

**Hamilton Thorne Ltd**  
**Financial Statements**  
*December 31, 2009*

## **Management's Statement of Responsibility for Financial Reporting**

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To the Shareholders of Hamilton Thorne Ltd.:

Management is responsible for the preparation and presentation of the accompanying consolidated financial statements, including responsibility for significant accounting judgments and estimates in accordance with Canadian generally accepted accounting principles and ensuring that all information in the Management Discussion and Analysis ("MD&A") is consistent with the statements. This responsibility includes selecting appropriate accounting principles and methods, and making decisions affecting the measurement of transactions in which objective judgment is required.

In discharging its responsibilities for the integrity and fairness of the consolidated financial statements, management designs and maintains the necessary accounting systems and related internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded and financial records are properly maintained to provide reliable information for the preparation of consolidated financial statements.

The Board of Directors and Audit Committee are composed primarily of Directors who are neither management nor employees of the Company. The Board is responsible for overseeing management in the performance of its financial reporting responsibilities, and for approving the financial information included in the MD&A. The Committee fulfils these responsibilities by reviewing the financial information prepared by management and discussing relevant matters with management and external auditors. The Committee is also responsible for recommending the appointment of the Company's external auditors.

Meyers Norris Penny LLP, an independent firm of Chartered Accountants, is appointed by the shareholders to audit the financial statements and report directly to them; their report follows. The external auditors have full and free access to, and meet periodically and separately with, both the Committee and management to discuss their audit findings.

*"Meg Spencer"*

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**Chief Executive Officer**

*"John R. Freeman"*

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**Chief Financial Officer**



MEYERS NORRIS PENNY LLP

## Auditors' Report

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To the Shareholders of Hamilton Thorne Ltd:

We have audited the consolidated balance sheet of Hamilton Thorne Ltd (the "Company") as at December 31, 2009 and the consolidated statements of operations and comprehensive loss, shareholders' equity (deficiency) and cash flows for the year 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 on our audit.

We conducted our audit in accordance with Canadian 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 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 December 31, 2009 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The financial statements as at December 31, 2008 and for the year then ended were prepared in accordance with accounting principles generally accepted in the United States of America and were audited in accordance with auditing standards generally accepted in the United States of America by other auditors who expressed an opinion without reservation on those statements (including a reconciliation from accounting principles generally accepted in the United States of America to Canadian generally accepted accounting principles) in their report dated August 12, 2009. The financial statements have been subsequently restated for the change in accounting basis of preparation from accounting principles generally accepted in the United States of America to Canadian generally accepted accounting principles and we have audited the adjustments to the 2008 financial statements and in our opinion such adjustments, in all material respects, are appropriate and have been properly applied.

*Meyers Norris Penny LLP*

Toronto, Ontario  
April 21, 2010

Chartered Accountants  
Licensed Public Accountants



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**Hamilton Thorne Ltd**  
**Consolidated Balance Sheets**  
*As at December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

	<b>2009</b>	<b>2008</b>
<b>Assets</b>		
Current		
Cash and cash equivalents	1,356,371	5,029
Accounts receivable	499,875	958,239
Inventories (note 7)	512,300	633,212
Prepaid expenses and other current assets	72,689	45,161
Note receivable, officer (note 23)	23,813	22,963
	<b>2,465,048</b>	<b>1,664,604</b>
Capital assets (note 8)	90,481	131,920
Other assets	72,454	116,881
	<b>2,627,983</b>	<b>1,913,405</b>
<b>Liabilities</b>		
Current		
Accounts payable and accrued liabilities	1,171,562	1,093,551
Notes payable (note 9)	83,037	5,051,069
Capital lease obligations, current (note 10)	5,753	5,888
Deferred revenue	35,881	22,382
	<b>1,296,233</b>	<b>6,172,890</b>
Capital lease obligations, non-current (note 10)	7,904	14,725
Preferred shares, subject to redemption (note 12)	-	1,389,593
Long-term debt (note 12)	5,050,000	-
	<b>6,354,137</b>	<b>7,577,208</b>
<b>Shareholders' Equity (Deficiency)</b>		
Common shares (notes 13, 14 & 15)	24,341,938	2,000,813
Preferred shares (note 12)	-	19,065,033
Warrants (notes 13 & 16)	344,949	456,615
Contributed surplus (note 17)	199,767	38,956
Accumulated deficit	(28,612,808)	(27,225,220)
	<b>(3,726,154)</b>	<b>(5,663,803)</b>
	<b>2,627,983</b>	<b>1,913,405</b>

Nature of operations and going concern (note 1)

Commitments (note 20)

Approved by the Board of Directors

*"Bruno Maruzzo"*

**Bruno Maruzzo**

**Chairman of the Audit Committee**

*"Dean Gendron"*

**Dean Gendron**

**Director**

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

**Hamilton Thorne Ltd**  
**Consolidated Statements of Operations and Comprehensive Loss**  
For the years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

	2009	2008
<b>Sales</b>	<b>4,794,693</b>	5,757,406
<b>Cost of sales</b>	<b>1,769,658</b>	2,037,313
	<b>3,025,035</b>	3,720,093
<b>Expenses</b>		
Research and development	<b>843,948</b>	814,097
Sales and marketing	<b>1,938,541</b>	2,267,597
General and administrative	<b>1,551,157</b>	1,386,007
	<b>4,333,646</b>	4,467,701
Loss from operations	<b>(1,308,611)</b>	(747,608)
Other income (expense)		
Interest expense including accretion (notes 9, 10, 11 & 12)	<b>(367,191)</b>	(468,607)
Interest income	<b>867</b>	1,253
Loss from continuing operations	<b>(1,674,935)</b>	(1,214,962)
Loss from discontinued operations (note 2)	-	(26,277)
<b>Net loss and comprehensive loss for the year</b>	<b>(1,674,935)</b>	(1,241,239)
Loss per share		
Basic	\$ (0.10)	\$ (0.08)
Diluted	\$ (0.10)	\$ (0.08)
Weighted average number of common shares outstanding		
Basic	17,504,453	16,035,067
Diluted	17,513,961	16,035,067

