PALADIN LABS INC.

(FORMERLY GERIATR$_X$ PHARMACEUTICAL CORPORATION)

FINANCIAL STATEMENTS

DECEMBER 31, 1996

AUDITOR'S REPORT

To the Shareholders of
Paladin Labs Inc.
(Formerly Geriatr$_x$ Pharmaceutical Corporation)

We have audited the balance sheet of Paladin Labs Inc. (formerly Geriatr$_x$ Pharmaceutical Corporation) as at December 31, 1996 and January 4, 1996 and the statements of operations, deficit and changes in financial position for the periods then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based upon our audit.

We have conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examination, on a test basis, of 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 financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1996 and January 4, 1996 and the results of its operations and the changes in its financial position for the periods then ended in accordance with generally accepted accounting principles applied on a consistent basis.

Bessner Gallay Schapira Kreisman
CHARTERED ACCOUNTANTS

Montreal, Quebec
January 17, 1997

PALADIN LABS INC.
(FORMERLY GERIATR$_X$ PHARMACEUTICAL CORPORATION)
BALANCE SHEET
AS AT DECEMBER 31, 1996

	December 31, 1996 $	January 4, 1996 $
ASSETS		
CURRENT		
Cash	9,255	1,035,943
Marketable securities - at cost which approximates market value	749,430	-
Accounts receivable	39,949	422
Income taxes recoverable	30,859	-
	829,493	1,036,365
OTHER ASSETS (Note 2)	2,651,008	4,191,509
	3,480,501	5,227,874
LIABILITIES		
CURRENT		
Accounts payable - Shareholder	321,769	182,467
- Other	12,729	31,450
	334,498	213,917
SHAREHOLDERS' EQUITY		
CAPITAL STOCK (Note 3)	8,616,390	8,616,389
CONTRIBUTED SURPLUS	86,513	86,513
DEFICIT	(5,556,900)	(3,688,945)
	3,146,003	5,013,957
	3,480,501	5,227,874

CONTINGENT LIABILITY (Note 9)

APPROVED ON BEHALF OF THE BOARD:

"Jonathan Goodman" Director

"Mark Beaudet" Director

PALADIN LABS INC.
(FORMERLY GERIATR$_X$ PHARMACEUTICAL CORPORATION)
STATEMENT OF DEFICIT
FOR THE YEAR ENDED DECEMBER 31, 1996

	December 31, 1996 $	January 4, 1996 (11 months) $
Balance, beginning of period	(3,688,945)	(3,521,811)
Net loss	(1,867,955)	(167,134)
BALANCE, END OF PERIOD	(5,556,900)	(3,688,945)

PALADIN LABS INC.
(FORMERLY GERIATR$_X$ PHARMACEUTICAL CORPORATION)
STATEMENT OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31, 1996

	December 31, 1996	January 4, 1996 (11 months)
	$	$
REVENUES		
Income from distribution of pharmaceutical products	40,703	-
Interest earned	37,586	-
	78,289	-
EXPENSES		
Amortization	283,162	13,433
Consulting	-	4,290
Interest and bank charges	2,516	12,008
Investor relations	10,109	6,653
Office expenses	554	2,352
Professional fees	26,295	84,446
Regulatory fees	2,795	5,718
Rent	-	8,970
Salaries and wage levies	57,327	-
Taxes and licences	28,795	25,200
Telecommunications	-	1,264
Travel and promotion	1,620	2,800
	413,173	167,134
Research and development expense (Note 4)	258,877	-
	672,050	167,134
LOSS BEFORE UNDERNOTED ITEMS	(593,761)	(167,134)
Write-down of pharmaceutical product rights (Note 5)	1,257,340	-
LOSS BEFORE INCOME TAXES	(1,851,101)	(167,134)
Provision for large corporation tax	16,854	-
NET LOSS	(1,867,955)	(167,134)
LOSS PER SHARE	(0.50)	(0.53)

PALADIN LABS INC.
(FORMERLY GERIATR$_X$ PHARMACEUTICAL CORPORATION)
STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEAR ENDED DECEMBER 31, 1996

	December 31, 1996 $	January 4, 1996 (11 months) $
OPERATING ACTIVITIES		
Net loss for the period	(1,867,955)	(167,134)
Add items not affecting cash:		
Amortization	283,162	13,433
Write-down of pharmaceutical product rights	1,257,340	-
	(327,453)	(153,701)
Changes in working capital non-cash items relating to operations	42,195	162,356
	(285,258)	8,655
INVESTING ACTIVITIES		
Additions to other assets	(1)	(4,043,750)
Acquired through issuance of common shares	1	4,043,750
Common shares issued for cash	-	1,000,000
	-	1,000,000
INCREASE (DECREASE) IN CASH	(285,258)	1,008,655
Cash, beginning of period	1,035,943	27,288
CASH, END OF PERIOD	750,685	1,035,943
CASH COMPRISES THE FOLLOWING:		
Cash	9,255	1,035,943
Marketable securities	749,430	-
	750,685	1,035,943

1. **Accounting Policies**

The company is incorporated under the B.C. Companies Act and is in the business of developing, producing and marketing pharmaceuticals on a worldwide basis. The financial statements are prepared on the basis of generally accepted accounting principles and the most significant accounting policies followed by the company are described below:

Pharmaceutical Product Rights and Licences

Rights and licences, pertaining to pharmaceutical products, which were purchased by the company, are valued at cost except for the acquisition during the current year from the company's parent which is recorded at a value of $1, the parent company's carrying amount, pursuant to generally accepted accounting principles for related party transactions applicable to fiscal periods commencing after October 1, 1995. The amortization expense and the related accumulated amortization is computed by the straight-line method for reporting purposes based upon their useful lives of thirteen to fifteen years.

