

Financial Statements

**Consolidated Financial Statements for the
Years Ended December 31, 2007 & 2006**

Ceapro Inc.

Management's Report

To the Shareholders of **Ceapro Inc.**,

The accompanying consolidated financial statements of Ceapro Inc., and all information presented in this annual report, are the responsibility of Management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared by Management in accordance with Canadian generally accepted accounting principles. The financial statements include some amounts that are based on the best estimates and judgments of Management. Financial information used elsewhere in the annual report is consistent with that in the financial statements.

To further the integrity and objectivity of data in the financial statements, Management of the Company has developed and maintains a system of internal controls, which Management believes will provide reasonable assurance that financial records are reliable and form a proper basis for preparation of financial statements, and that assets are properly accounted for and safeguarded.

The Board of Directors carries out its responsibility for the financial statements in the annual report principally through its Audit Committee. The Audit Committee is appointed by the Board, and all of its members are outside and unrelated Directors. The Committee meets periodically with Management and the external auditors to discuss internal controls over the financial reporting process and financial reporting issues, to make certain that each party is properly discharging its responsibilities, and to review quarterly reports, the annual report, the annual financial statements, management discussion and analysis, and the external auditors' report. The Committee reports its findings to the Board for consideration when approving the financial statements for issuance to the shareholders. The Company's auditors have full access to the Audit committee, with and without Management being present.

The financial statements have been audited by the Company's auditors, Stout & Company LLP, the external auditors, in accordance with auditing standards generally accepted in Canada on behalf of the shareholders.

Sincerely,

SIGNED "Mark J. Redmond, Ph. D."
President and Chief Executive Officer

SIGNED "Branko Jankovic, CA"
Chief Financial Officer

Auditors' report

To the Shareholders of Ceapro Inc.,

We have audited the consolidated balance sheets of Ceapro Inc. as at December 31, 2007 and 2006, and the consolidated statements of net loss and comprehensive loss, and deficit and cash flows for the years 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 audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance 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, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Edmonton, Canada
March 6, 2008 except as to
Note 9(a) and Note 17(b) which
are as of April 21, 2008

SIGNED: "Stout & Company LLP"
Chartered Accountants

Financial Statements

CEAPRO INC. Consolidated Balance Sheets

	As at December 31	
	2007	2006
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,282,326	\$ 310,926
Accounts receivable	708,165	634,256
Inventories	156,584	160,456
Prepaid expenses and deposits	130,100	178,751
	2,277,175	1,284,389
RESTRICTED CASH (note 7)	50,000	-
DEPOSITS ON PROPERTY AND EQUIPMENT	-	167,828
PROPERTY AND EQUIPMENT (note 3)	2,260,418	610,629
	\$ 4,587,593	\$ 2,062,846
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 494,413	\$ 335,616
Current portion deferred revenue	107,007	105,000
Callable debt (note 4)	-	36,313
Current portion of long-term debt (note 5)	112,638	36,609
Current portion of royalties payable (note 6)	138,185	130,456
	852,243	643,994
DEFERRED ROYALTY REVENUE EMPLOYEE FUTURE BENEFITS OBLIGATION (note 7)	328,377	369,764
LONG-TERM DEBT (note 5)	283,648	219,340
ROYALTIES PAYABLE (note 6)	1,499,768	400,122
	69,905	125,827
	3,033,941	1,759,047
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (note 8(b))	5,016,395	2,508,059
CONTRIBUTED SURPLUS (note 8(c))	259,329	128,478
DEFICIT	(3,722,072)	(2,332,738)
	1,553,652	303,799
	\$ 4,587,593	\$ 2,062,846

CONTINGENCIES (note 9)

Approved on Behalf of the Board

Signed " John Zupancic"
Director

Signed " Edward Taylor"
Director

See accompanying notes

Financial Statements

CEAPRO INC.

Consolidated Statements of Net Loss and Comprehensive Loss, and Deficit

Years ended December 31

	2007	2006
Revenue		
Sales (note 10)	\$ 3,447,694	\$ 3,310,323
Cost of goods sold	1,793,997	1,413,976
Gross margin	1,653,697	1,896,347
Expenses		
General and administration	1,258,885	1,020,296
Royalties	325,733	317,355
Sales and marketing	418,816	342,207
Amortization	120,444	146,779
Interest on long-term debt	42,954	45,133
Interest on callable debt and other	875	1,220
	2,167,707	1,872,990
(Loss) income from operations	(514,010)	23,357
Other income (expenses)		
Research and product development	(695,661)	(365,424)
Bioenergy Feasibility Study	(91,121)	-
Other (loss) income (note 11)	(88,542)	69,710
	(875,324)	(295,714)
Loss before income taxes	(1,389,334)	(272,357)
Income taxes (note 12)		
Current	-	164,792
Reduction as a result of applying non-capital losses carried forward against the current year's taxable income	-	(164,792)
NET LOSS AND COMPREHENSIVE LOSS FOR THE YEAR	(1,389,334)	(272,357)
Deficit, beginning of year	(2,332,738)	(2,060,381)
Deficit, end of year	\$ (3,722,072)	\$ (2,332,738)
Net loss per common share:		
Basic	\$ (0.03)	\$ (0.01)
Diluted	\$ (0.03)	\$ (0.01)
Weighted average number of common shares outstanding	42,337,607	37,188,901