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

**Hamiton Thorne Ltd**  
**Consolidated Statements of Shareholders' Equity (Deficiency)**

*For the Years Ended December 31, 2009 and 2008*

*(Expressed in U.S. Dollars)*

	Common Shares		Preferred Shares		Warrants	Contributed Surplus	Accumulated Deficit	Total
	Shares	Dollars	Shares	Dollars				
<b>December 31, 2007</b>	<b>8,500</b>	<b>2,000,813</b>	<b>28,610</b>	<b>18,247,257</b>	<b>456,615</b>	-	<b>(25,958,914)</b>	<b>(5,254,229)</b>
Stock based compensation (note 17)	-	-	-	-	-	38,956	-	38,956
Spin-off of molecular biology business and related change in redemption value (note 2)	-	-	-	817,776	-	-	(25,067)	792,709
Net loss	-	-	-	-	-	-	(1,241,239)	(1,241,239)
<b>December 31, 2008</b>	<b>8,500</b>	<b>2,000,813</b>	<b>28,610</b>	<b>19,065,033</b>	<b>456,615</b>	<b>38,956</b>	<b>(27,225,220)</b>	<b>(5,663,803)</b>
Stock based compensation (note 17)	-	-	-	-	-	33,980	-	33,980
Issuance of shares in private placement, net of expenses (note 13)	13,957	903,775	-	-	271,035	-	-	1,174,810
Issuance of shares to settle debt (notes 11 & 13)	4,142	475,000	-	-	-	-	-	475,000
Issuance of agent options (note 13)	-	(73,914)	-	-	73,914	-	-	-
Conversion of preferred shares (note 13)	35,355	20,579,562	(28,610)	(19,065,033)	-	-	-	1,514,529
Exercise of warrants (note 16)	8,911	456,702	-	-	(456,615)	-	-	87
<b>Balances - pre-merger and prior to recording loss for the year</b>	<b>70,865</b>	<b>24,341,938</b>	<b>-</b>	<b>-</b>	<b>344,949</b>	<b>72,936</b>	<b>(27,225,220)</b>	<b>(2,465,397)</b>
Calotto Capital equity balances pre-merger (note 3)	22,211,925	1,569,214	-	-	-	157,412	(941,449)	785,177
Calotto Capital shares consolidated on the basis of one share for every 7.712255 share outstanding (note 3)	(19,331,840)	-	-	-	-	-	-	-
Reverse takeover adjustment (note 3)	-	(1,569,214)	-	-	-	(157,412)	1,726,626	-
Issued to shareholders of HTI pursuant to merger agreement (note 3)	21,464,207	-	-	-	-	-	-	-
Reverse takeover costs incurred (note 3)	-	-	-	-	-	-	(497,830)	(497,830)
Stock based compensation (note 17)	-	-	-	-	-	126,831	-	126,831
Net loss	-	-	-	-	-	-	(1,674,935)	(1,674,935)
<b>December 31, 2009</b>	<b>24,415,157</b>	<b>24,341,938</b>	<b>-</b>	<b>-</b>	<b>344,949</b>	<b>199,767</b>	<b>(28,612,808)</b>	<b>(3,726,154)</b>

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

**Hamilton Thorne Ltd**  
**Consolidated Statements of Cash Flows**  
*For the years ended December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

	2009	2008
<b>Cash flows from operating activities</b>		
Net loss for the year	(1,674,935)	(1,241,239)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	113,136	134,325
Non-cash interest expense/accretion	124,936	175,064
Share-based compensation expense	160,811	38,956
Changes in non-cash operating assets and liabilities:		
Accounts receivable	458,364	(24,883)
Inventories	120,912	75,390
Prepaid expenses and other current assets	(28,378)	52,163
Other assets	(2,878)	4,710
Accounts payable and accrued liabilities	68,356	(70,342)
Deferred revenue	13,499	7,101
	<b>(646,177)</b>	<b>(848,755)</b>
<b>Cash flows from investing activities</b>		
Purchase of capital assets	(59,305)	(132,383)
<b>Cash flows from financing activities</b>		
Deferred financing costs	34,913	(34,913)
Proceeds from debt	1,167,195	1,058,113
Payments on debt	(617,183)	(90,031)
Proceeds from exercise of warrants	87	-
Issuance of common share units - net of expenses	1,174,810	-
Net cash acquired in RTO	794,832	-
Reverse takeover costs incurred	(497,830)	-
	<b>2,056,824</b>	<b>933,169</b>
<b>Net Increase (decrease) in cash and cash equivalents</b>	<b>1,351,342</b>	<b>(47,969)</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>5,029</b>	<b>52,998</b>
<b>Cash and cash equivalents, end of year</b>	<b>1,356,371</b>	<b>5,029</b>

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

**Hamilton Thorne Ltd**  
**Notes to the Consolidated Financial Statements**  
*For the years ended December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

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**1. Nature of Operations and Going Concern**

***Nature of Operations***

Hamilton Thorne Ltd. (the "Company" or "HTL") was created on October 28, 2009 by the reverse takeover ("RTO") by Hamilton Thorne, Inc. ("HTI") of Calotto Capital Inc. ("Calotto")(the "Transaction"). Calotto was incorporated under the Business Corporations Act (Ontario) on February 19, 2007 and was classified as a Capital Pool Company as defined in Policy 2.4 of the TSX Venture Exchange (the "Exchange"). Accordingly, Calotto had no assets other than cash and no commercial operations.

Calotto's fiscal year-end previously ended on January 31. Just prior to the RTO, Calotto changed its fiscal year-end to December 31 to coincide with HTI's year-end and changed its name to Hamilton Thorne Ltd.

The Company operates in one reportable segment and its principal business is the development, manufacture and sale of advanced laser systems and instruments for living cell applications in the regenerative medical research and fertility markets.

***Going Concern***

These consolidated financial statements have been prepared on the "going concern" basis, which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

Certain principal conditions and events are prevalent which indicate that there is doubt about the Company's ability to continue as a going concern for a reasonable period of time in future. The Company has incurred substantial recurring losses to date and it reports a shareholders' deficiency at December 31, 2009.

In the future, it may be necessary for the Company to raise additional funds to fund expanding sales and continued development and introduction of new products to its family of products. To date the Company has raised financing through successive sales of equity, bridge financings and expanding bank loans.

The consolidated financial statements have been prepared on a going concern basis and do not include any adjustments to the amounts and classifications of the assets and liabilities that might be necessary should the Company be unable to continue in business. If the "going concern" assumption were not appropriate for these consolidated financial statements then adjustments would be necessary to the carrying value of assets and liabilities, the reported expenses and the balance sheet classifications used.

**Hamilton Thorne Ltd**  
**Notes to the Consolidated Financial Statements**  
*For the years ended December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

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**2. Spin-off**

On May 5, 2008, the Company completed the spin-off of its molecular biology business to Thorne Diagnostics, Inc. ("TDI"), a newly formed corporation (the "Spin-off"). In consideration of the transfer of certain assets, including certain contracts and license agreements, historical data, intellectual property and five employees, TDI issued shares of common and preferred stock to the Company. These shares were immediately distributed to the Company's shareholders on a pro-rata basis in the form of a dividend. The Company did not recognize any gain or loss on the spin-off as the fair value of the shares received from TDI approximated the fair value of the assets, contracts and agreements transferred. The spin-off was undertaken as the molecular biology business was not a strategic fit with the Company's core equipment business.

The molecular biology business never generated any revenues and the net loss from the discontinued operations for the year ended December 31, 2008 was \$26,277 which includes only amounts recorded through May 5, 2008, the date of the spin-off. The reported loss consisted primarily of research and development and payroll expenses offset by the reversal of an accrual relating to termination pay for an employee of TDI. The financial results for the molecular biology business is reported as a single line item in "Loss from discontinued operations" for the year ended December 31, 2008. Net assets of the molecular biology business were \$25,067 at May 5, 2008 and consisted primarily of property and equipment net of the accrual above.

**3. Reverse Takeover Accounting**

Pursuant to the terms of the Merger Agreement, dated October 12, 2009, HTI became a wholly owned subsidiary ("legal subsidiary") of the Company and 303.89 common shares of HTL were issued in exchange for each common share of HTI outstanding. In addition, all warrants and options of HTI outstanding were similarly converted into warrants and options to purchase common shares of HTL at the same 303.89 conversion rate, on economically equivalent terms and conditions.

Prior to the effective date of the transaction, Calotto undertook a consolidation of its common shares in a ratio of 1 for 7.712255, thereby reducing the common shares outstanding from 22,211,925 shares to 2,880,085 shares. Similarly, options to purchase common shares outstanding were reduced from 2,220,001 to 287,854. In addition, immediately preceding the RTO, HTI raised gross proceeds of \$2,065,107 (Cdn\$2,200,000), including conversion of debt of \$475,000 (Cdn\$503,500) in a brokered private placement, issuing units consisting of one share of common stock and a warrant to purchase one share of common stock priced at Cdn\$121.556 (\$114.675) per unit (see note 13). The costs, including agent's commission and expenses, of the private placement amounted to \$415,297.

