

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This management discussion and analysis ("MD&A") was performed by management using information available as of July 19, 2010 and should be read in conjunction with our audited consolidated financial statements for the year ended March 31, 2010 and the related notes included thereto. These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). All amounts are expressed in Canadian dollars unless otherwise indicated. Additional information relating to Pacgen Biopharmaceuticals Corporation ("Pacgen" or the "Company") can be obtained from SEDAR at www.sedar.com. On June 8, 2010, Pacgen completed a share consolidation ("Share Consolidation") on a two to one basis. All common shares, warrants and options and per share amounts have been retroactively restated in this MD&A to reflect the Share Consolidation.

The forward-looking statements in this discussion regarding our expectations of our future performance, liquidity and capital resources and other non-historical statements include numerous risks and uncertainties, as described in the "Risk Factors" section of our Annual Information Form dated July 31, 2008, which is available on SEDAR at www.sedar.com. The words "anticipates", "believes", "estimates", "expects", "intends", "may", "could", "plans", "projects", "will", "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, level of activity, performance or achievements to be materially different from those implied by such statements. Such factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, dependence on collaborative partners, and our ability to protect our intellectual property. We undertake no obligation to revise or update forward looking statement in this discussion whether as a result of new information, future events or otherwise. Accordingly, readers should not place undue reliance on forward looking statements in this discussion.

OVERVIEW

We are 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. We identify innovative therapeutic drug candidates globally, and develop these drug candidates, with collaborative partners in accordance to the United States Food and Drug Administration (the "FDA") regulatory standards, to feed the product development pipelines of the pharmaceuticals industry. We currently have two product pipelines in our technology portfolio: PAC-113, an anti-fungal for the treatment of oral Candidiasis, and PAC-G31P, a novel peptide therapeutic designed to treat inflammatory diseases characterized by non-beneficial neutrophil.

PAC-113 is a 12 amino-acid antimicrobial peptide derived from a naturally occurring histatin protein found in saliva. This peptide alters the permeability of fungal cell membranes causing cell death. We are developing PAC-113 in a mouthrinse formulation for the topical treatment of oral Candidiasis. Oral Candidiasis, or thrush, is usually seen as a secondary consequence arising from one of a number of primary or underlying medical conditions including HIV/AIDS, cancer, diabetes, asthma and xerostomia (abnormal dryness of the mouth). We obtained our rights to PAC-113 through a sublicense agreement with Demegen, Inc. (the "Demegen Sublicense") in February 2005. The Demegen Sublicense provides us with exclusive worldwide rights to develop and commercialize PAC-113 for human oral disease conditions. Since obtaining these rights, we have completed formulation optimization work, a Phase I/II proof of concept clinical study, as well as a Phase IIb dose-ranging study. The data from our clinical studies demonstrates that PAC-113 is effective in the treatment of oral Candidiasis. The data also suggests that PAC-113 compares favourably to the efficacy demonstrated by Nystatin, a current standard of care. We are currently working with a collaborative partner to develop PAC-113 for the treatment of oral Candidiasis for commercialization in China. We are currently seeking for collaborative partners for regions outside of China.

PAC-G31P is a small recombinant protein that is a synthetic analogue of the human cytokine called Interleukin-8 which is the key chemokine involved in neutrophil recruitment. We are developing PAC-G31P to treat inflammatory diseases. Non-beneficial neutrophil recruitment is a key characteristic of a number of acute and chronic inflammatory conditions, including acute respiratory distress syndrome, severe asthma, chronic obstructive pulmonary disease, pneumonia, Crohn's Disease, rheumatoid arthritis and ischemia/reperfusion injury. We obtained exclusive worldwide rights to PAC-G31P technology for the prevention and treatment of severe inflammatory diseases characterized by neutrophil over-recruitment in April 2006, through the acquisition of IL Therapeutics Inc. ("ILT"). Since taking over the PAC-G31P program, we conducted a number of preclinical and mechanistic studies, and initiated formulation development work. PAC-G31P is currently in preclinical development. We are currently

seeking for a joint-venture partner to conduct preclinical studies to add data to our package for out licensing purposes.

We currently hold the rights to 26 patents and 31 patent applications in the United States and other jurisdictions relating to products in our development pipeline. We also hold 2 granted patents and 7 patent applications and intellectual properties to two other research compounds that we no longer develop.

CORPORATE DEVELOPMENT SINCE LAST FISCAL YEAR

In April 2009, we appointed Mr. Tsong Chin Lin to our board of directors. Mr. Lin brings to Pacgen over 30 years of management experience in leading industrial technology companies. Mr. Lin currently serves as Chairman, President and Chief Executive Officer of General Biologicals Corporation (“GBC”). Prior to GBC, he served as Chief Executive Officer of Megamedia Corporation and in various leadership roles at General Instrument of Taiwan Ltd.

On June 8, 2009, we signed a share purchase agreement (the “Acquisition Agreement”) with the shareholders of Xphase Pharmaceuticals Inc. (“Xphase”). Pursuant to the Acquisition Agreement, we agreed to issue 1.5 million common shares (or 3.0 million pre-consolidated common shares) to Xphase shareholders in exchange for 100% ownership of Xphase as well as management services of Xphase principals (“the Xphase Acquisition”). Upon the achievement of certain pre-defined business development milestones within 12 months from the closing date, Xphase shareholders would be entitled to additional 1.75 million common shares (or 3.5 million pre-consolidated common shares). We completed this acquisition following the approval of the TSX Venture Exchange in August 2009, and issued 1.5 million common shares (or 3 million pre-consolidated common shares) to the shareholders of Xphase.

Following the completion of the Xphase Acquisition, we appointed Dr. Yiu Chung Lee from Xphase, and Mr. Fred Huang, co-founder of Pacgen, to our board of directors. Following these appointments, our board of directors consists of Mr. Chung Yu Wang (Chairman), Mr. Kevin McGarry (lead independent director), Dr. Alan Moore, Dr. Telvin Ju, Mr. Tsong Chin Lin, Dr Yiu Chung Lee and Mr. Fred Huang. In addition, we appointed the following Xphase principals to our management team:

(i) *Dr. Yiu Chung Lee as Chief Executive Officer (“CEO”)*

Dr. Lee, an experienced entrepreneur, brings to Pacgen more than 20 years of pharmaceutical development experience earned in various settings, including pharmaceutical company, biotechnology company as well as contract research organization. Prior to co-founding Xphase, Dr. Lee previously held positions in Eli Lilly Canada Inc., Patheon Inc. and PharmEng Technology Inc.

(ii) *Dr. Beverly Incedon as Vice President, Research and Development*

Dr. Incedon brings to Pacgen more than 14 years of pharmaceutical industry experiences and extensive knowledge in drug development and manufacturing operations. Prior to joining Xphase, Dr. Incedon served as Director, Research and Development at Eli Lilly Canada Inc. Dr. Incedon also previously held positions in Glaxo Wellcome Inc. (Canada) and Syntex Inc.

(iii) *Mr. Joel Cheng as Vice President, Business Development*

Mr. Cheng has over 26 years of experience in sales, marketing, business development and corporate management in the North America. Prior to co-founding Xphase, Mr. Cheng served as Senior Director at PharmEng International Inc. Mr. Cheng also previously held positions in MDS, SCIEX and Hewlett Packard/Agilent Technologies.

(iv) *Mr. Gabriel Lam as Senior Director, Greater China Operations*

Mr. Lam has over 25 years of experience in business operations. Prior to co-founding Xphase, Mr. Lam served as Senior Director at PharmEng International Inc. Mr. Lam also previously held various managerial positions in Rootlink Technic Inc. and Hewlett Packard/Agilent Technologies.

The management team also includes existing members, Ms. Christina Yip and Dr. Lewis Choi, serving as Chief Financial Officer, and Vice President, Intellectual Properties and Scientific Affairs, respectively. Mr. Chung Yu Wang resigned as interim CEO but continues to assume his interim President role. Mr. Fred Huang resigned as Senior Vice President and Chief Operating Officer.

In January 2010, we entered into collaboration research and development agreements with Shanghai based New Summit Biopharma Co. (“New Summit Bio”). Under the terms of the agreements, New Summit Bio would collaborate with Pacgen to raise funding and to develop PAC-113 for the treatment of oral candidiasis for commercialization in China.

On April 19, 2010, we announced that we had arranged a non-brokered private placement (the “Financing”) of \$600,000 of subscription receipts (“Subscription Receipts”) subject to satisfactory completion of certain conditions, including the approval of the TSX Venture Exchange. We also announced that we had initiated a financial restructuring (the “Financial Restructuring”) to reduce our indebtedness and that we would seek shareholder approval for a consolidation of our common shares on a two to one basis (the “Share Consolidation”).

In May 2010, we closed the Financing and that obtained shareholder approval at the special meeting of shareholders held on May 25, 2010 for the Share Consolidation. Under the Financing, we issued an aggregate of 10 million Subscription Receipts at a price of \$0.06 per Subscription Receipt for gross proceeds of \$600,000. Upon completion of the Share Consolidation, each Subscription Receipt will be automatically exercised, for no additional consideration, for one common share.

On June 8, 2010, we announced completion of the Share Consolidation and that our common shares commenced trading on the TSX Venture Exchange on the consolidated basis. We issued 22,618,143 common shares pursuant to the Financing and the Financial Restructuring. The 22,618,143 common shares include (i) an aggregate of 10,000,001 common shares issued in connection with the automatic exercise of the 10 million Subscription Receipts of the Financing, and (ii) an aggregate of 12,618,142 common shares issued in connection with the settlement of conversion of an aggregate of approximately \$879,000 of indebtedness as part of the Financial Restructuring. All common shares issued under the Financing and the Shares for Debt Conversion were subject to a four-month holding period which would end on September 29, 2010 and October 9, 2010, respectively. Following the issuance of these shares and the Share Consolidation, we had 41,690,490 of common shares issued and outstanding.

RESEARCH AND DEVELOPMENT UPDATE

We carry out our research and development activities primarily through contract research organizations, and have significantly scaled down these activities in recent years due to financial constraints. We have not initiated any new research and development studies since June 2008, following the completion of our PAC-113 Phase IIb clinical studies. The current development status of each of our research and development programs is as follows:

PAC-113

In May 2007, we completed a Phase I/II proof of concept trial which involved 107 seropositive HIV patients with oral Candidiasis. The clinical trial was conducted at sites in the United States and South Africa. The results showed that PAC-113 was generally safe, well tolerated, and active in the treatment of oral Candidiasis with clinical cure rates comparable to the current standard of care. Based on these results, we initiated a Phase IIb dose-ranging trial to optimize PAC-113 dose and formulation.

In June 2008, we completed the Phase IIb dose-ranging trial. The results demonstrated that PAC-113 was effective in the treatment of oral Candidiasis and compared favorably to the efficacy demonstrated by Nystatin, a current standard of care.

The Phase IIb dose-ranging trial involved 223 seropositive HIV patients with oral Candidiasis, and was conducted at sites in the United States and South Africa. The objectives of the trial were to identify an optimal dose of PAC-113 from among the three doses studied, and to determine the relative efficacy of this PAC-113 dose as compared to Nystatin in eliminating clinical signs and symptoms of oral Candidiasis. Additionally, safety and tolerance and the microbiological response of *Candida albicans* to treatment were also measured.

