

Consolidated Financial Statements

Quest PharmaTech Inc.

Six months ended July 31, 2014

(Unaudited)

Quest PharmaTech Inc.

National Instrument 51 – 102
Continuous Disclosure Obligations

Notice

Pursuant to Part 4.3 (3) of National Instrument 51 – 102, these unaudited interim consolidated financial statements of Quest PharmaTech Inc. for the six month period ended July 31, 2014 have not been reviewed by the Company's auditors.

Quest PharmaTech Inc.**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**
(see note 1 – going concern uncertainty)

As at

	Jul 31, 2014 (Unaudited) \$	Jan 31, 2014 (Audited) \$
ASSETS		
Current		
Cash	253,675	742,447
Accounts receivable	7,641	39,194
Prepaid expenses	27,518	34,480
	288,834	816,121
Non current		
Property and equipment <i>[note 4]</i>	41,930	49,346
Intangibles <i>[note 3]</i>	25,738	36,387
	67,668	85,733
	356,502	901,854
LIABILITIES		
Current		
Accounts payable and accrued liabilities	586,232	813,487
Demand loans <i>[note 10]</i>	1,370,000	870,000
Share subscriptions received <i>[note 6]</i>	200,000	—
Current portion of deferred revenue <i>[note 14]</i>	643,300	643,300
	2,799,532	2,326,787
Long term portion of deferred revenue <i>[note 14]</i>	666,050	987,700
	3,465,582	3,314,487
SHAREHOLDERS' DEFICIENCY		
Common shares <i>[note 6]</i>	25,813,875	25,813,875
Warrants <i>[note 6]</i>	400,000	400,000
Contributed surplus	2,252,965	2,252,965
Deficit	(31,575,920)	(30,879,473)
	(3,109,080)	(2,412,633)
	356,502	901,854

See accompanying notes

Quest PharmaTech Inc.

**CONSOLIDATED STATEMENTS OF
LOSS AND COMPREHENSIVE LOSS**

	For the three months ended July 31		For the six months ended July 31	
	2014	2013	2014	2013
	\$	\$	\$	\$
REVENUE				
Investment financing revenue <i>[note 14]</i>	160,825	—	321,650	—
EXPENSES				
General and administrative	138,533	188,863	331,327	311,005
Research and development	309,978	417,618	644,052	641,569
	448,511	606,481	975,379	952,574
Loss before the undernoted	(287,686)	(606,481)	(653,729)	(952,574)
Other income (expense)				
Financial income	31	65	87	65
Financial expenses <i>[notes 5 and 10]</i>	(26,210)	(31,171)	(44,097)	(60,569)
Foreign exchange gain (loss)	772	(2,539)	1,292	(2,438)
	(25,407)	(33,645)	(42,718)	(62,942)
Net and comprehensive loss for the period	(313,093)	(640,126)	(696,447)	(1,015,516)
Basic and diluted loss per share	(\$0.003)	(\$0.008)	(\$0.007)	(\$0.012)

See accompanying notes

Quest PharmaTech Inc.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' DEFICIENCY

	Share capital \$	Equity portion of convertible debenture \$	Shares to be issued \$	Warrants \$	Contributed surplus \$	Contributed surplus – investment financing \$	Deficit \$	Total Shareholders' Deficiency \$
Balance, February 1, 2013	24,623,875	60,000	500,000	200,000	1,916,715	1,100,000	(30,607,143)	(2,206,553)
Funding received <i>[note 14]</i>						2,550,000		2,550,000
Balance transfer		(60,000)			60,000			
Share based compensation <i>[note 8]</i>	—	—	—	—	69,500	—	—	69,500
Net loss for the period	—	—	—	—	—	—	(1,015,516)	(1,015,516)
Balance, July 31, 2013	24,623,875	—	500,000	200,000	2,046,215	3,650,000	(31,622,659)	(602,569)
Balance, February 1, 2014	25,813,875	—	—	400,000	2,252,965	—	(30,879,473)	(2,412,633)
Net loss for the period	—	—	—	—	—	—	(696,447)	(696,447)
Balance, July 31, 2014	25,813,875	—	—	400,000	2,252,965	—	(31,575,920)	(3,109,080)

