

SQI Diagnostics Inc.

Interim Consolidated Financial Statements

For the Period Ended December 31, 2010

NOTICE TO READER

The accompanying unaudited interim consolidated financial statements have been prepared by the company's management and the company's independent auditors have not performed a review of these consolidated financial statements

SQI Diagnostics Inc.
Interim Consolidated Balance Sheets
As at December 31, 2010
(Amounts are in thousands of dollars)

	December 31, 2010 (Unaudited)	September 30, 2010 (audited)
Assets		
Current		
Cash and cash equivalents	\$ 6,471	\$ 9,408
Amounts receivable	16	3
Inventory (Note 4)	516	260
Prepays and deposits	204	165
Due from related party (Note 5)	67	66
	7,274	9,902
Due from related party (Note 5)	32	32
Property and equipment (Note 6)	2,821	2,731
Patents and trademarks	476	469
	\$ 10,603	\$ 13,134

Liabilities

Current

Accounts payable and accrued liabilities	\$ 568	\$ 972
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Shareholders' Equity

Capital stock (Note 8)	35,048	35,026
Warrants (Note 9)	1,674	1,799
Employee share purchase loan (Note 8)	(10)	(10)
Contributed surplus (Note 11)	9,063	8,832
Deficit	(35,740)	(33,485)
	10,035	12,162
	\$ 10,603	\$ 13,134

Approved by the Board "Peter Winkley"
Director (Signed)

 "Claude Ricks"
Director (Signed)

SQI Diagnostics Inc.**Interim Consolidated Statements of Operations and Deficit**

(Amounts are in thousands of dollars, except per share amounts)

	Three Month Period Ended December 31, 2010	Three Month Period Ended December 31, 2009
Revenue		
Product sales	\$ 9	\$ -
Consulting fees (Note 7)	9	5
	18	5
Expenses		
Salaries and wages	159	124
General and administrative (Note 7)	170	85
Professional and consulting fees	107	121
Sales and marketing	106	64
Stock based compensation (Note 13)	115	49
Research and development costs	1,499	1,054
Amortization - property and equipment	113	102
Amortization - patents and trademarks	28	28
	2,297	1,627
Loss before the undernoted items	(2,279)	(1,622)
Interest income	24	3
Interest expense	-	(1)
	24	2
Net loss	(2,255)	(1,620)
Deficit, beginning of period	(33,485)	(25,412)
Deficit, end of period	\$ (35,740)	\$ (27,032)
Loss per share		
Basic and diluted	\$ (0.07)	\$ (0.06)
Weighted average number of common shares outstanding		
Weighted average number of shares	33,759	27,930

SQI Diagnostics Inc.
Interim Consolidated Statements of Cash Flows
(Amounts are in thousands of dollars)

	Three Month Period Ended December 31, 2010	Three Month Period Ended, December 31, 2009
Cash provided by (used in)		
Operations		
Net loss	\$ (2,255)	\$ (1,620)
Items not affecting cash		
Amortization - patents and trademarks	28	28
- property and equipment	113	102
Stock-based compensation	115	49
Loss on sale of property and equipment	43	-
Interest Accrual	(1)	-
	(1,957)	(1,441)
Net changes in non-cash working capital		
Amounts receivable	(13)	(10)
Inventory	(255)	(293)
Prepays and deposits	(39)	(75)
Accounts payable and accrued liabilities	(404)	260
	(2,668)	(1,559)
Investing		
Purchase of property and equipment	(249)	(23)
Additions to patents and trademarks	(35)	(63)
Sale of property and equipment	2	-
	(282)	(86)
Financing		
Proceeds from private placement and exercise of warrants and stock options, net of share issuance costs	13	6,161
	13	6,161
Net change in cash and cash equivalents	(2,937)	4,516
Cash and cash equivalents, beginning of period	9,408	3,180
Cash and cash equivalents, end of period	\$ 6,471	\$ 7,696
Supplemental Disclosure		
Cash paid for interest	\$ -	\$ 1

1. NATURE OF OPERATIONS

SQI Diagnostics Inc., (the "Company"), has its head office and development centre in Toronto, Ontario. The Company is a medical systems company that develops proprietary technology in multiplexing, miniaturization and automation. The Company provides laboratories the ability to simultaneously analyse multiple biomarkers, deliver accurate and quantitative patient results in less time, significantly reduce labour cost, and increase profits when compared with current diagnostic instrumentation.