See accompanying notes

Financial Statements

CEAPRO INC. Consolidated Statements of Cash Flows

	Years ended December 31	
	2007	2006
Operating Activities		
Net loss and comprehensive loss for the year	\$ (1,389,334)	\$ (272,357)
Items not affecting cash and cash equivalents		
Amortization	120,444	146,779
Recognition of deferred royalty revenue	(39,390)	(37,820)
Employee future benefits obligation	64,308	59,394
Stock based compensation	70,241	25,592
	(1,173,731)	(78,412)
Changes in Non-Cash Working Capital Items		
Restricted cash	(50,000)	-
Accounts receivable	(73,909)	348,091
Inventories	3,872	67,702
Prepaid expenses and deposits	48,651	(87,990)
Accounts payable and accrued liabilities	158,797	50,753
Deferred revenue	10	(174,092)
	87,421	204,464
	(1,086,310)	126,052
Investing Activities		
Purchase of property and equipment	(1,770,233)	(77,785)
Deposits on property and equipment	167,828	(167,828)
	(1,602,405)	(245,613)
Financing Activities		
Repayment of long-term debt	(436,731)	(33,519)
Repayment of callable debt	(36,313)	(45,271)
Proceeds from long-term debt	1,612,406	-
Proceeds from issuance of share capital	2,692,100	-
Proceeds from exercise of stock options	163,876	89,227
Share capital issue costs	(287,030)	-
Decrease in royalties payable	(48,193)	(17,995)
	3,660,115	(7,558)
Increase (decrease) in cash and cash equivalents	971,400	(127,119)
Cash and cash equivalents at beginning of year	310,926	438,045
Cash and cash equivalents at end of year	\$ 1,282,326	\$ 310,926
Supplementary information		
Interest paid	\$ 43,829	\$ 46,353
Royalties paid	375,926	373,170
Cash and cash equivalents consist of:		
Cash on deposit with banks	\$ 8,047	\$ 165,251
CAD\$ term deposit	\$ 1,000,000	\$ -
US\$ term deposit	\$ 274,279	\$ 145,675
	\$ 1,282,326	\$ 310,926

See accompanying notes

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1 NATURE OF BUSINESS OPERATIONS AND GOING CONCERN

Ceapro Inc. (the "Company") is incorporated under the Canada Business Corporations Act and is listed on the TSX Venture Exchange. The Company's primary business activities relate to the marketing and development of various health and wellness products and technology relating to plant extracts.

These financial statements have been prepared on a going concern basis which assumes that the Company will continue in operation for the foreseeable future and accordingly will be able to realize its assets and discharge liabilities in the normal course of operations. Since inception, the Company has accumulated net losses, negative operating cash flow and has not yet achieved consistent profitability. The Company has relied on the proceeds of public and private offerings of equity securities and debentures, debt, and other income offerings to support the Company operations. The Company potentially faces material financial exposures related to litigation issues that are presently uncertain. The Company's ability to continue as a going concern is dependant on obtaining additional financial capital, achieving profitability, and generating positive cash flow to continue as a going concern.

These financial statements do not reflect the adjustments that might be necessary to the carrying amount of reported assets, liabilities and revenues and expenses and the balance sheet classification used if the Company were unable to continue operations.

2 ACCOUNTING POLICIES

(a) Use of estimates

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The significant areas requiring the use of management estimates relates to amortization of property and equipment, the assumptions used in determining stock based compensation, and the interest rate used in determining the value of employee future benefits obligation. Actual results could differ from those estimates.

(b) Principles of consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Ceapro Technology Inc., Ceapro Veterinary Products Inc., Ceapro Active Ingredients Inc., Ceapro BioEnergy Inc., and Ceapro USA Inc.

(c) Cash and cash equivalents

Cash and cash equivalents are defined as amounts on deposit with financial institutions and readily convertible term deposits.

(d) Revenue recognition

Revenue from the sale of health and wellness products is recognized as revenue at the time the products are shipped to customers.

The sale of royalty interests are recorded as deferred royalty revenue and are matched to future royalty expenses.

Royalty, licenses, and product development fees are recorded in accordance with the terms of the applicable agreements.

(e) Inventories

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

Inventory of work-in-process and active ingredients is valued at the lower of cost and net realizable value on an average cost basis.

Inventory of finished veterinary products is valued at the lower of cost and replacement cost on a first-in, first-out basis.

2 ACCOUNTING POLICIES (continued)

(f) Property and equipment

Property and equipment are recorded at cost and are amortized over their estimated useful lives as follows:

Manufacturing equipment	10 years straight line
Office equipment	20% declining balance
Computer equipment and software	30% declining balance
Leasehold Improvements	Over the term of the lease

A change was made in the company's estimate of the useful life of manufacturing equipment from 20% declining balance to straight line amortization over 10 years. This is considered to be a change in an accounting estimate. The impact of this change in accounting estimate in 2007 is lower amortization expense in the amount of \$86,844. The future impact of this change is lower amortization expense until the manufacturing equipment is fully amortized.

