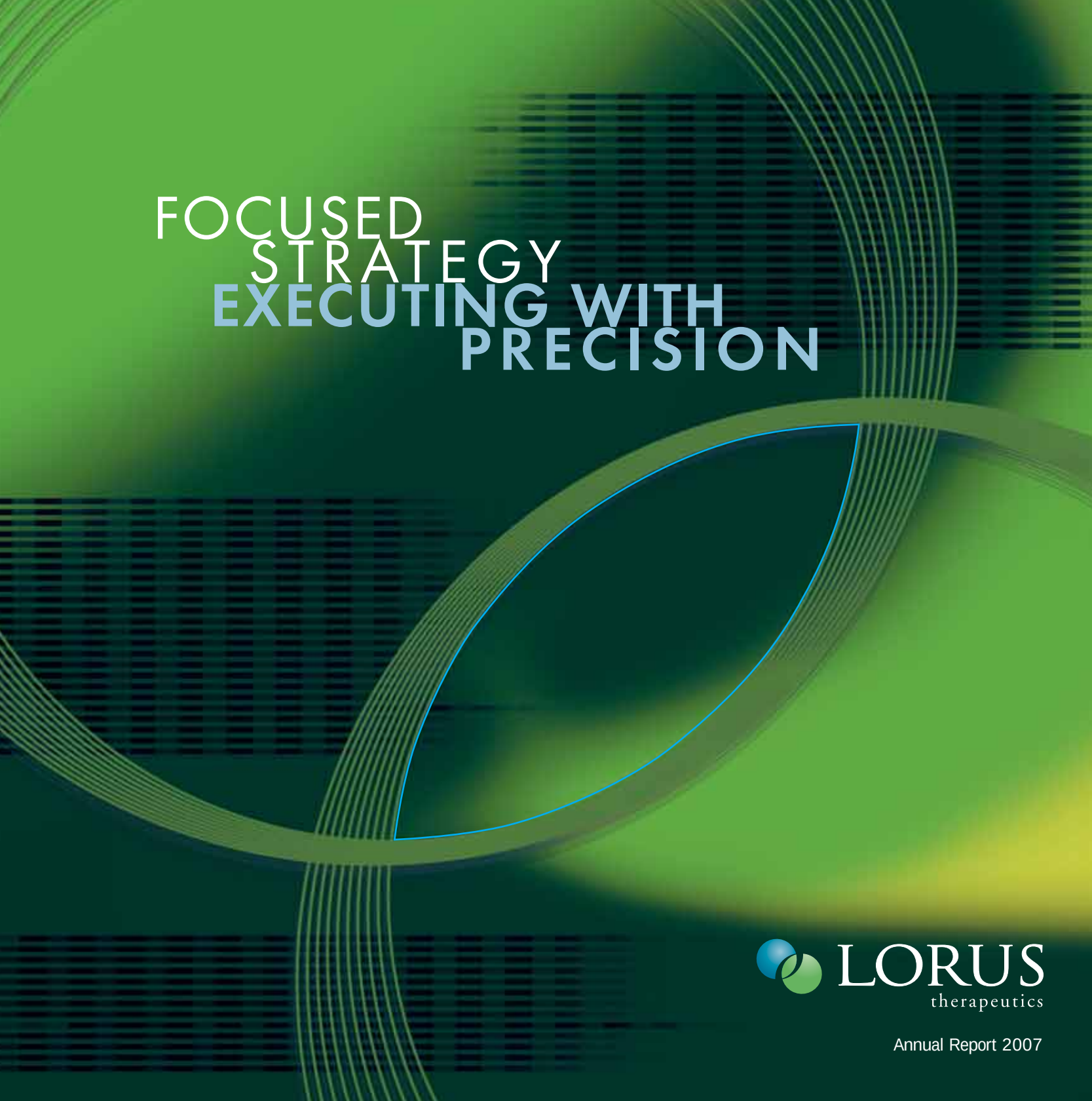
FOCUSED STRATEGY EXECUTING WITH PRECISION



LORUS therapeutics

Annual Report 2007

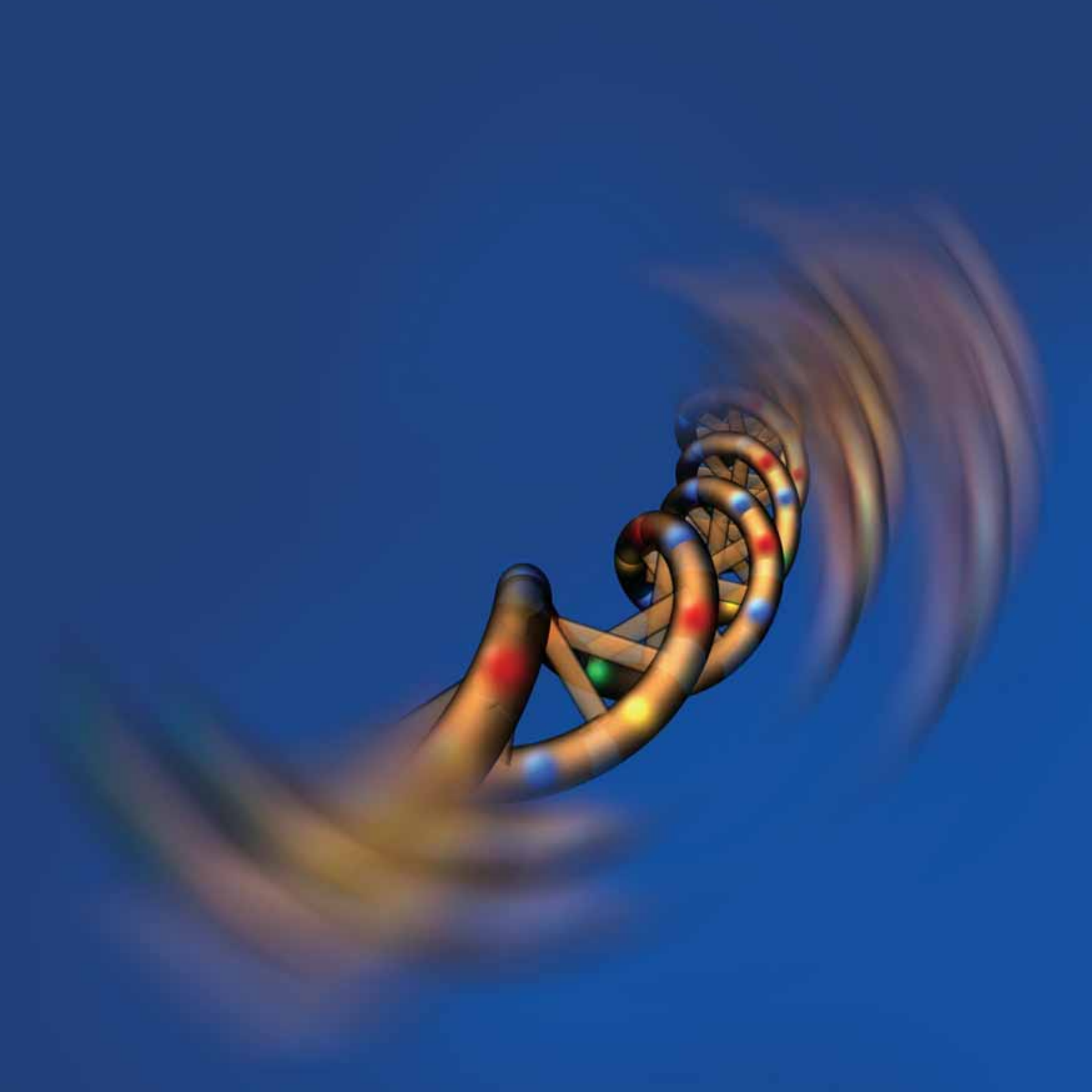
BUILDING SHAREHOLDER VALUE BY:

PURSUING RESEARCH AND DEVELOPMENT PROGRAMS WITH MULTIPLE PRODUCT AND COMMERCIAL OPPORTUNITIES;

ACCELERATING THE DEVELOPMENT OF THE MOST PROMISING DRUG CANDIDATES IN THE CLINIC;

ESTABLISHING PARTNERSHIPS WITH BOTH ACADEMIC AND CORPORATE PARTNERS.

LORUS therapeutics



OUR MISSION REFLECTS:

- Our commitment to discovering, developing, and delivering effective and well-tolerated drugs to manage cancer and enhance the lives of cancer patients.
- Our commitment to our shareholders to ensure we deliver product candidates with the maximum potential to increase value.
- Our commitment to *quality of life*.

Lorus has assembled a broad platform of innovative products with the potential to be used alone or in combination with chemotherapy to manage cancer. We collaborate with academic, biotechnology, and pharmaceutical companies to maximize the value of our products and minimize the time to market. Our success will benefit our shareholders, partners, employees, and ultimately, the patients whose health and well-being depend on new innovations.

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PRODUCT DEVELOPMENT

Cancer is a complex biological process, and Lorus believes that a range of therapeutic options is important for successful cancer treatment. Lorus' research and development program focuses on three technologies with a common objective: to create drugs that contribute to an improved quality of life for cancer patients, which are well tolerated by patients and can be used in combination with other leading therapies to enhance their effectiveness.

DNA/RNA-Based Therapeutics

Lorus is developing both DNA- and RNA-based drug candidates for cancer therapy. Our DNA-based therapies include antisense and gene therapy technologies. Antisense therapy represents a highly selective and targeted genetic approach to decrease expression of disease-causing genes, providing the potential of reducing malignancy while avoiding adverse side effects common with other forms of therapy. GTI-2040, our lead antisense drug, targets the R2 component of ribonucleotide reductase, which is overexpressed in a variety of cancers. In addition, Lorus has discovered that certain cancer types can be treated using a gene therapy approach, which is designed to restore gene expression in cancer cells and suppress tumour growth.

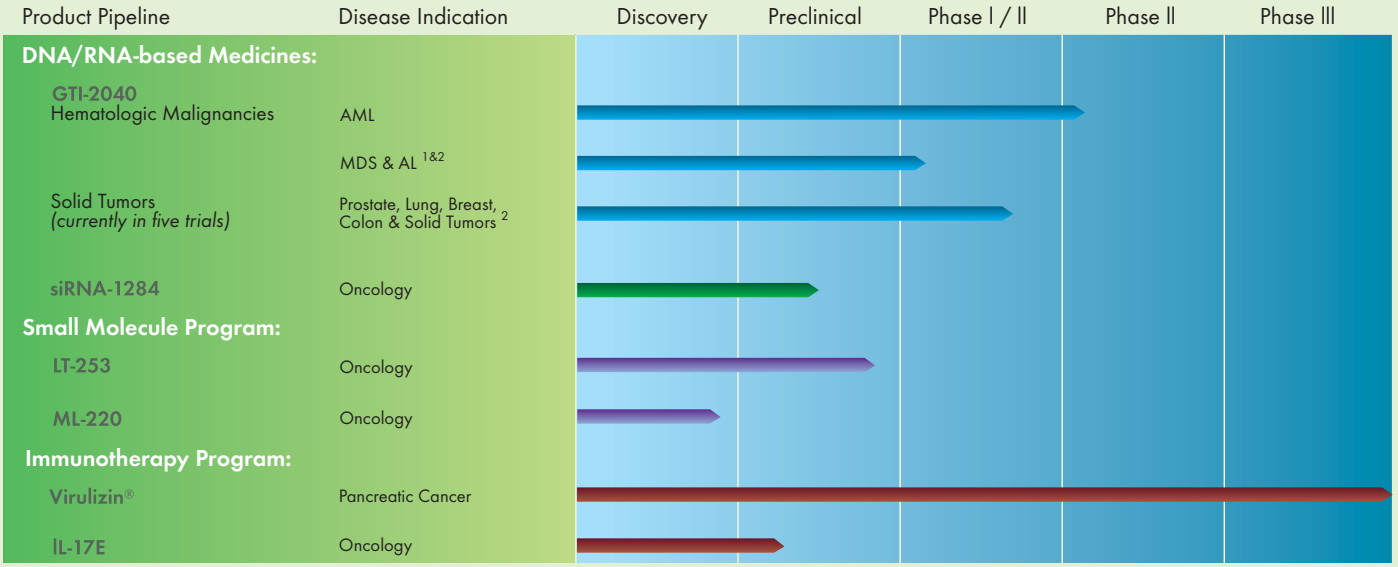
As a complement to our antisense therapy, we are exploiting RNA interference technology using a novel class of small interfering RNA (siRNA) molecules. We believe this technology has strong potential as a therapy for a variety of diseases including cancer, and may also be used for a range of new applications including target validation for drug discovery and therapeutics.

Small Molecule Program

Lorus possesses robust small molecule drug screening technologies and preclinical scientific expertise, which we are using to create a strong and sustainable drug candidate pipeline. Our proprietary group of novel small molecule compounds, which include lead compounds LT-253 and ML-220, have unique structures and modes of action, and are promising candidates for the development of novel anticancer agents with high safety profiles.

Immunotherapy Program

Lorus has two immunotherapy technologies for cancer treatment, both of which stimulate the immune system to fight cancer. Virulizin®, our most advanced immunotherapy drug activates macrophages and Natural Killer (NK) cells, and induces expression of several anticancer cytokine proteins. One of these cytokines, interleukin-17E (IL-17E), has shown potent anticancer activity in preclinical research, and represents Lorus' next generation of immunotherapy.



1 Acute Leukemias
2 US-NCI sponsored trials

"OUR FOCUS ON PIPELINE DEVELOPMENT IS FUELLED BY A REVITALIZED BUSINESS STRATEGY FOR LONG-TERM GROWTH. LORUS HAS THE FOCUS, THE PEOPLE, AND THE VISION TO CONTINUE BUILDING AS A LEADER IN ONCOLOGY. IN A SINGLE YEAR, WE'VE MADE GREAT STRIDES IN OUR PRODUCT PIPELINE BY SETTING A NEW STRATEGY FOR ACCELERATED SUCCESS."

LETTER TO SHAREHOLDERS

Dear Shareholder:

It is with great pleasure I share with you the highlights of 2007 and our plans for 2008. We believe Lorus[1] has made significant advances over the past year that will continue to bring us closer to our goal in the fight against cancer.

We have made strategic and operational changes to better position Lorus for success while our underlying philosophy and mandate remain the same: a commitment to improving the *quality of life* of cancer patients through development of safer and more effective cancer therapies. By repositioning our product portfolio and strategic focus, we believe Lorus is emerging as a stronger company than before.

Our strength is in the quality of our people. We are fortunate to have a team as dedicated as they are to increasing shareholder value. The near and long-term success of Lorus is based on the quality of our science and we take pride in our ability to discover and develop novel products and technologies for the management of cancer.

A *Focused* Product Development Strategy

Much of the work completed in 2007 represents the culmination of many years of research. In 2007, we adopted a straightforward strategy of focusing our resources on our lead product development programs. At this time, Lorus does not have the resources to move forward aggressively with a wide variety of products. Attempting do so, we believe, would dilute our efforts and impede the overall development process.

In 2007, we made important advances in preclinical and clinical development of our product candidates and the breadth of our Intellectual Property estate. Our most visible accomplishments have been in our progress with GTI-2040 and LT-253. For example, based on positive clinical data from our recently completed clinical trial of GTI-2040 in relapsed and refractory Acute Myeloid Leukemia (AML) in combination with Ara-C, Lorus announced initiation of a more advanced Phase II clinical trial in AML patients. With this trial we hope to confirm the clinical responses that we have seen with this drug combination in AML, and increase our understanding of how GTI-2040 works to enhance Ara-C activity in this cancer.