During fiscal 2009 the Company obtained Health Canada licenses and self authorization to sell in the EU and during fiscal 2010 received United States Food & Drug Administration (FDA) clearance of its SQiDworks and IgXPLEX Rheumatoid Arthritis (RA) system. During fiscal 2010 the Company obtained a Health Canada license for its IgXPLEX Celiac microarray test kits that run on the Company's automated SQiDworks platform. The Company has earned limited revenues from its IgXPLEX RA and IgXPLEX Celiac test kits run on installed SQiDworks platforms to date and as such is considered to be a development stage company. The Company has a pipeline of additional autoimmune diagnostic products in various stages of development and commercialization. The Company expects to generate revenues from its IgXPLEX RA and IgXPLEX Celiac products as it grows its installed base of customers as well as from products to be launched as they complete commercialization. The continuation of the Company's research, development and commercialization activities is dependent upon the Company's ability to successfully generate product revenues, or to finance its cash requirements through further equity financings.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles, within the framework of the significant accounting policies summarized below:

Basis of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary. Inter-company balances and transactions are eliminated upon consolidation.

Cash and Cash Equivalents

Cash and cash equivalents include bank deposits and highly liquid money market investments such as bankers acceptance notes, treasury bills, cashable money market funds, and cashable guaranteed investment certificates.

Inventory

Inventory is valued at the lower of cost and replacement cost, with cost determined on a first-in, first-out basis.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Property and Equipment

Property and equipment are recorded at cost and are amortized on the straight-line basis over their estimated useful lives as follows:

Computer hardware	-	3 years
Computer software	-	3 years
Laboratory fixtures and equipment	-	10 years
Office equipment	-	10 years
Leasehold improvements	-	10 years

Patents and Trademarks

The costs relating to initial patent and trademark fees are deferred and amortized over 10 years on a straight-line basis. Patents and trademarks are recorded net of accumulated amortization of \$656,000 (September 30, 2010 - \$627,000).

Research and Development Costs

Research costs are charged to operations in the period in which they are incurred. Development costs are expensed as incurred or deferred if they meet the criteria for deferral under Canadian generally accepted accounting principles and are expected to provide future benefits with reasonable certainty.

At December 31, 2010, the Company was developing IgXPLEX diagnostics assays for celiac, vasculitis, lupus (SLE), Crohn's (IBD), antiphospholipid syndrome and our second generation, fully quantitative IgXPLEX RA assay. The Company continued its work to complete scientific discovery and assay design work for a diagnostic assay to detect and measure infliximab (also referred to as anti-TNF) in the blood of autoimmune patients. Deferral criteria have not been met, and accordingly, all development costs have been expensed in the period.

Impairment of Long-Lived Assets

Long-lived assets comprise property and equipment and intangible assets with finite lives (patents and trademarks). The Company recognizes an impairment loss for a long-lived asset when events or changes in circumstances cause its carrying value to exceed the total undiscounted cash flows expected from its use and eventual disposition. An impairment loss is measured as the excess of the carrying value of the asset over its fair value.

Revenue Recognition

Product sales are recognized upon the shipment of products to customers, if a signed contract exists, the sales price is fixed and determinable, collection of the resulting receivables is reasonably assured and any uncertainties with regard to customer acceptance are insignificant. Sales are recorded net of discounts and sales returns.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

The Company also provides consulting services from time to time. Consulting fee revenue is recognized when services are completed, amounts are invoiced to customers and collectability is reasonably assured.