(g) Research and product development expenditures

Research costs are expensed when incurred. Product development costs are also expensed when incurred unless they are significant and meet generally accepted criteria for deferral. Costs are reduced by government grants and investment tax credits where applicable.

(h) Foreign currency

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at year end exchange rates and non-monetary assets at the exchange rates prevailing when the assets were acquired. Foreign currency denominated revenue and expense items are translated at the rate of exchange in effect at the time of the transaction. Foreign currency gains or losses arising on translation are included in income.

(i) Income taxes

The liability method is used for determining income taxes. Under this method, future income tax assets and liabilities are recognized for the estimated tax recoverable or payable that would arise if assets and liabilities were recovered or settled at the financial statement carrying amounts. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the year in which temporary differences are expected to be recovered or settled. Changes to these balances, including changes due to changes in income tax rates, are recognized in income in the period in which they occur. The amount of the future income tax assets recognized is limited to the amount that is more likely than not to be realized.

(j) Lease Obligations

Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incidental to the ownership of property is classified as a capital lease. At the inception of a capital lease, an asset and an obligation are recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair value at the beginning of the lease. All other leases are accounted for as operating leases wherein payments are expense as incurred.

(k) Government assistance

Government assistance is periodically granted to the Company under available government incentive programs. Government assistance relating to research and development expenditures is recorded as a reduction of the expenditures when received.

2 ACCOUNTING POLICIES (continued)

(l) Investment tax credits

Investment tax credits relating to qualifying scientific research and experimental development expenditures are accrued provided there is a reasonable assurance that the credits will be realized. When recorded, the investment tax credits are accounted for as a reduction of the related expenditures.

(m) Net loss per common share

Basic net loss per common share is computed by dividing the net loss by the weighted average number of common shares outstanding during the year. Diluted per share amounts reflect the potential dilution that could occur if convertible securities and convertible debt were converted to common shares. The treasury stock method of calculating diluted per share amounts is used whereby any proceeds from the conversion of convertible securities or convertible debt that are in-the-money are assumed to be used to purchase common shares of the Company at the average market price during the period. When the Company is in a net loss position, the conversion of convertible securities and debt is considered to be anti-dilutive.

(n) Stock based compensation

Stock based compensation is accounted for using the fair value method whereby compensation expense related to these programs is recorded in the statement of net loss, comprehensive loss and deficit with a corresponding increase to contributed surplus. The fair value of options granted is determined at the date of grant and expensed over the vesting period. The value of the warrants issued to agents is recorded as share issue costs with a corresponding increase to contributed surplus.

Consideration paid on the exercise of stock options and warrants is credited to share capital. Upon the exercise of the stock options and warrants, consideration received together with the amount previously recognized in contributed surplus is recorded as an increase to share capital. The Company does not incorporate an estimated forfeiture rate for stock options and agents warrants that may not vest, but accounts for forfeitures as they occur.

(o) Employee future benefits

The Company accrues its obligations under an employee defined retirement benefit plan and related costs, net of plan assets. The cost of retirement benefits earned by employees is determined using the accumulated benefit method and management's best estimate of expected plan investment performance and retirement ages of employees. Past service costs relating to plan amendments are accrued and recognized in the year the amendments occur.

(p) Impairment of long-lived assets

In the event that facts and circumstances indicate that the carrying value of the long-lived assets may be impaired, the Company performs a recoverability evaluation. If the evaluation indicates that the carrying value is not recoverable from undiscounted cash flows attributable to the assets, then an impairment loss is measured by comparing the carrying amount of the asset to its fair value.

(q) Recently adopted accounting pronouncements

Effective January 1, 2007, the Company adopted the revised CICA Handbook section 1506 "Accounting Changes", which requires that: (a) a voluntary change in accounting principles can be made if, and only if, the changes result in more reliable and relevant information, (b) changes in accounting policies are accompanied with disclosures of prior period amount and justification for the change, and (c) for changes in estimates, the nature and amount of the change should be disclosed. The Company has not made any voluntary change in accounting policies since the adoption of the revised standard.

2 ACCOUNTING POLICIES (continued)

Effective January 1, 2007, the Company prospectively adopted without restatement, the new CICA Handbook sections 3855 - Financial Instruments - Recognition and Measurement, 1530 - Comprehensive Income, and 3865 - Hedges. These sections provide standards for the recognition, measurement, disclosure, and presentation of financial assets, financial liabilities and derivatives. The standards prescribe when a financial instrument is to be recognized on the balance sheet and at what amount. They also specify how gains and losses on financial instruments are to be presented.

The standards relating to comprehensive income require the reporting and presentation of among other things, certain unrealized gains and losses outside of net income or loss as a separate component of shareholders' equity. Comprehensive income is defined as a change in equity (net assets) of an enterprise during a period from transactions and other events and circumstances from non-owner sources. The Company has no financial instruments or activities that give rise to other comprehensive income (loss).