The transaction was effective October 28, 2009 and has been accounted for as an RTO transaction in accordance with guidance provided in Emerging Issues Committee Abstract No. 10 - Reverse Takeover Accounting (EIC 10). As Calotto did not qualify as a business for accounting purposes, according to the definition in Emerging Issues Committee Abstract No. 124 - Definition of a Business (EIC-124) the transaction has been accounted for as an issuance of shares by HTI for the net monetary assets of Calotto followed by a recapitalization of HTI.

The net assets of the Company received were as follows:

Cash	794,832
Less current liabilities	<u>9,655</u>
Net assets acquired	<u>785,177</u>

**Hamilton Thorne Ltd**  
**Notes to the Consolidated Financial Statements**  
*For the years ended December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

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**3. Reverse Takeover Accounting** *(Continuing from previous page)*

Pursuant to the RTO transaction, the financial statements for the year ended December 31, 2009 reflect the assets, liabilities and results of operations of HTI prior to the RTO. The consolidated assets, liabilities and results of operations of Calotto and HTI are included subsequent to the RTO. The consolidated financial statements are issued under the the legal parent (the Company), but are deemed to be a continuation of the legal subsidiary. Net loss per share has also been adjusted for all periods presented in accordance with the guidance provided in EIC Abstract No. 10. Accordingly, the shares issued in respect of the private placement and the settlement of the debt in the current year have not been included in the calculation of basic and fully diluted earnings per share in the prior year.

The costs of the RTO amounted to \$497,830. Under the provisions of EIC-10 these costs are to be charged to retained earnings to the extent of cash in the non-operating public company (Calotto), with the excess, if any, to be charged as an expense. At the time of the closing of the transaction Calotto had \$794,832 in cash; therefore the entire amount of the transaction costs have been charged to accumulated deficit.

The Company changed its fiscal year end from January 31 to December 31 as a result of the RTO.

**4. Significant Accounting Policies**

These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP").

The financial statements as at December 31, 2008 and for the year then ended were originally prepared in accordance with generally accepted accounting principles in the United State of America. The change in the basis of accounting required the reclassification of preferred shares, subject to redemption, from equity to liabilities on the balance sheet. In addition, the dividends related to preferred shares, subject to redemption, were reclassified to interest expense rather than a distribution in the statement of shareholders' equity (deficiency).

The significant accounting policies followed by the Company are as follows:

***Principles of Consolidation***

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary Hamilton Thorne, Inc. All significant inter-company balances and transactions have been eliminated on consolidation. The Company has no interest in variable interest entities.

***Use of Estimates***

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting periods. Significant items subject to estimates and assumptions include, but are not limited to, the estimated useful life of assets, inventory obsolescence, the measurement and determination of stock-based compensation and warrants, legal liabilities, warranty provision, bad debt expense, and allowance for doubtful accounts. Actual results could differ from those estimates. Significant changes in the assumptions with respect to future business plans and cash flows could result in impairment of intangible assets and property and equipment. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

**4. Significant Accounting Policies** *(Continuing from previous page)*

***Cash and Cash Equivalents***

Cash and cash equivalents include demand deposits held with banks. Cash equivalents are carried at fair value and accounts are subject to any withdrawal restrictions or penalties.

***Inventories***

Inventories are measured at the lower of cost and net realizable value. Costs of inventory are calculated on an average cost basis. In determining net realizable value, the Company considers factors such as current selling price, product lifecycle and future sales volumes. Allowances for slow-moving or obsolete inventory are recorded when considered appropriate.

***Property and Equipment***

Property and equipment are recorded at cost and are amortized over their estimated useful lives using the following methods and rates:

Machinery and equipment	2-5 years straight line
Leasehold improvements	Term of the lease, straight line
Furniture and fixtures	5-10 years straight line

***Capital Leases***

The Company's policy is to record leases, which transfer substantially all benefits and risks incidental to ownership of property, as acquisition of property and equipment and to record the corresponding obligations as liabilities. Obligations under capital leases are reduced by rental payments, net of imputed interest.

***Impairment of Long-lived Assets***

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Management reviews the carrying value of the assets and considers whether an impairment charge should be recorded. The review is based on the assessment of technological changes; the Company's intended use and on the projected estimated undiscounted cash flows expected to be generated from the underlying assets. Any impairment results in an impairment of the assets and a charge to income during the year to the extent that the asset's carrying value exceeds its fair value, generally determined on a discounted cash flow basis.

***Revenue Recognition***

The Company recognizes revenue from product sales upon shipment (provided there is persuasive evidence of an arrangement), when there are no uncertainties surrounding acceptance, when collection is considered probable, when the sales price is fixed or determinable and only perfunctory Company obligations included in the arrangement, if any, remain to be completed.

**4. Significant Accounting Policies** *(Continuing from previous page)*

The Company also sells service contracts for service and maintenance of the underlying product beyond the warranty period. The Company defers revenue upon entering into the agreement and recognizes revenue ratably over the contract period. Unrecognized revenue at year end is shown on the balance sheet as deferred revenue.

***Research and Development***

Research costs are expensed as incurred. Development costs are charged to operations as incurred unless such costs meet all criteria under GAAP for deferral and amortization. No development costs have been deferred to date.

***Income Taxes***

The Company follows the asset and liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on the differences between the basis for assets and liabilities on the balance sheet and their corresponding tax values, using the substantively enacted tax rates and laws that are expected to be in effect when the differences are expected to be realized or settled. A valuation allowance is recorded to recognize tax benefits only to the extent that, based on available evidence, it is more likely than not that they will not be realized.

***Financial Instruments - Recognition and Measurement***

The Company classifies financial assets and liabilities as held-for-trading, available-for-sale, held-to-maturity, loans and receivables or other financial liabilities depending on their nature. Financial assets and financial liabilities are all recognized at fair value on their initial recognition, except for those arising from certain related party transactions which are accounted for at the transferor's carrying amount or exchange amount in accordance with the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3840, Related Party Transactions.

Financial assets and liabilities classified as held-for-trading are measured at fair value, with gains and losses recognized in net income/loss. Cash and cash equivalents are classified as held-for-trading. Financial assets classified as available-for-sale are measured at fair value, using quoted market prices when available, with unrealized gains and losses being recognized as other comprehensive income until realized. Investments in private companies are recorded at cost as reliable fair market value is not available for such investments. If an unrealized loss is considered other than temporary, the unrealized loss is recorded in net income/loss. Short-term investments and investments are classified as available-for-sale.

Financial assets classified as loans and receivables are measured at amortized cost, using the effective interest rate method of amortization. The carrying amount of trade receivables and other receivables is a reasonable approximation of fair value due to the short-term nature of these financial instruments.

Other financial liabilities are measured at amortized cost, using effective interests rate method of amortization. The carrying amount of the accounts payable is a reasonable approximation of fair value due to the short-term nature of this financial instrument. The carrying value of the long-term debt and convertible debentures approximates their fair value and the carrying value of the convertible debentures is being accreted to its face value over the term of the debentures such that they will be recorded at their full value when they become due and payable in less than a year.

**4. Significant Accounting Policies** *(Continuing from previous page)*

The Company has elected to account for transaction costs related to the issuance of financial instruments as a reduction of the carrying value of the related financial instruments.

The fair value of these financial instruments is described in note 22.

