KPMG

Unaudited Consolidated Financial Statements of

ALARIS ROYALTY CORP.

For the three months ended March 31, 2010 and year ended December 31, 2009

ALARIS ROYALTY CORP.

Consolidated Balance Sheets, Unaudited

	March 31, 2010	December 31, 2009
Assets		
Current assets:		
Cash	$ 4,966,797	$ 3,826,000
Accounts receivable	158,184	2,470
Prepaid expenses	138,012	103,472
Future income taxes (note 10)	3,075,125	2,996,000
	8,338,118	6,927,942
Investment tax credit receivable (note 10)	11,030,007	11,030,007
Future income taxes (note 10)	24,228,085	22,248,900
Equipment (note 4)	70,656	74,477
Investments (note 3)		
Preferred LP units	111,174,642	111,124,642
Intangible assets	13,026,840	13,070,150
	124,201,482	124,194,792
	$ 167,868,348	$ 164,476,118
Liabilities and Shareholders' Equity/(Deficit)		
Current liabilities:		
Accounts payable and accrued liabilities	$ 347,412	$ 939,085
Dividends payable	941,187	802,604
Future income taxes (note 10)	47,808	47,808
Bank indebtedness (note 5)	3,541,667	2,850,000
Subordinated debt (note 5)	6,500,000	6,500,000
	11,378,074	11,139,497
Bank indebtedness (note 5)	18,058,333	19,700,000
Future income taxes (note 10)	4,188,467	1,347,755
Deferred credit (note 10)	22,917,637	23,661,017
Shareholders' equity/(deficit):		
Shareholder's capital (note 6)	113,590,934	111,125,039
Warrants (note 6)	627,830	845,000
Contributed surplus	1,880,733	1,471,333
Deficit	(4,773,660)	(4,813,523)
	111,325,837	108,627,849
Commitments (note 12)		
Subsequent event (note 13)		
	$ 167,868,348	$ 164,476,118

See accompanying notes to consolidated financial statements.

ALARIS ROYALTY CORP.

Consolidated Statements of Operations and Deficit, Unaudited

	Three months ended March 31, 2010	Three months ended March 31, 2009
Revenues:		
Royalties and distributions	$ 4,192,862	$ 4,598,615
Interest and other	1,160	1,837
	4,194,022	4,600,452
Expenses:		
Interest	483,651	575,479
Non-cash stock based compensation (note 8)	441,500	441,044
Salaries and benefits	218,212	212,911
Corporate and office	211,069	151,465
Legal and accounting fees	103,739	137,272
Stock based compensation (note 8)	50,213	73,341
Depreciation and amortization	47,130	57,938
	1,555,514	1,649,450
Net Income before taxes	2,638,508	2,951,002
Future income tax expense (note 10)	39,027	54,375
Net Income and other comprehensive income for the period	2,599,481	2,896,627
Deficit, beginning of period	(4,813,523)	(13,239,854)
Dividends to shareholders (note 7)	(2,559,618)	(2,828,584)
Deficit, end of period	$ (4,773,660)	$ (13,171,811)
Earnings per share, basic	$ 0.22	$ 0.32
Earnings per share, fully diluted	$ 0.21	$ 0.30
Weighted average shares outstanding, basic	11,581,030	9,124,004
Weighted average shares outstanding, fully diluted	12,133,003	9,727,554

See accompanying notes to consolidated financial statements.

ALARIS ROYALTY CORP.