The company has not participated in any hedging activities. As a result the standards relating to hedges have had no impact on the consolidated financial statements for the year ended December 31, 2007

The Company has cash and cash equivalents that are classified as held-for-trading. Accounts receivable are classified as loans and receivables. Accounts payable and accrued liabilities are classified as other liabilities. The carrying value approximates the fair value for each of these instruments due to the short term nature.

The long term debt is classified as other liabilities and in the opinion of management the carrying value approximates the fair value.

The adoption of these new standards concerning financial instruments and comprehensive income has had no impact on the consolidated financial statements for the year ended December 31, 2007.

(r) Future accounting pronouncements

Capital disclosures

Section 1535, Capital Disclosures establishes disclosure requirements concerning capital such as qualitative information about the Company's objectives, policies and processes for managing capital; quantitative data about what the Company regards as capital; and whether the Company has complied with any externally imposed capital requirements and, if not, the consequences of such non-compliance. The Company is presently evaluating the impact of this new standard, but does not expect the adoption of this standard to have a material impact on its financial position and results of operations. This section is effective for fiscal years beginning on or after October 1, 2007.

Financial Instruments - Disclosures and Financial Instruments - Presentation

Section 3862, *Financial Instruments - Disclosures* and Section 3863, *Financial Instruments - Presentation* replace Section 3861, *Financial Instruments - Disclosure and Presentation*, deals with revising and enhancing the Company's disclosure requirements, and carrying forward unchanged the Company's presentation requirements. The Company is presently evaluating the impact of these new standards, but does not expect the adoption of these standards to have a material impact on its financial position and results of operations. This section is effective for fiscal years beginning on or after October 1, 2007.

Inventories

Section 3031, *Inventories*, replaces Section 3030, *Inventories*, revising and enhancing the Company's standards for the measurement and disclosure of inventories. The Company is presently evaluating the impact of this new standard, but does not expect the adoption of this standard to have a material impact on its financial position and results of operations. This section is effective for fiscal years beginning on or after January 1, 2008.

2 ACCOUNTING POLICIES (continued)

Going Concern

Section 1400, *General Standards of Financial Statement Presentation* was amended to provide guidance on the assessment of whether an entity is a going concern and related disclosures. The company is presently evaluating the impact of this new standard, but does not expect the adoption of this standard to have a material impact on its financial position and results of operations. This Section is effective for fiscal years beginning on or after January 1, 2008.

3 PROPERTY AND EQUIPMENT

	2007		
	Cost	Accumulated Amortization	Net Book Value
Manufacturing equipment	\$ 2,577,649	\$ 521,110	\$ 2,056,539
Office equipment	66,249	42,494	23,755
Computer equipment and software	181,275	89,150	92,125
Leasehold improvements	95,991	7,992	87,999
	<u>\$ 2,921,164</u>	<u>\$ 660,746</u>	<u>\$ 2,260,418</u>

	2006		
	Cost	Accumulated Amortization	Net Book Value
Manufacturing equipment	\$ 964,280	\$ 431,389	\$ 532,891
Computer equipment	120,637	72,309	48,328
Office equipment	66,013	36,603	29,410
	<u>\$ 1,150,930</u>	<u>\$ 540,301</u>	<u>\$ 610,629</u>

4 CALLABLE DEBT

	2007	2006
Loan, payable at \$4,166 per month, principal and interest at 8%, secured by specific manufacturing equipment carrying value of \$122,802 (2006 - \$153,502) and a general security agreement, due November, 2007. The loan was repaid in full during the year.	\$ -	\$ 36,313

5 LONG-TERM DEBT

	2007	2006
Loan, payable at \$17,384 per month, principal and interest at 5.49%, secured by a general security agreement, due January, 2013.	\$ 1,612,406	-
Loan, payable at \$6,161 per month, principal and interest at 8.85%, secured by a general security agreement, due January, 2010. The loan was consolidated with the 5.49% loan during the year.	-	436,731
Less current portion	112,638	36,609
	<u>\$ 1,499,768</u>	<u>\$ 400,122</u>

Estimated principal payments due in the next five years are as follows:

2008	\$ 112,638
2009	129,502
2010	136,794
2011	144,496
2012	152,631
Thereafter	936,345
	<u>\$ 1,612,406</u>

5 LONG-TERM DEBT (continued)

The effective interest rate of 5.49% is a preferred rate and the monthly payments of \$17,384 reflect this preferred rate. In the event of default of any terms and conditions of the loan and enforcement of these terms and conditions by the lender, the preferred interest rate will be cancelled from the date of enforcement of the action. If such a circumstance were to arise, the interest rate would become 7.49% and result in monthly payments of \$18,925. The company is in compliance with all terms and conditions.