See accompanying notes

Quest PharmaTech Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the three months ended July 31		For the six months ended July 31	
	2014	2013	2014	2013
	\$	\$	\$	\$
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES				
Net loss for the period	(313,093)	(640,126)	(696,447)	(1,015,516)
Add (deduct) items not involving cash				
Amortization	9,033	10,302	18,065	22,414
Share-based compensation <i>[note 8]</i>	—	69,500	—	69,500
Investment financing revenue <i>[note 14]</i>	(160,825)	—	321,650	—
Net changes in working capital <i>[note 11]</i>	(34,088)	(205,202)	(188,740)	(99,506)
NET CASH FLOWS USED IN OPERATING ACTIVITIES	(498,973)	(765,526)	(1,188,772)	(1,023,108)
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES				
Increase in demand and other loans <i>[note 10]</i>	500,000	—	500,000	200,000
Repayment of demand loans	—	(200,000)	—	(200,000)
Repayment of convertible debenture <i>[note 5]</i>	—	(400,000)	—	(400,000)
Share subscriptions received <i>[note 6]</i>	200,000	—	200,000	—
Investment agreement funding <i>[note 14]</i>	—	2,000,000	—	2,050,000
NET CASH FLOWS FROM FINANCING ACTIVITIES	700,000	1,400,000	700,000	1,650,000
CASH FLOWS USED IN INVESTING ACTIVITIES				
Purchase of property and equipment	—	—	—	(3,619)
NET CASH FLOWS USED IN INVESTING ACTIVITIES	—	—	—	(3,619)
Net increase (decrease) in cash and cash equivalents	201,027	634,474	(488,772)	623,273
Cash and cash equivalents, beginning of period	52,648	45,436	742,447	56,637
Cash and cash equivalents, end of period	253,675	679,910	253,675	679,910

See accompanying notes

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

1. CORPORATE INFORMATION AND GOING CONCERN UNCERTAINTY

Corporate information

Quest PharmaTech Inc. (the “Company”) is a biotechnology company committed to the development and commercialization of oncology product candidates. It is developing a series of products for the treatment of cancer based on its pipeline of SonoLight compounds and monoclonal antibodies which target certain tumor antigens that are presented in a variety of cancers. The Company believes that by combining these antibodies with other cancer therapies such as chemotherapy, photodynamic therapy or radioimmuno therapy, it can potentially further complement and enhance treatment outcomes compared to antibody treatment alone.

The Company is incorporated under the Business Corporations Act (Alberta). The Company’s functional currency is the Canadian dollar. The principal address of the Company is 8123 Roper Road NW, Edmonton, Alberta, T6E 6S4.

The Company is publicly traded on the TSX Venture Exchange under the symbol “QPT”.

Going concern uncertainty

The Company’s consolidated financial statements have been prepared on a going concern basis which presumes the realization of assets and discharge of liabilities in the normal course of business for the foreseeable future. The Company has experienced significant operating losses and cash outflows from operations since its inception.

The Company has incurred a net loss of \$696,447 for the six months ended July 31, 2014 and as at July 31, 2014 had a working capital deficiency of \$2,510,698 (January 31, 2014 - \$1,510,666) and a shareholders’ deficiency of \$3,109,080 (January 31, 2014 - \$2,412,633). Accordingly, there is a material uncertainty that may cast significant doubt regarding the Company’s ability to continue as a going concern.

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

1. CORPORATE INFORMATION AND GOING CONCERN UNCERTAINTY [CONTINUED]

The Company's ability to continue as a going concern is uncertain and is dependent upon its ability to raise additional capital to successfully complete its research and development programs, commercialize its technologies, conduct clinical trials and receive regulatory approvals for its products. It is not possible at this time to predict the outcome of these matters. The Company's consolidated financial statements do not reflect any adjustments to the classifications and carrying values of assets and liabilities that may be required should the Company be unable to continue as a going concern and therefore be required to realize its assets and discharge its liabilities in other than the normal course of business. The Company intends to address this uncertainty through new share or debt issuances, licensing arrangements and/or strategic partnerships.

