ZECOTEK MEDICAL SYSTEMS INC.

CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS
ENDED JULY 31, 2007 AND 2006

"Forging strong relationships. Providing clear business advice."

berris mangan

CHARTERED ACCOUNTANTS

AUDITORS' REPORT

To the Shareholders of:
Zecotek Medical Systems Inc.

We have audited the consolidated balance sheets of Zecotek Medical Systems Inc. as at July 31, 2007 and 2006 and the consolidated statements of 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 the financial statements based on our audit.

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 positions of the Company as at July 31, 2007 and 2006 and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Berris Mangan

CHARTERED ACCOUNTANTS

Vancouver, B.C.
November 15, 2007

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A PARTNERSHIP OF INCORPORATED PROFESSIONALS

ZECOTEK MEDICAL SYSTEMS INC.
CONSOLIDATED STATEMENTS OF LOSS AND DEFICIT
(Expressed in Canadian Dollars)

Years ended July 31, 2007 and 2006

	2007	2006
ASSETS		
Current		
Cash and cash equivalents	$ 1,577,863	$ 249,014
Short term investments *(note 4)*	-	3,500,000
Accrued interest receivable	5,416	28,935
Goods and services tax recoverable	34,346	121,702
Prepaid expenses	46,601	10,752
Total Current Assets	1,664,226	3,910,403
Due from related parties *(note 5)*	65,209	78,511
Restricted short term investments *(note 4)*	20,000	20,000
Deposits *(notes 15 (j), 16)*	653,689	73,233
Property and equipment *(note 6)*	567,151	122,405
Equipment under capital lease (note 7)	48,643	-
Patent costs *(note 8)*	137,112	71,348
Intangible assets and development costs *(note 9)*	1	1
Total Assets	$ 3,156,031	$ 4,275,901
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	$ 325,344	$ 219,032
Current portion of obligations under capital lease	6,764	-
Share subscription received *(note 20(b))*	14,145	-
Liabilities of discontinued operations *(note 13)*	53,254	53,254
	399,507	272,286
Obligations under capital lease	34,471	-
Shareholders' Equity		
Share capital *(note 10(b))*	21,809,339	16,246,313
Contributed surplus *(note 10(g))*	2,955,552	1,558,457
Deficit	(22,042,838)	(13,801,155)
Total Shareholders' Equity	2,722,053	4,003,615
Nature of Business and Going Concern Uncertainty *(note 1)*		
Commitments *(note 15)*		
Contingent Liabilities *(note 16)*		
Subsequent Events *(note 20)*		
Total Liabilities and Shareholders' Equity	$ 3,156,031	$ 4,275,901

Approved, on behalf of the Board:

"Faouzi Zerrouk"
Director

"Erich Sager"
Director

See accompanying Notes to Consolidated Financial Statements

ZECOTEK MEDICAL SYSTEMS INC.
CONSOLIDATED STATEMENTS OF LOSS AND DEFICIT
(Expressed in Canadian Dollars)

Years ended July 31, 2007 and 2006

	2007	2006
REVENUE		
Interest income	$ 74,040	$ 44,153
EXPENSES		
General and administrative *(note 12)*	5,207,903	2,174,562
Research and development *(notes 11, 14(a),(c))*	2,919,790	595,787
Impairment loss *(note 9)*	-	2,990,606
Amortization	112,600	26,828
Foreign exchange	75,430	(8,965)
	8,315,723	5,778,818
Net loss for the year	(8,241,683)	(5,734,665)
Deficit, Beginning of Year	(13,801,155)	(7,778,490)
Excess of purchase price over carrying amount of intangible assets acquired *(notes 9(ii) and 10(b)(ii))*	-	(288,000)
Deficit, End of Year	$(22,042,838)	$(13,801,155)
Loss per common share – basic and diluted	$(0.22)	$(0.20)
Weighted average number of common shares outstanding – basic and diluted *(note 10(f))*	37,590,137	28,219,900

See accompanying Notes to Consolidated Financial Statements

ZECOTEK MEDICAL SYSTEMS INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Expressed in Canadian Dollars)

Years ended July 31, 2007 and 2006

	2007	**2006**
Operating Activities:		
Net loss for the year	$(8,241,683)	$(5,734,665)
Adjustments for items not involving cash:		
Amortization – property and equipment	110,945	26,828
Amortization – patent costs	1,655	-
Stock-based compensation *(note 10(e))*	1,530,686	1,074,620
Impairment loss *(note 9)*	-	2,990,606
	(6,598,397)	(1,642,611)
Changes in non-cash working capital:		
Accrued interest receivable	23,519	(28,935)
Goods and services tax recoverable	87,356	(58,877)
Prepaid expenses	(35,849)	(10,752)
Accounts payable and accrued liabilities	106,312	173,383
Net Cash Used in Operating Activities	(6,417,059)	(1,567,792)
Investing Activities:		
Proceeds on disposal of **(**purchase of**)** short term investments	3,500,000	(2,500,000)
Deposits paid	(580,456)	(60,073)
Acquisition of property and equipment	(547,107)	(97,349)
Development costs incurred	-	(1,202,313)
Patent costs incurred	(67,419)	(71,348)
Acquisition of intangible assets	-	(288,000)
	2,305,018	(4,219,083)
Financing Activities:		
Proceeds from shares issued, net of issuance costs	5,429,437	5,859,337
Share subscriptions received	14,145	-
Repayments of obligations under capital lease	(15,994)	-
Advances from related parties	13,302	60,306
Advances to related parties	-	(6,352)
	5,440,890	5,913,291
Increase in cash and cash equivalents	1,328,849	126,416
Cash and cash equivalents, Beginning of Year	249,014	122,598
Cash and cash equivalents, End of Year	$ 1,577,863	$ 249,014

See accompanying Notes to Consolidated Financial Statements

(Expressed in Canadian Dollars)

1. NATURE OF BUSINESS AND GOING CONCERN UNCERTAINTY

Nature of Business

Zecotek Medical Systems Inc. (the "Company") is a development stage enterprise which was incorporated on November 25, 1983 under the laws of the Province of British Columbia, Canada. The Company changed its name from Equicap Financial Corp. on February 10, 2005.