The optimal dose of PAC-113 demonstrated a 34% increase in the primary endpoint efficacy level (complete clinical cure rate at Day 19) for the Per Protocol analysis as compared to Nystatin, and a 50% increase in the corresponding Intent to Treat analysis. Secondary efficacy endpoints showed similar trends among the three PAC-113 doses and the Nystatin group. The results also confirmed that PAC-113 was generally safe and well-tolerated.

The next development milestone in the United States is to meet with the FDA to discuss the requirements of the final stage of development. We are currently seeking for a collaborative partner to develop and market for the North American regions, as well as other regions outside of China.

The development plan for PAC-113 for the market in China is expected to be finalized by our collaborative partner following a meeting with the China State Food and Drug Administration (“sFDA”). New Summit Bio and Pacgen are currently focusing on fund raising activities in China, and plan to schedule a meeting with the sFDA shortly after the completion of fund raising. Based on the analysis of New Summit Bio, we expect that certain bridging studies are required prior to initiation of a pivotal clinical trial in China. These bridging studies would include studies, at both the pre-clinical and clinical level, conducted in accordance to the standards of sFDA.

PAC-G31P

We previously conducted certain preclinical studies primarily through our collaboration with the University of Saskatchewan, St. Michael’s Hospital and the University of Iowa. The results from these studies provided additional preclinical data to confirm the mechanism of action of PAC-G31P and the potential use of PAC-G31P in different animal models.

The next development milestone is to conduct necessary studies to enable an investigational new drug application (“IND”) filing with the FDA. We expect these studies to include preclinical safety and toxicology studies at Good Laboratory Standards (“GLP”) level, as well as manufacturing and formulation work at Good Manufacturing Practice Standards (“GMP”) level. We plan to out-license PAC-G31P program to a collaborative partner to undertake these IND enabling studies. Currently, we are seeking for a joint-venture partner to conduct certain preclinical studies to add data to our package for out-licensing purposes.

SELECTED ANNUAL FINANCIAL INFORMATION

The following table sets forth consolidated financial data for the fiscal years ended March 31, 2010, 2009, and 2008:

	For the year ended March 31,		
	2010	2009	2008
Net loss for the period	\$(1,625,315)	\$(2,282,640)	\$(5,974,712)
Per share loss, basic and fully diluted	\$(0.04)	\$(0.06)	\$(0.19)
Total assets	\$707,927	\$1,676,523	\$3,024,237
Total long-term liabilities	—	\$216,459	—

Since our inception, we have not generated any revenue, other than income from interest earned on our excess cash balances. The primary factors affecting the magnitude of our net losses in these fiscal years were the scope of our product developments, and the level of internal operational activities to support our corporate and business development objectives. We have scale-downed our operations since fiscal year ended March 31, 2008 (“Fiscal 2008”) due to financial constraints.

In Fiscal 2008, in response to the recent global financial market downturn, we undertook a comprehensive review of our product development programs, operations and projected cash requirements with the view of conserving cost and deferring cash outflows. Our cost saving programs started in November 2007. In Fiscal 2008, we eliminated certain administrative positions, reduced our management salaries and focused our development efforts primarily on our lead program, PAC-113. In the year ended March 31, 2009 (“Fiscal 2009”), following the completion of our PAC-113 Phase IIb clinical trial in June 2008, we further tighten up our operating expenditures, deferred further research and development studies, and focused our operational activities primarily in financing and business development. In the year ended March 31, 2010 (“Fiscal 2010”), we continued to operational focus in financing and business development activities.

RESULTS OF OPERATIONS

For Fiscal 2010, we recorded a net loss of \$1,625,315 (\$0.09 per common share), compared to a net loss of \$2,282,640 (\$0.13 per common share) for Fiscal 2009. The decrease in net loss by \$657,325 in Fiscal 2010, as compared to Fiscal 2009, was mainly due to a decrease in expenses and other losses by \$429,602 and \$227,723, respectively. Operating expenditures, excluding non-recurring charges, for Fiscal 2010 were \$1,143,964, compared to \$2,010,932 in Fiscal 2009. The reduced operating expenses was offset by non-recurring charges amounted to \$437,366 in connection to write-downs of assets in Fiscal 2010. Other losses for Fiscal 2010 were \$43,985, compared to \$271,708 in Fiscal 2009. The decline in other losses was primarily due to an increase in foreign exchange gain, which was partially offset by an increase in financing and interest expenses.

Research and Development Expenditures

Research and development expenses, net of expense recovery, for Fiscal 2010 were \$202,399, compared to \$586,597 for Fiscal 2009. The decrease in research and development expenditures was primarily due to the reduced research and development activities in Fiscal 2010. There was no new research and development study initiated since June 2008. The following provides a summary of the research and development expenditures by programs for the two most recent fiscal years and since inception:

Project	For the year ended March 31,		Cumulative from
	2010	2009	Inception to March 31, 2010
PAC-113			
Expense	\$84,472	\$1,154,902	\$5,553,618
Recovery	—	(865,287)	(865,287)
	84,472	289,615	4,688,331
PAC-G31P	120,496	272,306	2,220,099
Other Projects	(2,569)	24,676	193,177
	\$202,399	\$586,597	\$7,101,607

PAC-113

Development expenses, net of expense recovery, for Fiscal 2010 decreased by \$205,143, as compared to those incurred in Fiscal 2009. The reduced development expenditures were mainly due to our decision to defer further development of PAC-113 until a collaborative partner is secured and new funding is raised. We completed our Phase IIb clinical study in June 2008 and obtained favorable results from this clinical study. Using these results and other data we accumulated, we secured a collaborative partner, New Summit Bio, for the Chinese region. We are seeking for collaborative partners in North America regions.

The development expenditures in Fiscal 2010 include annual license fees, as well as expenditures associated with the continuation of stability studies and clinical trial insurance. The development expenditures in Fiscal 2009 include annual license fees, as well as expenditures associated with the completion of Phase IIb clinical trial and the continuation of stability studies and clinical trial insurance. In Fiscal 2009, as part of our financial settlement with a vendor, we recovered \$747,214 of the Phase IIb clinical trial expenditures. This expense recovery, together with the underlying accretion interest expense of \$118,073, reduced total expenditures for PAC-113 in Fiscal 2009 by \$865,287.

For the fiscal year ending March 31, 2011 (“Fiscal 2011”), we expect to incur research and development expenditures for PAC-113 through our collaborative partnership with New Summit Bio. New Summit Bio and Pacgen are currently focusing on fund raising activities in China are currently focusing on fund raising activities in China, and plan to schedule a meeting with the sFDA shortly after the completion of fund raising. Based on the analysis of New Summit Bio, we expect that certain bridging studies are required prior to initiation of a pivotal clinical trial in China. These bridging studies would include studies, at both the pre-clinical and clinical level, conducted in accordance with the standards of sFDA

PAC-G31P

Research expenditures for Fiscal 2010 decreased by \$151,810, as compared to those incurred in Fiscal 2009. We have not initiated any new research studies for this program since Fiscal 2008. Research expenditures in Fiscal 2010 were primarily related to patenting and balance of research commitment under license. Research expenditures in Fiscal 2009 were related continuation of certain research studies and patenting.

For Fiscal 2011, we expect to incur minimal research and development expenditures for PAC-G31P until a joint-venture partner is secured. Patenting related expenditures, which our licensor has agreed to finance as part of our settlement arrangement with them, will be the primarily the research expenditures expected in Fiscal 2011.

General and Administration Expenditures

General and administration expenditures for Fiscal 2010 were \$581,420, compared to \$999,832 for Fiscal 2009. The decrease of \$418,412 was primarily attributable to the implementation of our cost control programs. The following provides a summary of the general and administration expenditures for the two most recent fiscal years and since inception:

General and Administration Expenditures	For the year ended March 31,		Cumulative from
	2010	2009	Inception to March 31, 2010
Salaries and benefits	\$ —	\$307,808	\$2,440,714
Management fees	189,408	—	189,408
Consulting and professional fees	83,760	466,382	1,907,038
Travel and accommodation	54,198	48,202	391,606
Business development and market research	58,490	—	194,640
Other general overhead	195,564	177,440	1,484,814
	<u>\$581,420</u>	<u>\$999,832</u>	<u>\$6,608,220</u>

In comparative to the same line item in Fiscal 2009:

- Salaries and benefits declined by \$307,808 due to our arrangement to replace all full time employment positions with consultant positions. All consultant positions were compensated by stock based compensation in Fiscal 2010.
- Management fees in Fiscal 2010 were related to management services acquired through the Xphase Acquisition. The purchase price of Xphase was recorded as prepaid management fees and amortized over one-year service period starting April 1, 2009.
- Consulting and professional fees declined by \$382,621 in Fiscal 2010, mainly due to our cost cutting measures to internalize our business development activities. The decline in consulting and professional fees is also due to professional fees incurred for an abandoned merger in Fiscal 2009.
- Travel and accommodation expenses were relatively the same in both fiscal years.
- The business development and market research expenses in Fiscal 2010 were related to an extension fee paid to preserve a right to acquire certain intellectual properties, which we subsequently abandoned.
- The increased in other general overhead by \$18,124 primarily related to allocation of certain internal overhead from research and development to general administration due the change of our operational focus.

For Fiscal 2011, we expect our general and administration expenditures to be lower than those incurred in Fiscal 2010. Expenditures associated with the Xphase Acquisition and purchase right extension fees in Fiscal 2010 are non-recurring.

Stock-based Compensation

Stock-based compensation, a non-cash item included in operating expenses, reduced to \$146,053 in Fiscal 2010, compared to \$160,687 in Fiscal 2009. Stock-based compensation attributable to research and development operations and general administration for Fiscal 2010 was \$27,314 [2009 - \$62,391] and \$118,739 [2008 - \$98,296], respectively. The decrease in stock-based compensation was primarily due to the reduced number of options vested during Fiscal 2010 as compared to Fiscal 2009.

Amortization and Write-Downs

Amortization related to property and equipment for Fiscal 2010 reduced to \$22,118 from \$26,842 for Fiscal 2009. The decrease of \$4,424 was due to disposition of certain property and equipment in Fiscal 2009. Amortization related to technology, licenses and rights for Fiscal 2010 reduced to \$191,974 from \$236,974 for Fiscal 2009 for a difference of \$45,000 due to a write-down of intangible asset of \$244,408 in Fiscal 2010.

In Fiscal 2010, we recorded a write-down of \$244,408, the remaining net book value of PAC-G31P technology as a result of our impairment test of long-lived assets. In the same fiscal year, we also wrote off \$192,958 of advance paid to a vendor as a result of the uncertainty surrounding continuation of our planned research and development studies.

Other Loss

Other loss in Fiscal 2010 was \$43,985, compared to \$271,708 in Fiscal 2009. The decrease of \$227,723 in other loss was mainly due to the increased interest and other income by \$7,208 and increased foreign exchange gain by \$387,029 and decreased loss on disposal of property by \$6,520 in Fiscal 2010, as compared to those in Fiscal 2009. These credit balances were offset by increased financing and interest expenses by \$173,034 in Fiscal 2010, as compared to those in Fiscal 2009.