2. BASIS OF PREPARATION

The unaudited consolidated financial statements of the Company were prepared following the same accounting policies as disclosed in Note 3 in the audited consolidated financial statements for the years ended January 31, 2014 and 2013. These unaudited consolidated financial statements for the six months ended July 31, 2014 should be read in conjunction with the consolidated financial statements for the years ended January 31, 2014 and 2013 and the notes thereto. These unaudited consolidated financial statements for the six months ended July 31, 2014 do not include all of the required disclosures for annual consolidated financial statements.

Statement of Compliance

These consolidated financial statements have been prepared by management in accordance with IAS 34 "Interim Financial Reporting" using accounting principles consistent with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB").

These consolidated financial statements were approved and authorized for issuance by the Board of Directors on September 9, 2014.

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention with the exception of financial instruments which have been measured at fair value.

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

3. INTANGIBLE ASSETS

	July 31, 2014		January 31, 2014	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
IgE technology	63,892	38,154	63,892	27,505
Immunotherapy technology	237,500	237,500	237,500	237,500
Hypocrellin based technology and licenses	2,476,822	2,476,822	2,476,822	2,476,822
CDK technology	225,000	225,000	225,000	225,000
	3,003,214	2,977,476	3,003,214	2,966,827
Net book value	25,738		36,387	

During the three and six months ended July 31, 2014, amortization of intangible assets was \$5,324 and \$10,648, respectively (2013 – \$5,324 and \$12,490, respectively).

CORE TECHNOLOGIES

AllergoOncology technology and licenses (“IgE technology”)

During September, 2012, the Company signed a technology purchase agreement with Advanced Immune Therapeutics, Inc. (“AIT”) to acquire the proprietary rights and intellectual property related to an allegrooncology technology based on tumor associated Immunoglobulin E (IgE) antibody for the treatment of cancer. Under the terms of the agreement, consideration for the purchase consisted of payment of \$40,000 U.S. for past patent costs and the issuance of 500,000 common shares, valued for accounting purposes at \$0.05 per common share which reflected the closing price of the common shares on the date of issuance (\$25,000). The agreement requires the Company to make milestone and royalty payments to AIT on future revenues. The Company is amortizing this asset on a straight-line basis over a three year period.

Immunotherapy technology and licenses (“Immunotherapy technology”)

During September, 2009, the Company signed a technology purchase agreement with Paladin Labs Inc. (“Paladin”) to acquire the proprietary rights and intellectual property related to an antibody immunotherapy technology. Under this technology, the Company acquired product candidates consisting of five monoclonal antibodies targeting certain tumor antigens that are presented in a variety of cancers. Under the terms of the agreement, consideration for the purchase consisted of a cash payment of \$37,500 and the issuance of 1,500,000 common shares upon the effective date of the purchase and an additional 1,500,000 common shares to be issued no later than December 31, 2010. The common shares issued on the effective date and those issued prior to December 31, 2010 were valued for accounting purposes at \$0.04 per share which reflected the closing price of

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

3. INTANGIBLE ASSETS [CONTINUED]

the common shares on the effective date of the purchase (\$60,000 and \$60,000 respectively). Under the terms of the agreement a further 2,000,000 common shares were contingently issuable upon successful future financing initiatives by the Company. On October 22, 2010, the Company decided to take control over the technology and issued the final 3,500,000 common shares under the agreement. The 2,000,000 common shares issued on October 22, 2010 reflecting the contingent consideration were valued for accounting purposes at \$0.04 per share which reflected the closing price of the common shares at that date (\$80,000). The agreement also requires the Company to make milestone and royalty payments to Paladin on future revenues. This intangible asset is fully amortized.

Hypocrellin-based technology and licenses (proprietary rights)

The Company's subsidiary, Sonolight, holds the exclusive worldwide license to develop, commercialize and exploit several proprietary inventions involving a class of sonosensitizers and their use in cancer and non-cancer therapies. Sonolight signed a licensing agreement dated March 6, 2001 with the University of Alberta. The license agreement is for a term of 25 years. The agreement requires royalty payments upon successful sales and marketing of products developed using the technology. The Company has amortized this asset on a straight-line basis over a three-year period that commenced August 1, 2001. This intangible asset is fully amortized.