Stock-Based Compensation and Other Stock-Based Payments

The Company applies a fair value based method of accounting for all stock-based payments. Accordingly, stock-based payments are measured at the fair value of the consideration received or the fair value of the equity instruments issued or liabilities incurred, whichever is more reliably measurable. Stock-based compensation is charged to operations over the vesting period and the offset is credited to contributed surplus. Consideration received upon the exercise of stock options is credited to share capital at which time the related contributed surplus is transferred to share capital.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at rates of exchange in effect at each transaction date. Revenue and expenses are translated at the rate of exchange at each transaction date. Gains or losses on translation are included in operations.

Income Taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on temporary differences between financial reporting and tax bases of assets and liabilities, as well as for the benefit of losses available to be carried forward to future years for tax purposes. Future income tax assets and liabilities are measured using enacted or substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future income tax assets are recorded in the financial statements if realization is considered more likely than not.

Investment Tax Credits

Investment tax credits are accrued when qualifying expenditures are incurred and there is reasonable assurance that the credits will be realized. Investment tax credits earned with respect to current expenditures for qualified research and development activities are included in the statements of operations as a reduction of research and development costs. Investment tax credits associated with capital expenditures are reflected as reductions in the carrying amounts of capital assets.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Financial Instruments

Financial instruments are measured initially at fair value and thereafter based on their classification.

The Company has classified and measured its financial instruments as follows:

<u>Financial Instrument</u>	<u>Classification</u>	<u>Measurement Basis</u>
Cash and cash equivalents	Held-for-trading	Fair value
Amounts receivable	Loans and receivable	Amortized cost
Due from related party	Loans and receivable	Amortized cost
Accounts payable and accruals	Other financial liabilities	Amortized cost

Comprehensive Income

The Company has not presented a statement of comprehensive income as it has no other comprehensive income.

Loss Per Share

Basic loss per share is computed using the weighted average number of common shares outstanding during the period. Diluted loss per share is computed using the weighted average number of common and potential common shares outstanding during the period. Potential common shares consist of the incremental common shares issuable upon the exercise of stock options and warrants determined using the treasury stock method.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenue and expenses during the period. Actual results could differ from those estimates.

Significant areas requiring the use of management estimates relate to the determination of the useful lives of property and equipment and patents and trademarks for amortization purposes, valuation of ITC's receivable, valuation of stock options and warrants and valuation allowance on future tax assets.

3. RECENT ACCOUNTING PRONOUNCEMENTS ISSUED AND NOT YET APPLIED

Business Combinations

In January 2009, the CICA issued Section 1582, Business Combinations, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. In addition, the CICA issued Sections 1601, Consolidated Financial Statements, and 1602, Non-Controlling Interests, which replaces the existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements, while section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

These standards apply 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 with earlier application permitted. The Company is currently evaluating the new sections to determine the potential impact of any future transactions on its consolidated financial statements.

International Financial Reporting Standards

The CICA plans to converge Canadian Generally Accepted Accounting Principles with International Financial Reporting Standards (~~%IFRS+~~) over a transition period expected to end in 2011, when IFRS will be fully adopted. The transition date of October 1, 2010 for the Company will require restatement for comparative purposes of amounts reported by the Company for the year ended September 30, 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS on its financial statements.

4. INVENTORY

Inventory consists of component parts that are to be used in the future production of SQiDworksⁱ Platform and IgXPlex consumable assays.