The increase in interest and other income was due to rental income we generated from subleasing part of our office facility. Foreign exchange gain increase was mainly due to the appreciation of the Canadian dollar, in comparison with the US dollar, on our US denominated other payable as well as accounts payable and accrued liabilities. The increase in financing and interest expenses in Fiscal 2010 was due to the accretions of interest of other payable and convertible debentures issued during Fiscal 2009.

SUMMARY OF QUARTERLY RESULTS

Set forth below is the selected consolidated financial data for each of the last eight quarters:

	4th Quarter Ended Mar 31, 2010 ("Q4 2010")	3rd Quarter Ended Dec 31, 2009 ("Q3 2010")	2nd Quarter Ended Sep 30, 2009 ("Q2 2010")	1st Quarter Ended Jun 30, 2009 ("Q1 2010")
Research and development, net of recovery	\$(131,102)	\$(19,675)	\$(14,916)	\$(36,706)
General and administration	(164,284)	(103,445)	(259,210)	(54,481)
Stock based compensation	(19,316)	(109)	(95,933)	(30,695)
Amortization and write-downs	(217,256)	(307,675)	(63,341)	(63,186)
Other income (loss)	17,127	(37,277)	100	(23,935)
Net loss for the period	(514,831)	(468,181)	(433,300)	(209,003)
Basic and diluted loss per common share	\$(0.03)	\$(0.02)	\$(0.02)	\$(0.01)

	4th Quarter Ended March 31, 2009 ("Q4 2009")	3rd Quarter Ended Dec 31, 2008 ("Q3 2009")	2nd Quarter Ended Sep 30, 2008 ("Q2 2009")	1st Quarter Ended Jun 30, 2008 ("Q1 2009")
Research and development, net of recovery	\$(87,804)	\$537,658	\$(155,264)	\$(881,187)
General and administration	(118,457)	(277,673)	(298,815)	(304,887)
Stock based compensation	40,879	(51,410)	(91,346)	(58,810)
Amortization and write-downs	(64,895)	(66,307)	(66,307)	(66,307)
Other income (loss)	(80,710)	(163,966)	(30,722)	3,690
Net loss for the period	(310,987)	(21,698)	(642,454)	(1,307,501)
Basic and diluted loss per common share	\$(0.02)	\$(0.00)	\$(0.04)	\$(0.07)

Summary of Quarterly Results

The primary factors affecting the magnitude of our losses in the various quarters were (i) the implementation of our cost control programs in different stages since Fiscal 2008 (ii) recovery of part of our Phase IIb clinical expenditures and an underlying accretion interest expense in Fiscal 2009, and (iii) expenditures associated with our PAC-113 Phase I/II and Phase IIb clinical trials in Fiscal 2009.

Research and development expenditures were maintained at relatively the same level throughout Fiscal 2010, except Q4 2010 when we recorded the remaining research commitments of \$100,000 under our license agreement with the University of Saskatchewan. Research and development expenditures were primarily related to patenting, license maintenance and continuation of stability studies and clinical insurance. There was no new research and development study initiated since June 2008. General and administration expenditures were higher in Q2 2010, as compared to Q1 2010, primarily due to (i) inclusion of six-month amortization of management fees of \$94,704 following the completion of the Xphase Acquisition in June 2009 and (ii) an extension fee of \$58,490 paid to preserve a right to acquire certain intellectual properties, which we subsequently abandoned. Stock based compensation was higher in Q2 2010 due to the 1.9 million options grant to management consultants, including Xphase principals, to support our ongoing operations. These options were vested immediately upon grant. The increased amortization and write-downs in Q3 2010 was due to the write-down of \$244,408, the remaining net book value of PAC-G31P technology as a result of our impairment test of long-lived assets. The increased amortization and write-downs in Q4 2010 was due a wrote-off of \$192,958 of advance paid to a vendor as a result of the uncertainty surrounding continuation of our planned research and development studies.

Research and development expenditures were in a declining trend throughout Fiscal 2009 as a result of (i) our decision to focus our development efforts primarily on the completion of PAC-113 Phase IIb clinical study and to scale down of PAC-G31P research and development activities (ii) further reduction in research and development activities following the completion of the Phase IIb study in June 2008, and (iii) a recovery of \$747,214 (approximately US\$604,000) of expenditure associated with PAC-113 Phase IIb in the second half of 2009 and an underlying accretion of interest of \$118,073. General and administration expenditures were also in a declining trend as a result of our cost control programs. The cost control programs in Fiscal 2009 involved (i) replacement of five full-time positions with two consultant positions (ii) appointment of Chairman of our board of directors to act as our interim President and Chief Executive Officer, and (iii) elimination of all director fees effective February 2008.

FOURTH QUARTER RESULTS

	4th Quarter Ended	4th Quarter Ended
	Mar 31, 2010	March 31, 2009
Research and development, net of recovery	\$(131,102)	\$(87,804)
General and administration	(164,284)	(118,457)
Stock based compensation	(19,316)	40,879
Amortization and write-downs	(217,256)	(64,895)
Other income (loss)	17,127	(80,710)
Net loss for the period	(514,831)	(310,987)
Basic and diluted loss per common share	\$(0.03)	\$(0.02)

The increase of 203,844 in net loss was primarily due to increases in operating expenses of \$301,681 in Q4 2010, as compared to those in Q3 2009. The increased operating expenses were offset by an increase of \$97,837 in other income.

The increase in research and development expenses by \$43,298 was primarily due to the recognition of the remaining research commitments of \$100,000 under our license agreement with the University of Saskatchewan. There was no new research and development study initiated since June 2008. Further development on PAC-113 and PAC-G31P would be subject to funding from existing partner or new partners.

The increase in general and administration expenses by \$45,827 was primarily attributable to the quarterly amortization of management fees of \$47,352 from the Xphase Acquisition. Stock based compensation increased by \$60,195 due to year-end adjustments to fair value estimates for options granted to consultants in Fiscal 2009.

The increase in amortization and write-downs by \$152,361 was primarily due to the \$192,958 write-off of advance paid to a vendor, as a result of the uncertainty surrounding continuation of our planned research and development studies. This increase was offset by a decrease in amortization of intangible assets due to a write down of net book value of PAC-G31P technology in Q3 2010.

Other income increased by \$97,837 mainly due to increase in foreign exchange gain as a result of appreciation of the Canadian dollar, in comparison with the US dollar, on our US denominated other payable as well as accounts payable and accrued liabilities. The increase in foreign exchange gain was offset by a reduction in accretion expenses of other payable and convertible debentures due to maturities of some of these financial instruments.

LIQUIDITY AND CAPITAL RESOURCES

Sources and Uses of Cash

Since inception, our operational activities were financed mainly from equity financings, other than issuance of convertible debentures in Fiscal 2009 and the cash acquired from IL Therapeutics Inc. in fiscal year ended March 31, 2007.

Cash used in operating activities for Fiscal 2010 was \$258,376, compared to \$1,752,558 for Fiscal 2009. Cash used in operating activities was comprised of net loss, add-backs or adjustments not involving cash and net change in non-cash working capital items. The decrease of \$1,494,182 in cash used in operating activities in Fiscal 2010, as compared to Fiscal 2009, was primarily due to a decline in operating expenses requiring cash and the delay of payments to trade accounts. Cash used in investing activities in Fiscal 2010 was \$22,654, compared to \$3,775 in Fiscal 2008. The increase of cash used in investing activities was primarily due to cash used in connection to the Xphase Acquisition.

Cash used in financing activities in Fiscal 2010 was \$19,581, compared to \$614,500 cash provided by financing activities in Fiscal 2009. Cash used in financing activities in Fiscal 2010 was associated with the Financing of \$600,000 of Subscription Receipts closed in May 2010. Cash provided by financing activities in Fiscal 2009 was from our private placement financing of convertible debentures.

As of March 31, 2010, we had a working capital deficiency of \$2,112,280 (March 31, 2009 - \$1,023,213). Given the working capital deficiency and our contractual obligations as of March 31, 2010, there is a risk that we may not be able to meet our financial obligations and sustain our operations over the next year without raising new capital and a financial restructuring.

Subsequent to Fiscal 2010, we closed the Financing of \$600,000 of Subscription Receipts in May 2010. Of the Subscription Receipts, \$300,000 was collected in our trust account and recorded as restricted cash as of March 31, 2010. In connection to this Financing, we initiated the Financial Restructuring and agreed to seek shareholder approval for the Share Consolidation. Under the Financing, we issued an aggregate of 10 million Subscription Receipts at a price of \$0.06 per Subscription Receipt for gross proceeds of \$600,000. On June 8, 2010, following the completion of the Share Consolidation, all Subscriptions Receipts were automatically converted into 10,000,001 common shares.

As of the date of this MD&A, we have completed substantially all of our negotiations with our creditors. The Financial Restructuring involves restructuring of approximately \$2.3 million of indebtedness and commitments as detailed in *note 21* to our audited consolidated financial statements for Fiscal 2010 and summarized in the following table:

	Indebtedness on Date of Settlement	Form of Settlements			
		Common Shares	Cash	Cash Discounts or Credits	Other
		\$	\$	\$	\$
Convertible debentures ^[ii]	658,289	658,289	—	—	—
Other payable ^[iii]	597,568	—	203,160	394,408	—
Demegen Sub-license ^[iv]	179,796	157,327	22,469	—	—
US License ^[v]	292,104	—	—	—	292,104
Other liabilities ^[vi]	562,730	69,281	145,550	255,043	92,856
	2,290,487	884,897	371,179	649,451	384,960

[i] All US denominated amounts were converted into Canadian Dollars at the closing rate on March 31, 2010 of CAD\$1.00 = US\$0.9844.

[ii] On June 8, 2010, we issued 10,971,485 common shares at price of \$0.06 per share to settle these debentures

[iii] On July 7, 2010, we issued a payment of US\$200,000 (\$203,160) to settle our indebtedness with this creditor.

[iv] On June 8, 2010, we issued a payment of US\$22,120 (\$22,469) and 700,000 common shares at an average price of \$0.22 per share to settle our indebtedness and certain upcoming license commitments with Demegen, Inc for our PAC-113 license.

[v] In June 2010, we completed our negotiation with the University of Saskatchewan (the "University"), our licensor for PAC-G31 technology. The parties agreed that the University will be entitled to up to 20% of new capital raised by our subsidiary, IL Therapeutics Inc. and that the indebtedness plus interest shall be repaid in full by June 30, 2012.

[vi] The aggregate amount of indebtedness to other creditors was settled in various arrangements we entered into or agreed to subsequent to Fiscal 2010, as detailed in *note 21 [b][v]* to our consolidated financial statements.

We expect to use up to \$400,000 of the net proceeds from the Financing to settle its obligations from the Financial Restructuring. We estimate that the remaining net proceeds should be sufficient to finance our core business operations and financial obligations over the next fiscal year.

