

AUDIOTECH HEALTHCARE CORPORATION

SCHEDULE A: CONSOLIDATED FINANCIAL STATEMENTS

YEAR ENDED SEPTEMBER 30, 2004

CONSOLIDATED BALANCE SHEETS

CONSOLIDATED STATEMENT OF OPERATIONS AND DEFICIT

CONSOLIDATED STATEMENT OF CASH FLOWS

NOTES TO CONSOLIDATED STATEMENTS

Consolidated Financial Statements of

**AUDIOTECH HEALTHCARE
CORPORATION**

Year ended September 30, 2004



KPMG LLP
Chartered Accountants

200 – 206 Seymour Street
Kamloops, BC V2C 6P5
Canada

Telephone (250) 372-5581

Telefax (250) 828-2928

www.kpmg.ca

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Audiotech Healthcare Corporation as at September 30, 2004 and September 30, 2003 and the consolidated statements of earnings, 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 September 30, 2004 and September 30, 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in black ink that reads 'KPMG LLP' in a cursive, stylized font.

Chartered Accountants

Kamloops, Canada

January 21, 2005

AUDIOTECH HEALTHCARE CORPORATION

Consolidated Balance Sheets

September 30, 2004, with comparative figures for 2003

	2004	2003
Assets		
Current assets:		
Cash	\$ 608,295	\$ 329,875
Term deposit	15,962	25,673
Accounts receivable	361,187	266,521
Inventory	73,343	64,002
Prepaid expenses	5,916	27,050
	<u>1,064,703</u>	<u>713,121</u>
Property, plant and equipment (note 2)	519,455	310,196
Goodwill	942,775	942,775
	<u>\$ 2,526,933</u>	<u>\$ 1,966,092</u>

Liabilities and Shareholders' Equity

Current liabilities:		
Accounts payable and accrued liabilities	\$ 512,313	\$ 425,802
Unearned revenue	36,427	26,515
Current portion of long-term debt	151,170	643,944
Current portion of obligation under capital lease	13,630	-
	<u>713,540</u>	<u>1,096,261</u>
Long-term debt (note 3)	959,812	361,722
Obligation under capital lease (note 4)	24,337	-
Shareholders' equity:		
Share capital (note 5)	1,635,840	1,635,840
Other paid in capital (note 3)	176,000	-
Cumulative translation account	(24,529)	(16,017)
Deficit	(958,067)	(1,111,714)
	<u>829,244</u>	<u>508,109</u>
Commitments (note 10)		
	<u>\$ 2,526,933</u>	<u>\$ 1,966,092</u>

See accompanying notes to consolidated financial statements.

On behalf of the Board:

"Osvaldo (Ozzie) Iadarola" Director "Grant Robertson" Director

AUDIOTECH HEALTHCARE CORPORATION

Consolidated Statements of Operations and Deficit

Year ended September 30, 2004, with comparative figures for 2003

	2004	2003
Sales	\$ 3,629,914	\$ 3,167,466
Direct clinic costs:		
Materials and freight	1,308,584	1,316,461
Selling expenses	200,541	126,871
Rent, utilities and clinic overheads	397,639	393,962
Amortization	82,073	84,029
Salaries and benefits	1,045,668	906,236
	<u>3,034,505</u>	<u>2,827,559</u>
	595,409	339,907
Expenses:		
General and administrative	56,431	100,210
Amortization	1,618	1,363
Professional fees	62,519	31,956
Foreign exchange	7,436	15,372
Interest on long-term debt	84,962	89,437
Salaries and benefits	180,034	205,565
	<u>393,000</u>	<u>443,903</u>
Income (loss) before other expenses	202,409	(103,996)
Other expenses:		
Loss on disposal of equipment	19,428	1,370
Amortization of debenture discount	29,334	-
	<u>48,762</u>	<u>1,370</u>
Net earnings (loss) for the year	153,647	(105,366)
Deficit, beginning of year	(1,111,714)	(1,006,348)
Deficit, end of year	<u>\$ (958,067)</u>	<u>\$ (1,111,714)</u>
Weighted average number of shares outstanding	13,329,825	13,329,825
Earnings (loss) per share (basic and diluted)	\$ 0.012	\$ (0.008)

See accompanying notes to consolidated financial statements.