[1] On July 10, 2007 (the "Arrangement Date"), the Company completed a plan of arrangement and corporate reorganization with, among others, 4325231 Canada Inc. ("Old Lorus"), 6707157 Canada Inc. and Pinnacle International Lands Inc. As a result of the plan of arrangement and reorganization, among other things, each common share of Old Lorus was exchanged for one common share of the Company and the assets (excluding certain future tax attributes and related valuation allowance) and liabilities of Old Lorus (including all of the shares of the subsidiaries held by it) were transferred, directly or indirectly, to the Company and/or its subsidiaries. References in this Annual Report to the Company, Lorus, "we", "our", "us" and similar expressions, unless otherwise stated, are references to Old Lorus prior to the Arrangement Date and the Company after the Arrangement Date.

Consistent with Lorus' focus on leukemic indications to advance the development of GTI-2040, the Company has also recently initiated a study and development strategy in Myelodysplastic Syndrome (MDS), an additional indication with a large unmet need, through the US National Cancer Institute Cancer Therapy Evaluation Program (NCI CTEP) sponsored program.

GTI-2040 continues to have future opportunities in solid tumors as well. Five NCI CTEP sponsored studies are nearing completion in various solid tumor indications. The multiple clinical studies conducted under the NCI CTEP agreement present an opportunity to select the most promising development path for GTI-2040 in solid tumors, and Lorus hopes to pursue these additional opportunities in collaborative or partnership arrangements.

A *Focused* Financial Framework

Maintaining a strong financial position is the cornerstone of our business model. In general, biotech companies did not fare well on the capital markets in 2007 and Lorus was not immune to this trend. In August 2006 we successfully completed two financing transactions that provided $12.2 million (gross) in proceeds that have already enhanced the advancement of our product pipeline. In July 2007 we completed a non-dilutive financing transaction that, subject to post closing adjustments, we expect will ultimately result in net proceeds of approximately $7 million inclusive of an amount held in escrow.

"THE DISCOVERY AND DEVELOPMENT OF NOVEL CANCER PRODUCTS AND TECHNOLOGIES REMAINS THE CORNERSTONE OF OUR FUTURE. IN 2008, WE ARE COMMITTED TO MOVING CLOSER TO ACHIEVING OUR GOAL. WE BELIEVE OUR SHAREHOLDERS AND CANCER PATIENTS DESERVE NOTHING LESS."

A *Focused* Path Forward

We enter 2008 with great enthusiasm and commitment. This is a critical, yet exciting time in the Company's history and without doubt there will be many challenges ahead. But we believe we have set in motion significant operational and strategic changes that will better position Lorus for 2008 and beyond.

We strengthened our Board of Directors by adding several new members who bring to Lorus a combination of experience and accomplishment in areas such as capital markets, product development and business development within the biopharmaceutical industry. We have also instituted a near-term commitment to further build on our senior management with skills and experience closely matched to the needs of the new focus for development of our lead technologies and corporate strategies. With this vision in place, I am excited about our opportunities for the future.

Our success is dependent on the commitment of our employees and the continued support of our shareholders. I want to express my appreciation to all those who have supported us over the past year and continue to provide support in the important work that lies ahead. The road from discovery to regulatory approval is a long one that requires dedication and conviction. For those of you who have stood by us over the years, and for those patients who have participated in our clinical studies, and are looking forward to the promise of new treatment alternatives, we are fortunate to take this journey with you as we continue with determination to achieve our goals.

Sincerely yours,

Aiping Young
President and Chief Executive Officer

FOCUSED STRATEGY

LORUS' STRATEGY IS TO *FOCUS* ON THE DEVELOPMENT OF OUR PRODUCTS USING SEVERAL THERAPEUTIC APPROACHES. EACH APPROACH IS DEPENDENT ON A DIFFERENT TECHNOLOGY, WHICH WE BELIEVE MITIGATES THE DEVELOPMENT RISKS ASSOCIATED WITH A SINGLE TECHNOLOGY PLATFORM.

DNA/RNA-BASED THERAPEUTICS

Lorus' DNA/RNA-based technologies include antisense, siRNA and gene therapy technologies.

ANTISENSE PROGRAM

GTI-2040 is a lead candidate for antisense clinical development.

Drug candidate GTI-2040

GTI-2040 has made significant progress in the past year with the selection of a lead disease indication, acute myeloid leukemia (AML). Our focus on AML for GTI-2040 development reflects the significant unmet need with current therapies for AML, one of the most prevalent types of leukemia.

Last year we completed a dose escalation study of GTI-2040 in combination with high dose Ara-C (HiDAC) in patients with refractory and relapsed AML. This study demonstrated safety and appropriate dosing of the combination regimen and showed promising clinical response in patients under 60 years of age. Importantly, this clinical response correlated with downregulation of R2, the cellular target of GTI-2040, and high intracellular levels of GTI-2040 were demonstrated in circulating and bone marrow leukemic cells.

Based on these favourable findings and an ensuing review of the proposed AML development program with the U.S. Food and Drug Administration, Lorus decided to advance the program into Phase II. Following the successful completion of this Phase II study, Lorus intends to develop a registration clinical plan for GTI-2040 in AML. GTI-2040 already has orphan drug status in the United States for use in the treatment of AML.

Consistent with our primary focus on AML, we have initiated a trial sponsored by the National Cancer Institute Cancer Therapy Evaluation Program (NCI CTEP) with GTI-2040 in high grade Myelodysplastic Syndromes (MDS) and Acute Leukemias (AL). High grade MDS patients typically have a survival expectation of one year or less and their diseases may frequently progress to AML. GTI-2040 is also being studied in combination with various chemotherapy drugs in five ongoing NCI CTEP sponsored trials. These studies target various solid tumours, non-small cell lung, hormone refractory prostate, colorectal, and breast cancers, and represent a significant non-dilutive capital deployment on our product pipeline.

RNAi THERAPEUTICS

Lorus is developing the potential of RNA interference (RNAi) technology for silencing of disease-causing genes with double stranded RNA molecules known as small interfering RNA (siRNA). Interest in siRNA-based therapeutics peaked this past year, and pharmaceutical and biotechnology companies worldwide are developing siRNAs for a range of diseases, including viral diseases, age-related macular degeneration and cancer. Our lead siRNA drug, siRNA-1284, has demonstrated potent antitumor activity in preclinical studies, which we presented in a recent peer-reviewed publication.

Drug candidate siRNA-1284

Our goal is to advance siRNA-1284 into clinical development. We are conducting studies to determine the range of antitumor efficacy for siRNA-1284 and are seeking to broaden the siRNA program by evaluating the effectiveness of siRNA molecules on other disease targets. We believe this drug candidate has potential for value-enhancing development collaborations.

"AT LORUS, WE ARE DRIVEN AND INSPIRED BY THE OPPORTUNITY TO PROLONG LIVES AND ALLEVIATE SUFFERING. THIS INVOLVES VIGOROUSLY MOVING FORWARD OUR CORE CLINICAL PROGRAM WHILE LAYING THE FUTURE GROUNDWORK FOR OUR PROMISING PIPELINE."

Peter Murray
Director of Clinical Development

GENE THERAPY

Lorus has built a gene therapy platform that shows promise in preclinical studies. Our lead drug candidate is a novel tumor suppressor that plays an important role in determining the malignant potential of tumour cells.

Lorus is currently assessing potential academic and/or corporate partners with strong gene delivery platforms. The goal is to use an effective vector/delivery system with our gene to target specific organs and tissues for selective inhibition of tumour growth and metastasis.

EXECUTING WITH PRECISION

OUR FOCUS ON THREE THERAPEUTIC TECHNOLOGIES AND THE COLLECTIVE EXPERIENCE OF OUR TEAM POSITIONS US TO DISCOVER AND DEVELOP NEW DRUG CANDIDATES FOR THE TREATMENT OF CANCER.

SMALL MOLECULE PROGRAM

Lorus has developed a group of potent small molecule compounds that are promising candidates for the development of novel anticancer agents. These compounds have novel chemical structures and unique modes of action. Lorus has identified two molecules from this program, LT-253 and ML-220, as lead candidates for further development.

Drug candidate LT-253

LT-253 is the first anticancer small molecule selected from a platform of a new class of small molecules discovered at Lorus. During 2006 we made substantial progress in the characterization of the mechanisms of action and in the preclinical development of LT-253. The results of characterization studies were presented at the 2006 annual meeting of the American Association for Cancer Research (AACR) and early formulation studies were published in the September 2006 issue of Cancer Chemotherapy and Pharmacology. LT-253 is a promising drug candidate for the treatment of colon carcinoma and non-small cell lung cancer based on its potent *in vitro* anti-proliferative activity, its efficacy in *in vivo* animal models of human colon and lung cancers, and its safety profile. Formal GLP toxicology studies are planned to be initiated in different animal species to support the filing of an IND application for the initiation of a Phase I clinical trial.

Lorus is also pursuing other candidates at earlier stages of development. These include:

- ***LT-253 second generation derivatives for oral administration***

Further structural modifications of LT-253 produced derivatives optimized for oral absorption. Animal efficacy studies are in progress.

- ***ML-220 platform***

Lorus is developing novel derivatives that target cancer relevant genes, which are critical in a major signaling pathway involved in tumorigenesis and represent important new cancer targets. Lead optimization of ML-220 yielded several novel derivatives that showed potent target inhibitory activity *in vitro* and in cancer cells, and growth inhibitory activity against prostate and renal carcinoma cell lines.

IMMUNOTHERAPY PROGRAM

Over the past two decades, immunotherapy has emerged as one of the most significant advances in cancer therapy. We have two immunotherapy products in our pipeline, Virulizin® and IL-17E.

Virulizin®

Lorus' lead immunotherapy product has completed a Phase III clinical trial for the first line treatment of pancreatic cancer in combination with gemcitabine. Top-line results from the trial did not meet the primary endpoint of the trial but exploratory analysis showed promising trends in specific patient populations. Virulizin® treatment was very well tolerated with no major additional side effects. Lorus is now in active discussions with potential corporate partners for further clinical development of Virulizin®.

Drug candidate IL-17E

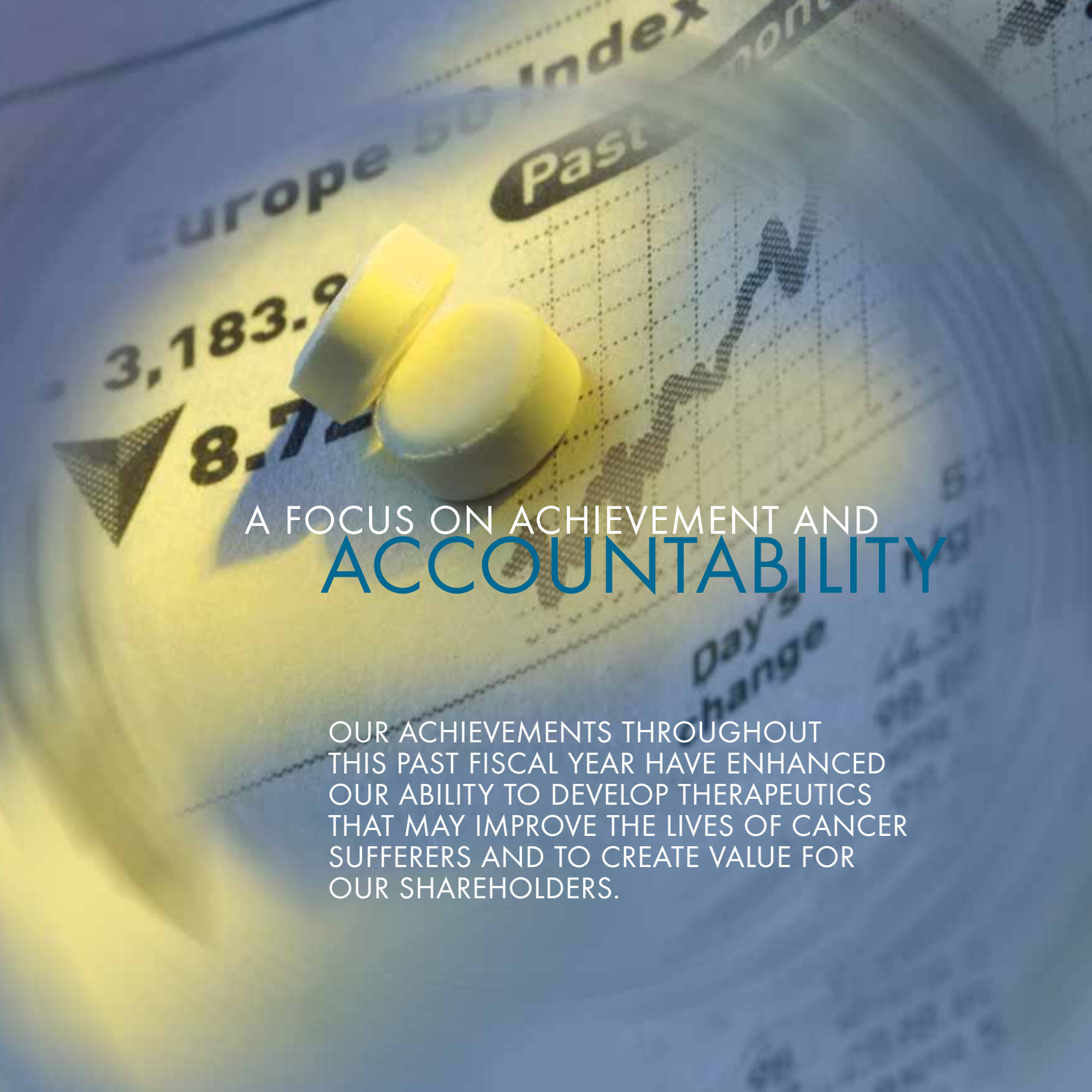
Lorus' scientists were the first to discover that IL-17E had anticancer activity against a range of human cancers. Over the past year, we have further evaluated IL-17E to define its anticancer mechanism and have also improved patent protection for the use of IL-17E as a cancer therapeutic. Our goal is to identify codevelopment opportunities for IL-17E with a potential partner.

"WE ARE FOCUSED ON DISCOVERING AND DEVELOPING NEW CANCER THERAPIES AND DETERMINING THE BASIS FOR NOVEL APPROACHES THAT CAN LAY THE FOUNDATION FOR SIGNIFICANT ADVANCES IN THE MANAGEMENT OF CANCER."

Yoon Lee
Director of Research

"AS WE MOVE FORWARD, WE WILL FOCUS ON INCREASING THE VALUE OF PRODUCTS, AND COMMERCIAL OPPORTUNITIES FOR OUR LEAD PRODUCT CANDIDATES BY SEEKING STRATEGIC ALLIANCES WITH LEADING ACADEMIC AND CORPORATE PARTNERS."

Saeid Babaei
Director of Corporate Development



A FOCUS ON ACHIEVEMENT AND ACCOUNTABILITY

OUR ACHIEVEMENTS THROUGHOUT THIS PAST FISCAL YEAR HAVE ENHANCED OUR ABILITY TO DEVELOP THERAPEUTICS THAT MAY IMPROVE THE LIVES OF CANCER SUFFERERS AND TO CREATE VALUE FOR OUR SHAREHOLDERS.