Consolidated Statements of Cash Flows, Unaudited

	Three months ended March 31, 2010	Three months ended March 31, 2009
Cash provided by (used in):		
Operations:		
Net Income for the period	$ 2,599,481	$ 2,896,627
Add non-cash items:		
Depreciation and amortization	47,130	57,938
Non cash stock based compensation (note 8)	441,500	441,044
Income tax expense	39,027	54,375
	3,127,138	3,449,984
Change in non-cash working capital	(781,924)	131,575
	2,345,214	3,581,559
Investing:		
Purchase of preferred LP units	(50,000)	–
	(50,000)	–
Financing:		
Proceeds from exercise of warrants	2,216,625	-
Dividends to shareholders	(2,421,042)	(3,284,375)
Repayment of debt	(950,000)	(300,000)
	(1,154,417)	(3,584,375)
Increase/(decrease) in cash	1,140,797	(2,816)
Cash, beginning of period	3,826,000	1,743,936
Cash, end of period	$ 4,966,797	$ 1,741,120

See accompanying notes to consolidated financial statements

1. Basis of presentation:

Alaris' operations are conducted through a partnership. The partnership's operations consist primarily of investments in operating entities, typically in the form of long-term license and royalty arrangements or preferred limited partnership interests.

2. Significant accounting policies:

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. A comprehensive list of significant accounting policies are included in the audited financial statements for the years ended December 31, 2009 and 2008.

3. Investments:

March 31, 2010	Acquisition cost	Capitalized costs	Accumulated amortization	Net cost
LifeMark Health	$ 59,500,000	$ 291,362	$ –	$ 59,791,362
Lower Mainland Steel	51,000,000	333,280	–	51,333,280
Diligence costs capitalized	–	50,000	–	50,000
Total Preferred LP Units	110,500,000	674,642	–	111,174,642
End of the Roll	7,200,000	74,920	(454,643)	6,820,276
MEDIchair	6,500,000	83,758	(377,195)	6,206,564
Total Intangible Assets	13,700,000	158,678	(831,838)	13,026,840
	$ 124,200,000	$ 833,320	$ (831,838)	$ 124,201,482
December 31, 2009				
Lifemark Health	$ 59,500,000	$ 291,362	$ –	$ 59,791,362
Lower Mainland Steel	51,000,000	333,280	–	51,333,280
Total Preferred LP Units	110,500,000	624,642	–	111,124,642
End of the Roll	7,200,000	74,920	(431,910)	6,843,010
MEDIchair	6,500,000	83,758	(356,618)	6,227,140
Total Intangible Assets	13,700,000	158,678	(788,528)	13,070,150
	$ 124,200,000	$ 783,320	$ (788,528)	$ 124,194,792

3. Investments (continued):

Royalties and distributions:

	Three months ended March 31, 2010	Three months Year ended March 31, 2009
LifeMark Health	$ 2,661,876	$ 1,971,441
Lower Mainland Steel	840,000	1,910,265
End of the Roll	388,520	419,615
MEDIchair	302,466	297,294
	$ 4,192,862	$ 4,598,615

I – Preferred LP Units

(a) Investment in LifeMark Health Limited Partnership (“LifeMark Health”):

The Corporation holds 900,000 class A preferred partnership units ("LifeMark A Units") and 5,050,000 class B preferred partnership units ("LifeMark B Units") in LifeMark Health (the "LifeMark Investment") and were acquired as follows:

	A Units	B Units	Cost
December 31, 2008	900,000	3,750,000	$ 46,500,000
June 30, 2009	–	100,000	1,000,000
October 22, 2009	–	1,200,000	12,000,000
December 31, 2009	900,000	5,050,000	$ 59,500,000

Pursuant to the LifeMark Health partnership agreement (the "LifeMark Partnership Agreement") dated December 30, 2004, the LifeMark A Units entitle the Corporation to receive an annual preferred distribution (the "A Unit Preferred Distribution") in priority to distributions on LifeMark Health's other partnership units in a minimum amount of $1.46 million. The minimum amount is adjusted in each subsequent fiscal year to the greater of (i) $1.46 million; and (ii) the A Unit Preferred Distribution for the prior fiscal year multiplied by the percentage increase in LifeMark Health's Same Clinic Sales (as defined in the LifeMark Partnership Agreement), being generally LifeMark Health's annual revenue from clinics that have been open for at least two years, for the previous year. Distributions on the LifeMark A Units are receivable monthly.