NON-CORE TECHNOLOGIES (CDK technology (proprietary rights))

The Company owns the worldwide rights to develop, manufacture and sell the CDK technology, a novel immunomodulator with anti-cancer properties. As consideration for its acquisition of the technology, the Company must issue 400,000 common shares as certain milestones outlined in the technology purchase agreement are met. To date, the Company has issued 200,000 shares under the agreement: 100,000 shares issued in fiscal 2004 and 100,000 shares in fiscal 2003. These shares have been recorded at a value that represents the closing price of the common shares on the date the shares were issued. The Company amortized this asset on a straight-line basis over a three-year period, which commenced on August 1, 2002. This intangible asset is fully amortized. During fiscal 2009, the Company determined that it will not proceed with further development with respect to the CDK technology.

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

4. PROPERTY AND EQUIPMENT

	July 31, 2014		January 31, 2014	
	Cost \$	Accumulated amortization \$	Cost \$	Accumulated amortization \$
Computer equipment	83,255	79,315	83,255	78,620
Furniture and fixtures	12,114	11,915	12,114	11,880
Office equipment	31,494	31,173	31,494	31,116
Manufacturing and research and development equipment	457,983	423,551	457,983	417,475
Leasehold improvements	5,220	2,182	5,220	1,629
	590,066	548,136	590,066	540,720
Net book value		41,930		49,346

During the three and six months ended July 31, 2014, amortization of property and equipment was \$3,708 and \$7,417, respectively (2013 - \$4,947 and \$9,924, respectively).

5. CONVERTIBLE DEBENTURE

On March 23, 2005, the Company entered into an agreement to issue a \$1,000,000 principal amount 8% convertible debenture with a one-year maturity to two arm's-length parties. The debenture was collateralized by the Company's Hypocrellin-based technology, one of its core technologies (note 3). The debenture was repayable in blended monthly installments of \$6,667 with the balance, including accrued interest, due on March 22, 2006. The debenture had a conversion feature whereby it could be converted into common shares of the Company at a price of \$0.45 per common share and could be redeemed at any time by the Company. The Company obtained extensions to the maturity date and as at April 30, 2012, the maturity date had been extended to September 22, 2012. In connection with the extensions the debenture interest rate was revised from 8% to 9% per annum and the debenture conversion price was amended from \$0.45 to \$0.25 per common share. During 2008, the Company made principal payments of \$500,000 against the convertible debenture. During fiscal 2013, the Company made a principal payment of \$100,000 against the convertible debenture. During the six month period ended July 31, 2013, the Company made a principal payment of \$400,000 against the convertible debenture, which is now repaid in full.

During the three and six months ended July 31, 2013, the Company incurred \$9,000 and \$18,000, respectively, in interest under this convertible debenture.

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

6. SHARE CAPITAL

Authorized

Unlimited number of common shares without nominal or par value
Unlimited number of first preferred shares
Unlimited number of second preferred shares

The first and second preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions and conditions attached to the shares of each series.

Issued

	Number of common shares	Amount \$
Common shares		
At January 31, 2013	83,697,580	24,623,875
Shares issued pursuant to a private placement	5,000,000	500,000
Shares issued pursuant to the investment financing	3,000,000	90,000
Shares issued pursuant to a private placement	10,000,000	600,000
At January 31, 2014	101,697,580	25,813,875
At July 31, 2014	101,697,580	25,813,875

In October, 2013, the Company issued 5,000,000 common shares to a related party pursuant to a May, 2012 \$500,000 private placement. The shares were valued at \$0.10 per common share, which represented the closing price of the common shares in May, 2012.

In October, 2013, the Company issued 3,000,000 common shares to a related party pursuant to the termination and settlement of an Investment Financing agreement (note 14). The shares were valued at \$0.03 per share which represented the closing price of the common shares on the date of issue.