2007 HIGHLIGHTS	2008 MILESTONES
CORPORATE	
Completed a financing transaction resulting in $12.2 million in gross proceeds.	By leveraging our extensive expertise in oncology, Lorus intends to seek partnerships and collaborative arrangements for its lead drugs. By forming strategic alliances, Lorus will gain access to the financial and commercial resources necessary to develop and market its products.
Further strengthened our financial position by completing a non-dilutive financing transaction that, subject to post closing adjustments, is expected to result in net proceeds of approximately $7 million inclusive of an amount held in escrow.	A near-term commitment to further build on our senior management with skills and experience closely matched to the needs of the new focus for development of our lead technologies and corporate strategies.
DEVELOPMENT	
Initiated a new clinical study in high grade Myelodysplastic Syndrome (MDS) and Acute Leukemias (AL) with GTI-2040 as a single agent.	Develop a registration clinical program for GTI-2040 based upon data emerging from leukemia trials now underway.
Announced further pharmacodynamic and efficacy findings for the first AML clinical trial with GTI-2040 in combination with cytarabine at the annual meeting of the American Society of Clinical Oncology. Additional data on pharmacokinetics and leukemia cell uptake of GTI-2040, in support of continued development in relapsed and refractory AML patients, were presented at the American Association of Pharmaceutical Scientists annual meeting.	Progress LT-253 to the stage where an application to start a Phase I clinical trial can be submitted in calendar year 2008. Formal GLP toxicology studies will be an important major part of our activities for this program.
Initiated a more advanced Phase II clinical trial in order to further the development of GTI-2040 for the treatment of AML patients.	Expand our collaborations through new alliances with leading clinical institutions, opinion leaders and academic partners.
Announced continued success in the development of Lorus' 'Small Molecule Program' with the selection of lead compound LT-253 following extensive preclinical studies.	Continue to build drug discovery and development capabilities to further enrich our pipeline. Lorus intends to put extensive medicinal chemistry efforts into its drug development program to identify more novel cancer targeting agents.
Announced continued success in the development of 'siRNA Technology' with the selection of lead compound siRNA-1284 and publication of preclinical results.	Lorus will remain opportunistic by continuing to seek novel technologies and product candidates to further expand its pipeline.

August 7, 2007

PLAN OF ARRANGEMENT AND CORPORATE REORGANIZATION

On July 10, 2007 (the "Arrangement Date"), the Company completed a plan of arrangement and corporate reorganization with, among others, 4325231 Canada Inc. (formerly Lorus Therapeutics Inc.) ("Old Lorus"), 6707157 Canada Inc. and Pinnacle International Lands, Inc. As a result of the plan of arrangement and reorganization, among other things, each common share of Old Lorus was exchanged for one common share of the Company and the assets (excluding certain future tax attributes and related valuation allowance) and liabilities of Old Lorus (including all of the shares of its subsidiaries held by it) were transferred, directly or indirectly, to the Company and/or its subsidiaries. The Company continued the business of Old Lorus after the Arrangement Date with the same officers and employees and continued to be governed by the same board of directors as Old Lorus prior to the Arrangement Date. Therefore, the Company's operations have been accounted for on a continuity of interest basis and accordingly, the consolidated financial statement information below reflect that of the Company as if it had always carried on the business formerly carried on by Old Lorus. References in this MD&A to the Company, Lorus, "we", "our", "us" and similar expressions, unless otherwise stated, are references to Old Lorus prior to the Arrangement Date and the Company after the Arrangement Date.

The following discussion should be read in conjunction with the audited financial statements for the year ended May 31, 2007 and the accompanying notes for 6650309 Canada Inc. (subsequently renamed Lorus Therapeutics Inc.) ("New Lorus") and the financial statements of Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.) ("Old Lorus") presented in the Supplemental Financial Information (collectively the "Financial Statements") set forth elsewhere in this report. The Financial Statements, and all financial information discussed below, have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). All amounts are expressed in Canadian dollars unless otherwise noted.

OVERVIEW

Lorus Therapeutics Inc. is a life sciences company focused on the discovery, research and development of effective anticancer therapies with a high safety profile. Lorus has worked to establish a diverse, marketable anticancer product pipeline, with products in various stages of development ranging from preclinical to multiple Phase II clinical trials. A growing intellectual property portfolio supports our diverse product pipeline.

Our success is dependent upon several factors, including establishing the efficacy and safety of our products in clinical trials, securing strategic partnerships, obtaining the necessary regulatory approvals to market our products and maintaining sufficient levels of funding through public and/or private financing.

We believe that the future of cancer treatment and management lies in drugs that are effective, safe and have minimal side effects, and therefore improve a patient's quality of life. Many of the cancer drugs currently approved for the treatment and management of cancer are toxic with severe side effects, and we therefore believe that a product development plan based on effective and safe drugs could have broad applications in cancer treatment. Lorus' strategy is to continue the development of our product pipeline using several therapeutic approaches. Each therapeutic approach is dependent on different technologies, which we believe mitigates the development risks associated with a single technology platform. We evaluate the merits of each product throughout the clinical trial process and consider commercialization as appropriate. The most advanced anticancer drugs in our pipeline, each of which flow from different platform technologies, are antisense, small molecules and immunotherapeutics.

Our net loss for 2007 decreased 46% to $9.6 million ($0.05 per share) compared to a net loss of $17.9 million ($0.10 per share) in 2006. Research and development expenses in 2007 decreased to $3.4 million from $10.2 million in 2006. The close of the Virulizin® Phase III clinical trial in 2006 as well as staff reductions resulting from the November 2005 corporate changes (described below) continue to contribute to the decrease in net loss over 2006. We utilized cash of $6.3 million in our operating activities in 2007 compared with $13.1 million in 2006; the lower utilization is consistent with lower research and development activities and lower general and administrative expenses. At the end of 2007

we had cash and cash equivalents and marketable securities of $12.4 million compared to $8.3 million at the end of 2006. As a result of the Arrangement, the Company expects that, subject to the post closing adjustments, it will receive net proceeds of approximately $7 million inclusive of an amount held in escrow.

RESULTS OF OPERATIONS

Revenues

Revenues for the year increased to $107 thousand compared with 2006 revenue of $26 thousand and $6 thousand in 2005. The increase in revenue in 2007 is related to increased laboratory services work performed by Lorus personnel on behalf of other companies.

Research and Development

Research and development expenses totalled $3.4 million in 2007 compared to $10.2 million in 2006 and $14.4 million in 2005. The decrease in spending compared with 2006 and 2005 is due to the close of our Virulizin® Phase III clinical trial for the treatment of advanced pancreatic cancer in 2006 as well as a reduction in headcount in November 2005. The ongoing research and development costs relate to the GTI-2040 and GTI-2501 clinical development programs ongoing as well as our small molecule preclinical program. A significant portion of the Company's GTI-2040 Phase II testing costs are covered by the US NCI with Lorus continuing to be responsible for any additional GTI-2040 manufacturing costs, thus reducing our overall research and development costs.

General and Administrative

General and administrative expenses totalled $3.8 million in 2007 compared to $4.3 million in 2006 and $5.3 million in 2005. The decrease in general and administrative costs is the result of staff reductions, and a continued focus on lowering costs in all areas of the business. The cost savings realized during the current year is partially offset by charges incurred under the mutual separation agreement entered into with Dr. Jim Wright discussed under "Corporate Changes" below.

Stock-Based Compensation

Stock-based compensation expense totalled $503 thousand in 2007 compared with $1.2 million in 2006 and $1.5 million in 2005. The decrease in stock-based compensation expense in 2007 is the result of reduced fair values on the stock options issued, due to a decline in our stock price, as well as a significant number of unvested options that were forfeited during the year, reducing the overall expense.

During 2006, employees of the Company (excluding directors and officers) were given the opportunity to choose between keeping 100% of the options they held at the existing exercise prices or forfeiting 50% of the options held in exchange for having the remaining 50% of the exercise prices of the options re-priced to $0.30 per share. Employees holding 2,290,000 stock options opted for re-pricing their options, resulting in the amendment of the exercise price of 1,145,000 stock options and the forfeiture of 1,145,000 stock options during the quarter ended February 28, 2006. The 2005 expense represents the amortization of the estimated fair value of stock options granted since June 1, 2002 applicable to the current service period as well as a charge of $208 thousand recorded in the second quarter of 2005 representing the increase in value attributed to the shareholder approved amendment to the stock option plan to extend the contractual life of all options outstanding from five years to ten years.

Depreciation and Amortization

Depreciation and amortization expenses decreased to $403 thousand in 2007 as compared to $771 thousand in 2006 and $564 thousand in 2005. The decrease in depreciation and amortization expense is the result of reduced capital asset purchases during fiscal 2007 and 2006. In 2006, the Company took a write-down of $250 thousand on certain furniture and equipment whose carrying value was deemed to be unrecoverable and in excess of the fair value of the underlying assets.

Interest Expense

Non-cash interest expense was $1.0 million in 2007 compared with $882 thousand in 2006 and $300 thousand in 2005. These amounts represent interest at a rate of prime plus 1% on the $15.0 million convertible debentures. The increase in interest expense in 2007 compared with 2006 is a function of higher interest rates due to increases in the prime rate in late 2006. In 2005, the interest accrued based on the cash advanced beginning October 6, 2004 when the first tranche of $5 million was advanced through to May 31, 2005 when the entire $15.0 million had been advanced. All interest accrued on the debentures to date has been paid in common shares of the Company.

Accretion in Carrying Value of Secured Convertible Debentures

Accretion in the carrying value of the Company's secured convertible debentures amounted to $935 thousand in 2007 compared with $790 thousand in 2006 and $426 thousand in 2005. The accretion charges arise as under GAAP the Company has allocated the proceeds from each tranche of the debentures to the debt and equity instruments issued on a relative fair value basis resulting in the $15.0 million debentures having an initial cumulative carrying value of $9.8 million as of their dates of issuance. Each reporting period, the Company is required to accrete the carrying value of the convertible debentures such that at maturity on October 6, 2009, the carrying value of the debentures will be the face value of $15.0 million. The increase in expense in 2007 compared with 2006 is due to a higher effective rate of interest.

Amortization of Deferred Financing Charges

Amortization of deferred financing charges totalled $110 thousand in 2007 compared with $87 thousand in 2006 and $84 thousand in 2005. The deferred financing charges relate to the convertible debenture transaction and will be amortized using the effective interest rate method over the five-year life of the debt commencing October 6, 2004.

During the year, the Company incurred approximately $1.3 million in deferred arrangement costs associated with negotiating the arrangement agreement outlined below (see Subsequent Events). The agreements were completed and signed in July 2007. These costs will be netted against proceeds from the arrangement in the first quarter of fiscal 2008.

Interest and Other Income

Interest income totalled $503 thousand in 2007 compared to $374 thousand in 2006 and $524 thousand in 2005. The increase from 2006 to 2007 is due to a higher average cash and marketable securities balances in 2007 and higher interest rates during 2007. Higher average cash and marketable securities balances were primarily a function of the funds received as part to of the August 2006 private placements.

Loss for the Year

Net loss for the year decreased to $9.6 million or $0.05 per share in 2007 compared to $17.9 million or $0.10 per share in 2006 and $22.1 million or $0.13 per share in 2005. The decrease in net loss in 2007 compared with 2006 is due to lower research and development costs resulting from the close of our Virulizin® Phase III clinical trial as well as staff reductions due to corporate changes, lower general and administrative costs due to staff reductions and lower legal, consulting and investor relations charges, depreciation and amortization and higher interest income and offset by higher accretion costs. The decrease in net loss in 2006 compared with 2005 is primarily due to lower research and development costs resulting from the wind down of the Phase III Virulizin® clinical trial.

Corporate Changes

Dr. Jim Wright resigned as the President and Chief Executive Officer of the Company effective September 21, 2006. The Company accrued a liability based on a mutual separation agreement executed during the year. As a result, we recorded severance compensation expense of $500 thousand recorded in general and administrative expense. All amounts payable under the mutual separation agreement were paid during the third quarter of fiscal 2007.

In November 2005, as a means to conserve cash and refocus operations, Lorus scaled back some activities related to the Virulizin® technology and implemented a workforce reduction of approximately 39% or 22 employees. As a result, the Company recorded severance compensation expense for former employees of $557 thousand. Of this expense, $468 thousand is presented in the income statement as general and administrative expense and $89 thousand as research and development expense. Accounts payable and accrued liabilities at May 31, 2006 includes severance and compensation expense liabilities relating to the Company's November 2005 corporate changes of $154 thousand that were paid out by December 2006.

LIQUIDITY AND CAPITAL RESOURCES

Since its inception, Lorus has financed its operations and technology acquisitions primarily from equity and debt financing, the exercise of warrants and stock options, and interest income on funds held for future investment. We continue to leverage the ongoing costs of the six GTI-2040 Phase II clinical trials through work being done by the US NCI at its cost. These trials are currently in the late stages of completion; Lorus intends to continue an expanded GTI-2040 trial at its own cost. The Company has sufficient GTI-2040 drug to support ongoing trials. The Company is currently in the assessment phase of results from its GTI-2501 Phase II clinical trial and is not incurring significant costs thereon. We will continue the development of our small molecule program from internal resources until their anticipated completion.

We have not earned substantial revenues from our drug candidates and are therefore considered to be in the development stage. The continuation of our research and development activities and the commercialization of the targeted therapeutic products are dependent upon our ability to successfully finance and complete our research and development programs through a combination of equity financing and payments from strategic partners. We have no current sources of payments from strategic partners. In addition, we will need to repay or refinance the secured convertible debentures on their maturity should the holder not choose to convert the debentures into common shares. There can be no assurance that additional funding will be available at all or on acceptable terms to permit further clinical development of our products or to repay the convertible debentures on maturity. If we are not able to raise additional funds, we may not be able to continue as a going concern and realize our assets and pay our liabilities as they fall due. The financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis were not appropriate for our financial statements, then adjustments would be necessary in the carrying value of the assets and liabilities, the reported revenues and expenses and the balance sheet classifications used.

We believe our current level of cash and marketable securities and the additional funds available upon the successful reorganization (described below) are sufficient to execute our current planned expenditures for the next twelve months.

Operating Cash Requirements

Lorus utilized cash in operating activities of $6.3 million in 2007 compared with $13.1 million in 2006 and $18.7 million in 2005. The decrease in cash used in operating activities in 2007 is due to lower research and development and general and administrative expenses, as described above and higher interest income. The significant decrease in cash used in operating activities in 2006 compared with 2005 is due to lower research and development expenses, offset by lower interest income.

Cash Position

At May 31, 2007, Lorus had cash and cash equivalents and marketable securities totalling $12.4 million compared to $8.3 million at the end of 2006. The Company invests in highly rated and liquid debt instruments. Investment decisions are made in accordance with an established investment policy administered by senior management and overseen by the board of directors. Working capital (representing primarily cash and cash equivalents and marketable securities having maturities of less that one year) at May 31, 2007 was $6.2 million as compared to $5.8 million at May 31, 2006. As discussed below, subsequent to year end, the company completed a reorganization by way or an arrangement agreement that resulted in approximately $8.5 million in additional cash for Lorus, subject to a $600,000 holdback and post

closing adjustments, not including the costs. Also as a condition of the transaction, the holder of Lorus' $15.0 million secured convertible debenture agreed to vote in favour of the transaction subject to the repurchase by Lorus of its outstanding three million common share purchase warrants at a purchase price of $252,000 upon closing of the Arrangement.

We do not expect to generate positive cash flow from operations in the next several years due to additional research and development costs, including costs related to drug discovery, preclinical testing, clinical trials, manufacturing costs and operating expenses associated with supporting these activities. Negative cash flow will continue until such time, if ever, that we receive regulatory approval to commercialize any of our products under development and revenue from any such products exceeds expenses.