***Comprehensive Income***

The Company had no other comprehensive income or loss transactions during the years ended December 31, 2009 and 2008.

***Stock-Based Compensation***

The Company has a stock-based compensation plan, which is described in note 17. The Company uses the fair value method to account for stock options granted to employees, directors and consultants, determined utilizing the Black-Scholes option pricing model. Options issued to employees, directors and consultants are recognized as an expense over the vesting period and the offset is credited to contributed surplus. Any consideration paid on exercise of stock options would be credited to share capital and the related contributed surplus transferred to share capital.

***Loss Per Share***

Basic loss per share is calculated by dividing the loss for the period by the weighted average number of common shares outstanding during the period. The diluted loss per share is calculated using the treasury stock method. Under this method, the dilutive effect on loss per share is recognized on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the year.

**5. Changes in Accounting Policies**

***Capital Disclosures***

Handbook Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such noncompliance. The Company has included disclosures recommended by the new Handbook section in note 21 to these financial statements.

***Goodwill and Intangible Assets and Research and Development Costs***

The CICA approved Handbook Section 3064, "Goodwill and Intangible Assets" which replaces the existing Handbook Sections 3062, "Goodwill and Other Intangible Assets" and 3450, "Research and Development Costs". This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2008, with earlier application encouraged. The standard provides guidance on the recognition, measurement and disclosure requirements for goodwill and intangible assets. There is no significant impact on adoption of the standard on the Company's financial statements.

**5. Changes in Accounting Policies** *(Continuing from previous page)*

***Fair value measurements***

In June 2009, the Canadian Institute of Chartered Accountants amended Section 3862 Financial Instruments – Disclosures to include enhanced disclosures relating to fair value measurements. The amendment establishes new requirements for disclosing fair value measurements recognized in the balance sheet using a three-tier fair value hierarchy based on the lowest level input that is significant to that fair value measurement.

This amendment is effective for annual financial statements relating to fiscal years ending after September 30, 2009. The adoption of these changes did not have a material impact on the Company's consolidated financial statements.

***Liquidity risk***

In June 2009, the Canadian Institute of Chartered Accountants amended Section 3862 Financial Instruments – Disclosures to include enhanced disclosures relating to liquidity risk in response to current market conditions. The amendment establishes new requirements for disclosing maturity analysis for derivative and non-derivative financial liabilities based on how the Company manages its liquidity risk.

This amendment is effective for annual financial statements relating to fiscal years ending after September 30, 2009. The adoption of these changes did not have a material impact on the Company's consolidated financial statements.

**6. New Accounting Pronouncements**

***Business Combinations***

Section 1582, Business Combinations, replaces Section 1581, Business Combinations. The section establishes standards for the accounting for a business combination. It provides the Canadian equivalent to the IFRS standard, IFRS 3 (Revised), Business Combinations. The section applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. The new standard is not expected to have a material effect on the Company's consolidated financial statements.

***Consolidated Financial Statements***

Section 1601, Consolidated Financial Statements and Section 1602, Non-Controlling Interests, together replace Section 1600, Consolidated Financial Statements. 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. It is equivalent to the corresponding provisions of IFRS standard, IAS 27 (Revised), Consolidated and Separate Financial Statements. The sections apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier adoption is permitted as of the beginning of a fiscal year. The Company is currently evaluating the impact of the adoption of these new sections on the consolidated financial statements.

**6. New Accounting Pronouncements** *(Continuing from previous page)*

***EIC-175***

In December 2009, the CICA issued EIC 175, Multiple Deliverable Revenue Arrangements, replacing EIC 142, Revenue Arrangements with Multiple Deliverables. The accounting changes summarized in EIC-175 are effective for fiscal years beginning on or after January 1, 2011, with early adoption permitted. Adoption may either be on a prospective basis or by retrospective application. If the Abstract is adopted early, in a reporting period that is not the first reporting period in the entity's fiscal year, it must be applied retroactively from the beginning of the Company's fiscal period of adoption. The Company is currently assessing the future impact of these amendments on its consolidated financial statements and has not yet determined the timing and method of adoption.

***International Financial Reporting Standards***

In February 2008, Canada's Accounting Standards Board (AcSB) confirmed that Canadian GAAP, as used by publicly accountable enterprises, will be fully converged into IFRS, as issued by the International Accounting Standards Board (IASB). The changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Therefore, the Company will be required to report under International Financial Reporting Standards ("IFRS") no later than in the first quarter of 2011, with restatement of comparative information. The conversion to IFRS will impact the Company's accounting policies, systems, disclosures and controls.

The Company completed the planning phase of its changeover plan in the fourth quarter of 2009 and is currently in a detailed assessment phase. The Company has identified the following phases of its conversion plan: preliminary impact assessment, detailed analysis and implementation. A diagnostic of the potential areas of impact has been undertaken and is currently being reviewed. A team has been identified to undertake the impact assessment and detailed analysis which will result in new accounting policies, quantification of statement impacts and preparation of pro-forma financial statements. Implementation will include the design of systems and reporting processes to support the conversion and training to sustain IFRS financial data and processes for 2011 and beyond.

**7. Inventories**

Inventories are stated at the lower of cost and net realizable value using the average cost method. Inventories are reviewed periodically for slow-moving or obsolete status based on sales activity, both projected and historical, and allowances are established for inventory that is determined to be excess or obsolete. During the year, the Company increased its allowance by \$32,000 (\$2,000 in 2008). No write down of inventories was recorded during 2009 (\$10,000 in 2008). Included in cost of sales are inventory costs of \$1,225,440 (\$1,447,345 in 2008).

	<b>2009</b>	<b>2008</b>
Raw materials and purchased parts	<b>497,514</b>	572,669
Work-in-progress	-	19,019
Finished goods	<b>14,786</b>	41,524
	<b>512,300</b>	633,212

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**8. Capital Assets**

Capital assets consist of the following at December 31:

	<i>Cost</i>	<i>2009 Accumulated Depreciation</i>	<i>Net Book Value</i>
Machinery and equipment	1,043,209	956,910	86,299
Furniture and fixtures	94,508	93,071	1,437
Leasehold improvements	35,129	32,384	2,745
	<b>1,172,846</b>	<b>1,082,365</b>	<b>90,481</b>

	<i>Cost</i>	<i>2008 Accumulated Depreciation</i>	<i>Net Book Value</i>
Machinery and equipment	984,597	859,974	124,623
Furniture and fixtures	94,508	91,786	2,722
Leasehold improvements	35,129	30,554	4,575
	<b>1,114,234</b>	<b>982,314</b>	<b>131,920</b>

**9. Notes Payable**

	<i>2009</i>	<i>2008</i>
Notes payable under bank line of credit	-	4,970,000
Notes payable, officers	56,006	56,069
Note payable, shareholder	25,000	25,000
Note payable, other	2,031	-
Total notes payable	<b>83,037</b>	5,051,069

**Notes payable under bank line of credit**

In October 2007, the Company consolidated two separate line of credit agreements with different banks into a line of credit with one financial institution. The agreement provides for a maximum borrowing of \$5,000,000. Borrowings under the agreement were payable on demand until September 30, 2009 when the agreement was amended to establish a loan termination date of October 1, 2011. Accordingly, the notes were reclassified to long term debt at December 31, 2009 (see note 11).

**Notes payable, officers**

See Note 23 Related Party Transactions for information on Notes payable, officers

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**9. Notes Payable** *(Continuing from previous page)*

**Note payable, shareholder**

In October 2006 a shareholder advanced the Company \$50,000 in return for a promissory note payable upon demand with interest at the prime rate (3.25% at December 31, 2009), plus 1%. In November 2006, \$25,000 of principal was repaid leaving \$25,000 outstanding at December 31, 2009 and 2008.