The activities of the Company are focused on the creation of advanced materials and integrated optoelectronic devices for high resolution medical imaging, optical precision surgery and biopharmaceutical research.

The Company has five wholly owned subsidiaries as follows:

Subsidiary	Date of incorporation	Main current or planned activity
Zecotek Crystals Inc.	August 6, 2004	Inactive
Zecotek Lasers Inc.	June 7, 2005	Inactive
Zecotek 3D Inc.	October 18, 2005	Inactive
Zecotek Medical Systems Singapore Pte. Ltd.	April 4, 2006	Holding company for Singapore subsidiaries
Zecotek Medical Systems AG	May 8, 2007	Swiss company for certification of medical technologies

Zecotek Medical Systems Sinagpore Pte. Ltd. holds 90% ownership interests in Zecotek Display Systems Pte. Ltd. and Zecotek Imaging Systems Pte. Ltd., and an 80% ownership interest in Zecotek Laser Systems Pte. Ltd.. These subsidiaries were incorporated in the 2006 year, with principal activities described as follows:

Subsidiary	Main planned activity
Zecotek Display Systems Pte. Ltd.	Research and development (and eventual exploitation) of 3D imaging technologies
Zecotek Imaging Systems Pte. Ltd.	Research and development (and eventual exploitation) of medical imaging technologies
Zecotek Laser Systems Pte. Ltd.	Research and development (and eventual exploitation) of medical laser technologies

Four other wholly owned subsidiaries of the Company, O-Tooz Energie Group Inc., FilmIndustry.com, Inc., DJscene.com Media, Inc. and OnlineConsortium.com Inc., have been inactive since August of 2001 (see note 13)

1. NATURE OF BUSINESS AND GOING CONCERN UNCERTAINTY - Continued

Going concern uncertainty

These financial statements have been prepared in accordance with generally accepted accounting principles on a going concern basis, which presumes that the Company will be able to realize assets and discharge liabilities in the normal course of business for the foreseeable future. The Company has incurred significant losses since its inception. To date, the Company has no products in commercial production or use and does not currently have any revenues other than interest earned on short-term investments. These factors, among others, raise uncertainty about the ability of the Company to continue as a going concern. The continued operations of the Company are dependent upon the ability of the Company to obtain further equity financing, the support of its principal shareholders, and to successfully bring its technologies to market and achieve future profitable operations, the outcome of which cannot be predicted at this time. Management of the Company is of the view that these objectives can be met and that the Company will continue as a going concern.

These financial statements do not give effect to adjustments, if any, which would be necessary should the Company be unable to continue as a going concern and, therefore, be required to realize its assets and liquidate its liabilities in other than the normal course of business and at amounts which may differ from those shown in the financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

The consolidated financial statements of the Company are prepared in accordance with Canadian generally accepted accounting principles. The consolidated financial statements include the accounts of the Company and its wholly and majority owned subsidiaries as identified in Note 1. All significant inter-company accounts and transactions have been eliminated upon consolidation.

No recognition is made of the share of a loss of a non-controlling interest in a subsidiary which would result in an asset to the company.

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 revenues and expenses during the period. Actual results may differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents consists of cash on hand, balances on deposit with banks and highly liquid market investments with original terms of maturity of less than ninety days at time of acquisition, intended for use in current operations.

Short Term Investments

Short term investments, which consist of financial instruments purchased with an original maturity of greater than ninety days and less than one year, are recorded at the lower of cost and estimated market value.

2. SIGNIFICANT ACCOUNTING POLICIES - Continued

Restricted Short Term Investments

Restricted short term investments are short term investments pledged as security or otherwise subject to restricted liquidity, and are recorded at the lower of cost and estimated market value.

Property and Equipment

Equipment, furniture, leasehold improvements, and vehicle are recorded at cost less accumulated amortization. Amortization of equipment, furniture and vehicle is provided on a declining balance basis over the expected useful lives at rates of 33.33%, 20% and 33.3% per annum, respectively. Leasehold improvements are amortized over the duration of the lease term on a straight-line basis.

Intangible Assets

Intangible assets represent the purchase costs of the LFS crystal, biophotonic and other technologies.

The cost of intangible assets which are determined to have an indefinite life is not amortized, but is tested for impairment on an annual basis, based on a comparison of the fair value of the intangible asset with its carrying amount. The carrying amount is adjusted for impairment as necessary and any excess of the carrying amount over the fair value of the intangible asset is charged to earnings in the current period.

Intangible assets which are determined to have a finite useful life are amortized on a systematic basis over the estimated remaining useful life.

Research and Development Costs

Research costs are expensed in the year incurred.

Development costs include all expenditures considered directly attributable to efforts by the Company to develop, and bring to commercial production, a new product. Such amounts are charged as an expense in the period incurred except in circumstances where the market and technical feasibility of the product have been established, and recovery of development costs can reasonably be regarded as assured, in which case such costs are capitalized.

Product registration costs related to efforts by the Company to acquire legal protections for its proprietary products, such as trademarks and patents, are capitalized if the Company believes that obtaining the trademark or patent, and recovery of the costs from future related revenues is reasonably assured, otherwise the costs are expensed. Capitalized costs are amortized on a straight-line basis over the estimated useful life of the trademark or patent upon granting.