We may seek to access the public or private equity markets from time to time, even if we do not have an immediate need for additional capital at that time. We intend to use our resources to fund our existing drug development programs and develop new programs from our portfolio of preclinical research technologies. The amounts actually expended for research and drug development activities and the timing of such expenditures will depend on many factors, including the progress of the Company's research and drug development programs, the results of preclinical and clinical trials, the timing of regulatory submissions and approvals, the impact of any internally developed, licensed or acquired technologies, our ability to find suitable partnership agreements to assist financially with future development, the impact from technological advances, determinations as to the commercial potential of the Company's compounds and the timing and development status of competitive products.

Financing

On July 10, 2007, the Company completed the Arrangement that had the effect of providing the Company with non-dilutive financing of $8.5 million in additional cash for New Lorus, subject to a $600,000 holdback, a post closing adjustment and not including the costs of the transaction. As a result, the Company expects that, subject to the post closing adjustments, net proceeds of the transaction will be approximately $7 million inclusive of the amount held in escrow to be received in July 2008. See "Subsequent Events," below.

On July 13, 2006 the Company entered into an agreement with High Tech Beteiligungen GmbH & Co. KG (High Tech) to issue 28.8 million common shares at $0.36 per share for gross proceeds of $10.4 million. The subscription price represented a premium of 7.5% over the closing price of the common shares on the Toronto Stock Exchange on July 13, 2007. The transaction closed on August 31, 2006. In connection with the transaction, High Tech received demand registration rights that will enable High Tech to request the registration or qualification of the common shares for resale in the United States and Canada, subject to certain restrictions. These demand registration rights expire on June 30, 2012. In addition, High Tech received the right to nominate one nominee to the board of directors of Lorus or, if it does not have a nominee, it will have the right to appoint an observer to the board. Upon completion of the transaction, High Tech held approximately 14% of the issued and outstanding common shares of Lorus Therapeutics Inc.

On July 24, 2006 Lorus entered into an agreement with Technifund Inc. to issue on a private placement basis, 5.0 million common shares at $0.36 per share for gross proceeds of $1.8 million. The transaction closed on September 1, 2006.

In 2007, Lorus issued common shares on the exercise of stock options for proceeds of $22 thousand (2006, nil, 2005 $112 thousand).

On October 6, 2004, we entered into an agreement to raise aggregate net proceeds of $13.9 million through the issuance of secured convertible debentures and warrants. The debentures are secured by a first charge over all of the assets of the Company. We received $4.4 million on October 6, 2004 (representing a $5.0 million debenture less an investor fee representing 4% of the $15.0 million to be received under the agreement), and $5.0 million on each of January 14 and April 15, 2005. All debentures issued under this agreement are due on October 6, 2009 and are subject to interest payable monthly at a rate of prime plus 1% until such time as the Company's share price reaches $1.75 for 60 consecutive trading days, at which time, interest will no longer be charged. Interest is payable in common shares of Lorus until Lorus' shares trade at a price of $1.00 or more after which interest will be payable in cash or common shares at the option of the debenture holder. Common shares issued in payment of interest will be issued at a price equal to the weighted average trading price of such shares for

the ten trading days immediately preceding their issue in respect of each interest payment. For the year ended May 31, 2007, the Company has issued 3,726,000 in settlement of $1.0 million in interest compared with 2,153,000 common shares in settlement of $882 thousand in interest in the previous year.

The $15.0 million principal amount of debentures is convertible at the holder's option at any time into common shares of the Company with a conversion price per share of $1.00.

The Company issued to the debt holder 3,000,000 warrants expiring October 6, 2009 to buy common shares of the Company at a price per share equal to $1.00. These warrants were repurchased by the Company subsequent to the year end as part of the Arrangement.

Use of Proceeds

In our prospectus dated August 11, 2006 related to the subscription of shares by High Tech, the Company indicated that proceeds from the financing would be used as follows: $8.6 million to fund the development of our product candidates, and the balance for working capital and general corporate purposes. Since the date of receipt of funds, the Company has incurred $1.2 million in research and development expenses on our immunotherapy and small molecule programs and $1.1 million on preliminary and discovery programs.

CONTRACTUAL OBLIGATIONS

At May 31, 2007, we had contractual obligations requiring annual payments as follows:

(Amounts in 000's)	Less than 1 year	1–3 years	4–5 years	5+ years	Total
Operating leases	118	8	–	–	126
Convertible debenture[1]	–	15,000	–	–	15,000
Total	118	15,008	–	–	15,126

[1] The convertible debentures as described above may be converted into common shares of Lorus at a conversion price of $1.00. In the event that the holder does not convert the debentures, Lorus has an obligation to repay the $15.0 million in cash. The amounts above excludes interest expense which is payable monthly by issuance of common shares which is calculated at a rate of prime plus 1% on the outstanding balance.

OFF-BALANCE SHEET ARRANGEMENTS

As at May 31, 2007, we have not entered into any off-balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

In 2007, we did not enter into any transactions with related parties. In order to effectively execute our business strategy, we expect to continue outsourcing various functions to the expertise of third-parties such as contract manufacturing organizations, contract research organizations, and other research organizations. These relationships are with non-related third-parties and occur at arm's length and on normal commercial terms.

SUBSEQUENT EVENTS

On July 10, 2007 Old Lorus and the Company completed a plan of arrangement and corporate reorganization with, among others, 6707157 Canada Inc. ("Investor") and Pinnacle International Lands, Inc. (the "Arrangement").

As part of the Arrangement, all of the assets and liabilities of Old Lorus (including all of the shares of its subsidiaries held by it), with the exception of certain future tax assets, were transferred, directly or indirectly, from Old Lorus to the Company. Securityholders in Old Lorus exchanged their securities in Old Lorus for equivalent securities in New Lorus on a one-for-one basis (the "Exchange") and the board of directors and management of Old Lorus continued as the board of directors and management of the Company. Lorus obtained substitutional listings of its common shares on both the Toronto Stock Exchange (TSX) and the American Stock Exchange (AMEX), and continues to specialize in the discovery, research and development of pharmaceutical products and technologies that were previously being performed by Old Lorus.

In connection with the Arrangement and after the Exchange, the share capital of Old Lorus was reorganized into voting common shares and non-voting common shares and the Investor acquired from Lorus and the Selling Shareholders (as defined below) approximately 41% of the voting common shares and all of the non-voting common shares by making an aggregate cash payment to New Lorus and the Selling Shareholders equal to approximately $8.5 million on closing of the transaction less, in the case of Lorus, an escrowed amount of $600,000, subject to certain post-closing adjustments and before transaction costs. The remaining 59% of the voting common shares of Old Lorus was distributed to the shareholders of Lorus who were not residents of the United States on a pro-rata basis, and shareholders of Lorus who were residents of the United States received a nominal cash payment in lieu of their pro-rata share of voting common shares of Old Lorus. After completion of the Arrangement, Lorus was not related to Old Lorus, which was subsequently renamed as 4325231 Canada Inc.

As a condition of the Arrangement, High Tech Beteiligungen GmbH & Co. KG and certain other shareholders of Old Lorus (the "Selling Shareholders"), agreed to sell to the Investor the voting common shares to be received by them under the Arrangement at the same price per share as was paid to shareholders who are residents of the United States. The proceeds received by the Selling Shareholders was nominal.

Also as a condition of the Arrangement, the holder of Old Lorus' secured convertible debenture agreed to vote in favour of the transaction subject to the repurchase by Lorus of its outstanding three million common share purchase warrants at a purchase price of $252,000 upon closing of the Arrangement.

Following the Arrangement, the Company has approximately $7.0 million in unrecognized future tax benefits resulting from non-capital losses carried forward, and scientific research and experimental development expenditures. In light of the uncertainty regarding our future ability to generate taxable income, management is of the opinion that it is not more likely than not that these tax assets will be realized in the foreseeable future and hence, a full valuation allowance has been recorded against these income tax assets. Consequently, no future income tax assets or liabilities are recorded on the balance sheets.

In addition, under the Arrangement, Lorus and its subsidiaries indemnified Old Lorus and its directors, officers and employees against any and all liabilities, losses, costs, expenses, claims and damages, other than for certain tax liabilities, related to the operations carried out by Old Lorus prior to and by the Company subsequent to, the transfer of assets, liabilities and operations to the Company.

RISK FACTORS

Before making an investment decision with respect to our common shares, you should carefully consider the following risk factors, in addition to the other information included or incorporated by reference into this report. The risks set out below are not the only risks we face. If any of the following risks occur, our business, financial condition, prospects or results of operations would likely suffer. In that case, the trading price of our common shares could decline and you may lose all or part of the money you paid to buy our common shares.

We have a history of operating losses. We expect to incur net losses and we may never achieve or maintain profitability.

We have not been profitable since our inception in 1986. We reported net losses of $9.6 million; $17.9 million and $22.1 million for the years ended May 31, 2007, 2006 and 2005, respectively. As of May 31, 2007, we had an accumulated deficit of $174.2 million.

To date we have only generated nominal revenues from the sale of Virulizin® in Mexico and we stopped selling Virulizin® in Mexico in July 2005. We have not generated any other revenue from product sales to date and it is possible that we will never have sufficient product sales revenue to achieve profitability. We expect to continue to incur losses for at least the next several years as we or our collaborators and licensees pursue clinical trials and research and development efforts. To become profitable, we, either alone or with our collaborators and licensees, must successfully develop, manufacture and market our current product candidates, GTI-2040, as well as continue to identify, develop, manufacture and market new product candidates. It is possible that we will never have significant product sales revenue or receive significant royalties on our licensed product candidates. If funding is insufficient at any time in the future, we may not be able to develop or commercialize our products, take advantage of business opportunities or respond to competitive pressures.

Our current and anticipated operations, particularly our product development requires substantial capital. We expect that our existing cash and cash equivalents, along with the funds available to us through the reorganization agreement described above, will sufficiently fund our current and planned operations through at least the next twelve months. However, our future capital needs will depend on many factors, including the extent to which we enter into collaboration agreements with respect to any of our proprietary product candidates, receive royalty and milestone payments from our possible collaborators and make progress in our internally funded research and development activities.

Our capital requirements will also depend on the magnitude and scope of these activities, our ability to maintain existing and establish new collaborations, the terms of those collaborations, the success of our collaborators in developing and marketing products under their respective collaborations with us, the success of our contract manufacturers in producing clinical and commercial supplies of our product candidates on a timely basis and in sufficient quantities to meet our requirements, competing technological and market developments, the time and cost of obtaining regulatory approvals, the extent to which we choose to commercialize our future products through our own sales and marketing capabilities, the cost of preparing, filing, prosecuting, maintaining and enforcing patent and other rights and our success in acquiring and integrating complementary products, technologies or companies. We do not have committed external sources of funding and we cannot assure you that we will be able to obtain additional funds on acceptable terms, if at all. If adequate funds are not available, we may be required to:

- engage in equity financings that would be dilutive to current shareholders;
- delay, reduce the scope of or eliminate one or more of our development programs; or
- obtain funds through arrangements with collaborators or others that may require us to relinquish rights to technologies, product candidates or products that we would otherwise seek to develop or commercialize ourselves; or license rights to technologies, product candidates or products on terms that are less favourable to us than might otherwise be available.

Our cash flow may not be sufficient to cover interest payments on our secured convertible debentures or to repay the debentures at maturity.

Our ability to make interest payments, if required to be paid in cash, and to repay at maturity or refinance our prime plus 1% convertible debentures due in approximately 14 months (October 2009) will depend on our ability to generate or raise sufficient cash or refinance them. We have never generated positive annual cash flow from our operating activities, and we may not generate or sustain positive cash flows from operations in the future. Our ability to generate sufficient cash flow will depend on our ability, or the ability of our strategic partners, to successfully develop and obtain regulatory approval for new products and to successfully market these products, as well as the results of our research and development efforts and other factors, including general economic, financial, competitive, legislative and regulatory conditions, many of which are outside of our control.

We may violate one or more of the operational covenants related to our convertible debentures that could result in an event of default and the requirement for early payment of our convertible debentures.

Our convertible debentures are subject to certain operational covenants. In the event that one of those covenants is breached by us, an event of default could be declared requiring the immediate payment of the face value of the debentures. This could result in our inability to pay and insolvency of the Company, a dilutive equity financing in attempt to raise funds to repay the debentures, or a significant reduction in cash available for us to use towards the development of our product candidates.

We may be unable to obtain partnerships for one or more of our product candidates which could curtail future development and negatively impact our share price.

Our product candidates require significant funding to reach regulatory approval upon positive clinical results. Such funding, in particular for Virulizin®, will be very difficult, or impossible to raise in the public markets. If such partnerships are not attainable, the development of these product candidates maybe significantly delayed or stopped altogether. The announcement of such delay or discontinuation of development may have a negative impact on our share price.

In addition, our strategy for the research, development and commercialization of our products requires entering into various arrangements with corporate collaborators, licensers, licensees and others, and our commercial success is dependent upon these outside parties performing their respective contractual responsibilities. The amount and timing of resources that such third-parties will devote to these activities may not be within our control. We cannot assure you that such parties will perform their obligations as expected. We also cannot assure you that our collaborators will devote adequate resources to our programs. In addition, we could become involved in disputes with our collaborators, which could result in a delay or termination of the related development programs or result in litigation. We intend to seek additional collaborative arrangements to develop and commercialize some of our products. We may not be able to negotiate collaborative arrangements on favourable terms, or at all, in the future, or that our current or future collaborative arrangements will be successful.

If we cannot negotiate collaboration, licence or partnering agreements, we may never achieve profitability.

Clinical trials are long, expensive and uncertain processes and Health Canada or the FDA may ultimately not approve any of our product candidates. We may never develop any commercial drugs or other products that generate revenues.

None of our products has received regulatory approval for commercial use and sale in North America. We cannot market a pharmaceutical product in any jurisdiction until it has completed thorough preclinical testing and clinical trials in addition to that jurisdiction's extensive regulatory approval process. In general, significant research and development and clinical studies are required to demonstrate the safety and effectiveness of our products before we can submit any regulatory applications.

Clinical trials are long, expensive and uncertain processes. Clinical trials may not be commenced or completed on schedule, and Health Canada or the FDA may not ultimately approve our product candidates for commercial sale. Further, even if the results of our preclinical studies or clinical trials are initially positive, it is possible that we will obtain different results in the later stages of drug development or that results seen in clinical trials will not continue with longer term treatment. Drugs in late stages of clinical development may fail to show the desired safety and efficacy traits despite having progressed through initial clinical testing. For example, positive results in early Phase I or Phase II clinical trials may not be repeated in larger Phase II or Phase III clinical trials. The results of our Phase III clinical trial of Virulizin® did not meet the primary endpoint of the study despite promising preclinical and early stage clinical data. All of our potential drug candidates are prone to the risks of failure inherent in drug development.

Preparing, submitting and advancing applications for regulatory approval is complex, expensive and time intensive and entails significant uncertainty. The results of our completed preclinical studies and clinical trials may not be indicative of future clinical trial results. A commitment of substantial resources to conduct time-consuming research, preclinical studies and clinical trials will be required if we are to complete development of our products. Clinical trials of our products require that we identify and enrol a large number of patients with the illness under investigation. We may not be able to enrol a sufficient number of appropriate patients to complete our clinical trials in a timely manner particularly in smaller indications such as Acute Myeloid Leukemia. If we experience difficulty in enrolling a sufficient number of patients to conduct our clinical trials, we may need to delay or terminate ongoing clinical trials and will not accomplish objectives material to our success that could affect the price of our common shares. Delays in planned patient enrolment or lower than anticipated event rates in our current clinical trials or future clinical trials may result in increased costs, program delays, or both.