AUDIOTECH HEALTHCARE CORPORATION

Consolidated Statements of Cash Flows

Year ended September 30, 2004, with comparative figures for 2003

	2004	2003
Cash flows from operating activities:		
Net earnings (loss)	\$ 153,647	\$ (105,366)
Items not involving cash:		
Amortization of plant and equipment	83,691	85,392
Loss on disposal of equipment	19,428	1,370
Amortization of debenture discount	29,334	-
	286,100	(18,604)
Change in non-cash operating working capital:		
Accounts receivable	(100,526)	(33,458)
Inventory	(11,182)	(17,357)
Prepaid expenses	20,628	(25,032)
Accounts payable	96,296	191,263
Unearned revenue	9,912	(10,781)
	301,228	86,031
Financing:		
Proceeds from long-term debt	1,082,192	-
Principal payments on long-term debt	(820,472)	(266,765)
Repayment of obligation under capital lease	(4,951)	-
	256,770	(266,765)
Investing:		
Purchases of property, plant and equipment	(286,009)	(56,961)
Proceeds on disposal of equipment	3,488	-
Reduction of term deposit	9,711	294,327
	(272,810)	237,366
Effect of changes in exchange rates on foreign denominated cash	(6,768)	(20,573)
Increase in cash	278,420	36,059
Cash, beginning of year	329,875	293,816
Cash, end of year	\$ 608,295	\$ 329,875
Supplemental cash flow information:		
Interest paid	\$ 112,474	\$ 113,732
Acquisition of equipment through capital lease	42,680	-

See accompanying notes to consolidated financial statements.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

Audiotech Healthcare Corporation (the "Company") is incorporated under the laws of the Province of Alberta. Its primary activity is the provision of hearing related services and sale of hearing related devices through its clinics in British Columbia, Alberta and Idaho.

1. Significant accounting policies:

(a) Basis of presentation:

The consolidated financial statements include the accounts of the Company's wholly-owned subsidiaries Canadian Hearing Care (BC) Inc., Canadian Hearing Care (Alberta) Inc., HearingDepot Inc., Canadian Hearing Network Canada Inc., American Hearing Care Corporation and Audiology and Hearing Aid Services, Inc.

All significant intercompany balances and transactions have been eliminated on consolidation.

(b) Inventory:

Inventory is recorded at the lower of cost, as determined on a specific item basis, and net realizable value.

(c) Property, plant and equipment:

Property, plant and equipment are recorded at cost. Property under capital lease is initially recorded at the present value of minimum lease payments at the inception of the lease. Amortization is provided using the following methods and annual rates:

Asset	Basis	Rate
Audiology equipment	Declining balance	20%
Computer equipment	Declining balance	30%
Leasehold improvements	Straight-line	20%

(d) Goodwill:

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values. Goodwill is allocated as of the date of the business combination to the Company's reporting units that are expected to benefit from the synergies of the business combination.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

1. Significant accounting policies (continued):

(d) Goodwill (continued):

Goodwill is not amortized and is tested for impairment annually, or more frequently if events or changes in circumstances indicate the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the unit is compared with its fair value. When the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not to be impaired and the second step of the impairment test is unnecessary. The second step is carried out when the carrying amount of a reporting unit exceeds its fair value, in which case the implied fair value of the unit's goodwill is compared with its carrying amount to measure the impairment loss, if any. The implied fair value of the goodwill is determined in the same manner as the value of goodwill is determined in a business combination described in the preceding paragraph, using the fair value of the reporting unit as if it was the purchase price. When the carrying amount of reporting unit goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess and is presented as a separate line item in the statement of operations and deficit.

(e) Revenue recognition:

Revenue from sales of product is recognized when title passes to the customer, net of an estimated allowance for sales returns. Service revenue is recognized at the time service is provided. Amounts received in advance for products which have not yet transferred title are recorded as unearned revenue.

(f) Foreign currency:

The Company's investment in its foreign operations is of a self-sustaining nature. Accordingly, assets and liabilities of foreign operations are translated to Canadian dollars at the exchange rates in effect at the balance sheet date and revenues and expenses are translated at average rates for the period. Related foreign currency translation adjustments are recorded as a separate component of shareholders' equity and included in the cumulative translation account.