3. Investments (continued):

(a) Investment in LifeMark Health Limited Partnership (“LifeMark Health”) (continued):

Pursuant to the LifeMark Partnership Agreement, the LifeMark B Units entitle the Corporation to receive an annual preferred distribution (the "B Unit Preferred Distribution") in priority to distributions on LifeMark Health's other partnership units, other than the LifeMark A Units, in an amount equal to the B Unit Preferred Distribution for the prior fiscal year multiplied by the percentage increase or decrease in LifeMark Health's Same Clinic Sales for the previous fiscal year. Distributions on the LifeMark B Units are receivable monthly.

LifeMark Health has the option at any time after December 30, 2009 (i) to repurchase all (but not less than all) of the LifeMark A and B Preferred Units at a pre-negotiated premium to the original purchase price.

(b) Investment in Lower Mainland Steel Limited Partnership (“LMS”):

The Corporation holds 510,000 Preferred partnership units ("LMS Units") in Lower Mainland Steel (the "LMS Investment"). 150,000 of the LMS Units were acquired on February 2, 2007 for an aggregate acquisition cost of $15 million. Alaris acquired another 360,000 LMS Units on December 21, 2007 for an aggregate acquisition cost of $36 million.

Pursuant to the LMS partnership agreement (the "LMS Partnership Agreement") dated April 2, 2007 and as amended December 21, 2007, the LMS Units entitle the Corporation to receive an annual preferred distribution (the “Preferred Distribution") in priority to distributions on LMS’ other partnership units. The base is in two distinct portions and is adjusted at two points (January 1st and April 1st) in each subsequent twelve month period to the Preferred Distribution for the prior twelve month period multiplied by the percentage increase or decrease in LMS’ Gross Profit (as defined in the LMS Partnership Agreement) for the most recently completed fiscal year. Effective January 1, 2010, the LMS Units will entitle the Corporation to receive approximately $2.0 million over the next twelve months based on the most recently completed fiscal year for LMS (September 30, 2009). Distributions on the LMS Units are paid monthly.

LMS has the option at any time after April 1, 2010 to repurchase all (but not less than all) of the LMS Units at a pre-negotiated premium to the original purchase price.

3. Investments (continued):

II – Intangible Assets

(c) Investment in End of the Roll Carpet and Vinyl ("End of the Roll"):

On May 1, 2005, the Corporation purchased certain intellectual property (the "ER IP") from End of the Roll for an aggregate purchase price of $7.2 million pursuant to an acquisition agreement (the "ER Acquisition Agreement") dated May 1, 2005 (the "End of the Roll Investment"). The ER IP includes End of the Roll's trademarks, trade names, website, and proprietary system for operating franchises. The ER IP was subsequently licensed to End of the Roll for a term (the "Term") of 80 years pursuant to a license agreement (the "ER License Agreement") dated May 1, 2005 in consideration of an annual royalty (the "Royalty"). The Royalty for the first 12-month period from May 1, 2005 to April 30, 2006 was $1.2 million (the "Initial Royalty"). The Royalty for each subsequent 12-month period during the Term is calculated by increasing or decreasing the Royalty for End of the Roll's fiscal year just ended by the percentage change in Same Store Sales (as defined in the ER License Agreement), being generally the total sales of all franchisee retail stores that have been open for at least two years, over the fiscal year immediately preceding the fiscal year just ended. Royalty payments are receivable monthly.

End of the Roll has the option at any time after May 1, 2010 to repurchase the ER IP (and terminate the Royalty) at a pre-negotiated premium to the original purchase price.

(d) Investment in MEDIchair Ltd. ("MEDIchair"):

On September 12, 2005, the Corporation purchased certain intellectual property (the "MEDIchair IP") from MEDIchair for an aggregate purchase price of $6.5 million (the "MEDIchair Investment") pursuant to an acquisition agreement (the "MEDIchair Acquisition Agreement") dated September 12, 2005. The MEDIchair IP includes MEDIchair's trademarks, trade names, website, and proprietary system for operating franchises. The MEDIchair IP was subsequently licensed to MEDIchair for a term (the "Term") of 80 years pursuant to a license agreement (the "MEDIchair License Agreement") dated September 12, 2005 in consideration of an annual royalty (the "Royalty"). The Royalty for the 12-month period from October 1, 2006 to September 30, 2007 was $1.053 million. The Royalty for each subsequent 12-month period during the Term is calculated by increasing or decreasing the Royalty in MEDIchair's fiscal year just ending by the percentage change in Same Store Royalties (as defined in the MEDIchair License Agreement), being generally the total annual royalties received by MEDIchair from all franchisees whose retail stores have been opened for at least two years over the fiscal year immediately preceding the fiscal year just ending, subject to a maximum percentage change in any year of 10%.