In addition, unacceptable toxicities or adverse side effects may occur at any time in the course of preclinical studies or human clinical trials or, if any products are successfully developed and approved for marketing, during commercial use of any approved products. The appearance of any such unacceptable toxicities or adverse side effects could interrupt, limit, delay or abort the development of any of our product candidates or, if previously approved, necessitate their withdrawal from the market. Furthermore, disease resistance or other unforeseen factors may limit the effectiveness of our potential products.

The clinical trials of any of our drug candidates could be unsuccessful, which would prevent us from advancing, commercializing or partnering the drug.

Our failure to develop safe, commercially viable drugs would substantially impair our ability to generate revenues and sustain our operations and would materially harm our business and adversely affect our share price. We may never achieve profitability.

As a result of intense competition and technological change in the pharmaceutical industry, the marketplace may not accept our products or product candidates, and we may not be able to compete successfully against other companies in our industry and achieve profitability.

Many of our competitors have drug products that have already been approved or are in development, and operate large, well-funded research and development programs in these fields. Many of our competitors have substantially greater financial and management resources, stronger intellectual property positions and greater manufacturing, marketing and sales capabilities, areas in which we have limited or no experience. In addition, many of our competitors have significantly greater experience than we do in undertaking preclinical testing and clinical trials of new or improved pharmaceutical products and obtaining required regulatory approvals. Consequently, our competitors may obtain Health Canada, FDA and other regulatory approvals for product candidates sooner and may be more successful in manufacturing and marketing their products than we or our collaborators are. Existing and future products, therapies and technological approaches will compete directly with the products we seek to develop. Current and prospective competing products may provide greater therapeutic benefits for a specific problem or may offer easier delivery or comparable performance at a lower cost. Any product candidate that we develop and that obtains regulatory approval must then compete for market acceptance and market share. Our product candidates may not gain market acceptance among physicians, patients, healthcare payers and the medical community. Further, any products we develop may become obsolete before we recover any expenses we incurred in connection with the development of these products. As a result, we may never achieve profitability.

If we fail to attract and retain key employees, the development and commercialization of our products may be adversely affected.

We depend heavily on the principal members of our scientific and management staff. If we lose any of these persons, our ability to develop products and become profitable could suffer. The risk of being unable to retain key personnel may be increased by the fact that we have not executed long term employment contracts with our employees, except for our senior executives. Our future success will also depend in large part on our ability to attract and retain other highly qualified scientific and management personnel. We face competition for personnel from other companies, academic institutions, government entities and other organizations.

We may be unable to obtain patents to protect our technologies from other companies with competitive products, and patents of other companies could prevent us from manufacturing, developing or marketing our products.

Patent protection

The patent positions of pharmaceutical and biotechnology companies are uncertain and involve complex legal and factual questions. The United States ("U.S.") Patent and Trademark Office and many other patent offices in the world have not established a consistent policy regarding the breadth of claims that it will allow in biotechnology patents. Further, allowable patentable subject matter and the scope of patent protection obtainable may differ between jurisdictions. If a patent office allows broad claims, the number and cost of patent interference proceedings in the U.S. or analogous proceedings in other jurisdictions and the risk of infringement litigation may increase. If it allows narrow claims, the risk of infringement may decrease, but the value of our rights under our patents, licenses and patent applications may also decrease. In addition, the scope of the claims in a patent application can be significantly modified during prosecution before the patent is issued. Consequently, we cannot know whether our pending applications will result in the issuance of patents or, if any patents are issued, whether they will provide us with significant proprietary protection or will be circumvented, invalidated or found to be unenforceable. Until recently, patent applications in the U.S. were maintained in secrecy until the patents issued, and publication of discoveries in scientific or patent literature often lags behind actual discoveries. Patent applications filed in the United States after November 2000 generally will be published 18 months after the filing date unless the applicant certifies that the invention will not be the subject of a foreign patent application. In many other jurisdictions, such as Canada, patent applications are published 18 months from the priority date. We cannot assure you that, even if published, we will be aware of all such literature. Accordingly, we cannot be certain that the named inventors of our products and processes were the first to invent that product or process or that we were the first to pursue patent coverage for our inventions.

Enforcement of intellectual property rights

Our commercial success depends in part on our ability to maintain and enforce our proprietary rights. If third-parties engage in activities that infringe our proprietary rights, our management's focus will be diverted and we may incur significant costs in asserting our rights. We may not be successful in asserting our proprietary rights, which could result in our patents being held invalid or a court holding that the third-party is not infringing, either of which would harm our competitive position. In addition, we cannot assure you that others will not design around our patented technology. Moreover, we may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office, European opposition proceedings, or other analogous proceedings in other parts of the world to determine priority of invention and the validity of patent rights granted or applied for, which could result in substantial cost and delay, even if the eventual outcome is favourable to us. We cannot assure you that our pending patent applications, if issued, would be held valid or enforceable. Additionally, many of our foreign patent applications have been published as part of the patent prosecution process in such countries.

Trademark protection

Protection of the rights revealed in published patent applications can be complex, costly and uncertain. In order to protect goodwill associated with our Company and product names, we rely on trademark protection for our marks. For example, we have registered the Virulizin® trademark with the U.S. Patent and Trademark Office. A third-party may assert a claim that the Virulizin® mark is confusingly similar to its mark and such claims or the failure to timely register the Virulizin® mark or objections by the FDA could force us to select a new name for Virulizin®, which could cause us to incur additional expense.

Trade secrets

We also rely on trade secrets, know-how and confidentiality provisions in our agreements with our collaborators, employees and consultants to protect our intellectual property. However, these and other parties may not comply with the terms of their agreements with us, and we might be unable to adequately enforce our rights against these people or obtain adequate compensation for the damages caused by their unauthorized disclosure or use. Our trade secrets or those of our collaborators may become known or may be independently discovered by others.

Our products and product candidates may infringe the intellectual property rights of others, which could increase our costs.

Our success also depends on avoiding infringement of the proprietary technologies of others. In particular, there may be certain issued patents and patent applications claiming subject matter which we or our collaborators may be required to license in order to research, develop or commercialize at least some of our product candidates, including Virulizin®, GTI-2040, GTI-2501 and small molecules. In addition, third-parties may assert infringement or other intellectual property claims against us based on our patents or other intellectual property rights. An adverse outcome in these proceedings could subject us to significant liabilities to third-parties, require disputed rights to be licensed from third-parties or require us to cease or modify our use of the technology. If we are required to license such technology, we cannot assure you that a license under such patents and patent applications will be available on acceptable terms or at all. Further, we may incur substantial costs defending ourselves in lawsuits against charges of patent infringement or other unlawful use of another's proprietary technology.

If product liability claims are brought against us or we are unable to obtain or maintain product liability insurance, we may incur substantial liabilities that could reduce our financial resources.

The clinical testing and commercial use of pharmaceutical products involves significant exposure to product liability claims. We have obtained limited product liability insurance coverage for our clinical trials on humans; however, our insurance coverage may be insufficient to protect us against all product liability damages. Further, liability insurance coverage is becoming increasingly expensive and we might not be able to obtain or maintain product liability insurance in the future on acceptable terms or in sufficient amounts to protect us against product liability damages. Regardless of merit or eventual outcome, liability claims may result in decreased demand for a future product, injury to reputation, withdrawal of clinical trial volunteers, loss of revenue, costs of litigation, distraction of management and substantial monetary awards to plaintiffs. Additionally, if we are required to pay a product liability claim, we may not have sufficient financial resources to complete development or commercialization of any of our product candidates and our business and results of operations will be adversely affected.

We have no manufacturing capabilities. We depend on third-parties, including a number of sole suppliers, for manufacturing and storage of our product candidates used in our clinical trials. Product introductions may be delayed or suspended if the manufacture of our products is interrupted or discontinued.

We do not have manufacturing facilities to produce supplies of Virulizin®, GTI-2040, GTI-2501, small molecule or any of our other product candidates to support clinical trials or commercial launch of these products, if they are approved. We are dependent on third-parties for manufacturing and storage of our product candidates. If we are unable to contract for a sufficient supply of our product candidates on acceptable terms, or if we encounter delays or difficulties in the manufacturing process or our relationships with our manufacturers, we may not have sufficient product to conduct or complete our clinical trials or support preparations for the commercial launch of our product candidates, if approved.

Dependence on contract manufacturers for commercial production involves a number of risks, many of which are outside our control. These risks include potential delays in transferring technology, and the inability of our contract manufacturer to scale production on a timely basis, to manufacture commercial quantities at reasonable costs, to comply with cGMP and to implement procedures that result in the production of drugs that meet our specifications and regulatory requirements.

Our reliance on contract manufacturers exposes us to additional risks, including:

- there may be delays in scale-up to quantities needed for clinical trials and commercial launch or failure to manufacture such quantities to our specifications, or to deliver such quantities on the dates we require;
- our current and future manufacturers are subject to ongoing, periodic, unannounced inspection by the FDA and corresponding Canadian and international regulatory authorities for compliance with strictly enforced cGMP regulations and similar standards, and we do not have control over our contract manufacturers' compliance with these regulations and standards;
- our current and future manufacturers may not be able to comply with applicable regulatory requirements, which would prohibit them from manufacturing products for us;
- if we need to change to other commercial manufacturing contractors, the FDA and comparable foreign regulators must approve these contractors prior to our use, which would require new testing and compliance inspections, and the new manufacturers would have to be educated in, or themselves develop substantially equivalent processes necessary for the production or our products; and
- our manufacturers might not be able to fulfill our commercial needs, which would require us to seek new manufacturing arrangements and may result in substantial delays in meeting market demand.

Any of these factors could cause us to delay or suspend clinical trials, regulatory submission, required approvals or commercialization of our products under development, entail higher costs and result in our being unable to effectively commercialize our products. We do not currently intend to manufacture any of our product candidates, although we may choose to do so in the future. If we decide to manufacture our products, we would be subject to the regulatory risks and requirements described above. We would also be subject to similar risks regarding delays or difficulties encountered in manufacturing our pharmaceutical products and we would require additional facilities and substantial additional capital. We cannot assure you that we would be able to manufacture any of our products successfully in accordance with regulatory requirements and in a cost effective manner.

Our operations involve hazardous materials and we must comply with environmental laws and regulations, which can he expensive and restrict how we do business.

Our research and development activities involve the controlled use of hazardous materials, radioactive compounds and other potentially dangerous chemicals and biological agents. Although we believe our safety procedures for these materials comply with governmental standards, we cannot entirely eliminate the risk of accidental contamination or injury from these materials. We currently have insurance, in amounts and on terms typical for companies in businesses that are similarly situated, that could coverall or a portion of a damage claim arising from our use of hazardous and other materials. However, if an accident or environmental discharge occurs, and we are held liable for any resulting damages, the associated liability could exceed our insurance coverage and our financial resources.

We have limited sales, marketing and distribution experience.

We have very limited experience in the sales, marketing and distribution of pharmaceutical products. There can be no assurance that we will be able to establish sales, marketing, and distribution capabilities or make arrangements with our collaborators, licensees or others to perform such activities or that such efforts will be successful. If we decide to market any of our products directly, we must either acquire or internally develop a marketing and sales force with technical expertise and with supporting distribution capabilities. The acquisition or development of a sales and distribution infrastructure would require substantial resources, which may divert the attention of our management and key personnel and have a negative impact on our product development efforts. If we contract with third-parties for the sales and marketing of our products, our revenues will be dependent on the efforts of these third-parties, whose efforts may not be successful. If we fail to establish successful marketing and sales capabilities or to make arrangements with third-parties, our business, financial condition and results of operations will be materially adversely affected.

Our interest income is subject to fluctuations of interest rates in our investment portfolio.

Our investments are held to maturity and have staggered maturities to minimize interest rate risk. There can be no assurance that interest income fluctuations will not have an adverse impact on our financial condition. We maintain all our accounts in Canadian dollars, but a portion of our expenditures are in foreign currencies. We do not currently engage in hedging our foreign currency requirements to reduce exchange rate risk.

Because of the uncertainty of pharmaceutical pricing, reimbursement and healthcare reform measures, if any of our product candidates are approved for sale to the public, we may be unable to sell our products profitably.

The availability of reimbursement by governmental and other third-party payers affects the market for any pharmaceutical product. These third-party payers continually attempt to contain or reduce the costs of healthcare. There have been a number of legislative and regulatory proposals to change the healthcare system and further proposals are likely. Significant uncertainty exists with respect to the reimbursement status of newly approved healthcare products. In addition, third-party payers are increasingly challenging the price and cost effectiveness of medical products and services. We might not be able to sell our products profitably or recoup the value of our investment in product development if reimbursement is unavailable or limited in scope.

RISKS RELATED TO OUR COMMON SHARES

Our share price has been and may continue to be volatile and an investment in our common shares could suffer a decline in value.

You should consider an investment in our common shares as risky and invest only if you can withstand a significant loss and wide fluctuations in the market value of your investment. We receive only limited attention by securities analysts and frequently experience an imbalance between supply and demand for our common shares. The market price of our common shares has been highly volatile and is likely to continue to be volatile. Factors affecting our common share price include:

- the progress of our and our collaborators' clinical trials, including our and our collaborators' ability to produce clinical supplies of our product candidates on a timely basis and in sufficient quantities to meet our clinical trial requirements;
- announcements of technological innovations or new product candidates by us, our collaborators or our competitors;
- fluctuations in our operating results;
- published reports by securities analysts;
- developments in patent or other intellectual property rights;
- publicity concerning discovery and development activities by our licensees;
- the cash and short term investments held us and our ability to secure future financing;

- public concern as to the safety and efficacy of drugs that we and our competitors develop;
- governmental regulation and changes in medical and pharmaceutical product reimbursement policies; and
- general market conditions.

Future sales of our common shares by us or by our existing shareholders could cause our share price to fall.

Additional equity financings or other share issuances by us could adversely affect the market price of our common shares. Sales by existing shareholders of a large number of shares of our common shares in the public market and the sale of shares issued in connection with strategic alliances, or the perception that such additional sales could occur, could cause the market price of our common shares to drop.

Conversion of our secured convertible debentures will dilute the ownership interest of existing shareholders.

The conversion of some or all of the convertible debentures will dilute the ownership interests of existing shareholders. Any sales in the public market of the common shares issuable upon such conversion could adversely affect prevailing market prices of our common shares. In addition, the existence of the secured convertible debentures may encourage short selling by market participants.

CRITICAL ACCOUNTING POLICIES

The Company periodically reviews its financial reporting and disclosure practices and accounting policies to ensure that they provide accurate and transparent information relative to the current economic and business environment. As part of this process, the Company has reviewed its selection, application and communication of critical accounting policies and financial disclosures. Management has discussed the development and selection of the critical accounting policies with the Audit Committee of the Board of Directors and the Audit Committee has reviewed the disclosure relating to critical accounting policies in this Management's Discussion and Analysis. Other important accounting polices are described in the Financial Statements.

Drug Development Costs

We incur costs related to the research and development of pharmaceutical products and technologies for the management of cancer. These costs include internal and external costs for preclinical research and clinical trials, drug costs, regulatory compliance costs and patent application costs. All research costs are expensed as incurred as required under GAAP.

Development costs, including the cost of drugs for use in clinical trials, are expensed as incurred unless they meet the criteria under GAAP for deferral and amortization. The Company continually assesses its activities to determine when, if ever, development costs may qualify for capitalization. By expensing the research and development costs as required under GAAP, the value of the product portfolio is not reflected on the Company's Financial Statements.