6 ROYALTIES PAYABLE

	2007	2006
Royalties payable pursuant to financial assistance received (note 6 (a))	\$ 125,829	\$ 181,751
Royalties payable pursuant to royalty interest offering (note 6 (c), (d), and (e))	82,261	74,532
	\$ 208,090	\$ 256,283
Less current portion	138,185	130,456
	\$ 69,905	\$ 125,827

- (a) In the year ended December 31, 1999, the Company received financial assistance in the amount of \$164,882 for the research and development of new products, patents, and markets. The Company is obligated to pay a 5% royalty (to a maximum of two times the financial assistance received) on sales generated from products developed using these funds. The portion of this obligation paid or accrued as at December 31, 2007 was \$329,764 (2006 - \$329,764). Pursuant to an agreement signed in March 2006, the terms of repayment were amended to allow all royalties payable as at December 31, 2005 in the amount of \$223,692 to be repaid \$13,981 per quarter commencing March 31, 2006. Royalties incurred subsequent to December 31, 2005 are to be repaid quarterly within 60 days of the quarter end.
- (b) In the year ended December 31, 2004, the Company received a commitment for financial assistance totaling \$250,000 for pre-market activities of CeaProve[®] (a health and wellness product) upon completion of project objectives as outlined and agreed to by both parties. In the year ended December 31, 2007, \$225,000 (2006 - \$225,000) of this commitment has been received. The Company is obligated to pay a royalty (to a maximum of two times the financial assistance received) on sales generated from CeaProve[®] on the following basis: 0% of revenues earned to December 31, 2005, 2.5% of revenues earned to December 31, 2006, and 5% thereafter until repaid. No royalties have been incurred during the current or prior years. The Company has repaid at December 31, 2007 \$nil (2006 - \$nil) of this obligation. Upon completion of the repayment of the financial assistance received, the Company will be required to repay \$19,750 advanced during the year ended December 31, 2002. The portion of this obligation paid or accrued as at December 31, 2007 was \$nil (2006 - \$nil).
- (c) In the year ended December 31, 2003, the Company completed a Royalty Income Unit offering through the terms described in an Offering Memorandum. Each royalty interest has a right to receive royalties equal to 0.00001% from the sale or licensing of the Company's active ingredients and animal health products, to a maximum cumulative amount of \$2.08 per unit. Proceeds from the offering of \$516,348 (before related expenses) represent the sale of a 5.163% royalty interest in the Company's future sales and licensing of active ingredients and animal health products. Maximum royalties payable are two times the amount invested or \$1,032,695. The portion of this obligation paid or accrued at December 31, 2007 was \$688,077 (2006 - \$490,055).
- (d) In the year ended December 31, 2003, the Company sold a 1.418% royalty interest in the Company's future sales and licensing of active ingredients and animal health products for \$141,796. In the year ended December 31, 2004, the Company sold an additional 1.724% royalty interest in the future sales and licensing of active ingredients and animal health products for \$172,401. The cumulative royalty interest of 3.142% for \$314,197 results in combined maximum royalties of two times the amount invested or \$628,394. The portion of this obligation paid or accrued at December 31, 2007 was \$452,252 (2006 - \$343,926).

6 ROYALTIES PAYABLE (continued)

- (e) On December 28, 2005 the Company sold a 2.285% royalty interest in the Company's future sales and licensing of active ingredients, animal health, and CeaProve® products for \$457,000. Maximum royalties payable are two times the amount invested or \$914,000. The portion of this obligation paid or accrued as at December 31, 2007 was \$154,421 (2006 - \$nil).
- (f) In the year ended December 31, 2005, the Company received a commitment for financial assistance totaling \$362,250 for product innovation development in the area of Veterinary Therapeutics and Active Ingredients. In the year ended December 31, 2007 \$362,250 (2006 - \$325,000) of the commitment has been received and nil was receivable at December 31, 2007 (2006 - \$37,250). The Company is obligated to pay a 2.5% royalty to a maximum of \$75,000 per quarter (to a maximum of two times the financial assistance received or \$724,500) on sales generated from products developed using these funds. These payments will commence when the royalty payments on investment agreements in note 6(a) are fully satisfied. The portion of the obligation paid or accrued at December 31, 2007 was \$nil (2006 - \$nil).
- (g) In the year ended December 31, 2005, the Company received a commitment for financial assistance totaling \$800,000 for pre-market activities of CeaProve® (a health and wellness product) upon completion of project objectives as outlined and agreed to by both parties. In the year ended December 31, 2007 \$510,000 of this commitment has been received (2006 - \$510,000). The Company is obligated to pay a royalty (to a maximum of one and a half times the financial assistance received or \$1,200,000) on sales of CeaProve® on the following basis: 0% of net sales and net sub-licensing revenues earned until royalty payments have been fully satisfied under the investment agreement in note 6(b), and 5% thereafter until repaid to a maximum of \$125,000 per quarter. No royalties have been incurred during the current year. The portion of this obligation paid or accrued as at December 31, 2007 was \$nil (2006 - \$nil).

7 EMPLOYEE FUTURE BENEFITS OBLIGATION

The Company has a partly funded non-registered, non-indexed defined retirement benefit plan for certain senior officers. The retirement benefit is two months' salary for each year they are employed by the Company.