In January, 2014, Company raised \$1,000,000 through the issuance of 10,000,000 units at \$0.10 per unit, each unit comprised of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share at \$0.15 per common share. The warrants expire on January 23, 2016. The shares were valued at \$0.06 per common share, which represented the closing price of the common shares on the date of issue. The common share purchase warrants were valued at \$0.04 per warrant using the Black-Scholes option valuation model.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

6. SHARE CAPITAL [CONTINUED]

The following options to purchase common shares were outstanding as at July 31, 2014:

Exercise price \$	Options outstanding #	Weighted average remaining life (years)	Options exercisable #
0.10	8,940,000	7.10	8,940,000
0.15	200,000	0.19	200,000
	9,140,000	7.29	9,140,000

The following schedule details the warrants and share-based payment transactions granted and expired:

		Shares issuable on exercise of			
		Warrants		Share options	
		Number of shares #	Weighted average exercise price \$	Number of shares #	Weighted average exercise price \$
Balance, January 31, 2013		10,000,000	0.10	6,915,000	0.10
Granted		10,000,000	0.15	2,525,000	0.10
Expired		(10,000,000)	0.10	(250,000)	0.17
Balance, January 31, 2014		10,000,000	0.15	9,190,000	0.10
Granted		—	—	—	—
Expired		—	—	(50,000)	—
Balance, July 31, 2014		10,000,000	0.15	9,140,000	0.10

Warrants

In January 2014, the Company issued 10,000,000 share purchase warrants exercisable at \$0.15 per common share pursuant to a private placement of units. The warrants were valued at \$0.04 per warrant using the Black-Scholes option valuation model with the following assumptions (dividend rate – 0.00%, volatility – 153.1%, risk-free interest rate – 0.96%, expected life – 2 years). The warrants expire 24 months from the date of issue, on January 23, 2016.

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

6. SHARE CAPITAL [CONTINUED]

Share options

For the three and six month periods ended July 31, 2014, the Company did not grant any share options under the Company's Share Option Plan.

For the six months ended July 31, 2013, the Company granted 2,500,000 share options, as per the Company's Share Option Plan. These share options had exercise prices ranging from \$0.10 to \$0.15. 2,050,000 were granted to employees and 450,000 were granted to non-employees (note 8).

Under the Company's Share Option Plan, the aggregate number of common shares eligible for issuance shall not exceed 12,000,000. At July 31, 2014, 2,860,000 options are available for issue.

Basic and diluted loss per share

Basic loss per share has been calculated using the weighted average number of common shares outstanding during the period (2014 – 101,697,580; 2013 – 83,697,580). For the periods presented, the calculation of loss per common share on a diluted basis excluded all potential common shares because the effect was anti-dilutive.

Private Placement Proceeds

During the 3 month period ended July 31, 2014, the Company received \$200,000 under a \$411,500 unit offering private placement. The units are issuable at \$0.06 per unit, each unit comprised of one common share and one half share purchase warrant. Each whole warrant is exercisable into one common share at an exercise price of \$0.10. The warrants carry a two year expiry. Subsequent to period end, the Company closed the private placement subject to TSX Venture Exchange approval (note 15).

7. CAPITAL DISCLOSURES

The Company is a biotechnology company and consistent with other companies in the industry, the Company's objectives when managing capital are to safeguard its accumulated capital in order to maintain its ability to continue as a going concern so that it can continue with its drug development program and strive to maximize shareholder value. Note 1 provides a discussion surrounding the Company's ability to continue as a going concern. Capital is defined by the Company as shareholders' deficiency (primarily comprised of share capital, contributed surplus and deficit) and current term debt consisting of demand loans. The Company manages its capital structures, and makes adjustments to it based on the needs of the Company's operations and the requirement for funding to continue with the Company's drug development program. The Company does this

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

7. CAPITAL DISCLOSURES [CONTINUED]

through new share or debt issuances, selling assets or licensing its technologies to third parties to fund operations. The Company is not subject to any externally imposed capital requirements.

8. SHARE-BASED PAYMENTS

For the six months ended July 31, 2013, the Company granted a total of 2,500,000 share options under the Company's Share Option Plan. 2,300,000 of the 2013 options vested during the period. The fair value of options vesting in 2013 of \$69,500 was recognized as a share-based payment expense and credited to contributed surplus for the six months ended July 31, 2013. There were no forfeitures of Company's share options during the six months ended July 31, 2014 and 2013.