(g) Stock-based compensation:

The Company has a stock-based compensation plan as described in note 5(b). The Company accounts for all stock-based payments to non-employees, and employee awards that are direct awards of stock, or call for settlement in cash or other assets, granted on or after January 1, 2002, using the fair value based method. No compensation cost is recorded for all other stock-based employee compensation awards. Consideration paid by employees on the exercise of stock options is recorded as share capital and contributed surplus. The Company discloses the pro forma effect of accounting for these awards under the fair value based method.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

1. Significant accounting policies (continued):

(g) Stock-based compensation (continued):

Under the fair value based method, stock-based payments to non-employees are measured at the fair value of the consideration received, or the fair value of the equity instruments issued or liabilities incurred, whichever is more reliably measurable. The fair value of stock-based payments to non-employees is periodically re-measured until counterparty performance is complete, and any change therein is recognized over the period and in the same manner as if the Company had paid cash instead of paying with or using equity instruments. The cost of stock-based payments to non-employees that are fully vested and non-forfeitable at the grant date is measured and recognized at that date.

Under the fair value based method, compensation cost attributable to awards to employees that call for settlement in cash or other assets is measured at the intrinsic value and recognized over the vesting period. Changes in intrinsic value between the grant date and the measurement date result in a change in the measure of compensation cost. For awards that vest at the end of the vesting period, compensation cost is recognized on a straight-line basis; for awards that vest on a graded basis, compensation cost is recognized on a pro-rata basis over the vesting period.

(h) Income taxes:

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment.

(i) Earnings per share:

Basic earnings per share are computed by dividing net earnings by the weighted average shares outstanding during the reporting period. Diluted earnings per share are computed similar to basic earnings per share except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of stock options, if dilutive. The number of additional shares is calculated assuming that outstanding stock options were exercised and the proceeds from such exercise were used to acquire shares of common stock at the average market price during the reporting period.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

1. Significant accounting policies (continued):

(j) Use of estimates:

The preparation of financial statements in conformity with 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 amounts of revenues and expenses during the year. Actual results could differ from those estimates.

2. Property, plant and equipment:

			2004	2003
	Cost	Accumulated amortization	Net book value	Net book value
Land	\$ 109,587	\$ -	\$ 109,587	\$ -
Construction in progress	67,295	-	67,295	-
Audiology equipment	943,839	675,479	268,360	263,294
Computer equipment	55,477	31,892	23,585	16,685
Leasehold improvements	55,856	41,811	14,045	30,217
	1,232,054	749,182	482,872	310,196
Audiology equipment under capital lease	42,680	6,097	36,583	-
	\$ 1,274,734	\$ 755,279	\$ 519,455	\$ 310,196

Amortization expense of \$83,691 (2003 - \$85,392) has been charged to earnings in the current year.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

3. Long-term debt:

	2004	2003
Convertible debentures, repaid during the year.	\$ -	\$ 581,160
Convertible debentures, bearing interest at 10% per annum, maturing April 2007. Debentures are convertible at the holder's option into common shares at prices of \$0.20 per common share in year 1, \$0.22 per common share in year 2 and \$0.25 per common share in year 3. Face value of debentures is \$629,000 and is recorded net of unamortized debenture discount of \$146,666.	482,334	-
Equipment loans repayable based on thirteen instalments per annum of \$3,935 each including interest at 5%. Unsecured. Due 2006.	90,595	144,587
Term loan, repayable in monthly instalments of \$4,167, plus an annual payment of interest at a rate of 5.5% per annum. Secured by all assets of the Company. Due 2009.	233,333	-
Term loan, repayable in quarterly instalments of \$6,308 plus interest at prime plus 2%. Secured by promissory note of the Company subordinated to the security agreement on the previous term line noted above, and a continuing guarantee. Due 2009.	126,160	-
Construction loan draws available to an approximate maximum of \$389,000, bearing interest at 8.5% per annum, repayable in monthly instalments of \$3,834 including interest beginning no later than April 1, 2005. Secured by a first position Deed of Trust on real property and guarantees of the Company. Due April, 2010.	67,295	-
Promissory notes repayable in monthly instalments of \$1,450 including interest at 10% per annum. Due June, 2005.	111,265	279,919
	1,110,982	1,005,666
Current portion of long-term debt	151,170	643,944
	\$ 959,812	\$ 361,722

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

3. Long-term debt (continued):

During the period, the Company issued new convertible debentures in the amount of \$629,000 and has allocated proceeds between the fair value of the equity and liability components as required for compound financial instruments. The fair value of the equity component was determined using the Black-Scholes option pricing model with residual proceeds assigned to the liability component. As a result, \$176,000 has been recorded as other paid in capital and \$453,000 as long-term debt. The discount to face value of the long-term debt is being amortized over the life of the debentures.