	2007	2006
Unfunded balance, beginning of year	\$ 219,340	\$ 159,946
Current service cost	37,918	35,117
Interest costs on accrued obligation	26,390	24,277
	\$ 283,648	\$ 219,340

Management is required to make a significant estimate regarding the discount rate used to determine the accrued employee future benefit obligation. These significant estimates are of a long-term nature, which is consistent with the nature of the employee future benefits. The discount rate used to determine the accrued benefit obligation as at December 31, 2007 was 4.22% (2006 - 4.65%).

An internally restricted cash balance of \$50,000 has been deposited in a term deposit to partly fund the obligation.

8 SHARE CAPITAL

(a) Authorized

Unlimited number of Class A voting common shares
Unlimited number of Class B non-voting common shares

(b) Issued - Class A common shares

	2007		2006	
	Number of Shares	Amount	Number of Shares	Amount
Balance at beginning of year	37,505,505	\$ 2,508,059	37,076,170	\$ 2,414,830
Changes during the year:				
Equity placements	8,684,190	2,692,100	-	-
Exercise of options	860,368	163,877	429,335	93,229
Equity component of stock based compensation, net	-	11,847	-	-
Share capital issue costs	-	(359,488)	-	-
	47,050,063	\$ 5,016,395	37,505,505	\$ 2,508,059

(c) Contributed surplus

The following table summarizes the changes in contributed surplus:

	2007	2006
Balance at beginning of year	\$ 128,478	\$ 106,888
Stock based compensation expense (note 8 (d)(h))	143,023	25,592
Exercise of stock options	(12,172)	(4,002)
	\$ 259,329	\$ 128,478

(d) Stock Options

The Company has granted stock options to eligible employees, directors, officers, and consultants under stock option plans that vest over periods ranging from eighteen months to five years and have a maximum term of five years.

The Company accounts for options granted under these plans in accordance with the fair value based method of accounting for stock based compensation. In the current year the Company granted 490,000 (2006 - 525,000) stock options. The application of the fair value based method requires the use of certain assumptions regarding the risk-free market interest rate, expected volatility of the underlying stock and life of the options. The weighted average risk-free rate used in 2007 was 4.21% (2006 - 4.23%), the weighted average expected volatility was 81% (2006 - 90%) which was based on prior trading activity of the Company's shares, and the weighted average expected life of the options was 5 years. The stock based compensation expense recorded during the current year relating to options granted in 2007 and 2006 was \$70,565 (2006 - \$24,850).

In addition, the Company recorded stock based compensation expense of \$nil (2006 - \$742) relating to options granted in 2003.

8 SHARE CAPITAL (continued)

A summary of the status of the Company's stock options at December 31, 2007 and 2006 and changes during the years ended on those dates is as follows:

	2007		2006	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise price
Outstanding at beginning of year	3,082,460	\$ 0.24	3,286,795	\$ 0.23
Granted	490,000	0.28	525,000	0.29
Expired	(404,000)	0.23	-300,000	0.28
Exercised	(860,368)	0.19	-429,335	0.21
Outstanding at end of year	2,308,092	\$ 0.26	3,082,460	\$ 0.24
Exercisable at end of year	1,768,092	\$ 0.26	2,757,460	\$ 0.23

The following table summarizes information about the Company's stock options outstanding:

Exercise Price	Year of Expiration	2007	2006
		Number of Options	Number of Options
\$0.28	2012	390,000	-
\$0.30	2012	100,000	-
\$0.30	2011	225,000	225,000
\$0.27	2011	150,000	150,000
\$0.28	2010	-	175,000
\$0.25	2008	1,443,092	1,742,292
\$0.17	2007	-	790,168
		2,308,092	3,082,460

(e) Warrants

A summary of the status of the Company's warrants at December 31, 2007 and 2006 and changes during the years ended on those dates is as follows:

	2007		2006	
	Number of Warrants	Average Exercise Price	Number of Warrants	Average Exercise Price
Outstanding at beginning of year	774,066	\$ 0.59	774,066	\$ 0.59
Issued	4,806,608	0.44	-	-
Expired	(774,066)	0.59	-	-
Outstanding at end of year	4,806,608	\$ 0.44	774,066	\$ 0.59

8 SHARE CAPITAL (continued)

The following table summarizes information about the Company's warrants outstanding:

Exercise Prices	Expiration Date	2007 Number Outstanding
\$ 0.31	February 27, 2009	464,513
\$ 0.45	February 27, 2009	4,342,095
		4,806,608

Exercise Prices	Expiration Date	2006 Number Outstanding
\$ 0.60	March 31, 2007*	682,666
\$ 0.75	December 28, 2007	91,400
		774,066

*The expiry date on these warrants was extended from September 30, 2006 to March 31, 2007.