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December 31, 2010 and 2009

5. DUE FROM RELATED PARTY

	December 31, 2010 (unaudited) (\$000s)	September 30, 2010 (audited) (\$000s)
Amount due from an officer and director, secured, bearing interest as described in note (i), principal amount of \$98,000 repayable in three equal payments on September 1, 2010, 2011 and 2012. Accrued interest of \$1,000 is due on September 1, 2011	\$ 99	\$ 98
Less: Current portion	(67)	(66)
	\$ 32	\$ 32

(i) Terms of the promissory note were amended on April 16, 2010 as follows: interest bearing at Canada Revenue Agency prescribed rate for taxable benefits to employees and shareholders on interest-free and low-interest loans, which was 1% per annum at December 31, 2010. Prior to amendment, the loan was bearing interest at 4.25% per annum during the year ended December 31, 2009 and non-interest bearing from October 1, 2009 to April 15, 2010.

(ii) As at December 31, 2010, the first payment of \$33,000 is in arrears.

6. PROPERTY AND EQUIPMENT

As at December 31, 2010 (unaudited):	Cost (\$000s)	Accumulated Amortization (\$000s)	Net (\$000s)
Computer hardware	\$ 265	\$ 151	\$ 114
Computer software	179	135	44
Laboratory fixtures and equipment	4,227	1,707	2,520
Office equipment	176	133	43
Leasehold improvements	263	163	100
	\$ 5,110	\$ 2,289	\$ 2,821

As at September 30, 2010 (audited):	Cost (\$000s)	Accumulated Amortization (\$000s)	Net (\$000s)
Computer hardware	\$ 193	\$ 141	\$ 52
Computer software	153	130	23
Laboratory fixtures and equipment	4,172	1,670	2,502
Office equipment	176	128	48
Leasehold improvements	263	157	106
	\$ 4,957	\$ 2,226	\$ 2,731

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7. RELATED PARTY TRANSACTIONS

Transactions with related parties occur in the normal course of business and are measured at the exchange amount. Related party transactions have been listed below, unless they have been disclosed elsewhere in the financial statements.

Included in general and administrative expense for the quarter ended December 31, 2010 is \$12,000 (2009 - \$12,000) related to recovery of occupancy costs from a corporation in which an officer of the Company is also an officer. Consulting fee revenue of \$9,000 for the quarter ended December 31, 2010 (2009 - \$5,000) was earned from this corporation. At quarter end, \$10,000 (September 30, 2010 - \$1,000) due from this corporation is included in amounts receivable.

8. CAPITAL STOCK

(a) Authorized

unlimited common shares

Issued - common shares

	Number (000s)	Value (\$000s)
Balance, September 30, 2009	27,193	\$ 22,366
Warrants exercised (Note 9(i))	970	2,008
Issued in connection with a private placement ⁽ⁱ⁾	4,678	12,295
Allocated to warrants	-	(1,424)
Options exercised	917	755
Share issuance costs ⁽ⁱ⁾	-	(974)
Balance, September 30, 2010 (audited)	33,758	\$ 35,026
Options exercised	8	22
Balance, December 31, 2010	33,766	\$ 35,048

(i) On December 4, 2009, pursuant to a private placement, the Company issued 2,398,104 units at a price of \$2.75 per unit, each unit comprised one common share of the Company and one-half common share purchase warrant, resulting in gross proceeds of \$6,595,000. Each whole warrant has an exercise price of \$4.00 per share and expires on December 4, 2011. The value of capital stock includes value attributable to the warrants in the amount of \$846,000, which has been included in warrant capital (see Note 9).

The Company paid a finder's fee in relation to the private placement satisfied through a cash payment of \$453,000 and the issuance of 143,886 compensation unit warrants with an exercise price of \$2.75 per unit and expiring on December 4, 2010, valued at \$125,000. Each unit entitles the purchaser to purchase one common share and one-half common share purchase warrant with an exercise price of \$4.00 per share, expiring on December 4, 2010. These warrants expired unexercised in the quarter. Total share issuance costs were \$611,000.

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On August 12, 2010, pursuant to a private placement the Company issued 2,280,000 units at a price of \$2.50 per unit, each unit comprised one common share of the Company and one-half common share purchase warrant, resulting in gross proceeds of \$5,700,000. Each whole warrant has an exercise price of \$5.00 and expires on August 12, 2012. The value of capital stock includes value attributable to the warrants in the amount of \$578,000, which has been included in warrant capital (see Note 9).