The construction loan balance as at September 30, 2004 consists of draws for costs incurred on the construction project to that date. The total loan is expected to be \$389,356 upon completion of construction in 2005.

The estimated principal repayments required in the next five years are as follows:

2005	\$	151,170
2006		161,922
2007		575,386
2008		84,343
2009		68,609
Thereafter		69,552
		<hr/>
		\$ 1,110,982

4. Obligation under capital lease:

The Company has financed certain equipment purchases by entering into a capital leasing arrangement. Capital lease repayments are due as follows:

	2004	2003
Year ended September 30:		
2005	\$ 15,216	\$ -
2006	15,216	-
2007	10,144	-
	<hr/>	
	40,575	-
Less: amount representing interest at 4.5% per annum	2,608	-
	<hr/>	
	37,967	-
Less: current portion	13,630	-
	<hr/>	
	\$ 24,337	\$ -

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

5. Share capital:

(a) Authorized and issued share capital:

	2004	2003
Authorized:		
Unlimited number of voting common shares without par value		
Unlimited number of first preferred shares, ranking in priority to all other classes of shares, issuable in one or more series with designation, rights, privileges, restrictions and conditions determined by the Board of Directors upon issuance		
Unlimited number of second preferred shares, ranking in priority to all other classes of shares with exception the holders of first preferred shares, issuable in one or more series with designation, rights, privileges, restrictions and conditions determined by the Board of Directors upon issuance		
Issued:		
13,329,825 common shares (2003 - 13,329,825 common shares)	\$ 1,635,840	\$ 1,635,840

(b) Stock options:

The Company's stock option plan allows the Company to issue incentive share purchase options to a rolling maximum of 10% of the Company's issued and outstanding shares to directors, senior officers, consultants and employees. Upon granting of stock options, the Company will conclude a written Stock Option Agreement with the recipient.

The option price can not be less than the Discounted Market Price provided the option price is not be less than \$0.10 per share. Discounted Market Price is defined in Policy 1.1 of the TSX Venture Exchange to mean the market price (which is typically the last closing price on the day before option is granted) less a discount which is prescribed based on the Company's share price. The applicable discount is 25% for share prices up to \$0.50 per share; 20% for share prices between \$0.51 and \$2.00 per share; and 15% for share prices above \$2.00 per share. The maximum term of any option will be ten years and the Company may terminate an option at any time without notice.

During the year, the Company granted 450,000 options to employees and directors of the Company under the terms of its stock option plan. As at September 30, 2004, the Company has 925,000 options outstanding with authority to issue a further 407,983 options based on the presently issued and outstanding share capital.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

5. Share capital (continued):

	2004 Number of options	Weighted average exercise price	2003 Number of options	Weighted average exercise price
Balance, beginning of year	545,000	\$ 0.28	1,280,000	\$ 0.29
Granted during the year	450,000	0.16	-	-
Expired during the year	(70,000)	(0.45)	(735,000)	(0.28)
Balance, end of year	925,000	\$ 0.21	545,000	\$ 0.28

Details of the Company's outstanding options at September 30, 2004 are as follows:

Exercise	Expiry	Price	Number
Employee	February 24, 2005	0.22	225,000
Employee	February 2, 2006	0.35	50,000
Employee	June 9, 2007	0.28	200,000
Employee	May 18, 2009	0.16	450,000
Balance, end of year			925,000

During the year, no compensation costs were recorded in the consolidated statement of earnings for options granted to employees (2003 - nil).