**Note payable, other**

During 2009 and 2008, the Company financed certain of its insurance premiums through installment notes with an insurance financing company. The Company financed \$17,714 and \$44,107 during the 2009 and 2008, respectively. The balances due as of December 31, 2009 and 2008 were \$2,031 and \$0, respectively.

**10. Capital Lease Obligations**

In January 2008, the Company entered into a financing lease to fund the purchase of software. The lease is payable over 48 months with a monthly payment of \$713. The following is a schedule by year of future minimum lease payments together with the present value of the lease payments as of December 31, 2009:

2010	8,552
2011	7,127
<hr/>	
Total minimum capital lease payments	15,679
Less amount representing interest	2,022
<hr/>	
Present value of minimum capital lease payments	13,657
Less current portion	5,753
<hr/>	
Non-current portion	7,904
<hr/>	

For the years ended December 31, 2009 and 2008, interest expense relating to the capital lease totaled \$3,021 and \$3,470, respectively.

**11. Long-term Debt**

	<b>2009</b>	<b>2008</b>
Notes payable under bank line of credit	<b>5,000,000</b>	-
Subordinated convertible note payable, shareholder	<b>50,000</b>	-
<hr/>		
Total long-term debt	<b>5,050,000</b>	-
<hr/>		

**11. Long-term Debt** *(Continuing from previous page)*

**Notes payable under bank line of credit**

As disclosed in Note 9, the notes provide for a maximum borrowing of \$5,000,000 and mature on October 1, 2011. The notes bear interest at the LIBOR 30 Day Index Rate plus 2% or lender's base rate less one-half percent based on the date of the borrowing at the borrower's election, but in no case will the rate be less than four percent per annum. As of December 31, 2009, borrowings totaled \$5,000,000 with interest at 4% and were classified as long-term debt on the balance sheet. Borrowings under the agreement are collateralized by substantially all the Company's assets and by letters of credit provided by two stockholders. The Company is in compliance with the one financial covenant in the agreement.

**Subordinated convertible note payable, shareholder**

A shareholder provided financing in the amount of \$400,000 to the Company in increments of \$100,000 in each of March, May, June and August of 2009 in the form of subordinated convertible notes, payable two years from the date of the note. The notes were convertible, at the option of the holder, in the next round of equity financing that raised a minimum of \$1.5 million (exclusive of the noteholders participation in the equity financing) at the same terms and conditions as other investors participating in the equity financing. In August and September 2009 a then director of the Company lent the Company \$75,000 and \$50,000, respectively, on subordinated convertible notes under the same terms and conditions as the four \$100,000 notes above. All these notes were subordinated to the Company's bank line of credit. In October 2009 immediately preceding the RTO, \$475,000 of these notes were converted to equity as part of the private placement (see note 13 below).

**12. Preferred Shares**

Immediately preceding the RTO in 2009 (see Note 3), all the preferred shares of Hamilton Thorne, Inc. ("HTI") were converted into common shares of HTI and were exchanged for a total of 10,744,034 common shares of the Company. The information as to numbers of shares and prices presented in this note refer to the terms of the preferred shares of HTI.

HTI was authorized to issue 200,000 shares of common and preferred stock with a par value of \$.01 of which 166,378 shares were common stock and 33,622 shares were preferred stock (the "Preferred Stock"). The authorized Preferred Stock was comprised of 6,243 shares designated as Series A Preferred Stock (the "Series A Preferred"), 8,676 shares designated as Series B Preferred Stock (the "Series B Preferred"), 12,894 shares designated as Series C-1 Preferred Stock (the "Series C-1 Preferred") and 5,809 shares designated as Series C-2 Preferred Stock (the "Series C-2 Preferred").

The Series A Preferred and Series B Preferred were convertible at any time at the option of the holder into shares of common stock, on a one for one basis, subject to adjustment, as defined in the agreement. Dividends were payable at the same rate (on an equal per share basis) as dividends are paid with respect to the common stock.

**12. Preferred Shares** *(Continuing from previous page)*

***Series C Preferred***

In December 2006 HTI entered into a Preferred Stock Purchase Agreement and amended its articles of incorporation authorizing 24,000 shares of Series C Redeemable Convertible Preferred Stock, \$.01 par value (the "Series C Preferred") (the "Series C Preferred Stock Agreement"). The Series C Preferred Stock Agreement was for the sale of 5,809 shares of the Company's Series C-2 Preferred at a price of \$430.40 per share for total proceeds of approximately \$2,500,000. In addition, HTI issued 11,789 shares of Series C-1 Preferred in exchange for approximately \$5,420,000 of debt and related accrued interest. In May 2008 HTI further amended its articles of incorporation reducing to 18,703 the number of authorized shares of Series C Preferred.

***Redeemable Preferred***

Shares of the Series C-2 Preferred were redeemable on December 14, 2011 upon the written notice of at least 50% of the shareholders of the Series C-2 Preferred. As a result of the spin-off the redemption price for the Series C-2 Preferred was reduced to \$279.76 per share (\$430.40 prior to May 13, 2008) plus all accrued and unpaid dividends. Accordingly, the Company provided \$817,776 as a charge to the Series C-2 Redeemable Preferred during 2008.

***Conversion***

Each share of Series A, Series B and Series C Preferred was convertible at the option of the holder thereof at any time into one share of common stock. The conversion feature for the Series C Preferred was subject to adjustment including, but not limited to, adjustment for dilutive issuances. Prior to the issuance of certain warrants in 2007 (See Note 16), the Series C-1 and Series C-2 Preferred were convertible into 11,789 and 5,809 shares of common stock, respectively, and after the issuance of the warrants, the Series C-1 and Series C-2 Preferred were convertible into 13,689 and 6,745 shares, respectively.

***Dividends***

The holders of shares of Series C-1 Preferred and Series C-2 Preferred were entitled to receive, out of any assets legally available, on a *paripassu* basis and prior and in preference to any declaration or payment of any dividend (payable other than in common stock) on the common stock, Series A Preferred or Series B Preferred. The Series C-1 Preferred and The Series C-2 Preferred accrued cumulative dividends at the rate of \$31.90 per share per annum (\$49.08 prior to May 13, 2008) for each share of the Series C-1 Preferred and \$22.38 per share per annum (\$34.43 prior to May 13, 2008) for each share of the Series C-2 Preferred. Dividends on the Series C Preferred accumulated but did not compound and the declaration and payment of any cash dividends were contingent upon, and payable out of, retained earnings. After such dividends, if any, were declared and paid upon the Series C-1 Preferred and Series C-2 Preferred, dividends could have been declared and paid on the Series A Preferred, Series B Preferred and/or common stock in such amounts as may be declared by the board of directors. The declaration and payment of any cash dividends on shares of Series A Preferred, Series B Preferred or common stock was contingent upon, and payable out of, retained earnings.

**12. Preferred Shares** *(Continuing from previous page)*

**Liquidation Preferences**

In the event of liquidation, dissolution, or winding up of the Company's business, the Series C-2 Preferred had a superior liquidation preference to any other class of stock consisting of \$559.52 per share (\$860.80 prior to May 13, 2008), plus all accumulated but unpaid dividends. The Series C-1 Preferred had a liquidation preference of \$797.58 per share (\$1,227.04 prior to May 13, 2008), plus any accumulated and unpaid dividends. Each share of the Series A and Series B Preferred had a liquidation preference in an amount equal to \$351.35 and \$837.63, respectively (\$540.54 and \$1,288.66, respectively, prior to May 13, 2008).