Contractual Obligations

As of March 31, 2010 and in the normal course of business we have obligations to make future payments, representing contracts and other commitments that are known, committed and non-cancellable.

	Contractual Obligations Payment Due by Period				
	Total	2011	2012-2013	2014-2015	Thereafter
Operating leases	\$50,131	\$50,131	—	—	—
License agreements ⁽¹⁾	304,740	50,790	101,580	101,580	50,790
Total	\$354,871	\$100,921	\$101,580	\$101,580	\$50,790

⁽¹⁾ Pursuant to the Demegen Sublicense, we have a commitment to pay minimum annual royalties of US\$50,000 as described in *note 16[c]* of our annual consolidated financial statements for Fiscal 2010. This commitment is converted into Canadian Dollars at the closing rate on March 31, 2010 of CAD\$1.00 = US\$0.9844. On June 8, 2010, we issued 150,000 common shares as payment for US\$20,000 (\$20,316) of the minimum annual royalties for Fiscal 2011.

Capital Risk Management

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

We include convertible debentures and equity comprised of issued share capital, contributed surplus and deficit in the definition of capital. Other than the issuance of convertible debentures in Fiscal 2009, we have financed our capital requirements primarily through share issuances since inception.

We manage our capital structure and make adjustments to it in light of changes in economic conditions and risk characteristics of the underlying assets. We may issue new shares or raise debt. We are not subject to any externally imposed capital requirements and the overall strategy with respect to capital management remains unchanged from the preceding fiscal year.

OUTSTANDING SHARE CAPITAL

As of July 19, 2010, there were 41,690,490 common shares issued and outstanding, 2,311,367 common share purchase warrants outstanding at a weighted average exercise price of \$0.60 per common share, and 1,480,000 incentive stock options outstanding at a weighted average exercise price of \$0.88.

OFF-BALANCE SHEET ARRANGEMENTS

We have no off-balance sheet arrangements.

FINANCIAL INSTRUMENTS

Our financial instruments consist of the following:

	March 31, 2010 \$	March 31, 2009 \$
<i>Financial assets</i>		
Cash and cash equivalents, measured at fair value	6,065	308,871
Restricted cash, measured at fair value	314,295	—
Amounts receivable, measured at amortized cost	2,277	15,155
<i>Financial Liabilities</i>		
Accounts payable and accrued liabilities, measured at amortized cost	933,320	911,688
Other payable, measured at amortized cost	589,164	625,423
Convertible debentures, measured at amortized cost	613,063	531,831
Subscription receipts, measured at amortized cost	300,000	—

Cash and equivalents and restricted cash are classified as held for trading. Amounts receivable are classified as loan and receivable. Accounts payable and accrued liabilities, subscription receipts, convertible debentures and other payable are classified as other financial liabilities.

Credit risk

Credit risk is the risk of a financial loss to us if counterparty to a financial instrument of ours fails to meet its contractual obligations. Credit risk arises from our cash on deposits with banks, and from time to time due to its holdings of short term investments. The carrying value of our cash and cash equivalents, restricted cash and accounts receivable is our maximum credit exposure at March 31, 2010. We have investment policies to mitigate against credit risks, and hold our cash balances with major banks in Canada. The restricted cash is cash balances held in trust accounts with major banks in Canada that is either subject to certain release conditions or the closing of a financing. Amounts receivable primarily consist of good and services tax due from the federal government of Canada.

Liquidity risk

Liquidity risk is the risk that we will not be able to meet our obligations as they come due. Our exposure to liquidity risk is dependent on our purchasing commitments and obligations and our ability to raise funds to meet commitments and sustain operations. We manage liquidity risk by continuously monitoring its actual and forecasted working capital requirements, and actively managing its financing activities. A discussion on our liquidity is provided in “*Liquidity and Capital Resources*” section of this MD&A.

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. We are exposed to interest rate risk on our convertible debentures and other payables which bear floating interest rates.

Currency risk

We are exposed to the financial risk related to the fluctuation of foreign exchanges rates. We operate primarily within Canada although a portion of our expenses are incurred in United States dollars (“US dollar”). We have 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 our results of operations, financial position or cash flows.

RELATED PARTY TRANSACTIONS

We incurred \$503 for consulting services provided by directors in the preceding fiscal year. These transactions were incurred in the normal course of business and recorded at their exchange amounts. As of March 31, 2010, we had the following amounts due to related parties:

	March 31, 2010 \$	March 31, 2009 \$
Accounts payable to directors, officers, or contract managers in connection to business expense reimbursements	49,786	1,666
Interest payable	27,277	2,467
Debentures held by officers or directors ⁽¹⁾	386,333	243,000
	<u>463,396</u>	<u>247,133</u>

⁽¹⁾ During the year ended March 31, 2010, two debenture holders, who hold convertible debentures of \$143,333, were appointed to be our director or officer.

CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT ESTIMATES

Our audited consolidated financial statements are prepared in accordance with Canadian GAAP. These accounting principles require us to make certain estimates and assumptions. We believe that the estimates and assumptions upon which we rely are reasonable based upon information available at the time that these estimates and assumptions are made. Actual results could differ from these estimates. 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, estimation of future income tax and determination of fair value of stock-based compensation. The significant accounting policies that we believe are the most critical in fully understanding and evaluating the reported financial results include the following:

Intangible Assets

Intangible assets are comprised of 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 lives of the underlying technologies. We determine the estimated useful lives for intangible assets based on a number of factors: legal, regulatory or contractual limitations; known technological advances; anticipated market size; and the existence or absence of competition. A significant change in any of the above factors may require a revision of the expected useful life of the intangible asset, resulting in accelerated amortization or an impairment charge, which could have a material impact on our results of operations. We evaluate the recoverability of the net book value of our intangible assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. If the carrying value of the underlying technology exceeds the estimated net recoverable value, calculated based on estimated undiscounted future cash flows, then the carrying value is written down to its fair value, based on the related estimated discounted cash flows. The amounts shown for technology licenses and rights do not necessarily reflect present or future values and the ultimate amount recoverable will be dependent upon the successful development and commercialization of products based on these rights.

Stock-based Compensation and Other Stock-based Payments

We grant stock options to employees, directors, and consultants pursuant to a stock option plan. We use 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. 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 earliest of the performance commitment date, service delivery date, or the grant date if they are fully vested and non-forfeitable.

The estimation of the fair value of stock options using the Black-Scholes option pricing model involves subjective assumptions of the expected life of the option, the expected volatility at the time the options are granted, and the risk-free interest rate. Changes in these assumptions can materially affect the measurement of the estimated fair value of our stock options, hence our results of operations.

CHANGE OF ACCOUNTING POLICIES

Effective April 1, 2009, we adopted CICA issued Section 3064, “Goodwill and Intangible Assets”, which replaces Section 3062, “Goodwill and Other Intangible Assets” and Section 3450, “Research and Development Costs”. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The adoption of these new standards did not have a material impact on our consolidated financial statements.

Effective April 1, 2009, we adopted CICA Emerging Issues Committee Abstract 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 be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This guidance is applicable to our financial periods ending on or after January 20, 2009 with retrospective application without restatement of prior periods. The adoption of these new standards did not have a material impact on our consolidated financial statement.

Effective March 31, 2010, we adopted amendments to CICA Section 3862, “Financial Instruments - Disclosures”. These amendments include enhanced disclosures relating to the fair value of financial instruments and the liquidity risk associated with financial instruments. Section 3862 now requires that all financial instruments measured at fair value be categorized into one of the three hierarchy levels as follows:

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

The new disclosure requirements pertaining to this section are contained in note 5 of these consolidated financial statements.

Amendments to CICA Section 3855 “Financial Instruments – Recognition and Measurement” were made to converge with international standards for impairment of debt instruments by changing the categories into which debt instruments are required or permitted to be classified. The adoption of these new standards did not have material impact on our consolidated financial statement.

FUTURE ACCOUNTING STANDARDS

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 our interim and annual financial statements beginning on January 1, 2011. We are in the process of evaluating the impact of these standards.

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 our interim and annual financial statements of the Company beginning on or January 1, 2011, with early adoption permitted. We are in the process of evaluating the impact of this standard.

In February 2008, the Canadian Accounting Standards Board (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. The Company will be required to report using IFRS commencing with its unaudited financial statements for the three months ended June 30, 2011, which must include the interim results for the three months ended June 20, 2010 prepared on the same basis. IFRS uses a conceptual framework similar to Canadian GAAP, but there are some significant differences on recognition, measurement and disclosures.

In fiscal year ending March 31, 2011, we plan to complete the process to transition to IFRS from the current Canadian GAAP. The first phase consists of an analysis of the impact of IFRS on Canadian GAAP as they apply to the Company. This analysis will take into account any potential impact on our current accounting policies, financial disclosures, information systems, internal control systems and on its business activities. An assessment of related training requirements will also be required. At this time, we are unable to indicate the consequences of this transition on our operations and our consolidated financial statements.

RISKS AND UNCERTAINTIES

Due to the inherent nature of our business, investing in our securities involves a high degree of risk and uncertainties. Such risk factors include, among others, our stage of development, lack of product revenues, additional capital requirements, risk associated with completion of clinical trials and obtaining regulatory approval, reliance on our collaborative partner, New Summit Bio, to raise funding for PAC-113 development for the Chinese market, dependence on lack of collaborative partners for PAC-113 regions outside of China, lack of collaborative partners for PAC-G31P at this time, dependence on collaborative partners to develop and commercialize our products, our ability to protect our intellectual property and our ability to stay competitive in a rapid changing industry environment.

We are in the early stage of development and have limited operating history. We have not generated any revenues to date from product sales, nor do we expect any product revenues for the immediate future. To achieve profitable operations, we must successfully develop our products that are currently in the research and development phase with collaborative partners. These product developments may take a number of years and involve significant risks and uncertainties. As a result, substantial capital is required to finance our product developments through collaborative partnerships.

The global economic crisis in recent years has led to a substantial reduction in capital in the credit markets, especially for companies in the development stage like Pacgen. This economic market environment has also affected our ability to secure collaborative partnerships that provide upfront licensing revenue or immediate funding for product developments. We are currently working with New Summit Bio to raise funding for PAC-113 development in China. We are also seeking collaborative partners for PAC-113 regions outside of China and a joint-venture partner to conduct certain preclinical studies to add data to our PAC-G31P package for out-licensing purposes. There can be no assurance that these partnership objectives can be met on a timely basis, or at all.

Despite the completion of our recent financing and financial restructuring, we have limited working capital on hand. We estimate that our current working capital would be sufficient to cover our core business operations and financial obligations over the fiscal year ending March 31, 2011. However, our funding requirements may change. We may be required to arrange financing earlier than expected. There can be no assurance that such financing will be available on favorable terms, if at all. If we are unable to obtain additional financing, we may be required to curtail or discontinue our operations.

We are also subject to other significant risks and uncertainties listed in the section entitled "Risk Factors" in our Annual Information Form dated July 31, 2008.