Had compensation costs been determined using the fair value based method at the grant dates for awards under the plan, the Company's pro forma net earnings, earnings per share and diluted earnings per share would have been as follows:

	2004	2003
Pro forma net earnings (loss)	\$ 119,647	\$ (105,366)
Pro forma earnings per share:		
Basic	0.01	(0.01)
Diluted	0.01	(0.01)

The compensation costs of \$34,000 (2003 - \$nil) reflected in these pro forma amounts were calculated using the Black-Scholes option pricing model, assuming a risk-free interest rate of 3.80%, a dividend yield of 0%, an expected volatility of 73% and expected lives of stock options of five years.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements

Year ended September 30, 2004

6. Income taxes:

Income tax expense differs from the amount that would be computed by applying the federal and provincial statutory tax rates of 35.60% (2003 - 37.60%) to earnings before income taxes. The reasons for the differences and related tax effects are as follows:

	2004	2003
Earnings (loss) before income taxes	\$ 153,647	\$ (105,366)
Tax (recovery) at applicable tax rate	54,698	(39,618)
Rate variance on self-sustaining foreign operation	(4,608)	(2,259)
Non-deductible items	7,025	3,296
Tax benefits of losses not recognized (utilized)	(57,115)	38,581
	\$ -	\$ -

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities at September 30, 2004 and 2003 are presented below:

	2004	2003
Future tax assets:		
Arising on non-capital loss carry forwards	\$ 262,891	\$ 333,025
Less: valuation allowance	(262,891)	(333,025)
	\$ -	\$ -

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements

Year ended September 30, 2004

7. Segmented information:

The Company operates a single operating segment, hearing related services and sale of hearing related devices, in Canada and the United States. Geographic segmented information is as follows:

	2004	2003
Revenue:		
Canada	\$ 2,299,029	\$ 1,737,167
United States	1,330,885	1,430,299
	<u>\$ 3,629,914</u>	<u>\$ 3,167,466</u>
Interest expense:		
Canada	\$ 105,136	\$ 104,569
United States	7,338	9,163
	<u>\$ 112,474</u>	<u>\$ 113,732</u>
Amortization expense:		
Canada	\$ 60,741	\$ 70,636
United States	22,950	14,756
	<u>\$ 83,691</u>	<u>\$ 85,392</u>
Earnings (loss) before income taxes:		
Canada	\$ 127,222	\$ (177,249)
United States	26,425	71,883
	<u>\$ 153,647</u>	<u>\$ (105,366)</u>
Equipment and leasehold improvements:		
Canada	\$ 239,247	\$ 262,910
United States	280,208	47,286
	<u>\$ 519,455</u>	<u>\$ 310,196</u>
Goodwill:		
Canada	\$ 448,661	\$ 448,661
United States	494,114	494,114
	<u>\$ 942,775</u>	<u>\$ 942,775</u>
Total assets:		
Canada	\$ 2,153,040	\$ 1,783,616
United States	373,893	182,476
	<u>\$ 2,526,933</u>	<u>\$ 1,966,092</u>

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

8. Related party transactions:

During the year the Company had the following transactions with related parties:

	2004	2003
Ampton Court Mortgage Corporation, a company controlled by a Director of the Company		
Interest paid	\$ -	\$ 3,120
Repayments of long-term debt	-	49,895
MediaWave Communications Corp., a company controlled by a Director of the Company		
Commissions paid	\$ 1,289	\$ 2,504
Internet services	1,732	1,732
Sherwood Real Estate Corp., a company controlled by a Director of the Company		
Rent paid	\$ 14,270	\$ -

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

9. Financial instruments:

The carrying values of cash, term deposit, accounts receivable and accounts payable and accrued liabilities approximate their fair values due to the relatively short periods to maturity of these items.

The fair value of the Company's long-term debt approximates its carrying value as there is a market rate of interest attached to the repayment.

Approximately 72% of the Company's accounts receivable are due from customers in Canada with the remainder due from customers in the United States. The maximum credit risk associated with the Company's financial assets is the carrying value of those assets. The Company's exposure to foreign exchange risk associated with self-sustaining foreign operations is limited to its net investment in those operations.

AUDIOTECH HEALTHCARE CORPORATION

Notes to Consolidated Financial Statements
Year ended September 30, 2004

10. Commitments:

The Company leases premises at various locations throughout British Columbia, Alberta and Idaho. The expected annual minimum lease payments under the terms of these agreements over the next five years are as follows:

2005	\$ 177,942
2006	122,629
2007	99,857
2008	80,230
2009	50,153
	<hr/>
	\$ 530,811

In addition, the Company has entered into a cost sharing agreement with an unrelated party to acquire land and construct a new hearing and balance facility in Idaho. The total cost of the project is estimated at \$1,030,000 of which the Company's share is approximately \$515,000. The project is expected to be completed and opened in the spring of 2005. At September 30, 2004 the Company has incurred costs of \$176,882 related to the project which have been recorded as land and construction in progress.