- (f) On March 31, 2005 the Company completed a private placement share offering of 682,666 Units, for aggregate gross proceeds of \$204,800. Each Unit was priced at \$0.30 and contained one common share of the Company and one common share purchase warrant entitling the holder thereof to acquire one additional common share at an exercise price of \$0.40 per share until September 30, 2005 and thereafter at a price of \$0.60 per common share until September 30, 2006. The expiry date on these warrants was extended from September 30, 2006 to March 31, 2007.
- (g) On December 28, 2005 the Company completed a Royalty Income Unit offering through the terms described in an Offering Memorandum, which resulted in proceeds of \$ 502,700 (914 units at \$550 per unit, net of related expense). Each unit is comprised of 100 Class A common shares of the Company ("common shares"), 100 Class A common share purchase warrants ("warrants"), and 100 royalty interests ("royalty interests"). Each warrant entitles the holder thereof to acquire one Class A common share at an exercise price of \$0.55 per share until June 28, 2006 and thereafter at a price of \$0.75 per share until December 28, 2007. Each royalty interest is a right to receive royalties equal to .000025% of the proceeds received by the Company from the sale or licensing of its active ingredients, animal health products, and CeaProve[®], up to a maximum cumulative amount of amount of \$10.00 per unit. Proceeds of \$457,000 related to royalty interest units and \$45,700 for common shares.
- (h) On June 27, 2007 the Company completed a brokered private placement unit offering of 8,684,190 units for aggregate gross proceeds of \$2,692,100. Each unit was priced at \$0.31 and contained one common share of the Company and one half of a common share purchase warrant. Each whole common share purchase warrant entitles the holder to acquire one additional common share at a price of \$0.45 per common share until February 27, 2009. As part compensation of the brokered private placement, a total of 464,513 broker warrants were issued. Each broker warrant entitles the holder to acquire one additional common share at a price of \$0.31 per common share. The company has recorded share capital issue costs and a corresponding increase in contributed surplus of \$72,458 to reflect the fair value of the warrants. The fair value of the warrants granted was calculated assuming the risk free interest rate was 4.56%, the expected life was 1.7 years and the expected volatility was 86%.

9 CONTINGENCIES

- (a) In 2002, Ceapro Inc. commenced litigation against a number of defendants in the Court of Queen's Bench of Saskatchewan (the "Saskatchewan Claim"). The defendants against whom the case proceeded to trial were the Government of Saskatchewan, Saskatchewan Government Growth Fund Ltd. (SGGF), Saskatchewan Government Growth Fund Management Corporation (SGGFMC), Gary K. Benson, Janice MacKinnon, and Can-Oat Milling Products Inc. The Saskatchewan Claim raises numerous causes of action against various of the defendants including a claim against all based in civil conspiracy. Ceapro claims damages in excess of \$19 million for loss of its investment in Canamino Inc., plus additional damages for loss of goodwill and other losses and for other relief.

9 CONTINGENCIES (continued)

As of December 31, 2007, the Saskatchewan Claim had proceeded part way through trial. Subsequently, after the close of Ceapro's case and prior to completion of the trial, all of the defendants filed non-suit applications. By a judgement dated February 19, 2008, four of the six defendants were successful and the trial judge dismissed all the claims against them. The aspect of the claim of civil conspiracy which was plead against all defendants was also dismissed against the remaining two defendants. The other allegations against the remaining two defendants, SGGF and SGGFMC, survived the non-suit application and the trial on those claims continued to the end of the trial on March 27, 2008. With respect to the dismissal ruling, Ceapro has brought an application to have a notice of appeal filed which was heard on April 14, 2008. The decision on this application has been reserved. The final trial judgement is now under reserved decision and a release of that decision is expected before June 30, 2008.

Legal fees and other direct costs associated with the lawsuit for all periods up to and including December 31, 2007 have been funded by the Company only from funds received from lawsuit contributors who, in exchange, have received interests in the proceedings, if any, from the Saskatchewan Claim; and through agreements with the Company's legal counsel to accept a portion of their fees on a contingency basis. Consequently, no costs associated with the lawsuit are included in the Company's financial statements. In addition, the Company was required to post a bond relating to legal costs up to \$305,000 which was secured by guarantees of certain members of the current and past Board of Directors and an Officer of the Company. The Company has indemnified the Board of Directors, certain past members of the Board of Directors, and an Officer in relation to the bond.

The outcome of the surviving aspects of the Saskatchewan Claim have not yet been determined. Until all decisions have been rendered, including any appellate rulings, the ultimate financial impact on the company remains uncertain, including any estimate of court costs. Ceapro may be successful in some aspects of the litigation and not others, and this could impact court costs. A significant court cost award against the Company could have a material impact on the Company's financial position. No provision has been made in the financial statements and the full financial impact, if any, will be recorded when the outcome of the litigation is known.

- (b) In the normal course of operations the Company may be subject to litigation and claims from customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the accounts where required. Although it is not possible to estimate the extent of potential costs, if any, management believes that the ultimate resolution of such contingencies would not have a material adverse effect on the financial position of the Company.

10 SALES

Substantially all sales are export sales to five distributors of the Company's products. The Company is therefore economically dependent on those distributors to maintain and expand the volume of product sales to existing and new customers.