Consolidated Financial Statements

Pacgen Biopharmaceuticals Corporation

(a development stage enterprise)

(Expressed in Canadian dollars)

March 31, 2010 and 2009

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, 2010 and 2009, and the consolidated statements of operations and comprehensive loss and cash flows for the years then ended and for the period from April 23, 2004 [inception] to March 31, 2010, and the consolidated statements of shareholders' deficiency for the years ended March 31, 2010 and 2009. These consolidated financial statements are the responsibility of the Company's management. 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 plan and perform an 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 financial position of the Company as at March 31, 2010 and 2009 and the 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, 2010 in accordance with Canadian generally accepted accounting principles.

Ernst & Young LLP

Vancouver, Canada,
July 23, 2010.

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, 2010	March 31, 2009
	\$	\$
ASSETS		
Current		
Cash and cash equivalents <i>[note 7]</i>	6,065	308,871
Restricted cash <i>[note 8]</i>	314,295	—
Amounts receivable	2,277	15,155
Prepaid expenses and other <i>[note 9]</i>	4,088	515,619
Total current assets	326,725	839,645
Deferred acquisition costs	—	3,775
Deferred financing costs	5,286	—
Property and equipment <i>[note 11]</i>	47,069	67,874
Intangible assets <i>[note 12]</i>	328,847	765,229
Total assets	707,927	1,676,523
LIABILITIES AND SHAREHOLDERS' DEFICIENCY		
Current		
Accounts payable and accrued liabilities	933,320	911,688
Other payable <i>[note 13]</i>	589,164	625,423
Convertible debentures <i>[note 14]</i>	613,063	318,831
Subscription receipts <i>[note 21[a]]</i>	300,000	—
Current portion of deferred leasehold inducement	3,458	6,916
	2,439,005	1,862,858
Convertible debentures <i>[note 14]</i>	—	213,000
Deferred leasehold inducement	—	3,459
Total liabilities	2,439,005	2,079,317
Commitments and contingencies <i>[notes 16 and 17]</i>		
Shareholders' deficiency		
Share capital <i>[note 15]</i>		
Issued and outstanding:		
Common shares <i>[note 15[a]]</i>	13,162,118	13,012,118
Preferred shares <i>[note 15[b]]</i>	—	—
Contributed surplus <i>[notes 14 and 15[e]]</i>	1,562,440	1,415,409
Deficit	(16,455,636)	(14,830,321)
Total shareholders' deficiency	(1,731,078)	(402,794)
Total liabilities and shareholders' deficiency	707,927	1,676,523

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, 2010 \$	Year ended March 31, 2009 \$	Cumulative from Inception to March 31, 2010 \$
EXPENSES			
Research and development <i>[note 6]</i>	202,399	1,451,884	7,966,894
Research and development expense recovery <i>[notes 6 and 13]</i>	—	(865,287)	(865,287)
	202,399	586,597	7,101,607
General and administration	581,420	999,832	6,608,220
Stock based compensation <i>[note 15[e]]</i>	146,053	160,687	1,233,913
Amortization of property and equipment <i>[note 11]</i>	22,118	26,842	107,515
Amortization of intangible assets <i>[note 12]</i>	191,974	236,974	903,896
Write-down of intangible assets <i>[note 12[b]]</i>	244,408	—	244,408
Write-off of prepaid expenses and other <i>[note 21[b][v](b)]</i>	192,958	—	216,325
	1,581,330	2,010,932	16,415,884
OTHER			
Interest and other income	46,331	39,123	315,808
Financing and interest expenses	(225,616)	(52,582)	(278,198)
Loss on disposal of property and equipment	—	(6,520)	(15,609)
Foreign exchange gain (losses)	135,300	(251,729)	(299,753)
	(43,985)	(271,708)	(277,752)
Loss before income taxes	(1,625,315)	(2,282,640)	(16,693,636)
Future income tax recovery	—	—	238,000
Net loss and comprehensive loss	(1,625,315)	(2,282,640)	(16,455,636)
Basic and diluted loss per common share <i>[note 15]</i>	(0.09)	(0.13)	
Weighted average number of common shares outstanding <i>[note 15]</i>	18,529,881	17,572,235	

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

CONSOLIDATED STATEMENTS OF CASH FLOWS

(expressed in Canadian dollars)

	Year ended March 31, 2010 \$	Year ended March 31, 2009 \$	Cumulative from Inception to March 31, 2010 \$
OPERATING ACTIVITIES			
Loss for the period	(1,625,315)	(2,282,640)	(16,455,636)
Add items not affecting cash:			
Accretion of convertible debentures	82,211	8,277	90,488
Accretion of other payable	93,126	9,675	102,801
Amortization of property and equipment	22,118	26,842	107,515
Amortization of intangible assets	191,974	236,974	903,896
Deferred leasehold inducement	(6,917)	(6,916)	(14,986)
Future income tax recovery	—	—	(238,000)
Loss on disposal of property and equipment	—	6,520	15,609
Management fees paid by equity	189,408	—	189,408
Stock based compensation	146,053	160,687	1,233,913
Unrealized foreign exchange (gain) loss	(128,660)	202,921	162,197
Write-off of prepaid expenses and other	192,958	—	216,325
Write-down of intangible assets	244,408	—	244,408
	(598,636)	(1,637,660)	(13,442,062)
Changes in non-cash working capital items relating to operations:			
Amounts receivable	13,001	(2,355)	141,340
Prepaid expenses and other	229,326	48,428	(297,307)
Accounts payable and accrued liabilities	97,933	(788,951)	661,723
Other payable	—	627,980	627,980
Cash used in operating activities	(258,376)	(1,752,558)	(12,308,326)
INVESTING ACTIVITIES			
Acquisition of assets	(21,341)	(3,775)	1,211,973
Proceeds from disposal of property and equipment	—	—	5,775
Purchase of property and equipment	(1,313)	—	(180,516)
Purchase of intangible assets	—	—	(59,743)
Leasehold inducement	—	—	18,444
Cash provided by (used in) investing activities	(22,654)	(3,775)	995,933
FINANCING ACTIVITIES			
Issuance of common shares for cash, net of share issuance costs	—	—	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
Restricted cash	(314,295)	—	(314,296)
Subscription receipts	300,000	—	300,000
Deferred financing costs	(5,286)	—	(5,286)
Advance from related party	—	—	694,836
Cash provided by (used in) financing activities	(19,581)	614,500	11,308,640
Decrease in cash and cash equivalents	(300,611)	(1,141,833)	(3,753)
Effect on foreign exchange rate changes	(2,195)	12,013	9,818
Cash and cash equivalents, beginning of period	308,871	1,438,691	—
Cash and cash equivalents, end of period	6,065	308,871	6,065
Other supplemental cash flow information			
Common shares and preferred shares issued for technology	—	—	2,480,000
Common shares and preferred shares issued as financing cost	—	—	204,090
Common shares issued to acquire assets and services [note 10]	189,408	—	189,408
Common shares issued to settle related party advance	—	—	718,836

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

**CONSOLIDATED STATEMENTS
OF SHAREHOLDERS' DEFICIENCY**

(expressed in Canadian dollars)

	Common Shares <i>[note 15]</i>		Preferred Shares		Contributed Surplus	Deficit	Total
	Number	Amount \$	Number	Amount \$	\$	\$	\$
Balance, March 31, 2008	17,572,347	13,012,118	—	—	1,163,776	(12,547,681)	1,628,213
Equity component of a private placement of convertible debentures <i>[note 11]</i>	—	—	—	—	90,946	—	90,946
Stock based compensation <i>[note 15[e]]</i>	—	—	—	—	160,687	—	160,687
Net loss	—	—	—	—	—	(2,282,640)	(2,282,640)
Balance, March 31, 2009	17,572,347	13,012,118	—	—	1,415,409	(14,830,321)	(402,794)
Shares issued to acquire assets <i>[note 10]</i>	1,500,000	150,000	—	—	—	—	150,000
Equity component of a private placement of convertible debentures <i>[note 14]</i>	—	—	—	—	978	—	978
Stock based compensation <i>[note 15[e]]</i>	—	—	—	—	146,053	—	146,053
Net loss	—	—	—	—	—	(1,625,315)	(1,625,315)
Balance, March 31, 2010	19,072,347	13,162,118	—	—	1,562,440	(16,455,636)	(1,731,078)

See accompanying notes

Pacgen Biopharmaceuticals Corporation
(a development stage enterprise)

**NOTES TO CONSOLIDATED
FINANCIAL STATEMENTS**

March 31, 2010 and 2009

(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 with 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, 2010, the Company has not generated any revenue from its operations and has accumulated a deficit of \$16,455,636. Therefore, the Company is considered to be in the development stage. Given its working capital deficiency as of March 31, 2010 of \$2,112,280 (2009 - \$1,023,213), the Company may not be able to meet its financial obligations and sustain its operations over the next year in the normal course, all of which cast substantial doubt about the Company’s ability to continue as a going concern without raising new capital and a financial restructuring. The Company has funded its operations primarily by share issuances. The Company’s ability to continue as a going concern is dependent upon its ability to obtain additional financing. 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 global economic crisis in recent years has led to a substantial reduction in capital in the credit markets, especially for companies in the development stage. Smaller life science technology companies, which are generally viewed as higher risk investments, continue to encounter difficulty in raising new capital. During the year ended March 31, 2009, the Company took cost cutting measures, deferred all major research and development of its drug candidates, closed a convertible debenture financing of \$610,000 [note 14], and negotiated with its major vendor to reduce its liabilities [note 13]. During the year ended March 31, 2010, the Company signed a share purchase agreement with the shareholders of Xphase Pharmaceuticals Inc. (“Xphase”) to acquire Xphase primarily for management services of Xphase principals and the right to acquire certain intellectual properties [note 10]. The Company also entered into agreements with New Summit Biopharma Co. to raise funding and develop PAC-113, one of the drug candidates of the Company, for the market in China. Subsequent to March 31, 2010, the Company completed a private placement financing of \$600,000, initiated a financial restructuring to further reduce its indebtedness, and effected a share consolidation of its common shares on the basis of one post-consolidation common share for every two pre-consolidation common shares [note 21].

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

The Company expects to use up to \$400,000 of the net proceeds from its financing completed in June 2010, to settle its obligations the financial restructuring. The Company estimates that the remaining net proceeds should be sufficient to finance its core business operations and financial obligations over the next fiscal year. The Company plans to continue to seek additional collaborative partners to finance and develop its drug candidates.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") 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 subsidiaries, IL Therapeutics Inc. incorporated in Canada under the Canada Business Corporations Act and Xphase Pharmaceuticals Inc. incorporated under the Business Corporations Act (Ontario). 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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2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

[d] Cash and cash equivalents

Cash and cash equivalents consist of unrestricted cash balances in bank accounts and highly liquid financial instruments with a maturity at the date of purchase of 90 days or less. Cash and cash equivalents are classified as held for trading and carried at fair values.

[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.

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. The impairment test conducted during the fiscal year ended March 31, 2010 resulted in the write-off of one of the intangible assets of the Company [note 12].

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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. In the fiscal year ended March 31, 2010, the Company recorded a write-off of an advance paid to a third party as a result of the uncertainty surrounding the continuation of its planned research and development studies in the region [note 9].

