4% per annum and will mature one year from the date of issuance. The principal amount plus any accrued interest will be repayable in cash upon the earlier of (i) maturity or (ii) closing of a merger or a financing transaction with a value to the Company of at least US\$1 million (approximately \$1.26 million). Early redemption by the Company is allowed upon 30 days written notice.

All debenture holders acknowledged and agreed that, prior to maturity, they may not demand from the Company payment of the principal amount, interest or any outstanding portion thereof. At anytime prior to maturity, the debenture holders have the rights to convert these convertible debentures into units of the Company (the "Units") at a conversion price of \$0.10 per Unit upon 10 days written notice. Each Unit will consist of one common share of the Company (a "Common Share") and one common share purchase warrant (a "Warrant"), each Warrant entitling a non-insider holder to purchase one Common Share at an exercise price of \$0.10 per Common Share at any time prior to 24 months following the date of issuance of the Warrant upon conversion of the convertible debentures. Each Warrant comprising the Units issuable upon conversion of convertible debentures issued to insiders of the Company entitles a holder to purchase one Common Share at an exercise price of \$0.10 per Common Share and will expire upon the earlier of the maturity date of the convertible debentures and the date that is 24 months following the date of issuance of the Warrants upon conversion of the convertible debentures. Prior to conversion, in the event that the share capital of the Company has been restructured or a business combination involving the Company has occurred (the "Fundamental Change"), the debenture holders are entitled to receive the equivalent new securities as if the debenture conversions had occurred prior to the occurrence of the Fundamental Change.

The Company is not restricted to obtaining other financing or issuing shares subsequent to the issuance of these convertible debentures.

The Company has classified the convertible debentures into its components being financial liabilities and equity components, respectively. The fair value of the liability component was estimated by discounting the future cash stream of debt at a discount rate of 25% which represents the estimated borrowing rate available for the Company for similar debentures having no conversion rights. The residual value was allocated to the equity component. The amount of total proceeds allocated to the liability components and equity components (contributed surplus) at the issuance were:

Allocation	Amount
	\$
Face value	614,500
Contributed surplus	(90,946)
	523,554
Short-term portion	(310,554)
	213,000

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11. CONVERTIBLE DEBENTURES (cont'd.)

The Company incurred legal and professional fees of \$30,097 associated with the financing. These financing costs together with an interest expense of \$11,912 associated with the convertible debentures were charged as expenses during the year ended March 31, 2009.

12. SHARE CAPITAL

[a] Common shares

	Number of Shares	Amount \$
Authorized		
Unlimited number of common shares without par value		
Balance, March 31, 2007	30,521,960	12,286,556
Issued for cash pursuant to a private placement [i]	4,622,733	725,562
Balance, March 31, 2008 and 2009	35,144,693	13,012,118

[i] On March 17, 2008, the Company closed a private placement of 4,515,003 units (the "Units") at \$0.20 per Unit for total gross proceeds of \$903,000. Each Unit was comprised of one common share of the Company and one common share purchase warrant. One common share purchase warrant entitled the holder to purchase one common share of the Company at \$0.30 per share until March 16, 2013. In connection with the private placement, the Company issued 107,730 units as compensation (the "Compensation Units") and 34,200 broker warrants (the "Broker's Warrants") to an agent. Each Compensation Unit was converted to one common share and one common share purchase warrant at no cost to the agent. Each Broker's Warrant is exercisable into one Unit at \$0.22 per Unit until March 16, 2010. Upon exercise, each Broker Warrant will convert to one common share, and one common share purchase warrant exercisable into one additional common share at \$0.30 per share until March 16, 2013. The Compensation Units and Broker's Warrants have an estimated value of \$40,960.

The Company adopted the residual approach in valuing the share purchase warrants attached to the private placement units issued. Under this approach, proceeds up to the Company's share market value are allocated to the shares and only the excess above the market value is allocated to the attached share purchase warrants. A value of \$2,535 has been allocated to these warrants as determined under the residual approach.

The Company also incurred professional and other financing costs of \$155,490.

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12. SHARE CAPITAL (cont'd.)

[b] Preferred shares

The authorized share capital of the Company also consists of an unlimited number of preferred shares without par value. As of March 31, 2009 and 2008, there were no preferred shares issued and outstanding.