MEDIchair has the option at any time after October 1, 2010 to repurchase the MEDIchair IP (and terminate the Royalty) at a pre-negotiated premium to the original purchase price.

4. Equipment:

Equipment consists of leasehold improvements, furniture and fixtures, and computer equipment. The amounts are net of accumulated depreciation of $108,354 (December 31, 2009 - $104,532).

5. Debt

The Corporation has a $25,000,000 secured revolving credit facility with a syndicate of Canadian chartered banks. Interest is payable at the lenders' prime rate plus 3.00% (5.25% at March 31, 2010). The term out date under the credit facility is December 17, 2010. If an extension is not received by December 17, 2010, the facility will be repaid in thirty-six equal monthly installments commencing January 18, 2011. As part of an amendment to the original facility, the banks required principal repayments of $950,000 on December 31, 2009 and then in each of the first three quarters in 2010 (total of $2.85 million). Therefore at March 31, 2010, the required principal repayments plus the first three months of potential repayments should the facility not be renewed are shown as a current liability. There are financial covenants under this facility and at March 31, 2010, the Corporation is in compliance with each of the covenants based on a letter received by the Corporation from the lending syndicate clarifying the exclusion of certain non-cash and extraordinary amounts in the calculation of the covenants for the remainder of the term of the agreement.

The Corporation has a $6,500,000 unsecured demand facility with a company controlled by its largest shareholder. Interest is payable at 13.00% per annum.

6. Shareholders equity:

The Corporation has authorized, issued and outstanding, 11,098,171 voting, 666,665 non-voting common shares.

Issued Common Shares	Number of Shares	Amount
Balance at December 31, 2009	10,799,098	$ 103,125,039
Issued in lieu of dividends on restricted share units	3,523	32,100
Warrants exercised in the period	295,550	2,216,625
Fair value of warrants exercised in the period	-	217,170
Balance at March 31, 2010 (Voting shares)	11,098,171	105,590,934
Non-voting shares	666,665	8,000,000
Balance at March 31, 2010 (Voting, non-voting)	11,764,836	$ 113,590,934

Issued Warrants	Number of Warrants	Amount
Balance at December 31, 2009	1,150,000	$ 845,000
Exercised during the period	(295,550)	(217,170)
Balance at March 31, 2010	854,450	$ 627,830

The warrants are exercisable at $7.50 at any time up to twenty-four (24) months from the date of their issue (October 22, 2011), subject to a mandatory exercise if, any time after twelve (12) months from their issue, if the volume weighted average price of the voting common shares on the Toronto Stock Exchange is above $9.00 per common share for twenty (20) consecutive trading days.

7. Dividends:

For January and February 2010, the Corporation had declared a dividend of $0.07 per voting and non-voting common share and in for March 2010, the dividend was increased to $0.08 per common share ($2,559,618 in aggregate). For the three months ended March 31, 2009, dividends of $2,828,584 were declared.

8. Stock-based compensation:

The Corporation has a Restricted Share Unit Plan (“RSU Plan”) and a Stock Option Plan as approved by shareholders at a special shareholders meeting on July 31, 2008 that authorizes the Board of Directors to grant awards of RSUs and Options subject to a maximum of ten percent of the issued and outstanding common shares of the Corporation.