**Voting Rights**

Each holder of shares of the Preferred Stock was entitled to notice of any stockholder meetings in accordance with the by-laws of the Company. Each holder of Preferred Stock was entitled to a number of votes equal to a number of shares of common stock into which the shares of Preferred Stock held by such holder could be converted, had voting rights and powers equal to the voting rights and powers of the holders of common stock and could vote together as a single class with holders of common stock and all series of Preferred Stock on all matters required by law.

**13. Private Placement**

In October 2009, immediately preceding the RTO, HTI completed a brokered private placement whereby HTI issued 13,956.531 (4,241,254 on a post-RTO basis) units (the "Units"). In addition, at the same time \$475,000 of debt was converted into 4,142.124 (1,258,751 on a post-RTO basis) Units. Each Unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share at a price of Cdn\$0.60 (\$0.566) for a period of eighteen months from the date of issuance.

The relative fair value of the warrants included in the private placement units were valued using the Black-Scholes option pricing model using the following fair value assumptions: dividend yield 0%, volatility 65%, expected life 1.5 years and risk free interest of 1%. The fair value of each warrant was \$0.05 and the fair value of the warrants was allocated to warrants in the amount of \$271,035.

The agent for the private placement received an 8% selling commission and options to acquire that number of Units equal to 8% of the number of Units sold pursuant to the offering and of the Units issued in the debt conversion for a total of 440,001 Units (post RTO).

The relative fair value of the agent options were valued using the Black-Scholes option pricing model using the following fair value assumptions: dividend yield 0%, volatility 65%, expected life 1.5 years and risk free interest of 1%. The fair value of each option was \$0.17 and the fair value of the options was allocated to warrants in the amount of \$73,914.

**14. Share Capital**

There are an unlimited number of common shares authorized. The issued and outstanding common shares are disclosed in the Consolidated Statements of Shareholders' Equity (Deficiency).

**15. Escrowed Shares**

Under the requirements of the Ontario Securities Commission and the TSX Venture Exchange, 15,511,613 common shares issued under the November 5, 2009 Qualifying Transaction ("Exchange Notice") and 310,272 options to purchase common shares are subject to Surplus Security Escrow Agreements. 570,523 shares are under a CPC Escrow Agreement and will be released as to 10% on the issuance of the Final Exchange Notice ("Initial Release") and as to 15% on each of the 6, 12, 18, 24, 30 and 36 months following the Initial Release. The remaining 14,941,090 shares and the 310,272 options are under a QT Escrow Agreement and will be released as to 5% on the Initial Release, 5% 6 months following, another 10% on each of the 12 and 18 months following, another 15% on each of the 24 and 30 months following and the final 40% 36 months following the Initial Release.

As at December 31, 2009, 14,707,511 common shares and 294,759 options were held in escrow under these agreements.

**16. Warrants**

During 2007, HTI issued warrants to purchase 7,318 shares (2,223,867 shares on a post-RTO basis) of common stock at \$0.01 per share. These warrants were issued to certain shareholders who provided letters of credit to secure the Company's line of credit. The Company recorded the value of these warrants of \$456,615 as additional interest expense during the year ended December 31, 2007. During 2005 and 2006 HTI issued warrants to purchase a total of 1,416 shares (484,099 shares on a post-RTO basis) of common stock at \$0.01 per share in conjunction with a bridge financing commenced in December 2005. The fair value of these warrants was deemed to be immaterial by management. During 2007 1,105 (335,798 warrants on a post-RTO basis) of the warrants were replaced with warrants to purchase 1,105 shares of Series C-1 Preferred at \$0.01 per share. Immediately preceding the RTO, all of these warrants were exercised to purchase HTI common shares totaling 2,707,966 shares on a post-RTO basis leaving none outstanding.

See Note 13 – Private Placement for warrants issued in the private placement and in conjunction with the debt conversion. All the 5,500,005 warrants and 440,001 agent options expire on April 28, 2011 and are outstanding at December 31, 2009.

**17. Stock Option Plans**

***2001 and 2007 Stock Option Plans of HTI***

HTI adopted the 2001 Stock Option Plan in May 2001 and the 2007 Stock Option Plan was adopted on April 24, 2007, collectively the "Plans". The Plans provided for the granting of incentive stock options and non-qualified stock options to directors, employees, consultants, and independent contractors who were employed by or perform services for HTI. The exercise prices and vesting schedules applicable to each option grant were determined by the board of directors or a committee thereof. At December 31, 2008, 8,996 options (2,733,794 on a post-RTO basis) were available for future grant under the Plans. Options generally vested over three years. Upon completion of the RTO, the HTI plans were terminated and each HTI stock option was cancelled and the holder received a replacement option of the Company under the 2009 Plan for the equivalent number of post-RTO shares at the original option price adjusted for the increase in the number of shares.

***2007 Stock Option Plan of Calotto***

Calotto adopted the 2007 Stock Option Plan (the "2007 Plan") on July 20, 2007. Under the 2007 Plan, the board of directors of Calotto may from time to time, in its discretion, and in accordance with the Exchange requirements, grant to directors, officers and technical consultants to Calotto, non-transferable Calotto Options to purchase Common Shares, exercisable for a period of up to five years from the date of grant. The number of Common Shares reserved for issuance under the 2007 Plan is equal to 287,854 Common Shares on a post-RTO basis.

The number of common shares reserved for issuance to any individual director or officer under the 2007 Plan may not exceed 5% of the issued and outstanding common shares and the number of common shares reserved for issuance to all technical consultants under the 2007 Plan may not exceed 2% of the issued and outstanding common shares. Options may be exercised no later than 90 days following cessation of the optionee's position with Calotto, provided that if the cessation of office, directorship, or technical consulting arrangement was by reason of death, the option may be exercised within a maximum period of one year after such death, subject to the expiry date of such option. If an optionee shall cease to be a director of Calotto upon Calotto successfully completing its Qualifying Transaction, then all unexercised options granted to such optionee shall expire one year from the date of the Final Exchange Bulletin issued by the Exchange in connection with such Qualifying Transaction which was November 5, 2009.

At December 31, 2009, there are 287,854 Calotto options outstanding, exercisable into 287,854 common shares under the 2007 Plan at an exercise price of Cdn\$0.7712255 per share that were all granted in 2007. There were no options granted, forfeited or terminated during 2008 or 2009. Options for 99,260 shares expire on July 20, 2012 and options for 188,594 shares will expire on November 5, 2010 due to termination of participants because of the completion of Calotto's Qualifying Transaction. No further options may be granted under the 2007 Plan.

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**17. Stock Option Plans** (Continuing from previous page)

**2009 Stock Option Plan**

On August 4, 2009 the Company adopted the 2009 Stock Option Plan (the "2009 Plan"). Under the 2009 Plan, the board of directors of the Company may from time to time, in its discretion, and in accordance with the Exchange requirements, grant to directors, employees, consultants and consultant companies options to purchase common shares, exercisable for a period of up to ten years from the date of grant. The 2009 Plan was approved by the shareholders of the Company in August 2009 and 3,431,830 shares are reserved for issuance under the 2009 Plan. As of December 31, 2009 there are 431,080 options available for future grants.