Stock-Based Compensation

We have applied the fair value based method to expense stock options awarded since June 1, 2002 using the Black-Scholes option-pricing model as allowed under CICA Handbook Section 3870. The model estimates the fair value of fully transferable options, without vesting restrictions, which significantly differs from the stock option awards issued by Lorus. The model also requires four highly subjective assumptions including future stock price volatility and expected time until exercise, which greatly affect the calculated values. The increase or decrease of one of these assumptions could materially increase or decrease the fair value of stock options issued and the associated expense.

Valuation Allowance for Future Tax Assets

We have a net tax benefit resulting from non-capital losses carried forward, and scientific research and experimental development expenditures. In light of the recent net losses and uncertainty regarding our future ability to generate taxable income, management is of the opinion that it is not more likely than not that these tax assets will be realized in the foreseeable future and hence, a full valuation allowance has been recorded against these income tax assets. Consequently, no future income tax assets or liabilities are recorded on the balance sheets.

The generation of future taxable income could result in the recognition of some portion or all of the remaining benefits, which could result in an improvement in our results of operations through the recovery of future income taxes.

In light of the fact that the Company believed that it could not fully utilize a significant portion of its future tax assets prior to their expiry, subsequent to the year-end, it underwent a reorganization that resulted in certain tax attributes not being carried forward to the successor entity. As a result, the Company will not have available to it approximately $39.8 million of its future tax assets.

Valuation of Long Lived Assets

We periodically review the useful lives and the carrying values of our long lived assets. We review for impairment in long lived assets whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. If the sum of the undiscounted future cash flows expected to result from the use and eventual disposition of an asset is less than its carrying amount, it is considered to be impaired. An impairment loss is measured at the amount by which the carrying amount of the asset exceeds its fair value; which is estimated as the expected future cash flows discounted at a rate commensurate with the risks associated with the recovery of the asset.

ACCOUNTING POLICY CHANGES

There were no new accounting policies implemented during the year-ended May 31, 2007. The following changes were implemented in 2006:

Variable Interest Entities

Effective June 1, 2005, the Company adopted the recommendations of CICA Handbook Accounting Guideline 15 (AcG-15), *Consolidation of Variable Interest Entities*, effective for fiscal years beginning on or after November 1, 2004. Variable interest entities (VIEs) refer to those entities that are subject to control on a basis other than ownership of voting interests. AcG-15 provides guidance for identifying VIEs and criteria for determining which entity, if any, should consolidate them. The adoption of AcG-15 did not have an effect on the financial position, results of operations or cash flows in the current period or the prior period presented.

Financial Instruments – Disclosure and Presentation

Effective June 1, 2005, the Company adopted the amended recommendations of CICA Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*, effective for fiscal years beginning on or after November 1, 2004. Section 3860 requires that certain obligations that may be settled at the issuer's option in cash or the equivalent value by a variable number of the issuer's own equity instruments be presented as a liability. The Company has determined that there is no impact on the Financial Statements resulting from the adoption of the amendments to Section 3860 either in the current period or the prior period presented.

Accounting for Convertible Debt Instruments

On October 17, 2005, the CICA issued EIC 158, *Accounting for Convertible Debt Instruments* applicable to convertible debt instruments issued subsequent to the date of the EIC. EIC 158 discusses the accounting treatment of convertible debentures in which upon conversion, the issuer is either required or has the option to satisfy all or part of the obligation in cash. The EIC discusses various accounting issues related to this type of convertible debt. The Company has determined that there is no impact on the Financial Statements resulting from the adoption of EIC 158 either in the current period or the prior period presented.

Section 3831, Non-Monetary Transactions

In June 2005, the CICA released a new Handbook Section 3831, *Non-monetary Transactions*, effective for all non-monetary transactions initiated in periods beginning on or after January 1, 2006. This standard requires all non-monetary transactions to be measured at fair value unless they meet one of four very specific criteria. Commercial substance replaces culmination of the earnings process as the test for fair value measurement. A transaction has commercial substance if it causes an identifiable and measurable change in the economic circumstances of the entity. Commercial substance is a function of the cash flows expected by the reporting entity.

RECENT ACCOUNTING PRONOUNCEMENTS

Comprehensive Income and Equity

In January 2005, the CICA released new Handbook Section 1530, *Comprehensive Income*, and Section 3251, *Equity*. Section 1530 establishes standards for reporting comprehensive income. The section does not address issues of recognition or measurement for comprehensive income and its components. Section 3251 establishes standards for the presentation of equity and changes in equity during the reporting period. The requirements in this section are in addition to Section 1530.

Section 3855, Financial Instruments – Recognition and Measurement

CICA Handbook Section 3855 establishes standards for the recognition and measurement of all financial instruments, provides a characteristics-based definition of a derivative instrument, provides criteria to be used to determine when a financial instrument should be recognized, and provides criteria to be used to determine when a financial liability is considered to be extinguished.

Section 3865, Hedges

Section 3865 establishes standards for when and how hedge accounting may be applied. Hedge accounting is optional.

These three Sections are effective for fiscal years beginning on or after October 1, 2006. An entity adopting these Sections for a fiscal year beginning before October 1, 2006 must adopt all the Sections simultaneously.

Section 3861, Financial Instruments – Disclosure and Presentation

Section 3861 discusses the presentation and disclosure of these items. In December 2006, the Canadian Institute of Chartered Accountants issued Section 3862, *Financial Instruments – Disclosure,* and Section 3863, *Financial Instruments – Presentation*, to replace Section 3861, *Financial Instruments – Disclosure and Presentation*. These new Sections are effective for interim and annual financial statements with fiscal years beginning on or after October 1, 2007, but may be adopted in place of Section 3861, before that date.

SELECTED ANNUAL FINANCIAL DATA

The following selected consolidated financial data has been derived from, and should be read in conjunction with, the accompanying audited Financial Statements for the year ended May 31, 2007 which are prepared in accordance with Canadian GAAP.

On July 10, 2007 (the "Arrangement Date"), the Company completed a plan of arrangement and corporate reorganization with among others 4325231 Canada Inc. (formerly Lorus Therapeutics Inc.) ("Old Lorus"), 6707157 Canada Inc. and Pinnacle International Lands Inc. As a result of the plan of arrangement and reorganization, among other things, each common share of Old Lorus was exchanged for one common share of the Company and the assets (excluding certain future tax assets and related valuation allowance) and liabilities of Old Lorus were transferred to the Company and/or its subsidiaries. The Company continued the business of Old Lorus after the Arrangement Date with the same officers and employees and continued to be governed by the same Board of Directors as Old Lorus prior to the Arrangement Date. Therefore, the Company's operations have been accounted for on a continuity of interest basis and accordingly, the consolidated financial statement information below reflect that of the Company as if it had always carried on the business formerly carried on by Old Lorus. Therefore, the following Information is taken from the financial statements of Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.) See "Supplementary Financial Information".

Consolidated Statements of Loss and Deficit

	Years Ended May 31		
(Amounts in Canadian 000's except for per common share data)	2007	2006	2005
REVENUE	$ 107	$ 26	$ 6
EXPENSES			
Cost of sales	16	3	1
Research and development	3,384	10,237	14,394
General and administrative	3,848	4,334	5,348
Stock-based compensation	503	1,205	1,475
Depreciation and amortization	402	771	564
Operating expenses	8,153	16,550	21,782
Interest expense on convertible debentures	503	882	300
Accretion in carrying value of secured convertible debentures	1,050	790	426
Amortization of deferred financing charges	110	87	84
Interest income	(503)	(374)	(524)
Loss for the period	9,638	17,909	22,062
Basic and diluted loss per common share	$ 0.05	$ 0.10	$ 0.13
Weighted average number of common shares outstanding used in the calculation of basic and diluted loss per share	204,860	173,523	172,112
Total assets	$ 15,475	$ 11,461	$ 27,566
Total long-term liabilities	$ 11,937	$ 11,002	$ 10,212

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth certain unaudited consolidated statements of operations data for each of the eight most recent fiscal quarters that, in management's opinion, have been prepared on a basis consistent with the audited Consolidated Financial Statements contained elsewhere in this annual report and includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the information presented.

Research and development expenses have decreased throughout 2007 in comparison with the same quarters in the prior year. This reduction is due to the close of our Phase III Virulizin® clinical trial as well as corporate changes in November 2005 to reduce headcount.

General and administrative expenses have remained relatively consistent across quarters in the current fiscal year with the exception of an increase for the quarter ended November 30, 2006 due to severance charges relating to the mutual separation agreement executed in September as described in the Corporate Changes section, above. Expenditures have continued to decline since Q2 2007 due to reduced headcount as well as reduced consulting, patent costs and investor relation costs.

Net loss decreased in Q3 and Q4 of 2007 as the result of reduced research and development and general and administrative expenditures.

	Fiscal 2007 Quarter Ended				Fiscal 2006 Quarter Ended			
(Amounts in 000's except for per common share data)	May 31, 2007	Feb. 28, 2007	Nov. 30, 2006	Aug. 31, 2006	May 31, 2006	Feb. 28, 2006	Nov. 30, 2005	Aug. 31, 2005
Revenue	$ 40	$ 37	$ 23	$ 7	$ 14	$ 5	$ 6	$ 1
Research and development	259	672	1,122	1,331	1,353	2,296	2,631	3,957
General and administrative	820	833	1,407	788	730	909	1,619	1,076
Net loss	(1,689)	(2,062)	(3,117)	(2,770)	(2,970)	(4,095)	(5,102)	(5,742)
Basic and diluted net loss per share	$ (0.01)	$ (0.01)	$ (0.01)	$ (0.01)	$ (0.02)	$ (0.02)	$ (0.03)	$ (0.03)
Cash used in operating activities	$ (89)	$ (1,805)	$ (2,585)	$ (1,814)	$ (1,940)	$ (3,956)	$ (2,360)	$ (4,809)

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to provide reasonable assurance that all material information required to be publicly disclosed by a public company is gathered and communicated to management, including the certifying officers, on a timely basis so that appropriate decisions can be made regarding public disclosure. As at the end of May 31, 2007, the certifying officers and other members of management evaluated the effectiveness of our disclosure controls and procedures (as this term is defined in the rules adopted by Canadian securities regulatory authorities and the United States Securities and Exchange Commission). This evaluation included a review of our existing disclosure and insider trading policy, compliance with regard to that policy, the disclosure controls currently in place surrounding our interim and annual financial statements, MD&A and other required documents and discussions with management surrounding the process of communicating material information to management and in turn the certifying officers and all procedures taking into consideration the size of the company and the number of employees. Based on the evaluation described above, the certifying officers have concluded that, as of May 31, 2007, the disclosure controls and procedures were effective to provide reasonable assurance that the information we are required to disclose on a continuous basis in annual and interim filings and other reports is recorded, processed, summarized and reported or disclosed on a timely basis as required.

OUTSTANDING SHARE DATA

As at August 7, 2007, the Company had 212,627,876 common shares issued and outstanding. In addition, the Company had issued and outstanding 12,494,389 stock options to purchase an equal number of common shares, and a $15.0 million convertible debenture convertible into common shares of Lorus at $1.00 per share.

At May 31, 2007, the Company recorded the repurchase of its 3.0 million warrants in accordance with the terms of an agreement with the Company's convertible debenture holder for $252,000 as related to the arrangement agreement which closed July 10, 2007. The amount was set up as a liability and the difference between the carrying value of the warrants and the amount paid was been credited to contributed surplus.

CAUTION REGARDING FORWARD-LOOKING STATEMENTS

This Management's Discussion and Analysis may contain forward-looking statements within the meaning of Canadian and U.S. securities laws. Such statements include, but are not limited to, statements relating to:

- *our expectations regarding future financings;*
- *our plans to conduct clinical trials;*
- *our expectations regarding the progress and the successful and timely completion of the various stages of our drug discovery, preclinical and clinical studies and the regulatory approval process;*
- *our plans to obtain partners to assist in the further development of our product candidates; and*
- *our expectations with respect to existing and future corporate alliances and licensing transactions with third parties, and the receipt and timing of any payments to be made by us or to us in respect of such arrangements,*

the Company's plans, objectives, expectations and intentions and other statements including words such as "anticipate", "contemplate", "continue", "believe", "plan", "estimate", "expect", "intend", "will", "should", "may", and other similar expressions.

Such statements reflect our current views with respect to future events and are subject to risks and uncertainties and are necessarily based upon a number of estimates and assumptions that, while considered reasonable by us are inherently subject to significant business, economic, competitive, political and social uncertainties and contingencies. Many factors could cause our actual results, performance or achievements to be materially different from any future results, performance, or achievements that may be expressed or implied by such forward-looking statements, including, among others:

- *our ability to obtain the substantial capital required to fund research and operations;*
- *our lack of product revenues and history of operating losses;*
- *our early stage of development, particularly the inherent risks and uncertainties associated with (i) developing new drug candidates generally, (ii) demonstrating the safety and efficacy of these drug candidates in clinical studies in humans, and (iii) obtaining regulatory approval to commercialize these drug candidates;*
- *our drug candidates require time-consuming and costly preclinical and clinical testing and regulatory approvals before commercialization;*
- *clinical studies and regulatory approvals of our drug candidates are subject to delays, and may not be completed or granted on expected timetables, if at all, and such delays may increase our costs and could delay our ability to generate revenue;*
- *the regulatory approval process;*
- *the progress of our clinical trials;*
- *our ability to find and enter into agreements with potential partners;*

- *our ability to attract and retain key personnel;*
- *our ability to obtain patent protection and protect our intellectual property rights;*
- *our ability to protect our intellectual property rights and to not infringe on the intellectual property rights of others;*
- *our ability to comply with applicable governmental regulations and standards;*
- *development or commercialization of similar products by our competitors, many of which are more established and have greater financial resources than we do;*
- *commercialization limitations imposed by intellectual property rights owned or controlled by third parties;*
- *our business is subject to potential product liability and other claims;*
- *our ability to maintain adequate insurance at acceptable costs;*
- *further equity financing may substantially dilute the interests of our shareholders;*
- *changing market conditions; and*
- *other risks detailed from time-to-time in our ongoing quarterly filings, annual information forms, annual reports and annual filings with Canadian securities regulators and the United States Securities and Exchange Commission, and those which are discussed under the heading "Risk Factors".*

Should one or more of these risks or uncertainties materialize, or should the assumptions set out in the section entitled "Risk Factors" underlying those forward-looking statements prove incorrect, actual results may vary materially from those described herein. These forward-looking statements are made as of the date of this annual information form or, in the case of documents incorporated by reference herein, as of the date of such documents, and we do not intend, and do not assume any obligation, to update these forward-looking statements, except as required by law. We cannot assure you that such statements will prove to be accurate as actual results and future events could differ materially from those anticipated in such statements. Investors are cautioned that forward-looking statements are not guarantees of future performance and accordingly investors are cautioned not to put undue reliance on forward-looking statements due to the inherent uncertainty therein.

ADDITIONAL INFORMATION

Additional information relating to Lorus, including Lorus' 2007 annual information form and other disclosure documents, is available on SEDAR at **www.sedar.com**. For any information filed prior to July 10, 2007 please access the information on SEDAR for 4325231 Canada Inc.

The accompanying consolidated financial statements of Lorus Therapeutics Inc. and other financial information contained in this annual report are the responsibility of Management and have been approved by the Board of Directors of the Company.

The consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles, using Management's best estimates and judgments where appropriate. In the opinion of Management, these consolidated financial statements reflect fairly the financial position and the results of operations and cash flows of the Company within reasonable limits of materiality. The financial information contained elsewhere in this annual report has been reviewed to ensure consistency with that in the consolidated financial statements. The integrity and objectivity of data in the financial statements and elsewhere in this annual report are the responsibility of Management.