The RSU Plan will settle in voting common shares which may be issued from treasury or purchased on the Toronto Stock Exchange. The Corporation has reserved 591,662 and issued 384,400 RSUs to management and Directors as of March 31, 2010. The RSUs issued to directors vest over a three-year period. The RSUs issued to management (290,650) do not vest until the end of the three-year period and are subject to certain performance conditions relating to operating cash flow per share. The stock-based compensation expense relating to the RSU Plan is based on the issue price at the time of grant and management’s estimate of the future performance conditions and will be amortized over the thirty-six month vesting period. Payments in lieu of dividends on the unvested RSUs are made monthly in accordance with the Corporation’s dividend policy. Payments to management are split evenly between cash and common shares.

For the three months ended March 31, 2010, the Corporation incurred stock-based compensation expenses of $491,713 which includes: $384,400 (non-cash expense) for the first quarter 2010 portion of the RSU Plan expense that is to be amortized over the thirty-six month vesting period of the plan; $50,213 for payments to staff and directors in lieu of dividends under the RSU Plan; $32,100 (non-cash expense) for shares issued in lieu of dividends under the RSU Plan; and $25,000 (non-cash expense) for the first quarter 2010 amortization of the fair value of outstanding stock options. The Corporation has reserved 323,973 and issued 319,150 options (219,150 in 2008 and 100,000 in 2009) that vest over a four-year period and expire in five years. The fair value of the warrants (note 6) and options were calculated using a Black-Scholes model with the following assumptions:

	Warrants 2009	Options 2008	Options 2009
Dividend yield	12%	12%	12%
Expected volatility	53%	38%	56%
Risk free rate of return	2.46%	2.73%	2.74%
Expected life	2 years	5 years	5 years
Weighted average value per option/warrant	$ 0.7348	$ 1.2400	$ 1.3430

9. Financial risk management

A review of the Corporation's financial risk management can be found in the audited financial statements for the years ending December 31, 2009 and 2008.

(a) Liquidity risk:

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they are due. The Corporation's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Corporation's reputation. The Corporation has the following financial instruments that mature as follows:

	Total	0-6 Months	6 mo – 1 yr	1 – 2 years	3 – 4 years
Accounts payable and accrued liabilities	347,412	347,412	0	0	0
Dividends payable	941,187	941,187	0	0	0
Bank indebtedness	21,600,000	1,900,000	1,641,667	13,133,333	4,925,000
Subordinated debt	6,500,000	6,500,000	0	0	0
Total	**29,388,599**	**9,688,599**	**1,641,667**	**13,133,333**	**4,925,000**

(b) Fair value of financial instruments:

The Corporation's financial instruments as at March 31, 2010 and December 31, 2009 include cash and cash equivalents, accounts receivable, investments, accounts payable and accrued liabilities, bank indebtedness and subordinated debt. The fair value of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and approximate their carrying amounts due to their short-terms to maturity.

Bank indebtedness bears interest at a floating market rate and accordingly the fair market value approximates the carrying value. The subordinated debt is due to the Corporation's largest shareholder and, accordingly, the fair value is not readily determinable. The fair values of the available for sale investments are not readily determinable with sufficient reliability due to the lack of similar instruments in the market.

(c) Debt covenants:

The Corporation manages capital by monitoring certain debt covenants set out in its credit facility. The Corporation has a maximum senior debt to contracted EBITDA of 1.5:1 (1.3:1 at March 31, 2010). EBITDA is defined as net income before interest expense, income taxes, depreciation and amortization. Additionally, a minimum tangible net worth requirement of $104,950,000 is in place ($117,818,133 at March 31, 2010). Tangible net worth is defined as subordinated debt plus shareholders equity. In order to acquire more royalties, the Corporation needs to access public equity markets to fund the acquisitions and manage the business within the bank covenants. The Corporation was in compliance with all debt covenants at March 31, 2010.