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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 tax 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 15[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 earliest of the performance commitment date, the service delivery date, or the grant date if they are fully vested and non-forfeitable.

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2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

[n] Financial instruments

The Company classifies its financial instruments into one of the following categories: held-to-maturity investments, available-for-sale financial assets, held-for-trading financial assets and liabilities, loans and receivables and other financial liabilities. Financial instruments are measured at fair value on initial recognition. After initial recognition, financial instruments are measured at their fair values, except for financial assets classified as held-to-maturity or loans and receivables and other financial liabilities which are measured at cost or amortized cost using the effective interest method.

The Company's financial instruments consist of cash and cash equivalents, restricted cash, amounts receivable, accounts payable and accrued liabilities, other payable, convertible debentures and subscription receipts. The following is a summary of the classification and measurement method the Company has applied to apply to each of its significant financial instruments:

Financial Instruments	Classification	Subsequent Measurement
Cash and cash equivalents	Held-for-trading	Fair value
Restricted cash	Held-for-trading	Fair value
Amounts receivable	Loan 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
Subscription receipts	Other financial liabilities	Amortized cost using the effective interest method

Net gains or losses for other financial liabilities at on initial recognition were recognized in the statement of operations. Transaction costs associated with the convertible debentures are charged as expense.

The Company's financial instruments are exposed to certain financial risks, including credit risk, liquidity risk, interest rate risk, and currency risk, disclosed in *note 5* of these consolidated financial statements.

[o] 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 effects of outstanding warrants and options disclosed in *note 15* are anti-dilutive for all periods presented.

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

[a] Goodwill and Intangible Assets

Effective April 1, 2009, the Company adopted CICA Section 3064, "*Goodwill and Intangible Assets*", which replaces Section 3062, "*Goodwill and Other Intangible Assets*" and Section 3450, "*Research and Development Costs*". Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets. The adoption of these new standards did not have a material impact on the Company's consolidated financial statements.

[b] Credit Risk and Fair Value of Financial Assets and Financial Liabilities

Effective April 1, 2009, the Company adopted the CICA issued Emerging Issues Committee Abstract 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 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 financial periods ending on or after January 20, 2009 with retrospective application without restatement of prior periods. The adoption of these new standards did not have a material impact on the Company's consolidated financial statement.

[c] Financial Instruments – Disclosures

Effective March 31, 2010, the Company adopted amendments to CICA Section 3862, "*Financial Instruments - Disclosures*". These amendments include enhanced disclosures relating to the fair value of financial instruments and the liquidity risk associated with financial instruments. Section 3862 now requires that all financial instruments measured at fair value be categorized into one of the three hierarchy levels as follows:

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

The new disclosure requirements pertaining to this section are contained in *note 5* of these consolidated financial statements.

[d] Financial Instruments – Recognition and Measurement

Amendments to CICA Section 3855 "*Financial Instruments – Recognition and Measurement*" were made to converge with international standards for impairment of debt instruments by changing the categories into which debt instruments are required or permitted to be classified. The adoption of these new standards did not have material impact on the Company's consolidated financial statement.

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3. CHANGES IN ACCOUNTING POLICIES

[e] New Accounting Pronouncements

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.

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 interim and annual 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 March 2009, the Canadian Accounting Standards Board (the “AcSB”) reconfirmed that Canadian public companies must change over to International Financial Reporting Standards (“IFRS”) for accounting periods commencing on or after January 1, 2011. The Company will be required to report using IFRS commencing with its unaudited interim financial statements for the three months ending June 30, 2011, which must include the interim results for the three months ending June 30, 2010 prepared on the same basis. IFRS uses a conceptual framework similar to Canadian GAAP, but there are some significant differences on recognition, measurement and disclosures.

In fiscal year ending March 31, 2011, the Company plans to complete the process to transition to IFRS from the current Canadian GAAP. The first phase consists of an analysis of the impact of IFRS on Canadian GAAP as they apply to the Company. This analysis will take into account any potential impact on the Company’s current accounting policies, financial disclosures, information systems, internal control systems and on its business activities. An assessment of related training requirements will also be required. At this time, the impact on the Company’s operations and its consolidated financial statements has not yet been determined.

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4. CAPITAL DISCLOSURES

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 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, 2009.

5. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments consist of cash and cash equivalents, restricted cash, amounts receivable, accounts payable and accrued liabilities, other payable, convertible debentures and subscription receipts. The Company has applied to each of its significant financial instruments, the classification and measurement method detailed in *note 2 [n]*. The amount of total gains on financial instruments is \$Nil and \$118,074 on other payable for the years ended March 31, 2010 and 2009, respectively, presented as research and development expense recovery on the statement of operations.

The Company is exposed to credit risk, liquidity risk and market risks including interest rate risk and currency risk detailed herein.

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5. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)

[a] Fair values

The fair values of the Company's amounts receivable, accounts payable and accrued liabilities and subscription receipts, approximates their carrying amounts due to their immediate or short-term maturity.

The financial instruments recorded at fair value on balance sheet are cash and cash equivalents, and restricted cash. These have been categorized into one of the three categories, based on a fair value hierarchy in accordance with CICA Handbook Section 3862.

Financial Instruments	Fair Value Measurement Using			March 31,
	Level 1	Level 2	Level 3	2010
	\$	\$	\$	\$
<u>Financial assets</u>				
Cash and cash equivalents	6,065	—	—	6,065
Restricted cash	314,295	—	—	314,295
	320,360	—	—	320,360

[b] 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. Credit risk arises for the Company from cash on deposits with banks, and from time to time due to its holdings of short term investments. 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.

The maximum credit exposure of the Company at period end is the carrying value of its cash and cash equivalents, restricted cash and accounts receivable. The Company held its cash balances with major banks in Canada and had no short term investment at March 31, 2010. The restricted cash is cash balances held in trust accounts with major banks in Canada that is either subject to certain release conditions or the closing of a financing. Amounts receivable primarily consist of goods and services tax due from the federal government of Canada.

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5. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (cont'd)

[c] 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 its purchasing commitments and obligations and its ability to raise 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, 2010, the Company had a working capital deficiency of \$2,112,280 (March 31, 2009 - \$1,023,213) and the following financial commitments:

	Contractual Obligations Payment Due by Period				
	Total	2011	2012-2013	2014-2015	Thereafter
Operating Leases <i>[note 16[a]]</i> :	\$50,131	\$50,131	—	—	—
License Agreements <i>[note 16 [c]]</i> :	304,740	50,790	101,580	101,580	50,790
Total	\$354,871	\$100,921	\$101,580	\$101,580	\$50,790

Given the working capital deficiency and financial commitments as of March 31, 2010, there is a risk that the Company may not be able to meet its financial obligations and sustain its operations without raising new capital and a financial restructuring.

Subsequent to the fiscal year ended March 31, 2010, the Company completed the Financing of \$600,000 *[note 21[a]]* and the Financial Restructuring to further reduce its indebtedness *[note 21[b]]*. The Company expects to use up to \$400,000 of the net proceeds from the Financing to settle its obligations from the Financial Restructuring. The Company estimates that the remaining net proceeds should be sufficient to finance its core business operations and financial obligations over the next fiscal year. The Company plans to continue to seek additional collaborative partners to finance and develop its drug candidates.

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5. FINANCIAL INSTRUMENTS (cont'd.)

[d] Market risk

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 years ended March 31, 2010 and 2009 by \$6,983 and \$569, respectively. An opposite impact would have occurred to net loss and cash used in operations had interest rate decreased by one percent. The Company does not use derivative instruments to reduce its exposure to interest rate risk.

Given the level of cash and cash equivalents held by the Company during the year ended March 31, 2010 and 2009, fluctuations in the market interest rates had no significant impact on its interest income.

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, 2010 and 2009, the Company had the following assets and liabilities denominated in US dollars:

	March 31, 2010 US\$	March 31, 2009 US\$
Cash and cash equivalents	1,730	14,802
Prepaid expenses	—	382,261
Accounts payable and accrued liabilities	277,972	(413,679)
Other payable	(588,272)	(495,856)
	(308,570)	(512,472)

Based on the above net exposures as at March 31, 2010 and 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 \$43,921 (March 31, 2009 - \$32,319) in the Company's net loss and comprehensive loss.

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6. RESEARCH AND DEVELOPMENT EXPENSES

Project	Year ended March 31, 2010 \$	Year ended March 31, 2009 \$	Cumulative from Inception to March 31, 2010 \$
PAC-113			
Expense	84,472	1,154,902	5,553,618
Recovery <i>[note 13]</i>	—	(865,287)	(865,287)
	84,472	289,615	4,688,331
PAC-G31P	120,496	272,306	2,220,099
Other Projects	(2,569)	24,676	193,177
	202,399	586,597	7,101,607

7. CASH AND CASH EQUIVALENTS

As at March 31, 2010, cash and cash equivalents include \$Nil [2009 - \$250,000] of subscription amounts received in trust accounts following the closing of a financing.

8. RESTRICTED CASH

As at March 31, 2010, restricted cash include \$300,000 [2009 - \$Nil] of subscription amounts received in trust accounts prior to the closing of a financing *[note 21[a]]* and \$14,295 [2009 - \$Nil] of cash on deposit subject to restriction.

9. PREPAID EXPENSES AND OTHER

As at March 31, 2010, prepaid expenses and other include \$Nil [2009 - \$482,146] of amounts advanced to third parties in connection with planned future research and development activities. During the fiscal year ended March 31, 2010, the Company recorded a write-off of the remaining balance of \$192,958 of prepaid expenses as a result of the uncertainty surrounding the continuation of its planned research and development studies in the region *[note 21 [b][v] b)]*.

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10. ACQUISITION OF XPHASE PHARMACEUTICALS INC.

On August 11, 2009, the Company completed its acquisition of all issued and outstanding shares of Xphase Pharmaceuticals Inc. ("Xphase"). The acquisition provided the Company with management services of Xphase principals at no additional compensation, other than grant of options priced at premium [note 15[d]]. The acquisition also provided the Company with the right to acquire the exclusive global rights, excluding China, of AF-05, a novel anti-anxiety drug candidate.

The consideration for the acquisition was 1.5 million common shares of the Company at an aggregate fair value of \$150,000. Upon the achievement of certain pre-defined business development milestones by June 10, 2010, an additional consideration of 1.75 million common shares of the Company would be issued to Xphase shareholders. The pre-defined business development milestones were not met, and the Company's obligations to issue the additional 1.75 million common shares expired on June 10, 2010.

As Xphase was a development stage company and did not meet the definition of a business under Canadian GAAP, the transaction was accounted for as an asset acquisition, and not as a business combination. The purchase price has been allocated to Xphase's identifiable assets and liabilities based on their fair market value:

	Amount
	\$
Identifiable assets acquired:	
Cash	4,742
Other current assets	947
Prepaid management fees	189,408
Liabilities assumed:	
Accounts payable and accrued liabilities	(7,414)
Other liabilities	(11,600)
	176,083
	\$
Consideration	
Equity securities	150,000
Acquisition expenses	26,083
	176,083

The prepaid management fees were amortized on a straight-line basis over the service period of one year starting April 1, 2009 when Xphase principals started performing their services.