In discharging its responsibility for the integrity and fairness of the financial statements, management maintains a system of internal controls designed to provide reasonable assurance, at appropriate cost, that transactions are authorized, assets are safeguarded and proper records are maintained. Management believes that the internal controls provide reasonable assurance that financial records are reliable and form a proper basis for the preparation of the consolidated financial statements, and that assets are properly accounted for and safeguarded. The internal control process includes management's communication to employees of policies that govern ethical business conduct.

The Board of Directors, through an Audit Committee, oversees management's responsibilities for financial reporting. This committee, which consists of three independent directors, reviews the audited consolidated financial statements and recommends the financial statements to the Board for approval. Other key responsibilities of the Audit Committee include reviewing the adequacy of the Company's existing internal controls, audit process and financial reporting with management and the external auditors.

The consolidated financial statements have been audited by KPMG LLP, Chartered Accountants, who are independent auditors appointed by the shareholders of the Company upon the recommendation of the Audit Committee. Their report follows. The independent auditors have free and full access to the Audit Committee.

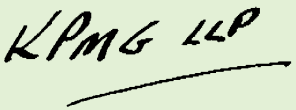
Aiping H. Young
President and Chief Executive Officer

Elizabeth Williams
Director of Finance (Acting Chief Financial Officer)

We have audited the balance sheet of 6650309 Canada Inc. as at May 31, 2007. This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the balance sheet is free of material misstatement. An audit of a balance sheet includes examining, on a test basis, evidence supporting the amounts and disclosures in that balance sheet. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall balance sheet presentation.

In our opinion, the balance sheet presents fairly, in all material respects, the financial position of the Company as at May 31, 2007 in accordance with Canadian generally accepted accounting principles.



Chartered Accountants, Licensed Public Accountants

Toronto, Canada
August 7, 2007

6650309 Canada Inc.
(subsequently renamed Lorus Therapeutics Inc.)

May 31, 2007

Assets

Cash	$	1

Shareholder's Equity

Capital stock (note 2)	$	1
Subsequent event (note 3)		

See accompanying notes to balance sheet.

On behalf of the Board:

Director

Director

Notes to the Balance Sheet

6650309 Canada Inc.
(subsequently renamed Lorus Therapeutics Inc.)
May 31, 2007

6650309 Canada Inc. (the "Company" or "New Lorus") was incorporated pursuant to the provisions of the Canada Business Corporation Act on November 1, 2006, and did not carry out any active business from the date of incorporation to May 31, 2007. From its incorporation to July 10, 2007, the Company was a wholly owned subsidiary of Lorus Therapeutics Inc. ("Old Lorus").

On July 10, 2007, Old Lorus and the Company completed a series of transactions (the "Arrangement") with an unrelated party, 6707157 Canada Inc. ("Investor") and its affiliate, Pinnacle International Lands, Inc. to reorganize Old Lorus' business (note 3).

1. Significant accounting policy:

The balance sheet of the Company has been prepared in accordance with Canadian generally accepted accounting principles.

2. Capital stock:

Authorized:		
Unlimited common shares		
Issued and outstanding:		
One common share	$	1

3. Subsequent event:

On July 10, 2007, Old Lorus and the Company completed a plan of arrangement and corporate reorganization with, among others, 6707157 Canada Inc. and Pinnacle International Lands, Inc. (the "Arrangement"). As part of the Arrangement, all of the assets and liabilities of Old Lorus (including all of the shares of its subsidiaries held by it), with the exception of certain future tax assets, were transferred, directly of indirectly, from Old Lorus to the Company. Securityholders in Old Lorus exchanged their securities in Old Lorus for equivalent securities in New Lorus (the "Exchange") and the board of directors and management of Old Lorus continued as the board of directors and management of New Lorus. New Lorus obtained substitutional listings of its common shares on both the Toronto Stock Exchange and the American Stock Exchange.

As part of the Arrangement, the Company changed its name to Lorus Therapeutics Inc. and will continue as a biopharmaceutical company, specializing in the research and development of pharmaceutical products and technologies for the management of cancer as a continuation of the business of Old Lorus.

The continuation of the research and development activities of New Lorus is dependent upon the Company's ability to successfully finance its cash requirements through a combination of equity financing and payments from strategic partners. The Company has no current sources of payments from strategic partners. The Company will need to repay or refinance the secured convertible debentures it has acquired as part of the Arrangement on their maturity in October 2009, should the holder not choose to convert the debentures into common shares. There can be no assurance that additional funding will be available at all or on acceptable terms to permit further clinical development of the Company's products or to repay the convertible debentures on maturity. If the Company is not able to raise additional funds, it may not be able to continue as a going concern and realize its assets and pay its liabilities as they fall due. The financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis were not appropriate for these financial statements, then adjustments would be necessary in the carrying value of the assets and liabilities, the reported revenues and expenses and the balance sheet classifications used.

Management believes that the Company's cash, marketable securities and the additional funds available upon the successful reorganization will be sufficient to execute the Company's current planned expenditures beyond the next 12 months.

In connection with the Arrangement and after the Exchange, the share capital of Old Lorus was reorganized into voting common shares and non-voting common shares and Investor acquired from New Lorus and Selling Shareholders (as defined below) approximately 41% of the voting common shares and all of the non-voting common shares of Old Lorus for a cash consideration of approximately $8.5 million on closing of the transaction less an escrowed amount of $600,000, subject to certain post-closing adjustments and before transaction costs. The remaining 59% of the voting common shares of Old Lorus were distributed to the shareholders of New Lorus who were not residents of the United States on a pro-rata basis. Shareholders of New Lorus who were residents of the United States received a nominal cash payment in lieu of their pro-rata share of voting common shares of Old Lorus. After completion of the Arrangement, New Lorus is not related to the former Lorus Therapeutics Inc., which was subsequently renamed 4325231 Canada Inc.

As a condition of the Arrangement, High Tech Beteiligungen GmbH & Co. KG and certain other shareholders of Old Lorus (the "Selling Shareholders") agreed to sell to Investor the voting common shares of Old Lorus to be received under the Arrangement at the same price per share as was paid to shareholders who are residents of the United States. The proceeds received by the Selling Shareholders was nominal.

Also as a condition of the Arrangement, the holder of Old Lorus' secured convertible debenture agreed to vote in favour of the transaction subject to the repurchase by New Lorus of its outstanding three million common share purchase warrants at a purchase price of $252,000 upon closing of the Arrangement.

Following the Arrangement, New Lorus and its subsidiaries have approximately $7.0 million of unrecognized future tax benefits resulting from non-capital losses carried forward, and scientific research and experimental development expenditures. In light of the uncertainty regarding the Company's ability to generate taxable income in the future, management is of the opinion that it is more likely than not that these future tax assets will not be realized in the foreseeable future and hence, a full valuation allowance will be recorded against these future tax assets.

In addition, under the Arrangement, New Lorus and its subsidiaries indemnified Old Lorus and its directors, officers and employees against any and all liabilities, losses, costs, expenses, claims and damages, other than for certain tax liabilities related to the operations carried out by Old Lorus prior to and by New Lorus subsequent to the transfer of assets, liabilities and operations to New Lorus. Management has not yet determined the fair value of this obligation.

The business of Old Lorus will be accounted for on a continuity of interest basis and accordingly, the consolidated financial statements of New Lorus will reflect the financial position, results of operations and cash flows as if New Lorus has always carried on the business formerly carried on by Old Lorus.

The summarized consolidated financial statements of Old Lorus as at May 31, 2007 and for the year then ended are as follows:

Balance sheet		
Assets:		
Current	$	9,005
Non-current		6,470
	$	15,475
Liabilities:		
Current	$	2,777
Secured convertible debentures		11,937
		14,714
Shareholders' equity		761
	$	15,475

Statement of operations		
Revenue	$	107
Operating expenses:		
Research and development		3,384
General and administrative		3,848
Other		921
		8,153
Interest and accretion expense		1,985
Amortization of deferred financing charges		110
Interest income		(503)
Loss for the year	$	(9,638)

We have audited the consolidated balance sheets of Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.) as at May 31, 2007 and 2006 and the consolidated statements of operations and deficit and cash flows for each of the years in the three-year period ended May 31, 2007 and for the period from inception on September 5, 1986 to May 31, 2007. 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 May 31, 2007 and 2006 and the results of its operations and its cash flows for each of the years in the three-year period ended May 31, 2007 and for the period from inception on September 5, 1986 to May 31, 2007 in accordance with Canadian generally accepted accounting principles.

We did not audit the consolidated financial statements of Lorus Therapeutics Inc. for the period from inception on September 5, 1986 to May 31, 1994. Those consolidated financial statements were audited by other auditors who issued a report without reservation on July 8, 1994.

KPMG LLP

Chartered Accountants, Licensed Public Accountants

Toronto, Canada
August 7, 2007

Supplemental Financial Information

Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.)

Consolidated Balance Sheets

(Expressed in thousands of Canadian dollars)

May 31	2007	2006
Assets		
Current assets:		
Cash and cash equivalents (note 11)	$ 1,405	$ 2,692
Marketable securities and other investments (note 4)	7,265	5,627
Prepaid expenses and other assets	335	515
	9,005	8,834
Marketable securities and other investments (note 4)	3,728	–
Fixed assets (note 5)	503	885
Deferred financing charges	371	481
Deferred arrangement costs (note 16)	1,262	–
Goodwill	606	606
Acquired patents and licenses (note 6)	–	655
	$ 15,475	$ 11,461
Liabilities and Shareholders' Equity (Deficiency)		
Current liabilities:		
Accounts payable	$ 1,104	$ 555
Liability to repurchase warrants (note 7)	252	–
Accrued liabilities	1,421	2,460
	2,777	3,015
Secured convertible debentures (note 12)	11,937	11,002
Shareholders' equity (deficiency):		
Share capital (note 7):		
Common shares	157,714	145,001
Equity portion of secured convertible debentures	3,814	3,814
Stock options	4,898	4,525
Contributed surplus	8,525	7,665
Warrants	–	991
Deficit accumulated during development stage	(174,190)	(164,552)
	761	(2,556)
Basis of presentation (note 1)		
Subsequent events (note 16)		
	$ 15,475	$ 11,461

See accompanying notes to consolidated financial statements.

On behalf of the Board:

Director

Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.)

Consolidated Statements of Operations and Deficit

(Expressed in thousands of Canadian dollars, except for per common share data)

	Years ended May 31			Period from inception September 5, 1986 to May 31, 2007
	2007	2006	2005	
Revenue	$ 107	$ 26	$ 6	$ 813
Expenses:				
Cost of sales	16	3	1	103
Research and development (note 10)	3,384	10,237	14,394	113,859
General and administrative	3,848	4,334	5,348	51,323
Stock-based compensation (note 8)	503	1,205	1,475	7,253
Depreciation and amortization of fixed assets	402	771	564	9,225
	8,153	16,550	21,782	181,763
	(8,046)	(16,524)	(21,776)	(180,950)
Other expenses (income):				
Interest on convertible debentures	1,050	882	300	2,232
Accretion in carrying value of convertible debentures (note 12)	935	790	426	2,151
Amortization of deferred financing charges	110	87	84	281
Interest	(503)	(374)	(524)	(11,424)
	1,592	1,385	286	(6,760)
Loss for the period	(9,638)	(17,909)	(22,062)	(174,190)
Deficit, beginning of period	(164,552)	(146,643)	(124,581)	–
Deficit, end of period	$ (174,190)	$ (164,552)	$ (146,643)	$ (174,190)
Basic and diluted loss per common share	$ (0.05)	$ (0.10)	$ (0.13)	
Weighted average number of common shares outstanding used in the calculation of basic and diluted loss per share (in thousands)	204,860	173,523	172,112	

See accompanying notes to consolidated financial statements.

Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.)

Consolidated Statements of Cash Flows

(Expressed in thousands of Canadian dollars)

	Years ended May 31			Period from inception September 5, 1986 to May 31, 2007
	2007	2006	2005	
Cash flows from operating activities:				
Loss for the period	$ (9,638)	$ (17,909)	$ (22,062)	$ (174,190)
Items not involving cash:				
Stock-based compensation	503	1,205	1,475	7,253
Interest on convertible debentures	1,050	882	300	2,232
Accretion in carrying value of convertible debentures	935	790	426	2,151
Amortization of deferred financing charges	110	87	84	281
Depreciation, amortization and write-down of fixed assets and acquired patents and licenses	1,057	2,342	2,260	21,786
Other	–	–	(38)	707
Change in non-cash operating working capital (note 11)	(310)	(462)	(1,166)	1,282
Cash used in operating activities	(6,293)	(13,065)	(18,721)	(138,498)
Cash flows from financing activities:				
Issuance of debentures, net of issuance costs	–	–	12,948	12,948
Issuance of warrants	–	–	991	37,405
Issuance of common shares, net of issuance costs (note 7)	11,654	–	112	109,025
Additions to deferred financing/arrangement charges	(1,262)	–	–	(1,507)
Cash provided by financing activities	10,392	–	14,051	157,871
Cash flows investing activities:				
Maturity (purchase) of marketable securities and other investments, net	(5,366)	13,056	6,974	(10,993)
Business acquisition, net of cash received	–	–	–	(539)
Acquired patents and licenses	–	–	(715)	
Additions to fixed assets	(20)	(75)	(599)	(6,069)
Proceeds on sale of fixed assets	–	–	–	348
Cash provided by (used in) investing activities	(5,386)	12,981	6,375	(17,968)
Increase (decrease) in cash and cash equivalents	(1,287)	(84)	1,705	1,405
Cash and cash equivalents, beginning of period	2,692	2,776	1,071	–
Cash and cash equivalents, end of period	$ 1,405	$ 2,692	$ 2,776	$ 1,405

Supplemental cash flow information (note 11)

See accompanying notes to consolidated financial statements.

Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.)
(Tabular amounts thousands of Canadian dollars, except per share amounts)
Years ended May 31, 2007, 2006 and 2005

1. Basis of presentation:

Lorus Therapeutics Inc. (subsequently renamed 4325231 Canada Inc.) ("Lorus" or the "Company") is a biopharmaceutical company specializing in the research and development of pharmaceutical products and technologies for the management of cancer. With products in various stages of evaluation, from preclinical through to Phase II trials, Lorus develops therapeutics that seek to manage cancer with efficacious low-toxicity compounds that improve patients' quality of life.

On November 1, 2006, the Company incorporated a wholly owned subsidiary, 6650309 Canada Inc. ("New Lorus"). On July 10, 2007, the Company completed a plan of arrangement and corporate reorganization with, among others, 6707157 Canada Inc. and Pinnacle International Lands, Inc., (the "Arrangement") which, among other things, resulted in New Lorus receiving cash of approximately $8.5 million, subject to a $600 thousand holdback and post-closing adjustment and before costs of the transaction. As part of the Arrangement, all of the assets and liabilities of the Company (including the shares of its subsidiaries held by it), with the exception of certain future tax assets, were transferred, directly or indirectly, from the Company to New Lorus. Securityholders in the Company exchanged their securities in the Company for equivalent securities of New Lorus. Also as part of the Arrangement, the Company changed its name from Lorus Therapeutics Inc. to 4325231 Canada Inc. and New Lorus changed its name from 6650309 Canada Inc. to Lorus Therapeutics Inc. and carried on the business formerly carried on by the Company (note 16).

The ability of 4325231 Canada Inc. to continue as a going concern is dependent upon the nature of the operations management pursues and the Company's ability to obtain financing to fund such operations. The outcome of these matters cannot be predicted with certainty at this time.