The Company paid a finder's fee in relation to the private placement satisfied through a cash payment of \$260,000 and the issuance of 57,000 compensation unit warrants with an exercise price of \$2.50 per unit and expiring on August 12, 2012, valued at \$62,000. Each unit entitles the purchaser to purchase one common share and one-half common share purchase warrant. Each whole warrant has an exercise price of \$5.00 per share, expiring on August 12, 2012. The total share issuance costs were \$363,000.

- (b) During the period ended September 30, 2007, the Company made a non-interest bearing loan to its officer, which was used to acquire 100,000 common shares. The loan has been accounted for as a share purchase loan and, accordingly, the \$10,000 loan balance has been deducted from share capital.

9. WARRANT CAPITAL

The following summarizes the change in warrants:

	Three Months Ended December 31, 2010 (\$000s)	Year Ended September 30, 2010 (audited) (\$000s)
Balance, beginning of period	\$ 1,799	\$ 461
Issued on private placement (Note 8))		1,424
Finder warrants (Note 8)		187
Exercise of warrants (i)		(213)
Expiry of warrants (Note 9 (i) and (ii))	(125)	(60)
Balance, end of period	\$ 1,674	\$ 1,799

- (i) During the year ended September 30, 2010, 194,200 warrants with an expiry of June 3, 2010 were exercised resulting in the issuance of 194,200 shares and net proceeds of \$291,000, 576,563 warrants with an expiry of June 29, 2010 were exercised resulting in the issuance of 576,563 shares and net proceeds of \$1,384,000 and 199,493 warrants with an expiry of April 26, 2010 were exercised resulting in the issuance of 199,493 shares and net proceeds of \$120,000. On exercise, \$213,000 (2009 - \$Nil) was transferred from warrant capital to share capital. The remaining 1,207,213 warrants with an expiry date of June 29, 2010 expired unexercised. On expiry, \$60,000 (2009 - \$Nil) was transferred from warrant capital to contributed surplus.
- (ii) During the quarter ended December 31, 2010 143,886 warrants with an expiry of December 4, 2010 expired unexercised, \$125,000 was transferred to contributed surplus upon expiry.

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10. WARRANTS

The Company had the following warrants outstanding at December 31, 2010:

Number of Warrants (000s)	Purchase Price	Expiry Date
107	\$ 1.25	January 22, 2011 (i)
1,199	\$ 4.00	December 4, 2011
237	\$ 1.90	December 23, 2011
1,140	\$ 5.00	August 12, 2012
57	\$ 2.50	August 12, 2012
2,740		

(i) Subsequent to the quarter ended December 31, 2010, these warrants were exercised.

11. CONTRIBUTED SURPLUS

The following summarizes the change in contributed surplus:

	Three Months Ended December 31, 2010 (\$000s)	Year Ended September 30, 2010 (audited) (\$000s)
Balance, beginning of period	\$ 8,832	\$ 8,431
Stock-based compensation (Note 13)	115	402
Options exercised (Note 12 (i))	(9)	(61)
Warrants expired (Note 9(i) and 9(ii))	125	60
Balance, end of period	\$ 9,063	\$ 8,832

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12. STOCK OPTIONS

The Company maintains a Stock Option Plan (the "Plan") for the benefit of directors, officers, employees and consultants. The aggregate number of common shares reserved for issuance under the Plan, together with any other employee stock option plans, options for services and employee share purchase plans, will not exceed 3,200,000. Options granted pursuant to the Plan will have terms not to exceed five years, and are granted at an option price which will not be less than the fair market price at the time the options are granted. All options granted to individual optionees, other than consultants, generally vest in three equal installments over a period of 36 months.