Impairment of Long-lived Assets

The Company reviews for the impairment of long-lived assets, including property and equipment and intangible assets with finite life, held for use, whenever changes in circumstances indicate that the carrying amount of an asset may not be recoverable from expected future cash flows. The assessment of recoverability is made based on projected undiscounted future net cash flows that are directly associated with the asset’s use and eventual disposition. The amount of the impairment, if any, is measured as the difference between the carrying amount and the fair value of the impaired assets, and is presented as an impairment loss in the current period.

2. SIGNIFICANT ACCOUNTING POLICIES - Continued

Foreign Currency Translation

The Company follows the temporal method of foreign currency translation for consolidation of its foreign subsidiaries' operations. Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rate in effect at each year-end date. Non-monetary assets and liabilities and related depreciation and amortization expenses are translated at the historical exchange rate. Revenue and expenses, other than depreciation and amortization, are translated at the average exchange rate for the year. The resulting exchange gain or losses on translation are included in operations for the year.

Stock-Based Compensation

The Company grants stock options to employees, directors, officers and consultants pursuant to the stock option plan described in Note 10(e). The fair value method of accounting for stock-based compensation transactions is used. The fair value of stock options is estimated at the date of grant using the Black-Scholes Option Pricing Model and is amortized over the vesting terms of the options.

Warrants

Proceeds from issuances by the Company of units consisting of shares and warrants are allocated based on the residual method, whereby the carrying amount of the warrants is determined based on any difference between gross proceeds and the fair market value of the shares. If the proceeds from the offering are less than or equal to the estimated fair market value of shares issued, a nil carrying amount is assigned to the warrants.

Share issue costs

Professional, agent and regulatory fees as well as other costs directly attributable to specific financing transactions are reported as deferred financing costs until the transactions are completed, if successful completion is considered reasonably assured. Share issue costs are charged to capital stock when the related shares are issued. Costs relating to financing transactions that are not completed or for which completion is considered unlikely, are charged to net income.

Income Taxes

The Company accounts for income taxes using the liability method of tax allocation. Future income taxes are recognized for the future income tax consequences attributable to differences between the carrying amounts of assets and liabilities and their respective income tax bases. Future income tax assets and liabilities are measured using substantively enacted income tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. The effect on future income tax assets and liabilities of a change in rates is included in earnings in the period that includes the enactment date. Future income tax assets are recorded in the financial statements if realization is considered more likely than not.

2. SIGNIFICANT ACCOUNTING POLICIES - Continued

Loss per Share

Basic loss per share is calculated using the weighted average number of shares outstanding during the year. The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is recognized based on the use of proceeds that could be obtained upon exercise of such options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the period. This calculation generally produces an anti-dilutive effect for loss years.

Tenant Inducements

Inducements received by the Company from landlords with respect to leased premises are deferred and recognized as a reduction of rent expense evenly over the term of the lease.

Asset Retirement Obligations

The Company recognizes the fair value of any liability for an asset retirement obligation in the period in which it is incurred by increasing the carrying amount of the related asset by the same amount as the liability that is recorded. The asset retirement cost is amortized over the asset's estimated useful life and charged to operations.

3. FINANCIAL INSTRUMENTS AND RISKS

The fair values of financial instruments are estimated at a specific point in time, based on relevant information about financial markets and specific financial instruments. As these estimates are subjective in nature, involving uncertainties and matters of significant judgment, they cannot be determined with precision. Changes in assumptions can significantly affect estimated fair values.

The carrying value of cash and cash equivalents, short term and restricted short term investments, accrued interest receivable, due from related parties, deposits, accounts payable and accrued liabilities, subscriptions received, obligations under capital lease, and liabilities of discontinued operations approximate their fair value.

Financial instruments that potentially subject the Company to concentration of credit risks consist principally of cash and short term investments. The Company places its cash in high credit quality financial institutions. Concentration of credit risks with respect to receivables is limited.

Financial risk is the risk to the Company’s results of operations that arises from fluctuations in interest rates and foreign exchange rates and the degree of volatility of these rates, as well as credit risk associated with the financial stability of the issuers of the financial instruments. The Company’s short term investments are invested in fixed rate securities. Some of the transactions of the Company’s Singapore operations are undertaken in Singapore dollars. The Company also incurs certain costs in US dollars. Accordingly, the Company is exposed to foreign exchange risk in respect to these currencies, and has not undertaken hedging activities to mitigate this risk. At July 31, 2007, the Company had a cash balance of $610,981 Singapore dollars, ($429,520 Canadian dollars), exposed to foreign exchange risk.

(Expressed in Canadian Dollars)

4. SHORT TERM INVESTMENTS

Short term investments were comprised of guaranteed investment certificates ("GIC") with a weighted average interest rate of 3.25% (2006 – 3.75%).

A GIC in the amount of $20,000 (2006 - $20,000) has been pledged as collateral for the Company's corporate credit cards and is presented on the balance sheet as Restricted short term investments.

5. AMOUNTS DUE FROM RELATED PARTIES

Details of amount due from related parties are as follows:

	2007	**2006**
Due from Dr. Faouzi Zerrouk	$ 60,023	$ 54,332
Due from Zecotek Laboratories Inc.	5,186	24,179
	$ 65,209	$ 78,511

Amounts due from Dr. Faouzi Zerrouk ("Dr. Zerrouk"), the Chairman of the Board of Directors, President and Chief Executive Officer, relate to travel and other advances.

Amounts due from Zecotek Laboratories Inc., a company controlled by Dr. Zerrouk, which is a subsidiary of a significant shareholder of the Company, Zecotek Holdings Inc., represent advances made pursuant to a Support Agreement (see note 14(a)).

The amounts due from related parties are non-interest bearing, unsecured and without fixed terms of repayment.