The number of common shares reserved for issuance to any individual director or officer under the 2009 Plan may not exceed 5% of the issued and outstanding common shares and the number of common shares reserved for issuance to all consultants under the 2009 Plan may not exceed 2% of the issued and outstanding common shares. Options may be exercised no later than 90 days following cessation of the optionee's position with the Company, provided that if the cessation of a participant was by reason of death or disability, the option may be exercised within a maximum period of one year after such death, subject to the expiry date of such option. Options granted may be "incentive stock options" for US participants. The exercise price per share shall be based on the closing sale price traded on an exchange on the first business day preceding the date of grant.

Information regarding stock option activity under the 2007 and 2009 Plans follows:

	<b>2007 Plan</b>		<b>2009 Plan</b>	
	<b>Number of Options</b>	<b>Weighted Average Exercise Price in Cdn \$</b>	<b>Number of Options</b>	<b>Weighted Average Exercise Price in Cdn \$</b>
Options outstanding at December 31, 2007	287,854	0.7712	387,764	0.2176
Granted	-	-	310,272	0.2176
Exercised or forfeited	-	-	-	-
Options outstanding at December 31, 2008	287,854	0.7712	698,036	0.2176
Granted	-	-	2,302,714	0.40
Exercised or forfeited	-	-	-	-
Options outstanding at December 31, 2009	287,854	0.7712	3,000,750	0.3576
Options exercisable at December 31, 2008	287,854	0.7712	222,859	0.2176
Options exercisable at December 31, 2009	287,854	0.7712	1,000,215	0.317

The weighted average grant date fair value of options granted in 2009 was \$0.19 (\$0.17 in 2008)

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**17. Stock Option Plans** *(Continuing from previous page)*

The fair value of options granted was determined using the Black-Scholes option pricing model with a weighted average volatility of 65% (2008 - 100%), risk-free interest rate of 3%, dividend yield of nil and an expected life of 6.25 years. Volatility was estimated by using the historical volatility of other companies that the Company considers comparable that have trading and volatility history. The expected life represents the period of time that options granted are expected to be outstanding. The risk-free rate is based on the US Treasury notes rates with a term similar to the expected life of the options.

The Company recorded stock-based compensation expense of \$160,811 and \$38,956 during the years ended December 31, 2009 and 2008, respectively. Amounts included in Research and development expenses totaled \$21,598 for 2009 (\$23,399 in 2008) with the balance included in General and administrative expenses.

At December 31, 2009, the following stock options were outstanding under the 2007 and 2009 Plans:

Expiration date	Exercise Price in Cdn \$	Number of Options Outstanding	Number of Options Exercisable	Weighted Average Life Remaining In Years
November, 2010	0.7712255	188,594	188,594	0.8
July, 2012	0.7712255	99,260	99,260	2.6
November, 2017	0.2176	387,764	258,914	7.9
January, 2018	0.2176	310,272	196,348	8.1
November, 2019	0.40	2,302,714	544,953	9.9
		3,288,604	1,288,069	8.7

**18. Segmented Information and Major Customers**

The Company's operations are comprised of a single reporting segment engaged within the United States. As such, the amounts reported and disclosed in the financial statements for sales, net loss, depreciation and total assets also represent segmented amounts.

The Company had sales to two customers that exceeded 10% of revenues in each of the years ended December 31, 2009 and 2008. Aggregate sales to the two customers were approximately \$1.2 million (25.6%) and \$1.5 million (25.9%) for the years ended December 31, 2009 and 2008, respectively.

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**19. Income Taxes**

A reconciliation of the differences between the statutory U.S. federal income tax expense (benefit) and the Company's effective tax expense at December 31 is as follows:

	<b>2009</b>		<b>2008</b>	
	<b>Tax Amount</b>	<b>Effective Rate</b>	<b>Tax Amount</b>	<b>Effective Rate</b>
Federal at statutory rates	<b>(569,478)</b>	<b>34.00%</b>	(422,021)	34.00%
State income taxes, net of federal benefit	<b>116,728</b>	<b>(7.07%)</b>	115,469	-9.30%
Permanent items:				
Interest on redeemable preferred shares	<b>42,477</b>	<b>(2.57%)</b>	59,936	-4.83%
Deferred assets transferred in spinout	-	-	242,546	-19.54%
Other permanent differences	<b>27,273</b>	<b>(1.13%)</b>	17,186	-1.38%
Change in valuation allowance	<b>383,000</b>	<b>(23.23%)</b>	(13,116)	1.05%
Income tax expense (recovery)	-	-	-	-

The significant components of the Company's future income tax assets are as follows at December 31:

	<b>2009</b>	<b>2008</b>
Future income tax assets		
Benefits of loss carryforwards	<b>8,910,000</b>	8,410,000
Warrants	-	183,000
Stock-based compensation	<b>58,000</b>	15,000
Capital assets	<b>70,000</b>	56,000
Other assets	<b>47,000</b>	38,000
Future tax assets	<b>9,085,000</b>	8,702,000
Less: Valuation allowance	<b>(9,085,000)</b>	(8,702,000)
Net future taxes	-	-

As a result of losses from operations, the Company has provided for a full valuation allowance due to the degree of uncertainty relating to the ultimate realization of the future tax assets.

At December 31, 2009, the Company had available net operating loss (NOL) carryforwards, to reduce future taxable income for US federal income tax purposes of approximately \$24,607,000 expiring through 2030 and approximately \$9,060,000 for state purposes. The future benefit of these federal NOL carryforwards may be limited by on an annual basis and in total under Section 382 of the United States Internal Revenue Code as a result of prior ownership changes and depending on the extent of future ownership changes. As a result of its valuation allowance, the Company has not currently recognized any benefit for these losses in its consolidated financial statements.

# Hamilton Thorne Ltd

## Notes to the Consolidated Financial Statements

For the years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars)

### 19. Income taxes (Continuing from previous page)

Net Operating Loss Carryovers (20 year carryover) are as follows:

	Loss	Expire in	Amount
Expiring	1998	2019	28,000
	1999	2020	304,000
	2000	2021	2,013,000
	2001	2022	3,013,000
	2002	2023	3,950,000
	2003	2024	3,129,000
	2004	2025	2,844,000
	2005	2026	2,644,000
	2006	2027	1,428,000
	2007	2028	2,264,000
	2008	2029	1,265,000
2009	2030	1,725,000	
		<u>24,607,000</u>	

#### U.S. income tax

U.S. federal tax legislation was enacted in 2004 to address perceived U.S. tax concerns in "corporate inversion" transactions. A "corporate inversion" generally occurs when a non-U.S. corporation acquires "substantially all" of the equity interests in, or the assets of, a U.S. corporation or partnership, if, after the acquisition, former equity holders of the U.S. corporation or partnership own a specified level of stock in the non-U.S. corporation. The tax consequences of these rules depend upon the percentage identity of stock ownership that results. Generally, in the "80-percent identity" transactions, i.e. former equity holders of the U.S. corporation owns 80% or more of the equity of the non-U.S. acquiring entity (excluding certain equity interests), the tax benefits of the inversion are limited by treating the non-U.S. acquiring entity as a domestic entity for U.S. tax purposes. In the "60-80 percent identity" transactions, the benefits of the inversion are limited by barring certain corporate-level "toll charges" from being offset by certain tax attributes of the U.S. corporation (e.g. loss carryforwards), and imposing excise taxes on certain stock based compensation held by "insiders" of the U.S. corporation.

Management is of the view that a corporate inversion has resulted from the RTO transaction completed during the year as disclosed in Note 3. However, management has not yet determined whether the Company is subject to the "80 percent" or the "60-80 percent" identity with respect to the transactions undertaken in the current year since the interpretation of which categories of stock ownership are to be considered under the inversion rules is not yet settled.