The Company used the Black-Scholes option pricing model to estimate the fair value of these options. The Company considers historical volatility of its common shares in estimating future share price volatility. The following assumptions were used:

Six months ended July 31	2013
	\$
Dividend yield	0.00%
Volatility	145.6 – 146.5 %
Risk-free interest rate	2.20 - 2.40%
Expected life (years)	10
Fair value per option	\$0.03 - \$0.04

9. SEGMENT DISCLOSURES

The Company is managed as one operating segment – biopharmaceutical/pharmaceutical products. Management assesses performance and makes resource decisions based on the consolidated results of operations of this operating segment. Substantially all of the operations of the Company are directly engaged in or support this operating segment. For the three and six month periods ended July 31, 2014, revenues of \$160,825 and \$321,650, respectively, were attributed to this operating segment. There was no revenue earned for the three and six month periods ended July 31, 2013.

10. DEMAND LOANS, INTEREST FREE LOAN AND RELATED PARTY TRANSACTIONS

During the year ended January 31, 2011, the Company entered into a demand loan agreement with one of its officers to provide up to \$1,000,000 bearing interest at 8% compounded annually to be used for the Company's operating expenditures. This financing is unsecured, with principal repayment to be made 30 days after demand and interest is payable monthly. As at July 31, 2014, the Company had drawn \$680,000 on this financing. During the year ended January 31, 2012, the

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

10. DEMAND LOANS, INTEREST FREE LOAN AND RELATED PARTY TRANSACTIONS [CONTINUED]

Company secured additional demand loan financing of \$100,000 from a director of the Company. This demand loan financing bears interest at 8% per annum, interest payable monthly and is unsecured with principal repayment to be made 30 days after demand. As at July 31, 2014, the Company had demand loan financing of \$90,000 from an officer of the Company. This demand loan financing bears interest at 8% per annum, interest payable monthly and is unsecured with principal repayment to be made 30 days after demand.

During the three month period ended July 31, 2014, the Company received \$500,000 in demand loan financings from unrelated third parties. These demand loan financings bears interest at 8% per annum, interest payable monthly and are unsecured with principal payment to be made 30 days after demand.

During the three and six month periods ended July 31, 2014, the Company incurred \$25,390 and \$42,361 respectively (2013 – \$20,732 and \$38,807, respectively) in interest under the demand loan financings, \$17,543 and \$34,514, respectively, with related parties (2013 – \$16,971 and \$34,514, respectively).

11. SUPPLEMENT CASH FLOW INFORMATION

NET CHANGE IN NON-CASH WORKING CAPITAL ITEMS RELATED TO OPERATING ACTIVITIES

	Three months ended July 31		Six months ended July 31	
	2014	2013	2014	2013
	\$	\$	\$	\$
Accounts receivable	29,708	(4,198)	31,553	2,293
Prepaid expenses	9,631	5,235	6,962	(3,745)
Accounts payable and accrued liabilities	(73,427)	(206,239)	(227,255)	(98,054)
	(34,088)	(205,202)	(188,740)	(99,506)

Quest PharmaTech Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and the demand loans.

a) Carrying value and fair value

The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and the demand loans approximate their fair value due to the immediate or short term maturity of these financial instruments. The fair value of the Company's financial instruments of cash and cash equivalents are measured using the Level 1 classification of the fair value hierarchy.

b) Risks

i) Foreign currency risk

The Company has certain assets and liabilities that are denominated in foreign currencies and are exposed to risks from changes in foreign exchange rates and the degree of volatility of these rates. Due to the limited number of transactions that are denominated in foreign currencies, the Company does not consider its exposure to foreign currency risk to be significant and currently does not use derivative instruments to reduce its exposure to this.

ii) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's exposure to liquidity risk is dependent on its ability to raise funds to meet its commitments and sustain its operations. The Company controls liquidity risk by managing its working capital and by securing additional funds through equity, debt or partnering transactions (see Capital Disclosures, note 7). In fiscal 2014 and 2015, the Company secured debt financing from its officers and from unrelated third parties to provide demand loan financing for operational expenditures. During fiscal 2013 and 2014, the company received investment financing (note 14) from a related party and also from a nonrelated party.