6. PROPERTY AND EQUIPMENT

	Cost	Accumulated Amortization	Amortized Cost
Equipment	$ 440,268	$ 83,137	$ 357,131
Furniture	59,724	12,750	46,974
Leasehold improvements	209,261	46,215	163,046
July 31, 2007	$ 709,253	$ 142,102	$ 567,151

(Expressed in Canadian Dollars)

6. PROPERTY AND EQUIPMENT - Continued

	Cost	Accumulated Amortization	Amortized Cost
Equipment	$ 122,409	$ 25,609	$ 96,800
Furniture	22,732	5,630	17,102
Leasehold improvements	17,007	8,504	8,503
July 31, 2006	$ 162,148	$ 39,743	$ 122,405

7. EQUIPMENT UNDER CAPITAL LEASE

	Cost	Accumulated Amortization	Amortized Cost
2007			
Vehicle	$ 57,227	$ 8,584	$ 48,643
2006	$ -	$ -	$ -

Equipment under capital lease is amortized on a straight-line basis over the lease term. The amount of amortization charged to expense for the 2007 year was $8,584.

8. PATENT COSTS

	Cost	Accumulated Amortization	Amortized Cost
2007	$ 138,767	$ 1,655	$ 137,112
2006	$ 71,348	$ -	$ 71,348

During the 2007 year, the company received a U.S. patent for its LFS crystal technology. The company has commenced amortization of the related patent costs over the twenty year life of the patent.

9. INTANGIBLE ASSETS AND DEVELOPMENT COSTS

Balance, July 31, 2005	**$ 1,788,293**
Acquisition of intangible assets *(note 9 (ii))*	**1**
Development costs incurred during the 2006 year	
LFS crystal technology	**185,905**
Biophotonic technology	**1,016,408**
Impairment loss for the 2006 year *(notes 9(i) and (ii))*	**(2,990,606)**
Balance, July 31, 2007 and July 31, 2006	**$ 1**

9. INTANGIBLE ASSETS AND DEVELOPMENT COSTS - continued

i) On December 31, 2004, the Company's subsidiary, Zecotek Crystals Inc., completed an Asset Purchase Agreement for the purchase of a Lutetium Fine Silicate ("LFS") crystal technology from Zecotek Holdings Inc., for total consideration of $1,636,333, consisting of cash of $280,333 and common shares, warrants and stock options of the Company with a total assigned value of $1,356,000. Legal expenses incurred in relation to the acquisition amounted to $35,460. Further development expenses of $302,405 representing salaries and fees paid to employees and consultants and other directly attributable costs for work undertaken to develop and commercialize the technology had been capitalized.

At July 31, 2006, the capitalized acquisition and development costs to that date, totalling $1,974,198, were written-down to a nominal carrying amount of $1. The technology has been licensed on a long term basis to a third party as described in Note 15(a). However, the ability of the Company to generate revenue from the technology under this agreement is unproven and uncertain. Therefore the Company does not have adequate assurance that the capitalized costs will be recovered in a reasonable period of time.

ii) Effective May 12, 2006, the Company and its Singapore subsidiaries, Zecotek Medical Systems Singapore Pte. Ltd. ("ZMSS"), Zecotek Display Systems Pte. Ltd., Zecotek Imaging Systems Pte. Ltd. and Zecotek Laser Systems Pte. Ltd. completed an asset purchase of certain biophotonics technology from Zecotek Holdings Singapore Pte. Ltd. of which Dr. Zerrouk is a majority shareholder. Consideration consisted of cash of $338,000, the issuance of 11,750,000 common shares of the Company (estimated market value of $0.90 per share) and preferred shares of all subsidiary companies of ZMSS which are convertible to 10% of the issued common shares of each subsidiary The cash payment and issuance of common shares of the Company was completed in May of 2006. The preferred shares were issued on December 5, 2006.

In conjunction with the asset purchase, the Company granted options to acquire 2,125,000 common shares of the Company at a price of $1.76 which may be exercised for a period of five years, to certain employees, directors, officers, and consultants, of the vendor and related companies.

Under the asset purchase agreement, the Company is responsible for any liabilities associated with the purchased assets, including any sales taxes arising as a result of the purchase and any contractual liabilities or liabilities associated with intellectual property rights.

The transaction was considered to be a Related Party transaction and consequently the purchased intangible assets were recorded at the nominal carrying amount of the related party vendor. Under this presentation, the shares issued as consideration for the purchase have also been recorded at a nominal amount. The cash portion of the consideration which was paid in the 2006 year ($258,000) has been recorded as an increase of the deficit balance.

As at July 31, 2006, the Company had incurred development costs related to this technology, including that described in Note 15(b), before and after the acquisition of the technology, totalling $1,016,408, which had been capitalized. These costs were written off as at July 31, 2006 as the Company was unable to establish reasonable assurance of future recovery of these costs based on projected cash flows derived from the technology.

iii) Effective March 28, 2007, the Company's Singapore subsidiary, Zecotek Laser Systems Pte. Ltd., completed two asset purchases of certain laser technologies from Inversion Fibre Lasers and Tekhnoscan as described in Note 15(i).