### 20. Commitments

The Company and its subsidiary are committed under operating leases for rental of offices and equipment. Future minimum annual rentals are as follows:

2010	420,734
2011	383,773
2012	368,851
2013	30,978
	<u>1,204,336</u>

# Hamilton Thorne Ltd

## Notes to the Consolidated Financial Statements

For the years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

### 21. Capital Management

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern in order to pursue the continued development and commercialization of its technologies and to provide financial flexibility. In the management of capital, the Company includes the components of shareholders' equity as well as its long-term debt. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of its underlying assets. To maintain or adjust its capital structure, the Company may attempt to issue new shares, raise new debt or enter into new capital leases. In order to maximize ongoing development efforts, the Company has not, to date, paid out dividends on its common shares. The Company believes the funds on hand and committed combined with projected cash flow from operations are sufficient to fund the Company's current business cash requirements for the year ending December 31, 2010. Despite income anticipated to be received during the year, it may become necessary to undertake additional equity or other financing to fund its on-going operations.

There are no externally imposed capital requirements.

The total capital as at December 31, 2009 and 2008 is calculated as follows:

	2009	2008
Bank line of credit	5,000,000	4,970,000
Preferred shares, subject to redemption	-	1,389,593
Other long-term debt	50,000	-
Shareholders' equity	(3,726,154)	(5,663,803)
	<b>1,323,846</b>	<b>695,790</b>

### 22. Financial Instruments

#### Fair Value

The Company's carrying value of cash, accounts receivable, notes receivable and accounts payable and accrued liabilities approximate their fair values due to the immediate or short term maturity of these instruments.

The carrying value of the notes payable and long-term debt approximate their fair value as the interest rates are consistent with the current market rates for debt with similar terms.

The following is a summary of the accounting model the Company has elected to apply to each of its significant categories of financial instruments outstanding at December 31, 2009:

Cash	Held-for-trading
Accounts receivable	Loans and receivables
Accounts payable and accrued liabilities	Other financial liabilities
Notes payable	Other financial liabilities
Obligations under capital leases	Other financial liabilities
Long-term debt	Other financial liabilities

# Hamilton Thorne Ltd

## Notes to the Consolidated Financial Statements

*For the years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)*

### 22. Financial Instruments *(Continuing from previous page)*

Carrying value and fair value of financial assets and liabilities are summarized as follows:

	<i>December 31, 2009</i>		<i>December 31, 2008</i>	
	<i>Carrying value</i>	<i>Fair value</i>	<i>Carrying value</i>	<i>Fair value</i>
Held-for-trading	<b>1,356,371</b>	<b>1,356,371</b>	5,029	5,029
Accounts and notes receivable	<b>523,688</b>	<b>523,688</b>	981,202	981,202
Other financial liabilities	<b>6,318,256</b>	<b>6,318,256</b>	6,165,233	6,165,233

Financial instruments recorded at fair value on the balance sheet are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices);

Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

Cash is classified as a Level 1 financial instrument. During the year, there have been no transfers of amounts between Level 1 and Level 2. There are no items classified in Level 3.

#### Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Financial assets and financial liabilities with variable interest rates expose the Company to cash flow interest rate risk. Financial assets and financial liabilities that bear interest at fixed rates are subject to fair value interest rate risk. All of the Company's notes payable and long-term debt bear interest at variable rates. The carrying value of the notes payable and long-term debt approximates their fair value as the interest rates are consistent with the current prime rate offered in the credit market. Increases in interest rates could have a material impact on the Company's net income and comprehensive income.

For the year ended December 31, 2009, a change in interest rate relating to the notes payable under the bank line of credit of 1% would have increased interest expense by approximately \$50,000 (approximately \$47,000 for 2008).

# Hamilton Thorne Ltd

## Notes to the Consolidated Financial Statements

*For the years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)*

### 22. Financial Instruments *(Continuing from previous page)*

#### Credit Risk

Credit risk arises from the potential that a counter party will fail to perform its obligations. The Company is exposed to credit risk from customers. In order to reduce its credit risk, the Company reviews a new customer's credit history before extending credit and conducts regular reviews of its existing customers' credit performance. Frequently the Company will request either a letter of credit or advance payment terms for new customers. An allowance for doubtful accounts is established based upon specific factors surrounding the credit risk of specific accounts, historical trends and other information. Over the past years, the Company has experienced few bad debt write offs and accordingly its allowance at December 31, 2009 is \$20,500. It is management's opinion that the Company is not exposed to any significant price or currency risk arising from these financial instruments.

As at December 31, 2009, the Company had a concentrated credit risk with three customers totaling 17%, 13% and 13% of its accounts receivable respectively (2008 - three customers accounted for 19%, 16% and 15% respectively). As of December 31, 2009 the Company's aging of receivables was approximately 59% under 30 days, 30% 30 to 60 days and 11% over 60 days (2008 - 52% under 30 days, 36% 30 to 60 days and 12% over 60 days).

#### Liquidity risk

Liquidity risk is the risk that the Company would not be able to meet its financial obligations as they come to maturity or can only do so at excessive costs. Based on the Company's ability to generate cash flows through its ongoing operations, management believes that cash flows are sufficient to cover its known operating and capital requirements, as well as its debt servicing costs. The Company however, could not, without restructuring its bank line of credit, meet its longer term commitments. Therefore, management evaluates that the Company's liquidity risk is moderate to high, at this time. The Company is now examining its options, which may include replacing or extending the current bank line, raising additional equity and other financing alternatives.

The maturity dates of the Company's financial liabilities as at December 31, 2009 are as follows:

	<i>Carrying amount</i>	<i>Contractual cash flows</i>	<i>Maturing in the next 12 months</i>	<i>Maturing in 13 to 36 months</i>
Accounts payable and accrued liabilities	1,171,562	1,171,562	1,171,562	-
Bank line of credit	5,000,000	5,000,000	-	5,000,000
Obligations under capital leases	15,679	15,679	8,552	7,127
Notes payable	133,037	133,037	133,037	-
Total	6,320,278	6,320,278	1,313,151	5,007,127

**Hamilton Thorne Ltd**  
**Notes to the Consolidated Financial Statements**

*For the years ended December 31, 2009 and 2008*  
*(Expressed in U.S. Dollars)*

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**23. Related Party Transactions**

At December 31, 2009, the Company was indebted to certain officers under various unsecured notes payable bearing interest at 7%. In December 2008 an officer of the Company lent \$50,000 on a promissory note payable, subordinated to the bank line of credit, with interest at the prime rate (3.25% at December 31, 2009), plus 1%. Total indebtedness to officers at December 31, 2009 amounted to \$56,006.

In January 2007, the Company lent \$20,000 to an officer on an unsecured promissory note payable at maturity on December 31, 2009, bearing interest at the prime lending rate (3.25% at December 31, 2008), plus 1%. At December 31, 2009 and 2008, total indebtedness to the Company totaled \$23,813 and \$22,963, respectively.

At December 31, 2009 an officer owed the Company approximately \$24,000 for certain advances made and for an advance against future pay.

See Notes 9 & 11 - Notes Payable and Long-term Debt for information on notes to shareholders.

**24. Cash Flow Supplementary Information**

	<b>2009</b>	<b>2008</b>
Interest paid in cash	192,714	263,295
Non-cash items during the years ended December 31:		
Equipment financed with capital lease	-	25,695
Conversion of debt to equity	475,000	-
Interest income on note receivable	850	1,221