11 OTHER (LOSS) INCOME

	2007	2006
Product Innovation Investment (note 6(f))	\$ -	\$ 37,250
Foreign exchange (losses) gains	(121,582)	32,828
Interest and other income (loss)	33,040	(368)
	\$ (88,542)	\$ 69,710

12 INCOME TAXES

(a) Non-capital losses

The Company has accumulated non-capital losses carried forward for income tax purposes of approximately \$5,216,900, the benefit of which has not been reflected in these consolidated financial statements. These losses may be applied against future taxable income within the limitations prescribed by the Income Tax Act and expire as follows:

2008	\$ 570,800
2015	293,400
2026	651,500
2027	3,701,200
	<u>\$ 5,216,900</u>

(b) Capital losses

The Company has accumulated capital losses of approximately \$6,807,000, which can be carried forward indefinitely to offset future capital gains.

(c) Scientific research and experimental development (SR & ED)

The Company has accumulated an SR & ED expenditure pool of approximately \$1,506,000, which can be carried forward indefinitely to be applied against future taxable income.

The Company has accumulated SR & ED investment tax credits of approximately \$37,000. These credits may be applied against future federal income taxes payable and expire as follows:

2008	\$ 16,000
2009	400
2012	20,600
	<u>\$ 37,000</u>

(d) Temporary differences

A future income tax asset reflects the net effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future income tax asset is as follows:

Income tax effect of deductible temporary differences:	2007	2006
Non-capital losses and SR & ED expenditures carried forward	\$ 1,983,000	\$ 1,190,000
Net capital losses carried forward	1,004,000	1,093,000
SR&ED investment tax credits	37,000	156,000
Undepreciated capital cost for tax purposes in excess of net book value	2,195,000	3,069,000
Deferred revenue recognized for tax purposes	129,000	152,000
Valuation allowance	(5,348,000)	(5,660,000)
	<u>\$ -</u>	<u>\$ -</u>

For consolidated financial statement purposes, no future income tax asset has been recorded at December 31, 2007 and 2006 as it is not more likely than not to be realized.

(e) Income tax reconciliation

The Company's consolidated income tax position comprises tax benefits and provisions arising from the respective tax positions of its taxable entities. The Company's income tax provision differs from that calculated by applying statutory rates for the following reasons:

	2007	2006
Income taxes (recovery) based on federal and provincial statutory income tax rate of 32.12% (2006 - 32.50%)	\$ (446,254)	\$ (88,516)
Tax effect of expenses that are not deductible	8,140	24,072
Tax effect of current year non-capital losses not recognized	1,188,826	211,734
Tax effect of property and equipment	(738,063)	86,373
Tax effect of deferred revenue recognized	(12,649)	(68,871)
Income tax reduction as a result of applying non-capital losses carried forward against current year taxable income	-	(164,792)
	<u>\$ -</u>	<u>\$ -</u>

13 RELATED PARTY TRANSACTIONS

Related party transactions during the years not otherwise disclosed in these consolidated financial statements are as follows:

	2007	2006
Royalties earned by employees and directors	\$ 59,233	\$ 118,098
Sale of lawsuit interests to employees and directors	25,000	195,000
Amounts payable to employees and directors included in royalties payable	13,272	25,107
Amounts receivable from directors and employees included in accounts receivable	8,500	150,000
Prepaid expense (accounts payable) related to director fees	(36,359)	44,066

These transactions are in the normal course of operations and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

14 SEGMENTED INFORMATION

The Company operates in one industry segment, which is the active ingredient product technology industry. The majority of the revenue is derived from sales in North America. All the assets of the Company, which support the revenues of the Company, are also located in North America. The distribution of revenue by location of customer is as follows:

	2007	2006
North America	\$2,364,387	\$2,273,867
Other	1,083,307	1,036,456
	\$3,447,694	\$3,310,323

15 FINANCIAL INSTRUMENTS

The estimated fair value of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities, callable debt, and current portions of long-term debt and royalties payable are estimated to approximate their carrying value due to their short-term nature.

The fair value of long-term debt, royalties payable, and employee future benefits obligation are estimated to approximate their carrying value using the Company's incremental borrowing rate or discounted cash flow analysis for similar types of borrowing arrangements.

The Company operates internationally, giving rise to exposure to market risks from changes in foreign exchange rates in relation to the resulting accounts receivable and accounts payable and accrued liabilities. The company is exposed, in its normal course of business to credit risk from customers. A significant portion (70%) of the outstanding accounts receivable at December 31, 2007 is due from one customer. No other single party accounts for a significant balance of accounts receivable.

It is management's opinion that the Company is not exposed to significant interest risk from these financial instruments.

16 LEASE COMMITMENTS

The Company is committed to future annual payments under operating leases for manufacturing facilities and office space as follows:

2008	\$ 157,969
2009	175,206
2010	95,266
	<u>\$ 428,441</u>

17 SUBSEQUENT EVENTS

- (a) Subsequent to December 31, 2007, the Company granted 345,000 stock options to employees, including 150,000 to two officers. The options have an exercise price of \$0.25 and expire in January 2013.

- (b) Subsequent to December 31, 2007 the company has received invoices from legal counsel for services rendered in furtherance of the Saskatchewan Claim in the amount of \$649,330. The legal invoices totaled \$432,212 for the months of January and February 2008 and \$217,118 for March 2008. See Note (9a)