10. Income taxes

Income tax expense is calculated by using the combined federal and provincial statutory income tax rates. The provision for income tax differs from that which would be expected by applying statutory rates. A reconciliation of the difference is as follows:

	Three months ended March 31, 2010	Year ended December 31, 2009
Earnings before income taxes	$ 2,638,508	$ 11,601,281
Combined federal and provincial statutory income tax rate	28.00%	29.00%
Expected income tax provision	$ 738,782	$ 3,364,371
Non-deductible expense	115,652	498,997
Decrease in valuation allowance	-	(4,963,992)
Loss carryforwards expired	-	2,780,171
Drawdown of deferred credit	(743,381)	(3,836,895)
Net impact of investment tax credits	-	(3,407,676)
Rate changes and other	(72,026)	(338,487)
	$ 39,027	$ (5,903,511)

The valuation allowance was decreased as a result of the extension of expiry dates for investment tax credits in 2009.

The income tax effect of the temporary differences that give rise to the Corporation's future income tax assets and liabilities are as follows:

10. Income Taxes (continued):

The income tax effect of the temporary differences that give rise to the Corporation's future income tax assets and liabilities are as follows:

	Three months ended March 31, 2010	Year ended December 31, 2009
Future income tax assets (liabilities):		
Non-capital losses and unclaimed scientific research and development expenses ("SRED")	$ 26,328,171	$ 27,040,431
Equipment	94,899	93,943
Share issue costs	880,134	962,065
Intangible assets	(1,478,768)	(1,489,600)
Investment tax credits	(2,757,502)	(2,757,502)
	$ 23,066,934	$ 23,849,337

The future income taxes as presented on the balance sheet are comprised of:

	Three months ended March 31, 2010	Year ended December 31, 2009
Current assets	$ 3,075,125	$ 2,996,000
Long-term assets	24,228,084	22,248,900
Current liabilities	(47,808)	(47,808)
Long-term liabilities	(4,188,467)	(1,347,755)
	$ 23,066,934	$ 23,849,337

As at March 31, 2010, the Corporation has non-capital losses available to reduce income tax in future years that expire from time to time as follows:

2012	$ 21,218,378
2013	21,537,689
2024 and later	3,381,931
	$ 46,137,999

10. Income Taxes (continued):

As at March 31, 2010, the Corporation has unused federal income tax credits which expire from time to time as follows (based on future earnings estimates, a portion of the tax credits will not be recognized):

2015	$ 50,210
2016	57,344
2017	133,712
2018	150,798
2019	1,623,342
2020	1,935,046
2021	1,295,097
2022	3,296,237
2023	1,840,597
2024	647,624
	$ 11,030,007

As at March 31, 2010, the Corporation has a deferred credit of $22,917,637:

Deferred credit on 2008 restructuring	$ 30,562,949
Drawdown in prior years	(6,901,931)
Drawdown in current period	(743,381)
	$ 22,917,637

The Corporation has research and development expenditures not deducted at the end of the year, to be deducted over an indefinite period for an amount of $58,131,473.

11. Related party transactions:

The Corporation has a $6.5 million demand loan with a company owned by its largest shareholder. For the three months ended March 31, 2010, the Corporation paid interest of $208,356 to this company (Three months ended March 31, 2009 - $208,356).

12. Commitments:

On March 25, 2009, the Corporation signed a seven-year lease at a new location that was to commence July 1, 2009 ending June 30, 2016. The commencement date was delayed until after December 1, 2009.

2010	$ 96,240
2011	128,320
2012	128,855
2013	134,736
2014	134,736
2015	134,736
2016	123,508
	$ 881,131

13. Subsequent event:

On April 27, 2010, the Corporation purchased Preferred partnership units in KMH Limited Partnership, a private healthcare business operating clinics in Ontario, for an aggregate acquisition cost of $3,000,000. Distributions on those preferred units are expected to be $525,000 in the first twelve months.

Also on April 27, 2010, the Corporation announced a bought deal financing for 1,600,000 common shares at $9.00 per share for total proceeds of $14,400,000 with an over-allotment for another 240,000 shares at the same price. The financing is expected to close on or around May 18, 2010. Proceeds will be used to purchase another $2,000,000 of preferred partnership units in KMH Limited Partnership, another $8,000,000 of preferred partnership units in LifeMark, and the repayment of subordinated debt.