(Expressed in Canadian Dollars)

10. SHARE CAPITAL

a) Authorized

The authorized share capital of the Company is an unlimited number of common voting shares with no par value.

b) Issued and outstanding common shares:

	Number of Shares #	Amount $
Balance, July 31, 2005	15,033,341	10,506,895
Private placement (i)	6,389,400	4,962,284
Acquisition of technologies (ii)	11,750,000	1
Exercise of options (iii)	130,000	114,133
Exercise of warrants (iv)	1,390,000	663,000
Balance, July 31, 2006	**34,692,741**	**16,246,313**
Private placement (v)	3,043,478	3,067,733
Exercise of options (vi)	553,000	584,671
Exercise of agent options (vii)	507,102	588,578
Exercise of warrants (viii)	1,016,957	1,322,044
Balance, July 31, 2007	**39,813,278**	**$ 21,809,339**

i) On May 12, 2006, the Company completed an offering of 6,389,400 units at $0.90 per unit for net cash proceeds of $5,128,837 after issuance expenses of $621,623. Each unit consists of one common share and one-half non-transferable share purchase warrant. Each whole warrant entitles the holder to purchase one additional common share for a period of eighteen months at a price of $1.30 per share. The Company allocated total proceeds of $5,750,460 to common shares and a nil value to the attached warrants. The Company also issued 638,940 agents' options to agents for corporate finance services rendered in relation to the transaction. Each agent option consists of the right to acquire a unit with the same terms as described above. The estimated fair value of agents' options granted was determined to be $166,553 ($0.52 per share), using the Black-Scholes option pricing model (note 10(d)).

ii) On May 12, 2006, pursuant to the Asset Purchase Agreement described in Note 9(ii), as partial consideration paid for the acquisition of biophotonic technology, the Company issued 11,750,000 common shares. The common shares are subject to escrow and are to be released according to a pre-determined schedule over three years to May of 2009. The shares were recorded at the nominal carrying amount of the related party vendor. Share issuance costs of $30,000 were incurred, which have been recorded as an increase of the deficit balance.

iii) During the year ended July 31, 2006, 120,000 options were exercised by a director and officer of the Company at $0.50 per share, and 10,000 options at $0.75 per share were exercised by an employee, for total cash proceeds of $67,500. Contributed surplus amounts of $43,650 and $2,983 respectively related to these options were consequently transferred to the share capital account.

iv) During the year ended July 31, 2006, 1,390,000 warrants were exercised at an approximate weighted average price of $0.48 per share for total cash proceeds of $663,000.

(Expressed in Canadian Dollars)

10. SHARE CAPITAL - Continued

b) Issued and outstanding common shares - Continued

v) On February 19, 2007, the Company issued, by way of a private placement, 3,043,478 common shares at $1.15 per share for gross proceeds of $3,500,000. The Company paid a finder's fee equal to 8% of the gross proceeds of the sale of the shares and issued non-transferable agent's warrants to purchase shares equal in number to 7% of the shares sold under the private placement. The warrants have an exercise price of $0.90 and expire two years from the date of placement. The estimated fair value of agents' warrants granted was determined to be $152,267 ($0.71 per share), using the Black-Scholes option pricing model (note 10(d)).

vi) During the year ended July 31, 2007, 553,000 options at an approximate weighted average price of $0.78 were exercised for total cash proceeds of $431,000. Contributed surplus amounts of $153,671 related to these options were consequently transferred to the share capital account.

vii) During the year ended July 31, 2007, 507,102 agent options at $0.90 per share were exercised for total cash proceeds of $456,392. Contributed surplus amounts of $132,187 related to these options were consequently transferred to the share capital account. One half share purchase warrant was attached to each share received in the exercise of options, giving rise to 253,551 warrants. These warrants expire November 12, 2007 and have an exercise price of $1.30.

viii) During the year ended July 31, 2007, 1,016,957 warrants were exercised at $1.30 per share for total cash proceeds of $1,322,044.

c) Common share purchase warrants

	Number of warrants	Weighted average exercise price
Balance, July 31, 2005	1,930,000	$ 0.59
Warrants granted	3,194,700	1.30
Warrants exercised	(1,390,000)	0.48
Warrants expired	(540,000)	0.87
Balance, July 31, 2006	**3,194,700**	**1.30**
Warrants exercised	(1,016,670)	1.30
Balance, July 31, 2007	**2,178,030**	**$ 1.30**

At July 31, 2007, the share purchase warrants outstanding and exercisable were as follows:

Number of common shares to be issued	Exercise price	Date of expiry
2,178,030	**$1.30**	**November 12, 2007**

(Expressed in Canadian Dollars)

10. SHARE CAPITAL - Continued

d) Agent's warrants and options

	Number of warrants	Weighted average exercise price
Balance, July 31, 2005	**-**	**$ -**
Agents' options granted	638,940	.90
Balance, July 31, 2006	**638,940**	**.90**
Agents' options exercised	(507,102)	.90
Agents' warrants granted on exercise of options	253,551	1.30
Agents' warrants exercised	(6,287)	1.30
Agents' warrants granted in private placement	213,043	.90
Balance, July 31, 2007	**592,145**	**$1.07**

At July 31, 2007, the agents' options and warrants outstanding and exercisable were as follows:

Number of common shares to be issued	Exercise price	Date of expiry
131,838	**$0.90**	**November 12, 2007**
247,264	**1.30**	**November 12, 2007**
213,043	**0.90**	**February 18, 2009**

The fair value of agents' options and warrants has been estimated at the date of grant of options using the Black-Scholes option pricing model using the following weighted average assumptions:

	2007	2006
Annualized stock volatility	77.9%	55.7%
Risk-free interest rate	4.1%	4.1%
Expected option/warrant life	2.0 years	1.5 years
Dividend payments	0.0%	0.0%

e) Stock options

On December 28, 2005, the Board of Directors approved a new stock option plan. Under the plan, the Company may grant options to purchase common shares in the Company to employees, directors, officers, and consultants of the Company. The exercise price of the options is to be determined by the Board of Directors but generally will be equal to or greater than the market price of the shares at the grant date. Options will vest according to the following schedule:

25% - on grant date
25% - six months after grant date
25% - twelve months after grant date
25% - eighteen months after grant date

(Expressed in Canadian Dollars)

10. SHARE CAPITAL - Continued

e) Stock options - Continued

The Company has reserved 5,200,000 common shares for issuance of stock options to employees, directors, officers and consultants of the Company. Expired options are added back to the available pool, which was 48,000 common shares at July 31, 2007.