The following summarizes the stock option activities under the Plan:

	December 31, 2010		December 31, 2009	
	Number of Options (000s)	Weighted Average Exercise Price	Number of Options (000s)	Weighted Average Exercise Price
Beginning balance	1,764	\$ 1.75	2,360	\$ 1.18
Granted	100	\$ 2.90	25	\$ 3.26
Exercised (i)	(8)	\$ 1.74	-	\$ -
Expired	-	\$ -	-	\$ -
Forfeited	(24)	\$ 1.96	-	\$ -
Ending balance	1,832	\$ 1.81	2,385	\$ 1.31
Exercisable	1,028	\$ 1.57	1,598	\$ 1.14

(i) On exercise of stock options, \$9,000 (2009 - \$0) was transferred from contributed surplus to share capital.

There are no other options outstanding that are not part of the Plan.

SQI Diagnostics Inc.
Notes to Interim Consolidated Financial Statements
December 31, 2010 and 2009

12. STOCK OPTIONS (Cont'd)

The Company had the following stock options outstanding under the Plan at December 31, 2010:

Number of Options (000s)	Exercise Price	Expiry Date
33	\$ 1.20	June 29, 2011
67	\$ 1.20	August 29, 2011
172	\$ 1.74	August 7, 2012
50	\$ 1.50	October 23, 2012
758	\$ 1.60	February 26, 2013
255	\$ 1.75	August 26, 2013
80	\$ 1.30	May 22, 2014
25	\$ 3.26	November 3, 2014
57	\$ 2.25	February 22, 2015
60	\$ 2.10	May 27, 2015
175	\$ 2.50	August 16, 2015
100	\$ 2.90	October 4, 2015
1,832		

13. STOCK-BASED COMPENSATION

The fair value of the options granted during the quarter ended December 31, 2010 was \$188,000 (2009 - \$53,000), which will be recognized over the vesting period of 36 months. The total compensation expense for the quarter ended December 31, 2010 was \$115,000 (2009 - \$49,000). The total amount credited to contributed surplus for the quarter ended December 31, 2010 was \$115,000 (2009 - \$49,000).

The fair value of each option granted has been estimated at the date of grant or the date when it became measurable using the Black-Scholes option pricing model with the following weighted average assumptions at the measurement date:

	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Dividend yield	0%	0%
Expected volatility	80%	80%
Risk-free interest rate	2.00%	1.98%
Expected life (years)	5.00	5.00
Weighted average grant date fair value	\$1.88	\$2.11

The Company has assumed no forfeiture rate as adjustments for actual forfeitures are made in the year they occur.

14. CONTINGENCIES

In the ordinary course of business, the Company may be contingently liable for litigation and claims with customers, suppliers, former employees or competitors. Management believes that adequate provisions have been recorded in accounts where required.

15. CAPITAL RISK MANAGEMENT

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern so that it can complete its lead assay commercialization efforts and receive the required regulatory approvals to sell and market its products and provide returns for shareholders and benefits for other stakeholders.

The capital structure of the Company consists of shareholders' equity. The Company is not subject to externally imposed capital requirements.

16. FINANCIAL RISK MANAGEMENT

a) Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's cash and cash equivalents are exposed to credit risk. The credit risk on cash and cash equivalents is small because the counterparties are highly rated Canadian banks.

b) 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. The Company's cash and cash equivalents are exposed to cash flow interest rate risk as the Company invests cash and cash equivalents at floating rates of interest in highly liquid instruments. Fluctuations in interest rates would not significantly impact interest income.

c) Currency Risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company is exposed to currency risk due to its purchases in US dollars. A 1% change in the foreign exchange rate would result in a change of approximately \$7,000 in the reported profit and loss.

d) Liquidity Risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities. The Company's accounts payable and accrued liabilities are all current. The Company ensures that it has sufficient capital to meet short term financial obligations after taking into account its cash on hand.

17. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current period's financial statement presentation.