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11. PROPERTY AND EQUIPMENT

	Cost	Accumulated	Net Book
	\$	Amortization	Value
	\$	\$	\$
March 31, 2010			
Computer equipment and software	46,919	37,483	9,436
Leasehold improvement	41,346	26,226	15,120
Office furniture and equipment	44,415	21,902	22,513
	132,680	85,611	47,069
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

For the year ended March 31, 2010, amortization of property and equipment was \$22,118 [2009 - \$26,842].

12. INTANGIBLE ASSETS

	March 31,	March 31,
	2010	2009
	\$	\$
Technology, licenses and rights		
Cost	1,477,151	1,477,151
Accumulated amortization	(903,896)	(711,922)
Write-down of technology, licenses and rights	(244,408)	—
	328,847	(765,229)

For the year ended March 31, 2010, amortization of intangible assets was \$191,974 [2009 - \$236,974].

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12. 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 sub-license, 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 \$59,742, 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, 2010 was \$328,847 (March 31, 2009 - \$385,821).

- [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, 2010 was \$Nil (March 31, 2009 - \$379,408). The impairment test conducted during the fiscal year ended March 31, 2010 resulted in the write-off of \$244,408 of the remaining balance of net book value of this technology.

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13. OTHER PAYABLE

On March 6, 2009, the Company entered into a settlement arrangement with a vendor for an outstanding account of approximately US\$1.3 million. As part of this settlement, the Company received from this vendor a credit note of approximately US\$604,000 as a research and development expense recovery and made an initial payment of US\$128,000 in the year ended March 31, 2009. The Company agreed to pay the balance amount of US\$580,000 over three minimum installments as follows:

Minimum Installments	Amount US\$
July 15, 2009	150,000
October 15, 2009	150,000
December 30, 2009	280,000
	580,000

Failure to make these minimum installments would further obligates the Company to pay interest at a rate of prime plus 6% on amounts due and outstanding from the respective due dates of the minimum installments. All amounts outstanding, including interest, were due and payable in full on December 30, 2009.

At March 6, 2009, the Company recorded the amount payable at the fair value estimated by discounting the future cash stream of the indebtedness at a discount rate of 25% which represents the estimated borrowing rate available for the Company for similar financial arrangements.

	Amount US\$	Discounted US\$	Discounted \$
Amount as of March 6, 2009	580,000	488,207	627,980
Accretion of discounted liability		7,649	9,675
Unrealized foreign exchange gain			(12,232)
Balance as of March 31, 2009	580,000	495,856	625,423
Accretion of discounted liability		84,144	93,126
Unrealized foreign exchange gain			(129,385)
Balance as of March 31, 2010	580,000	580,000	589,164

During the year ended March 31, 2010, no minimum installment was made. Accordingly, the Company recorded overdue interest of US\$8,273 (\$8,404) for the year ended March 31, 2010.

The Company renegotiated and signed a final settlement agreement in April 2010, with the vendor to settle the indebtedness, inclusive of interest payable, of US\$588,273 (\$597,568). In accordance to this final settlement agreement, the vendor agreed to write off US\$388,273 (\$394,408) of the indebtedness subject to receiving a cash payment of US\$200,000 (\$203,160) by June 7, 2010. In addition, the vendor is entitled to a contingency payment, capped at US\$100,000 (\$101,580), equal to 10% of the cash receipt from a disposition or licensing transaction, or multiple transactions, associated with the Company's technology portfolio, PAC-113 and PAC-G31P. On June 7, 2010, the Company issued a payment of US\$200,000 (\$203,160) to the vendor in accordance to the final settlement agreement. The resulting gain will be recorded in fiscal year ending March 31, 2011.

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14. 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 completed this Offering in two tranches in February 2009 and April 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.

The convertible debentures bear interest from the date of issuance at a rate of prime plus 4% per annum. The principal amount plus any accrued interest will be repayable in cash upon the earlier of (i) one year from the date of issuance or (ii) closing of a merger or a financing transaction with a value to the Company of at least US\$1 million (approximately \$1.02 million). 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 consists of one common share of the Company (a "Common Share") and one common share purchase warrant (a "Warrant"). Each Warrant is exercisable into one Common Share at a price of \$0.10 per Common Share and expires on (i) the second anniversary of the date of issuance of the Warrant for non-insider holders or (ii) the maturity date of the convertible debentures for insider holder. 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.

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14. CONVERTIBLE DEBENTURES (cont'd.)

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

The Company incurred legal and professional fees of \$30,097 associated with the financing. These financing costs were charged as expenses during the year ended March 31, 2009.

	Amount \$	Discounted \$
Balance upon initial recognition	614,500	523,554
Accretion of discounted liability		8,277
Balance as of March 31, 2009	614,500	531,831
Accretion of discounted liability		81,232
Balance as of March 31, 2010	614,500	613,063

As of March 31, 2010, no convertible debentures were converted into Units, and the first tranche of the debentures of \$364,500 were past due.

Subsequent to the fiscal year ended March 31, 2010, the Company entered into debt conversion agreements with all debenture holders to settle all past due debentures of \$614,500 together with \$43,789 of interest payable, as of April 22, 2010, with common shares of the Company [note 21[b][i]].

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15. SHARE CAPITAL

[a] Common shares

On May 25, 2010, the Company obtained shareholder approval at the special meeting of shareholders to consolidate its common shares on a two to one basis (the "Share Consolidation"). The Share Consolidation was completed on June 8, 2010. All common shares, warrants and options and per share amounts for the years ended March 31, 2010 and 2009 have been retroactively restated to reflect the Share Consolidation.

	Number of Shares	Amount \$
Authorized		
Unlimited number of common shares without par value		
Balance, March 31, 2008 and 2009	17,572,347	13,012,118
Issued pursuant to acquisition of assets	1,500,000	150,000
Balance, March 31, 2010	19,072,347	13,162,118

[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, 2010 and 2009, there were no preferred shares issued and outstanding.

[c] Common share purchase warrants

	Number	Weighted Average Exercise Price \$
Balance, March 31, 2008	4,599,471	1.44
Expired on December 7, 2008	(1,999,453)	2.32
Expired on December 7, 2008	(271,551)	2.10
Balance, March 31, 2009	2,328,467	0.60
Expired on March 16, 2010	(17,100)	0.44
Balance, March 31, 2010	2,311,367	0.60

Date of Expiry	Exercise Price	Number of Warrants
March 16, 2013	\$0.60	2,311,367

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15. SHARE CAPITAL (cont'd.)

[d] Share purchase options

	Number	Weighted Average Exercise Price \$
Balance March 31, 2008	250,000	4.50
Expired on December 7, 2008	(250,000)	4.50
Balance, March 31, 2009 and 2010	—	—

[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.

Details of stock option transactions for the years ended March 31, 2010 and 2009 are summarized as follows:

	Number	Weighted Average Exercise Price \$
Balance, March 31, 2008	1,317,000	1.98
Granted	87,500	0.52
Forfeited or expired	(497,833)	1.58
Balance, March 31, 2009	906,667	1.98
Granted	955,000	0.20
Forfeited or expired	(381,667)	1.80
Balance, March 31, 2010	1,480,000	0.88

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15. SHARE CAPITAL (cont'd.)

[e] Stock options (cont'd.)

At March 31, 2010, stock options to executive officers, directors and consultants were outstanding as follows:

Range of Exercise Price	Options Outstanding			Options Exercisable	
	Number of Common Shares Issuable	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price (\$)	Number of Common Shares Issuable	Weighted Average Exercise Price (\$)
\$0.20 - \$0.99	955,000	4.82	0.20	955,000	0.20
\$1.00 - \$1.99	75,000	5.16	1.26	53,333	1.26
\$2.00 - \$2.99	450,000	4.24	2.26	450,000	2.26
	1,480,000	4.67	0.88	1,458,333	0.88

Date of Expiry	Exercise Price	Number of Options Outstanding	Number of Options Exercisable
August 22, 2014	\$2.10	75,000	75,000
August 22, 2014	\$2.32	275,000	275,000
March 6, 2012	\$2.10	40,000	40,000
March 6, 2015	\$2.32	60,000	60,000
May 31, 2015	\$1.26	75,000	53,333
July 28, 2014	\$0.20	795,000	795,000
July 28, 2017	\$0.20	160,000	160,000
Balance, March 31, 2010		1,480,000	1,458,333

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15. SHARE CAPITAL (cont'd.)

[e] Stock options (cont'd.)

The estimated fair value of options granted during the fiscal year ended March 31, 2010, to non-employees including officers who performed services as consultants was \$114,600 (2009 - \$36,750). There were no options granted to employees in both fiscal years. The fair values of the stock options granted during the year ended March 31, 2010 and 2009 were estimated using the Black-Scholes valuation model with the following assumptions:

	2010	2009
Expected volatility	211.70%	124.50%
Expected life of options	5 - 8 years	5 years
Dividend yield	0.00%	0.00%
Risk free interest rate	2.68% - 2.93%	3.02%

The weighted average fair value of options granted during the years ended March 31, 2010 and 2009 was \$0.12 per option and \$0.42 per option. 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.

16. 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 September 30, 2010. Future minimum annual lease payments under the leases are as follows:

	\$
2011	50,131
	50,131

[b] Clinical research and development agreements

In the previous fiscal years, the Company entered into various clinical research and development agreements with third parties which require the Company to fund research and development expenditures. The Company subsequently cancelled all of its commitment, and there were no non-cancellable commitments as of March 31, 2010.

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16. COMMITMENTS (cont'd.)

[c] License agreements

- [i] Pursuant to the Demegen Sublicense [note 12(a)], 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. As of March 31, 2010, the Company was indebted to Demegen in the amount of US\$107,000 (\$108,691) for over-due minimum annual royalties.

Subsequent to March 31, 2010, following the completion of its financing and financial restructuring [note 21], the Company made a payment of US\$22,120 (\$22,469) and issued 500,000 common shares to settle its indebtedness of US\$107,000 (\$108,691). The Company further issued 150,000 common shares in exchange for a reduced minimum annual royalty by US\$20,000 (\$20,316) for fiscal year ending March 31, 2011.

- [ii] Pursuant to a license agreement between the Company's wholly owned subsidiary, ILT, and University of Saskatchewan (the "US License") [note 12(b)], 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 (amounting 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.

In accordance to the US License, the Company agreed to provide research funding to the University of Saskatchewan (the "University"). The research would cover but was 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. Of these research commitments, \$334,096 was paid and the remaining balance of \$165,904 was due on October 15, 2009.

In addition, the Company is also obligated to pay all fees and costs in connection with preparing, filing, maintaining and prosecuting patents. As of March 31, 2010, patent fees reimbursable to the University amounted to \$126,200.

Subsequent to March 31, 2010, the Company arranged settlement with the University for the indebtedness of \$292,104 plus interest stipulated pursuant to the US License [note 21].

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17. 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.