Stock option transactions and the number outstanding are summarized below:

	Number of options	Weighted average exercise price
Balance, July 31, 2005	1,360,000	$ 0.58
Options granted to employees, directors, officers and consultants *(notes 14(c) and (d))*	3,605,000	1.43
Options exercised	(130,000)	0.52
Balance, July 31, 2006	4,835,000	1.22
Options granted	720,000	1.04
Options exercised	(553,000)	0.78
Options expired	(533,000)	1.44
Balance, July 31, 2007	**4,469,000**	**$ 1.22**

At July 31, 2007, 3,545,250 options had vested, which have a weighted average exercise price of $1.17.

The estimated fair value of options granted to employees, directors, officers and consultants is amortized to expense over the vesting period of the options, resulting in compensation expense and addition to contributed surplus of $1,530,686 for the year ended July 31, 2007 (2006 – $1,074,620).

The weighted average fair value of stock options granted during the year ended July 31, 2007 has been estimated at the date of grant using the Black-Scholes option pricing model as $0.66 per share (2006 - $0.70) using the following weighted average assumptions:

	2007	2006
Annualized stock volatility	74.0%	55.2%
Risk-free interest rate	4.1%	4.3%
Expected option life	4.4 years	4.8 years
Dividend payments	0.0%	0.0%

(Expressed in Canadian Dollars)

10. SHARE CAPITAL - Continued

e) Stock options - Continued

The following summarizes options outstanding at July 31, 2007:

Exercise price	Number of options	Number of options Exercisable	Weighted average remaining life (years)
$0.50	560,000	560,000	2.42
$0.70	260,000	260,000	2.47
$0.72	100,000	100,000	3.49
$0.75	574,000	574,000	3.12
$0.80	160,000	80,000	4.46
$0.93	140,000	105,000	3.64
$0.99	100,000	75,000	3.93
$1.05	160,000	80,000	4.02
$1.10	300,000	150,000	4.48
$1.20	100,000	50,000	4.50
$1.55	240,000	180,000	3.85
$1.76	1,775,000	1,331,250	3.78
	4,469,000	3,545,250	3.53

The Black-Scholes model, used by the Company to calculate option values, was developed to estimate fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differs from the Company's stock option awards. This model also requires highly subjective assumptions, including future stock price, volatility, and expected time until exercise, which greatly affect the calculated values.

f) Escrow Shares

As at July 31, 2007 a total of 8,795,628 (2006: 12,724,378) of the issued shares were held in escrow, the release of which is subject to a pre-determined schedule through January of 2011. The escrowed shares are to be included in the computation of the weighted-average number of common shares outstanding. The number outstanding at the 2006 year end has been amended on that basis.

g) Contributed Surplus

	2007	2006
Balance, beginning of year	$ 1,558,457	$ 363,917
Options granted (note 10(e))	1,530,686	1,074,620
Agents' options granted (note 10(b)(i))	-	166,553
Options exercised (notes 10(b)(iii) and (vi))	(153,671)	(46,633)
Agents' options exercised (note 10(b)(vii))	(132,187)	-
Agents' warrants granted (note 10(b)(v))	152,267	-
Balance, end of year	$ 2,955,552	$ 1,558,457

(Expressed in Canadian Dollars)

11. RESEARCH AND DEVELOPMENT EXPENSES

During the year ended July 31, 2007, the Company incurred research and development expenses of $2,919,790 (2006 - $595,787) which it considered to not meet the criteria for initial capitalization of such costs, including costs not directly attributable to specific product development, such as overhead.

12. GENERAL AND ADMINISTRATIVE

	2007	2006
Consulting and other professional *(notes 14(c), (d) (e) and (f))*	$ 1,344,564	$ 515,301
Filing fees	65,318	45,618
Insurance	70,199	-
Legal	174,347	123,570
Marketing and promotion	26,023	7,680
Office and miscellaneous	112,676	53,735
Rent and storage	332,661	131,463
Salaries and benefits	1,166,183	108,421
Stock-based compensation *(note 10(e))*	1,530,686	1,074,620
Travel	385,246	114,154
Total	$ 5,207,903	$ 2,174,562

13. DISCONTINUED OPERATIONS

In the 2002 year, the Company's subsidiary, O-Tooz Energie Group Inc. ("O-Tooz"), disposed of its two healthy fast food outlets in Vancouver. The discontinued operation resulted in the default of lease agreement liabilities of approximately $108,000.

In January of 2005, the Company abandoned O-Tooz along with its other inactive subsidiaries, Djscene.com Media Inc., Online Consortium.com Inc. and FilmIndustry.com Inc. The liabilities of these discontinued operations have been segregated in the consolidated balance sheet.