[c] Common share purchase warrants

	Number	Weighted Average Exercise Price \$
Balance, March 31, 2007	7,936,401	1.21
Expired on December 7, 2007	(3,394,393)	1.30
Issued on March 17, 2008 [note 12(a)(i)]	4,515,003	0.30
Issued on March 17, 2008 [note 12(a)(i)]	107,730	0.30
Issued on March 17, 2008 [note 12(a)(i)] ⁽¹⁾	34,200	0.22
Balance, March 31, 2008	9,198,941	0.72
Expired on December 7, 2008	(2,748,906)	1.16
Expired on December 7, 2008	(1,250,000)	1.16
Expired on December 7, 2008	(543,102)	1.05
Balance, March 31, 2009	4,656,933	0.30

Date of Expiry	Exercise Price	Number of Warrants
March 16, 2013 [note 12(a)(i)]	\$0.30	4,622,733
March 16, 2010 [note 12(a)(i)] ⁽¹⁾	\$0.22	34,200
Balance, March 31, 2009	\$0.30	4,656,933

⁽¹⁾ Upon exercise, each Broker Warrant will convert to one common share and one common share purchase warrant exercisable into one additional common share at \$0.30 per share until March 16, 2013. After giving effect to the conversion of these Broker Warrants, there are 4,691,133 common share purchase warrants outstanding, at an average exercise price of \$0.30, as of March 31, 2009.

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12. SHARE CAPITAL (cont'd.)

[d] Share purchase options

	Number	Weighted Average Exercise Price \$
Balance March 31, 2007 and 2008	500,000	2.25
Granted	—	—
Expired [note 9(a)]	(500,000)	2.25
Balance, March 31, 2009	—	—

[e] Stock options

On August 22, 2006, the Company adopted a stock option plan (the "Stock Option Plan") providing the granting of options to employees, officers, directors, consultants and scientific advisory board members. The maximum number of common shares that are issuable under the Stock Option Plan is an aggregate of 10% of the issued and outstanding common share, calculated as at the award date of the options. The maximum number of common shares that may be optioned in favour of any single individual will not exceed 5% of the issued and outstanding common shares at the date of grant. The maximum number of common shares that may be optioned in favour of directors and senior officers under the Stock Option Plan is 10% of the issued and outstanding common shares at the date of grant.

During the years ended March 31, 2009 and 2008, the Company granted certain options and also cancelled certain options upon the option holders ceased to become eligible persons (the "Eligible Persons") as defined in the Stock Option Plan. Options granted to former employees who continued to perform services as consultants to the Company after their employment were kept, provided that such option holders remained as Eligible Persons. Details of stock option transactions are summarized as follows:

	Number	Weighted Average Exercise Price \$
Balance, March 31, 2007	2,499,000	1.02
Granted	229,000	0.70
Forfeited or cancelled	(94,000)	1.02
Balance, March 31, 2008	2,634,000	0.99
Granted	175,000	0.26
Forfeited or cancelled	(995,667)	0.79
Balance, March 31, 2009	1,813,333	0.99

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12. SHARE CAPITAL (cont'd.)

[e] Stock options (cont'd.)

At March 31, 2009, stock options to executive officers and directors, employees, consultants and clinical advisory board members were outstanding as follows:

Options Outstanding				Options Exercisable	
Range of Exercise Price	Number of Common Shares Issuable	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price (\$)	Number of Common Shares Issuable	Weighted Average Exercise Price (\$)
\$0.26 - \$0.45	40,000	4.40	0.26	40,000	0.26
\$0.50 - \$0.85	393,333	6.04	0.64	306,666	0.64
\$1.00 - \$1.05	530,000	4.04	1.05	520,000	1.05
\$1.10 - \$1.16	850,000	5.47	1.16	720,000	1.16
	1,813,333	5.05	0.99	1,586,666	0.99

As of March 31, 2009, stock options to employees, officers, directors, consultants and scientific advisory board members were outstanding as follows:

Date of Expiry	Exercise Price	Number of Options Outstanding	Number of Options Exercisable
August 22, 2014	\$0.50	10,000	10,000
August 22, 2011	\$1.05	150,000	150,000
August 22, 2014	\$1.05	210,000	200,000
August 22, 2014	\$1.16	730,000	630,000
March 6, 2012	\$1.05	100,000	100,000
March 6, 2015	\$1.05	50,000	50,000
March 6, 2015	\$1.16	120,000	90,000
March 27, 2015	\$0.65	233,333	233,333
May 31, 2012	\$1.05	20,000	20,000
May 31, 2015	\$0.63	150,000	63,333
Aug 28, 2013	\$0.26	40,000	40,000
Balance, March 31, 2009		1,813,333	1,586,666

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12. SHARE CAPITAL (cont'd.)

[e] Stock options (cont'd.)

The fair value of the stock options granted was estimated using the Black-Scholes valuation model with the following assumptions:

Volatility	88.90 – 136.31%
Expected life of options	2 – 5 years
Dividend yield	0.00%
Risk free interest rate	1.07 – 4.00%

The estimated fair value of options granted to employees including officers and directors, and non-employees are as follows:

	March 31 2009	March 31 2008
	\$	\$
Employees	116,487	331,853
Non-employees	44,200	14,495
	160,687	346,348

Option-pricing models require the use of highly subjective estimates and assumptions including the expected stock price volatility. Changes in the underlying assumptions can materially affect the fair value estimates.

13. COMMITMENTS

[a] Operating leases

The Company has entered into lease agreements for its office premises in Canada for terms up to five years expiring on March 28, 2012. Future minimum annual lease payments under the leases are as follows:

	\$
2010	101,372
2011	52,454
2012	3,537
2013	—
2014	—
	157,363

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13. COMMITMENTS (cont'd.)

[b] Clinical research and development agreements

The Company has entered into various clinical research and development agreements with third parties which require the Company to fund research and development expenditures of \$2,923,950 for the fiscal year ending March 31, 2010. Of these commitments, \$490,966 are non-cancellable and \$2,432,984 are cancellable for fiscal year ending March 31, 2010.

[c] License agreements

- [i] Pursuant to the Demegen Sublicense, the Company is required to make minimum annual royalty payments of US\$50,000 for the period until the expiry date of the last patent right and to pay an annual maintenance fee of US\$50,000 if any of the agreed clinical development milestones are not met [note 9(a)].
- [ii] Pursuant to a license agreement between the Company's wholly owned subsidiary, ILT, and University of Saskatchewan (the "US License"), the Company is responsible for up to \$510,000 of milestone payments linked to successful completion of preclinical proof of concept (\$60,000 paid), successful filing of investigational new drug application (\$25,000) and successful completion of Phase I to Phase III clinical studies (amount to \$425,000) of the licensed technology. The Company is also responsible for up to \$1,070,000 of milestone payments linked to marketing approval in five regions (United States, Europe, Japan, Canada and Hong Kong) and another one time payment of \$100,000 for an added indication in any country. The Company is further obligated to pay royalties on sales revenue and sub-licensing revenue.

Also as part of the US License, the Company has agreed to provide funding to the University of Saskatchewan. The research will cover but is not limited to research related to the licensed technology for not less than \$500,000 within the first five years of the term of the license agreement, with minimum \$100,000 per year for the first two years. \$334,907 has been paid to date. The Company is committed to provide funding for the remaining balance of \$165,095 by October 15, 2009.

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14. CONTINGENCIES

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

15. INCOME TAXES

At March 31, 2009, the Company has non-capital loss carryforwards and investment tax credits available to offset future taxable income and future income taxes payable in Canada, respectively that expire as follows:

	Federal Investment Tax Credits	Provincial Investment Tax Credits	Non-Capital Losses
	\$	\$	\$
2011	—	—	11,000
2015	—	—	287,000
2016	—	24,000	687,000
2017	—	45,000	—
2018	—	49,000	—
2019	—	15,000	—
2026	43,000	—	—
2027	118,000	—	2,008,000
2028	173,000	—	5,154,000
2029	51,000	—	3,512,000
	<u>385,000</u>	<u>133,000</u>	<u>11,659,000</u>

In addition, the Company has unclaimed tax deductions of approximately \$1,616,373 related primarily to scientific research and experimental development expenditures available to carryforward indefinitely to reduce taxable income of future years.