18. INCOME TAXES

At March 31, 2010, 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	—	34,000	—
2018	—	47,000	—
2019	—	16,000	—
2026	43,000	—	—
2027	99,000	—	2,083,000
2028	84,000	—	5,492,000
2029	30,000	—	3,538,000
2030	—	—	1,093,000
	<u>256,000</u>	<u>121,000</u>	<u>13,191,000</u>

In addition, the Company has unclaimed tax deductions of approximately \$1,132,910 related primarily to scientific research and experimental development expenditures, and \$591,776 of net capital losses available to carryforward indefinitely to reduce taxable income of future years.

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18. INCOME TAXES (cont'd.)

Significant components of the Company's future income tax assets and liabilities as of March 31, 2010 are shown below:

	2010	2009
	\$	\$
Future income tax assets:		
Tax basis in excess of accounting value	86,000	10,000
Share issuance costs	73,000	156,000
Research and development deductions and credits	565,000	1,086,000
Write-off of investment	148,000	154,000
Operating loss carryforwards	3,297,000	3,031,000
Total future income tax assets	4,169,000	4,437,000
Valuation allowance	(4,169,000)	(4,437,000)
Total future income tax assets	—	—
Future income tax liabilities:		
Intangible assets	—	—
Net future income tax liabilities	—	—

The potential income tax benefits relating to the net future income 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 income tax assets have been recognized as at March 31, 2010 and 2009.

The reconciliation of income tax attributable to operations computed at the statutory tax rates to income tax expenses using a 29.63% statutory tax rate [March 31, 2009 - 30.63%] is:

	2010	2009
	\$	\$
Income taxes at statutory rates	(481,000)	(699,000)
Benefits recognized	(88,000)	70,000
Gains not recognized or expenses not deductible for tax purposes	245,000	366,000
Benefit of non-capital losses not recognized	324,000	263,000
Future income tax recovery	—	—

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19. 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.

20. RELATED PARTY TRANSACTIONS

During the year ended March 31, 2010, the Company incurred \$Nil [2009 - \$503] of consulting services provided by directors and \$74,467 [2009 - \$7,941] of interest expenses related to convertible debentures held by directors or officers. These transactions were incurred in the normal course of business and recorded at their exchange amounts.

As of March 31, 2010, the Company had the following amounts due to related parties:

	March 31, 2010	March 31, 2009
	\$	\$
Accounts payable to directors, officers, or contract managers in connection to business expense reimbursements	49,786	1,666
Interest payable	27,277	2,467
Debentures held by officers or directors ⁽¹⁾	386,333	243,000
	463,396	247,133

⁽¹⁾ During the year ended March 31, 2010, two debenture holders, who hold convertible debentures of \$143,333, were appointed to be director or officer of the Company.

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21. SUBSEQUENT EVENTS

[a] Private Placement Financing

On April 19, 2010, announced that it had arranged a non-brokered private placement (the “Financing”) of \$600,000 of subscription receipts (“Subscription Receipts”) subject to satisfactory completion of certain conditions, including the approval of the TSX Venture Exchange. Of the Subscription Receipts, \$300,000 was collected in a trust account of the Company as of March 31, 2010.

In connection to the Financing, the Company had initiated a financial restructuring [note 21[b]] and agreed to seek shareholder approval for the Share Consolidation [note 15[a] and 21[c]].

On May 28, 2010, the Company announced closing of a non-brokered private placement of \$600,000 Subscription Receipts. Under the Financing, the Company issued an aggregate of 10 million Subscription Receipts at a price of \$0.06 per Subscription Receipt for gross proceeds of \$600,000. Upon completion of the Share Consolidation [note 21[c]], each Subscription Receipt would be automatically exercised, for no additional consideration, for one common share.

On June 8, 2010, following the completion of the Share Consolidation, all Subscriptions Receipts were converted to 10,000,001 common shares.

[b] Financial Restructuring

On April 19, 2010, the Company also announced that it had initiated a financial restructuring (the “Financial Restructuring”). The Financial Restructuring involves restructuring of approximately \$2.3 million of indebtedness and commitments as summarized in the following table:

	Indebtedness on Date of Settlement	Common Shares	Form of Settlements		
			Cash	Cash Discounts or Credits	Other
	\$	\$	\$	\$	\$
Convertible Debentures ^[i]	658,289	658,289			
Other Payable ^[ii]	597,568		203,160	394,408	
Demegen Sub-license ^[iii]	179,796	157,327	22,469		
US License ^[iv]	292,104				292,104
Other Indebtedness ^[v]	562,730	69,281	145,550	255,043	92,856
	2,290,487	884,897^(a)	371,179	649,451	384,960

(a) The Company issued 12,618,142 common shares to settle \$872,415 of these settlements on June 8, 2010. The Company is obligated to issue 122,875 common shares to settle the remaining balance of \$12,482.

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21. SUBSEQUENT EVENTS (cont'd.)

[b] Financial Restructuring (cont'd.)

[i] Convertible Debenture *[note 14]*

On April 22, 2010, the Company entered into debt conversion agreements with all debenture holders to settle its past due debentures in the aggregate of \$658,289, inclusive of principal amount due of \$614,500 and interest payable of \$43,789. In accordance with agreements, subject to the approval of the TSX Venture Exchange and shareholder approval of the Company to effect the Share Consolidation, all debenture holders agreed to convert the amounts of indebtedness into common shares at a conversion rate of \$0.06 per common shares.

On June 8, 2010, following the completion of the Share Consolidation, the Company issued 10,971,485 common shares to settle total amounts of indebtedness of \$658,289 in connection to the past due debentures.

[ii] Other Payable *[note 13]*

The Company entered into a final settlement agreement, effective March 25, 2010, with a vendor to settle its past due amount payable of US\$588,273 (\$597,568). In accordance with this agreement, the Company issued a payment of US\$200,000 (\$203,160) to the vendor on June 7, 2010, and the vendor wrote off the remaining balance of US\$388,273 (\$394,408). The vendor is entitled to a future contingency payment, capped at US\$100,000 (\$101,580), equal to 10% of the cash receipt from a disposition or licensing transaction, or multiple transactions, associated with the Company's technology portfolio, PAC-113 and PAC-G31P.

[iii] Demegen License *[note 16[i]]*

In accordance with the Demegen Sublicense, the Company was indebted to Demegen in the amount of US\$107,000 (\$108,691) of minimum royalties. On April 22, 2010, the Company entered into an amendment license agreement to arrange settlement for this indebtedness and to amend certain terms of the Demegen Sublicense (the "Amendment to Demegen License").

In accordance to the Amendment to Demegen License, the Company made a payment of US\$22,120 (\$22,469) and issued 500,000 common shares to settle its indebtedness of US\$107,000 (\$108,691) in June 2010. The Company also issued (i) 150,000 common shares to extend a development milestone timeline from June 30, 2010 to June 30, 2011 and (ii) 50,000 common shares to settle in advance US\$20,000 (\$20,316) of the minimum annual royalty of US\$50,000 (\$50,790) for the year ending March 31, 2011. The Amendment to Demegen License also provides the Company a right to further extend the development milestone timeline to June 30, 2012 at a fee of US\$50,000 (\$50,790), payable in cash or equivalent number of common shares of the Company. The share payment will be based on the prevailing market price of the common share of the Company on the date of extension notice.

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21. SUBSEQUENT EVENTS (cont'd.)

[b] Financial Restructuring (cont'd.)

[iv] US License [note 16[ii]]

In accordance to the US License, the Company was indebted to the University in the amount of \$292,104 which composed of \$165,904 of research funding commitment and \$126,200 of patent fees reimbursement.

Subsequent to March 31, 2010, the Company arranged settlement with the University for the indebtedness of \$292,104 plus interest stipulated in accordance to the US License [note 16[c]].

[v] Other Indebtedness [note 16[ii]]

The aggregate amount of indebtedness for other vendors settled was \$562,730 inclusive of the following:

- a) On April 22, 2010, the Company entered into a settlement agreement with a vendor to settle its indebtedness of US\$70,000 (\$71,106). In accordance with this agreement, the vendor is entitled to a future contingency payment, capped at US\$70,000 (\$71,106), equal to 10% of the cash receipt from (i) merger or acquisition transaction which give rise to a minimum cash reserve of US\$500,000 to the combined company, (ii) a financing transaction, or multiple transactions, from April 22, 2010 onward, which give rise to accumulated proceeds of US\$1 million or more and (iii) a disposition or licensing transaction, or multiple transactions, associated with the Company's technology portfolio, PAC-113 and PAC-G31P.

The settlement agreement also provides the vendor with a right until December 31, 2010, to convert its entitlement for future contingency payment of US\$70,000 into equity interest of the Company based on a pre-determined calculation, or 15% equity interest of the Company's subsidiary, IL Therapeutics Inc.

- b) On April 30, 2010, the Company completed its negotiation with a vendor for its indebtedness of US\$192,305 (\$195,343). The Company obtained agreement from this vendor to apply \$192,205 of its non-refundable advance payment of US\$382,261 with the vendor to offset the indebtedness. The Company offset the non-refundable advance payment against its indebtedness of US\$192,305 to the vendor and wrote off the remaining portion of US\$189,956 [\$192,958] of the advance payment in the year ended March 31, 2010.
- c) On May 25, 2010, the Company obtained agreements from its management and consultants to settle its indebtedness of \$56,799 in connection to business expense reimbursements with common shares of the Company. On June 8, 2010, the Company issued 946,657 common shares at a price of \$0.06 per share as settlement payments.

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21. SUBSEQUENT EVENTS (cont'd.)

[b] Financial Restructuring (cont'd.)

- d) On June 11, 2010, the Company obtained agreements from its consultants to settle its indebtedness of US\$19,488 (\$19,795) with cash payments of US\$7,200 and 122,875 common shares, to be issued at US\$0.10 per share.
- e) On July 7, 2010, the Company obtained agreement from a vendor to settle its indebtedness of \$26,750 with a cash payment of \$5,000 and a future contingency payment of \$21,750 payable upon licensing or sale of PAC-G31P technology of the Company.
- f) Subsequent to March 31, 2010, the Company also received cash discounts, in the aggregate of \$59,699, as part of its settlements with other vendors.

[c] Share Consolidation

On May 25, 2010, the Company obtained shareholder approval at the special meeting of shareholders to consolidate its common shares on the basis of two to one. The Share Consolidation was arranged in connection with the Financing and the Financial Restructuring. On June 8, 2010, the Company announced that it has obtained regulatory approvals to effect the Share Consolidation.

The disclosure of common shares and per share amounts for the years ended March 31, 2010 and 2009 have been adjusted to account for the Share Consolidation.

Following the Share Consolidation, the deemed exercise of the Subscription Receipts and completion of the Financial Restructuring, the Company has 41,690,490 post consolidation Common Shares issued and outstanding.

	Number of Shares
As of March 31, 2010, based on post consolidation basis	19,072,347
Shares issued pursuant to conversion of Subscription Receipts	10,000,001
Shares issued pursuant to debt conversion agreements with debenture holders	10,971,485
Shares issued pursuant to the Amendment Demegen License	700,000
Shares issued to settle expense reimbursements of management and consultants	946,657
	<u>41,690,490</u>

22. COMPARTIVE FIGURES

Certain comparative figures have been reclassified from statements previously presented to conform to the presentation of current year consolidated financial statements.