14. RELATED PARTY TRANSACTIONS

a) Pursuant to a Support Agreement dated January 1, 2005, which expired in May of 2006, the Company and its wholly-owned subsidiary, Zecotek Crystals Inc., paid fees during the 2006 year of $1,089,226 (2007- nil) to Zecotek Laboratories Inc., a company controlled by Dr. Zerrouk, in respect to research and development services for the development of the Company's technologies.

b) On May 12, 2006, the Company acquired biophotonic technologies from Zecotek Holdings Singapore Pte. Ltd., a company controlled by Dr. Zerrouk, as described in note 9(ii).

c) The Company paid research and development expenses during the 2007 year of $94,861 (2006 – $150,837) and consulting fees of $228,031 (2006 - $64,644) to Dr. Zerrouk. During the 2007 year, the Company provided Dr. Zerrouk with a furnished apartment with an annual rent of $96,320, the use of a vehicle with lease costs of $8,035 and an annual schooling and transport allowance of $132,441. During the 2006 year, the Company granted options to Dr. Zerrouk exercisable to acquire 900,000 common shares of the Company at a price of $1.76 per share until May 12, 2011. At July 31, 2007, $65,209 (2006 - $78,511) was owing to the Company by Dr. Zerrouk and companies controlled by Dr. Zerrouk.

d) Included in consulting expense for the 2007 year is $71,059 (2006 -$120,000) representing payments to a former director and officer of the Company. During the 2006 year, the Company granted options to the former director and officer exercisable to acquire 300,000 common shares of the Company at a price of $1.76 per share until May 12, 2011. During the 2007 year, 120,000 options with a price of $0.50 per share were exercised.

e) The Company paid consulting fees during the 2007 year of $132,500 (2006 - $20,000) to a company controlled by the Chief Financial Officer of the Company.

f) The Company paid consulting fees during the 2007 year of $80,980 (2006 - $3,000) to a director of the Company. At July 31, 2007 $14,149 (2006 - nil) of these fees were accrued as a liability. During the 2007 year, the Company granted options to the director to acquire 100,000 shares at a price of $1.20 until January 30, 2012.

g) During the 2007 year, another former officer exercised 200,000 options at a price of $0.70.

Except where otherwise noted, these transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

(Expressed in Canadian Dollars)

15. COMMITMENTS AND AGREEMENTS

a) Effective February 27, 2006, the Company completed an exclusive license agreement with a third party for the use of the patents, technical data and know-how of its proprietary LFS scintillation crystal technology. Under the agreement, the Company is to receive a royalty of a fixed percentage of the gross selling price for each unit of licensed product delivered, sold, or leased to a third party during the twenty year term of the agreement. To date the Company has not yet received any revenue under the agreement.

b) Effective June 27, 2006, Zecotek Medical Systems Singapore Pte. Ltd. ("ZMSS") entered into a Collaborative Research Agreement with the University of Washington ("UW") for joint development of a proprietary technology for use in medical imaging systems. Pursuant to the agreement, ZMSS is to pay a total of US$2,368,222 to UW for the development project, as billed by UW. As at July 31, 2007 a total of US$691,774 ($770,284 Canadian dollars) had been paid.

c) Effective May 1, 2006, ZMSS entered into an employment agreement with Dr. Zerrouk in respect to the positions of Chairman, President and Chief Executive Officer of the Company and its subsidiaries. The agreement provides for annual remuneration including salary and cost of living and relocation allowances totalling $558,000 Singapore dollars (approximately $392,000 Canadian dollars) and is for an indefinite term. In order to terminate the agreement, the Company must provide not less than twelve months notice, pay severance equal to twenty four month's salary and retain all stock options held by Dr. Zerrouk.

d) The Company has entered into office leases for its Vancouver and Singapore offices. The Company also has entered into an apartment lease for certain employees in Singapore. Minimum required lease payments under these agreements are as follows:

2008	245,580
2009	193,500
2010	80,630
	$ 519,710

e) Effective August 22, 2006, Zecotek Medical Systems Singapore Pte. Ltd. entered into a tenancy agreement for a furnished residence for Dr. Zerrouk in Singapore. Monthly rent of $12,000 Singapore dollars (approximately $9,000 Canadian dollars) is to be paid from September 1, 2006 to August 31, 2008, totalling $288,000 Singapore dollars (approximately $216,000 Canadian dollars). Minimum required lease payments under the agreement are as follows:

2008	108,000
2009	9,000
	$ 117,000

f) Effective August 24, 2006, the Company entered into a Collaborative Research Agreement with the University of British Columbia ("UBC") to jointly develop advanced light sources and optical systems for medical imaging products for the period from September 1, 2006 to December 31, 2009. Pursuant to the agreement, the Company paid $98,600 upon execution of the agreement, paid a further $98,600 on September 1, 2007 and is to make a final payment of $98,600 on September 1, 2008.

15. COMMITMENTS AND AGREEMENTS – Continued

g) Effective February 14, 2007, ZMSS entered into a Joint Research and Development and Technological Works Agreement with Professor Zair Sadygov ("Sadygov") in respect to a planned joint development of a proprietary technology for use in medical imaging systems. Pursuant to the agreement, ZMSS is to provide funding in the amount of US$150,000 to Sadygov for the development project.

h) Effective February 15, 2007, ZMSS entered into a Services Agreement with Sadygov, in respect to the position of Chief Scientist in the Company's development of medical imaging technology. The agreement provides for monthly remuneration of US$5,000 for a term of twelve months, renewable automatically unless notice of termination is given by either party with notice of 90 days.

i) Effective March 28, 2007 the Company's Singapore subsidiary, Zecotek Laser Systems Pte. Ltd. ("ZLS") completed two asset purchase agreements to acquire certain laser technologies from Inversion Fiber Co. Ltd. ("Inversion") and Tehknoscan JS Company ("Tehknoscan"). Inversion and Tehknoscan each received 5% of the issued common shares of ZLS. The asset purchases were recorded at nominal amounts, as no objectively determined significant value can be attributed to the purchased technologies or to the shares of ZLS.

   Under the asset purchase agreements, if, within six months of the effective dates, the Company closes a cash financing from an outside third party and issues shares the number of which is premised on a valuation of the Company lower than $100 million US dollars, Inversion and Tekhnoscan are each to be issued additional shares, such that each company will hold up to 7% of the issued fully participating common shares of ZLS. No steps have been taken in respect to the possible application of this provision as a result of the financing described in Note 20(a).