Research and Development Expense

Research and development costs are expensed in the year incurred.

Loss Per Share

Net loss per common share has been computed by dividing the loss applicable to common shareholders by the weighted average number of shares of common stock outstanding during the respective years. The result for the period ended January 4, 1996 has been adjusted to reflect the 1 for 10 share consolidation during the current period. Fully diluted loss per share is not presented as this calculation has an anti-dilutive effect on the loss per share.

2. **Other Assets**

Other assets consist of the following:

	Cost $	Accumulated Amortization $	December 31, 1996 Net $	January 4, 1996 Net $
Pharmaceutical product rights	2,696,601	178,699	2,517,902	4,043,750
Licence	190,500	57,394	133,106	147,759
	2,887,101	236,093	2,651,008	4,191,509

2. **Other Assets** - cont'd.

During the year, the company acquired from its parent, the exclusive rights to develop and further commercialize certain pharmaceutical products, in exchange for newly issued common shares of the company as described in Note 3d. The non-monetary exchange value of $386,879 attributed to the transaction was arrived at based upon the fair market value as determined by management, which consisted of the parent company's original development costs.

3. **Capital Stock**

a) The capital stock consists of the following:

Authorized:
100,000,000 common shares without nominal or par value.

Issued and fully paid:

	December 31, 1996		**January 4, 1996 (11 months)**	
	Number of Shares	**Amount $**	**Number of Shares**	**Amount $**
Balance, beginning of period	36,692,390	8,616,389	3,067,392	3,572,639
Consolidation of shares, 1 for 10	(33,023,151)	-	-	-
	3,669,239	8,616,389	3,067,392	3,572,639
Issued during the period				
Private placement (c)	-	-	6,666,666	1,000,000
For product rights (d)	154,752	1	26,958,332	4,043,750
BALANCE, END OF PERIOD	3,823,991	8,616,390	36,692,390	8,616,389

During the period, the authorized capital was reduced from 100 million to 10 million common shares as a result of a 1 for 10 share consolidation. The authorized capital was subsequently increased to 100 million shares by a special resolution.

3. **Capital Stock** - cont'd.

b) Of the issued and outstanding shares, 7,500 (January 4, 1996 - 75,000) are held in escrow.

c) The 666,667 (January 4, 1996 - 6,666,666) common shares issued by way of private placement in the prior year are subject to a holding period of one year throughout which they may not be traded. In addition, each of the shares has attached to it a share purchase warrant entitling the holder to purchase one additional share at $1.50 until January 4, 1997 and at $1.80 thereafter until January 4, 1998.

d) The 154,752 common shares issued in the current period and the 26,958,332 common shares issued in the prior period (2,695,833 shares after the 1 for 10 consolidation) for pharmaceutical product rights are subject to a holding period of one year throughout which they may not be traded, of which the restriction on the shares issued in the prior period expired on January 4, 1997.

e) The company has outstanding stock options entitling directors and an employee to purchase up to 83,058 common shares at a price of $1.21 for a period of five years ending December 10, 2001.

4. **Research and Development**

The research and development expense consists of the following:

	$
Research and development costs	281,086
Less: investment tax credits claimed	22,209
	258,877

5. **Write-Down of Pharmaceutical Product Rights**

The Directors of the company have ascertained that the values of certain pharmaceutical product rights, acquired in the prior year, have been significantly reduced due to market changes and regulatory issues. As a result, these rights, having an original cost of $1,347,150 and an unamortized value of $1,257,340 have been written off in the current fiscal period.

6. **Related Party Transactions**

The company entered into transactions with its parent which resulted in the following:

	December 31, 1996 $	January 4, 1996 (11 months) $
Purchase of pharmaceutical product rights (notes 1, 2, 3)	1	4,043,750
Research and development expenses	281,086	-
Income from distribution of pharmaceutical products	40,703	-

7. **Income Taxes**

a) As at December 31, 1996 the company had available income tax losses of approximately $2.5 million which may be applied against the taxable income of future years. These losses expire between 1997 and 2003.

b) As at December 31, 1996, the company had available investment tax credits, related to Scientific Research and Experimental Development expenditures amounting to approximately $757,000, of which the potential income tax benefit applicable thereto may be applied against income taxes payable in future years.

8. **Commitment**

During the current and prior period, the company entered into agreements with its parent, granting the parent the exclusive right to manufacture and distribute certain pharmaceutical products in Canada for a period of five years, commencing from the date of first commercial sale. Under the terms of these agreements, the company is entitled to receive the net profits from the sale of the products after deduction of all costs inclusive of a manufacturing and distribution fee.

9. **Contingent Liability**

The company is the defendant in a lawsuit alleging infringement of the Plaintiff's process patent. It is the opinion of management that this claim is unfounded as the Company's supplier is not using a process protected by patent. The plaintiff has frustrated the company's attempts to have the claim struck by repeatedly adjourning the matter. Consequently, no provision has been made for any ultimate loss which may be realized by the company as a result of this litigation. Such a loss, if any, will be reflected in the period in which it occurs.

10. **Comparative Figures**

Due to a change in control of the company, the fiscal year end has been changed to December 31, 1996. As a result, comparative figures are for the eleven months ended January 4, 1996

11. **Subsequent Event**

On January 3, 1997 a shareholder exercised 166,667 warrants, resulting in the issue of 166,667 common shares for a total consideration of $250,000 cash.