iii) Credit risk

Financial instruments that subject the Company to credit risk consist primarily of cash and cash equivalents and accounts receivable. To minimize its exposure to credit risk for cash equivalents, the Company invests surplus cash in short-term deposits that are fully guaranteed by the Company's financial banker, a major Canadian chartered bank. As the Company is a research and development company, the Company's exposure to credit risk related to accounts receivable is not considered to be significant. At period end, 100% of accounts receivable was due from one federal government agency.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT [CONTINUED]

iv) 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. The Company's cash and cash equivalents are comprised of highly liquid deposits or investments that earn interest at market rates. Interest on the demand loans is at fixed rates. Consequently, the Company is exposed to fair value changes on long-term debt when the market interest rate changes. Accounts receivable, accounts payable and accrued liabilities bear no interest. The Company manages its interest rate risk by maximizing the interest income earned on excess funds while maintaining the liquidity needed to conduct operations on a daily basis. The Company's policy limits the investing of excess funds to liquid government guaranteed deposits or guaranteed investment certificates.

13. COMPENSATION OF KEY MANAGEMENT

Key management includes directors and executives of the Company. The compensation paid or payable (including stock based compensation) to key management for services is shown below:

	Three months ended July 31		Six months ended July 31	
	2014	2013	2014	2013
	\$	\$	\$	\$
Salaries and short term employee benefits	99,000	139,000	198,000	233,000
Director compensation	—	16,500	—	16,500
	<u>99,000</u>	<u>155,500</u>	<u>198,000</u>	<u>249,500</u>

14. INVESTMENT FINANCING

During fiscal 2013, the Company signed an investment agreement with a related party to provide the Company with up to \$8,000,000 of funding over a 12-month period to support the Company's clinical trial programs and for operational expenditures. Under the investment agreement, the Company was required to issue up to 15,000,000 common shares and share up to 50% of future net revenues derived from the Company's immunotherapy and prostate cancer programs as funding milestones under the agreement are met. The Company received \$1,100,000 of funding during fiscal 2013 and \$50,000 of funding during fiscal 2014, which was recognized as deferred revenue. During fiscal 2014, the investment agreement was terminated along with conversion of the \$500,000 interest free loan in exchange for 3,000,000 common shares of the Company and 7% of future net revenues with this related party plus 3% of future net revenues to a maximum of \$5,000,000 to an unrelated party, derived from the Company's immunotherapy and prostate cancer

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the six months ended July 31, 2014

14. INVESTMENT FINANCING [CONTINUED]

programs. The shares issued were valued at \$90,000 and recorded in share capital with the remainder of funding received of \$1,560,000 recorded as a gain on settlement of investment agreement in the consolidated statements of loss and comprehensive loss for the year ended January 31, 2014.

During fiscal 2014, the Company entered into an investment agreement with a third party to provide up to \$12,000,000 of clinical development funding in return for the Company's common shares and future revenue sharing. Under this agreement, the Company is required to complete the phase II clinical trial on the Company's immunotherapy program, issue up to 10,000,000 common shares, and share up to 40% of future net revenues derived from the Company's immunotherapy, prostate cancer, IgE technology and dermatology programs. As at April 30, 2014, the Company has received \$2,000,000 of funding under this agreement, and is obligated to complete the Phase II clinical trial on the Company's immunotherapy program and share 40% of future net revenues from this program. A portion of this investment financing has been recognized as revenue in the consolidated statements of loss and comprehensive loss, based on the portion of the Phase II clinical trial completed in the periods subsequent to receipt of the funding. The remainder has been recorded as deferred revenue on the statements of financial position and will be recognized into income as the clinical trials are completed. Under the terms of the investment financing agreement, the Company was to receive an additional \$2,000,000 by December 31, 2013. As of the date of these financial statements, this funding had not been received and the Company has therefore terminated the agreement.

15. SUBSEQUENT EVENTS

Subsequent to period end, the Company closed a \$411,500 unit offering private placement, subject to TSX Venture Exchange approval. The units are issuable at \$0.06 per unit, each unit comprised of one common share and one half share purchase warrant. Each whole warrant is exercisable into one common share at an exercise price of \$0.10. The warrants carry a two year expiry.