   The asset purchase agreements also include provisions for a possible assignment of convertibility rights to the common shares of ZLS by which the ZLS shares could be exchanged for shares of the Company.

   As conditions of the asset purchase agreements, ZLS has entered into Manufacturing Agreements with Inversion and Tekhnoscan and Services Agreements with Dr. Sergey Babin ("Babin"), the sole shareholder and director of Inversion, and Dr. Sergey Kobtsev ("Kobstsev"), the majority shareholder and a director of Tekhnoscan.

   The manufacturing agreements appoint Inversion and Tekhnoscan as non-exclusive manufacturers of the laser systems for ZLS. Under these agreements, Inversion and Techknoscan are to manufacture laser systems at cost, as defined under the agreements.

   The services agreements with Babin and Kobtsev provide for monthly remuneration of US$8,000.00 each, and are each for terms of three years, subject to extension by mutual agreement of the parties.

j) As at July 31, 2007, the Company had paid a non-refundable deposit in the amount of $552,849, for the purchase of certain equipment.

(Expressed in Canadian Dollars)

16. CONTINGENT LIABILITIES

The landlord in respect to a tenancy agreement made by the Company for a residence to be used by Dr. Zerrouk in Singapore initiated a legal claim against ZMSS in October of 2006 in respect to the termination of the agreement by ZMSS. The dispute relates to changes to the original agreement which ZMSS claims were promised by the landlord. ZMSS terminated the tenancy agreement and demanded return of deposits of $45,000 Singapore dollars (approximately $31,635 Canadian dollars) from the landlord. The landlord has claimed loss of rental income of $360,000 Singapore dollars (approximately $253,080 Canadian dollars) over the term of the agreement (August 1, 2006 to July 31, 2008) and costs incurred to remove certain chattels. Management of the Company is of the view that the landlord's claim does not have merit, that ZMSS is not liable for the claims for damages made by the landlord, and that it will be successful in recovering the deposit. The outcome of this matter is uncertain. Any loss of the Company as a result of the claim will be recognized when that determination can reasonably be made.

17. GEOGRAPHIC INFORMATION

The Company has principal operations in Canada and Singapore. Geographic information by country is as follows:

Property and equipment, at amortized cost	**2007**	**2006**
Canada	$ 26,241	$ 41,832
Singapore	527,316	80,573
Other	13,594	-
	$ 567,151	$ 122,405
Revenue	**2007**	**2006**
Canada	$ 74,040	$ 44,153
Singapore	-	-
	$ 74,040	$ 44,153

18. INCOME TAXES

a) A reconciliation of the Canadian statutory tax rate to the effective rate for the Company is as follows:

	2007	**2006**
Statutory income tax rate	(34.1%)	(34.1%)
Tax losses not recognized	34.1%	34.1%
Effective tax rate	—	—

(Expressed in Canadian Dollars)

18. INCOME TAXES - continued

b) At July 31, 2007, the tax effects of temporary differences that give rise to the Company's future income tax assets are as follows:

	2007	2006
Non-capital losses subject to expiry	$ 2,692,000	$ 2,038,700
Intangible assets and development costs	500	522,400
Share issuance costs	264,000	257,000
Property and equipment	10,100	7,500
	2,966,600	2,825,600
Less: valuation allowance	(2,966,600)	(2,825,600)
	$ -	$ -

The valuation allowance reflects the Company's estimate that the benefit of the tax assets, more likely than not, will not be realized.

c) As at July 31, 2007, the Company and Zecotek Crystals Inc. have non-capital losses carried forward for Canadian tax purposes of approximately **$**7,894,478**,** available to reduce taxable income of future years, subject to certain restrictions. These losses expire commencing in the 2008 year as follows:

2008	1,406,327
2009	149,957
2010	99,190
2011	103,007
2015	1,478,231
2026	2,426,535
2027	2,231,231
	$7,894,478

19. STATEMENT OF CASH FLOWS – SUPPLEMENTARY INFORMATION

a) Cash paid for income taxes and interest is summarized as follows:

	July 31, 2007	July 31, 2006
Cash paid for income taxes	$ nil	$ nil
Cash paid for interest	$1,609	$ nil

19. STATEMENT OF CASH FLOWS – SUPPLEMENTARY INFORMATION -continued

b) Significant non-cash transactions occurring during the 2007 and 2006 years were as follows:

(i) During the 2007 year, the company acquired property and equipment with a cost of $57,227, for which the Company assumed obligations under capital lease.

(ii) On March 28, 2007, the Company issued shares of its Singapore subsidiary as consideration for asset purchases as described in Note 15(i).

(iii) On February 19, 2007, the company granted agents' warrants at an estimated fair value of $152,267, as described in note 10(b)(v).

(iv) On May 12, 2006, the Company issued 638,490 agents' options at an estimated fair value of $166,553, as describe in note 10(b)(i).

(iv) On May 12, 2006, the Company issued 11,750,000 common shares as partial consideration for the acquisition of technologies as described in notes 9(ii) and 10(b)(ii).

20. SUBSEQUENT EVENTS

a) On August 30, 2007, the Company completed a non-brokered private placement of 1,563,000 units issued at $1.60 per unit, resulting in gross proceeds of $2,500,800. Each unit consists of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one additional common share for a period of eighteen months at a price of $2.00 per share. The Company paid a finder's fee equal to 5% of the gross proceeds of the sale of the shares and issued non-transferable finder's warrants to purchase shares equal in number to 5% of the units sold under the private placement.

b) In August, 2007, agents' options to acquire 6,884 shares at $0.90 per share and warrants to acquire 6,116 shares at $1.30 per share were exercised for gross proceeds of $14,145. The amount was received prior to July 31, 2007 and was recorded as a liability at that date.