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15. INCOME TAXES (cont'd.)

Significant components of the Company's future tax assets and liabilities as of March 31, 2009 are shown below:

	2009	2008
	\$	\$
Future tax assets:		
Tax basis in excess of accounting value	10,000	(108,000)
Share issuance costs	156,000	235,000
Research and development deductions and credits	1,086,000	750,000
Write-off of investment in Pacgen Taiwan	\$309,400	—
Operating loss carryforwards	3,031,000	2,624,000
Total future tax assets	4,592,400	3,501,000
Valuation allowance	(4,592,400)	(3,501,000)
Total future tax assets	—	—
Future income tax liabilities:		
Intangible assets	—	—
Net future income tax liabilities	—	—

The potential income tax benefits relating to the net future tax assets have not been recognized in the consolidated financial statements as their realization did not meet the requirements of "more likely than not" under the liability method of tax allocation. Accordingly, no net future tax assets have been recognized as at March 31, 2009 and 2008.

The reconciliation of income tax attributable to operations computed at the statutory tax rates to income tax expenses using a 30.63% statutory tax rate [March 31, 2008 - 33.47%] is:

	2009	2008
	\$	\$
Income taxes at statutory rates	(699,000)	(2,034,000)
Expenses not deductible for tax purposes	436,000	122,000
Benefit of non-capital losses not recognized	263,000	1,793,000
Foreign tax rate difference	—	34,000
Future income tax recovery	—	(85,000)

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16. SEGMENTED INFORMATION

The Company operates primarily in one business segment with substantially all of its consolidated assets located in Canada and operations located in Canada.

17. RELATED PARTY TRANSACTIONS

During the year ended March 31, 2009, the Company incurred \$503 [2008 - \$130,819] of expenditures for services provided by related parties. These transactions were incurred in the normal course of business and recorded at their exchange amounts. Details of related party transactions during the years ended March 31, 2009 and 2008 are summarized as follows:

	March 31, 2009	March 31, 2008
	\$	\$
Consulting services provided by directors	503	3,186
Research services provided by a consulting firm of which a director is the principal	—	1,000
Research services provided by a consulting firm of which an officer is the principal	—	120,988
Research services provided by a university laboratory of which an officer is a professor	—	5,645
	503	130,819

18. SUBSEQUENT EVENTS

On June 8, 2009, the Company signed a share purchase agreement with the shareholders of Xphase Pharmaceuticals Inc. ("Xphase"). Xphase, a privately held pharmaceutical company, has the right to acquire the exclusive global rights, excluding China, of AF-05, a novel anti-anxiety drug candidate currently in Phase I clinical trial in China. Xphase also provides consulting and project management services to assist small to medium pharmaceutical and biotechnology companies globally.

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18. SUBSEQUENT EVENTS (cont'd.)

Pursuant to the share purchase agreement, the Company agrees to issue 3 million common shares of the Company to Xphase shareholders in exchange for 100% ownership of Xphase as well as management services of Xphase principals. Upon the achievement of certain pre-defined business development milestones, Xphase shareholders will be entitled to an additional 3.5 million common shares of the Company. The Company obtained regulatory approval to complete its acquisition of Xphase in July 2009. Following the acquisition of Xphase, the Company has positioned itself to become a global life-science technology transfer company focused on the commercial development of novel therapeutic drug candidates up to Phase II human proof of concept.

Subsequent to the year ended March 31, 2009, the Company continues to seek additional funding to finance its operations and obligations. The Company's management is considering all possible financing alternatives. There can be no assurance that such financing will materialize on a timely basis or obtained on favorable terms. If the Company is unable to obtain additional financing or complete a collaborative transaction, it may have to further scale back our operations, consider business combinations or shut down some or all of its operations.

Also subsequent to the year ended March 31, 2009, the Company updated the debtor of other payable [note 10] on the Company's financing progress, and notified that the minimum payment of US\$150,000 due on July 15, 2009 would be deferred. Both parties agreed to maintain close communication on the Company's financing progress. The Company started accrual of interest expenses on July 15, 2009 in accordance to the settlement agreement.