In relation to the net assets of and operations that were transferred on July 10, 2007, the Company has not earned substantial revenue from its drug candidates and is, therefore, considered to be a development stage company. The continuation of the Company's research and development activities is dependent upon the Company's ability to successfully finance its cash requirements through a combination of equity financing and payments from strategic partners. The Company has no current sources of payments from strategic partners. In addition, the Company will need to repay or refinance the secured convertible debentures on their maturity in October 2009 should the holder not choose to convert the debentures into common shares. There can be no assurance that additional funding will be available at all or on acceptable terms to permit further clinical development of the Company's products or to repay the convertible debentures on maturity. If the Company is not able to raise additional funds, it may not be able to continue as a going concern and realize its assets and pay its liabilities as they fall due. The consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis were not appropriate for these consolidated financial statements, then adjustments would be necessary in the carrying value of the assets and liabilities, the reported revenue and expenses and the balance sheet classifications used.

Management believes that the Company's current level of cash, marketable securities and the additional funds available upon the successful reorganization as described in note 16 will be sufficient to execute the Company's current planned expenditures beyond the next 12 months in New Lorus.

2. Significant accounting policies:

(a) Principles of consolidation:

The Consolidated Financial Statements include the accounts of Lorus, its 80% owned subsidiary, NuChem Pharmaceuticals Inc. ("NuChem"), and its wholly owned subsidiaries, GeneSense Technologies Inc. ("GeneSense") and 6650309 Canada Inc., which are all located in Canada. The results of operations for acquisitions are included in these Consolidated Financial Statements from the date of acquisition. All significant intercompany balances and transactions have been eliminated on consolidation.

The Consolidated Financial Statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP").

(b) Revenue recognition:

Revenue includes product sales, service, license and royalty revenue.

The Company recognizes revenue from product sales and provision of services when persuasive evidence of an arrangement exists, delivery has occurred, the Company's price to the customer is fixed or determinable and collectibility is reasonably assured. The Company allows customers to return product within a specified period of time before and after its expiration date. Provisions for these returns are estimated based on historical return and exchange levels, and third-party data with respect to inventory levels in the Company's distribution channels.

License fees are comprised of initial fees and milestone payments derived from a worldwide exclusive license agreement. Non-refundable license fees are recognized when the Company has no further involvement or obligation to perform under the arrangement, the fee is fixed and determinable and collection of the amount is deemed probable. Future non-refundable milestone payments receivable upon the achievement of third-party performance are recognized upon the achievement of specified milestones when the milestone payment is substantive in nature, achievement of the milestone was not reasonably assured at the inception of the agreement and the Company has no further significant involvement or obligation to perform under the arrangement.

The Company earned royalties from its distributor during the year ended May 31, 2005. Royalties from the distribution agreement are recognized when the amounts are reasonably determinable and collection is reasonably assured. In 2006, the distribution agreement was terminated and no royalties were earned during the years ended May 31, 2007 and 2006.

(c) Cash and cash equivalents:

The Company considers unrestricted cash on hand and in banks, term deposits and guaranteed investment certificates with original maturities of three months or less as cash and cash equivalents.

(d) Marketable securities and other investments:

Lorus invests in high quality fixed income government and corporate instruments with low credit risk.

Short-term investments, which consist of fixed income securities with a maturity of more than three months but less than one year, are recorded at their accreted value as they are held-to-maturity instruments. Long-term investments consist primarily of fixed income securities with a maturity of more than one year and are recorded at their accreted value as they are held-to-maturity instruments. All investments held at year end approximate fair value and are denominated in Canadian dollars.

(e) Fixed assets:

Fixed assets are recorded at cost less accumulated depreciation and amortization. The Company records depreciation and amortization at rates which are expected to charge operations with the cost of the assets over their estimated useful lives on a straight-line basis as follows:

Furniture and equipment	Over 3 to 5 years
Leasehold improvements	Over the lease term

(f) Research and development:

Research costs are charged to expense as incurred. Development costs, including the cost of drugs for use in clinical trials, are expensed as incurred unless they meet the criteria under Canadian GAAP for deferral and amortization. No development costs have been deferred to date.

(g) Goodwill and acquired patents and licenses:

Intangible assets with finite lives acquired in a business combination or other transaction are amortized over their estimated useful lives.

Goodwill represents the excess of the purchase price over the fair value of net identifiable assets acquired in the GeneSense business combination. Goodwill acquired in a business combination is tested for impairment on an annual basis and at any other time if an event occurs or circumstances change that would indicate that impairment may exist. When the carrying value of a reporting unit's goodwill exceeds its fair value, an impairment loss is recognized in an amount equal to the excess.

The Company capitalized the cost of acquired patent and license assets on the acquisitions of GeneSense and the NuChem compounds. The nature of this asset is such that it was categorized as an intangible asset with a finite life. These costs have now been fully amortized.

The Company has identified no impairment relating to goodwill and intangible assets for 2007 and 2006.

(h) Impairment of long-lived assets:

The Company periodically reviews the useful lives and the carrying values of its long-lived assets. The Company reviews for impairment in long-lived assets whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. If the sum of the undiscounted expected future cash flows expected to result from the use and eventual disposition of an asset is less than its carrying amount, it is considered to be impaired. An impairment loss is measured at the amount by which the carrying amount of the asset exceeds its fair value, which is estimated as the expected future cash flows discounted at a rate proportionate with the risks associated with the recovery of the asset.

(i) Stock-based compensation:

The Company has a stock-based compensation plan described in note 8. Prior to June 1, 2004, stock-based awards were accounted for using the intrinsic method with the exception of options with contingent vesting criteria for which the settlement method was used. On June 1, 2004, the Company adopted the fair value method of accounting for stock-based awards to employees, officers and directors granted or modified after June 1, 2004. This method requires the Company to expense, over the vesting period, the fair value of all employee stock-based awards granted or modified since June 1, 2002. Stock options and warrants awarded to non-employees are accounted for using the fair value method and expensed as the service or product is received. Consideration paid on the exercise of stock options and warrants is credited to capital stock. The fair value of performance-based options is recognized over the estimated period to achievement of performance conditions. Fair value is determined using the Black-Scholes option pricing model.

The Company has a deferred share unit plan that provides directors the option of receiving payment for their services in the form of share units rather than common shares or cash. Share units entitle the director to elect to receive, on termination of his or her services with the Company, an equivalent number of common shares, or the cash equivalent of the market value of the common shares at that future date. Lorus records an expense and a liability equal to the market value of the shares issued. The accumulated liability is adjusted for market fluctuations on a quarterly basis.

Shares issued under the alternate compensation plans ("ACP") are accounted for using the fair value of the common shares on the day they are granted.

(j) Investment tax credits:

The Company is entitled to Canadian federal and provincial investment tax credits, which are earned as a percentage of eligible research and development expenditures incurred in each taxation year. Investment tax credits are accounted for as a reduction of the related expenditure for items of a current nature and a reduction of the related asset cost for items of a long-term nature, provided that the Company has reasonable assurance that the tax credits will be realized.

(k) Income taxes:

Income taxes are accounted for using the asset and liability method. Under this method, future tax assets and liabilities are recorded for the future tax consequences attributable to differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases, and operating loss and research and development expenditure carryforwards. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability is settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the year that enactment or substantive enactment occurs. A valuation allowance is recorded for the portion of the future tax assets where the realization of any value is uncertain for which management has deemed to be 100% of the assets available.

(l) Loss per share:

Basic loss per common share is calculated by dividing the loss for the year by the weighted average number of common shares outstanding during the year. Diluted loss per common share is calculated by dividing the loss for the year by the sum of the weighted average number of common shares outstanding and the dilutive common equivalent shares outstanding during the year. Common equivalent shares consist of the shares issuable upon exercise of stock options, warrants and conversion of the convertible debentures calculated using the treasury stock method. Common equivalent shares are not included in the calculation of the weighted average number of shares outstanding for diluted loss per common share when the effect would be anti-dilutive.

(m) Deferred financing charges:

Deferred financing charges, comprised primarily of legal costs, represent costs related to the issuance of the Company's convertible debentures. Deferred financing charges are amortized using the effective interest rate method over the five-year term of the convertible debentures.

(n) Segmented information:

The Company is organized and operates as one operating segment, the research, development, and commercialization of pharmaceuticals. Substantially all of the Company's identifiable assets as at May 31, 2007 and 2006 are located in Canada.

(o) Foreign currency translation:

Foreign currency transactions are translated into Canadian dollars at rates prevailing on the transaction dates. Monetary assets and liabilities are translated into Canadian dollars at the rates in effect on the balance sheet dates. Gains or losses resulting from these transactions are accounted for in the loss for the period and are not significant.

(p) Use of estimates:

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the year. Actual results may differ from those estimates. Significant estimates include the valuation of the convertible debentures, the fair value of stock options granted and warrants issued and the useful lives of fixed and intangible assets.

(q) Recent Canadian accounting pronouncements not yet adopted:

(i) Comprehensive income and equity:

In January 2005, The Canadian Institute of Chartered Accountants ("CICA)" released Handbook Section 1530, *Comprehensive Income*, and Section 3251, *Equity*. Section 1530 establishes standards for reporting comprehensive income. The section does not address issues of recognition or measurement for comprehensive income and its components. Section 3251 establishes standards for the presentation of equity and changes in equity during the reporting period. The requirements in Section 3251 are in addition to Section 1530.

(ii) Financial instruments – recognition and measurement:

Section 3855, *Financial Instruments – Recognition and Measurement*, establishes standards for the recognition and measurement of all financial instruments, provides a characteristics-based definition of a derivative instrument, provides criteria to be used to determine when a financial instrument should be recognized, and provides criteria to be used to determine when a financial liability is considered to be extinguished.

(iii) Hedges:

Section 3865, *Hedges*, establishes standards for when and how hedge accounting may be applied. Hedge accounting is optional.

These three Sections are effective for fiscal years beginning on or after October 1, 2006. The Company has not yet determined the impact, if any, of the adoption of these standards on its results from operations or financial position, which became effective June 1, 2007.

(iv) Financial instruments – disclosure and presentation:

Section 3861, *Financial Instruments – Disclosure and Presentation,* discusses the presentation and disclosure of these financial instruments. In December 2006, the CICA issued Section 3862, *Financial Instruments – Disclosure*, and Section 3863, *Financial Instruments – Presentation*, to replace Section 3861. These new Sections are effective for interim and annual financial statements with fiscal years beginning on or after October 1, 2007, but may be adopted in place of Section 3861 before that date.

3. Changes in accounting policies:

No new accounting policies were adopted during the year ended May 31, 2007. The following accounting policies were adopted during the year ended May 31, 2006. For accounting policies adopted during the year ended May 31, 2005, refer to note 2 under the heading "Stock-based compensation".

(a) Variable interest entities:

Effective June 1, 2005, the Company adopted the recommendations of CICA Handbook Accounting Guideline 15 ("AcG-15"), Consolidation of Variable Interest Entities, effective for fiscal years beginning on or after November 1, 2004. Variable interest entities ("VIEs") refer to those entities that are subject to control on a basis other than ownership of voting interests. AcG-15 provides guidance for identifying VIEs and criteria for determining which entity, if any, should consolidate them. The adoption of AcG-15 did not have an effect on the financial position, results of operations or cash flows in the current period or the prior period presented.

(b) Financial instruments – disclosure and presentation:

Effective June 1, 2005, the Company adopted the amended recommendations of CICA Handbook Section 3860, *Financial Instruments – Disclosure and Presentation*, effective for fiscal years beginning on or after November 1, 2004. Section 3860 requires that certain obligations that may be settled at the issuer's option in cash or the equivalent value by a variable number of the issuer's own equity instruments be presented as a liability. The Company has determined that there is no impact on the consolidated financial statements resulting from the adoption of the amendments to Section 3860 either in the current period or the prior period presented.

(c) Non-monetary transactions:

In June 2005, the CICA released Handbook Section 3831, *Non-monetary Transactions*, effective for all non-monetary transactions initiated in periods beginning on or after January 1, 2006. This standard requires all non-monetary transactions to be measured at fair value unless they meet one of four very specific criteria. Commercial substance replaces culmination of the earnings process as the test for fair value measurement. A transaction has commercial substance if it causes an identifiable and measurable change in the economic circumstances of the entity. Commercial substance is a function of the cash flows expected by the reporting entity. The Company has not entered into any non-monetary transactions and, as such, this section is not applicable.

4. Marketable securities and other investments:

2007	Less than one year maturities	Greater than one year maturities	Total	Yield to maturity
Fixed income government investments	$ 1,549	$ –	$ 1,549	3.91%
Corporate instruments	5,716	3,728	9,444	3.89–4.11%
	$ 7,265	$ 3,728	$ 10,993	

2006	Less than one year maturities	Greater than one year maturities	Total	Yield to maturity
Fixed income government investments	$ 2,838	$ –	$ 2,838	3.55 – 3.64%
Corporate instruments	2,789	–	2,789	3.46 – 3.87%
	$ 5,627	$ –	$ 5,627	

At May 31, 2007 and 2006, the carrying values of short-term investments approximate their quoted market values. Short-term investments held at May 31, 2007 have varying maturities from one to ten months (2006 – one to six months). Long-term investments have maturities varying from one to five years (2006 – none greater than one year). Long-term investments are valued at carrying value that, by virtue of the nature of the investments, primarily interest bearing instruments, approximates their quoted market value.

5. Fixed assets:

2007	Cost	Accumulated depreciation and amortization	Net book value
Furniture and equipment	$ 2,670	$ 2,387	$ 283
Leasehold improvements	908	688	220
	$ 3,578	$ 3,075	$ 503

2006	Cost	Accumulated depreciation and amortization	Net book value
Furniture and equipment	$ 2,650	$ 2,136	$ 514
Leasehold improvements	908	537	371
	$ 3,558	$ 2,673	$ 885

During the year ended May 31, 2006, a write-down of $250 thousand was taken on certain furniture and equipment whose carrying value was deemed to be unrecoverable and in excess of the estimated fair value of the residual value of the underlying assets. The impairment charge was reported in the consolidated statements of operations and deficit in depreciation and amortization.

6. Acquired patents and licenses:

	2007	2006
Cost	$ 12,228	$ 12,228
Accumulated amortization	12,228	(11,573)
	$ –	$ 655

Amortization of $655 thousand (2006 – $1.6 million; 2005 – $1.7 million) has been included in the research and development expense reported in the consolidated statements of operations and deficit.

7. Share capital:

(a) Continuity of common shares and warrants:

	Common shares		Warrants	
	Number	Amount	Number	Amount
Balance, May 31, 2004	171,794	$ 143,670	13,110	$ 4,325
Interest payment (note 12)	421	300	–	–
Issuance under ACP (d)	50	37	–	–
Exercise of stock options	276	112	–	–
Convertible debentures (note 12)	–	–	3,000	991
Warrants expired unexercised	–	–	(13,110)	(4,325)
Balance, May 31, 2005	172,541	144,119	3,000	991
Interest payment (note 12)	2,153	882	–	–
Balance at May 31, 2006	174,694	145,001	3,000	991
Share issuance	33,800	11,641	–	–
Interest payments (note 12)	3,726	1,050	–	–
Exercise of stock options	46	22	–	–
Repurchase of warrants (g)	–	–	(3,000)	(991)
Balance, May 31, 2007	212,266	$ 157,714	–	$ –

(b) Contributed surplus:

	2007	2006	2005
Balance, beginning of year	$ 7,665	$ 6,733	$ 1,003
Forfeiture of stock options	121	932	–
Expiry of warrants	–	–	4,325
Expiry of compensation options	–	–	1,405
Repurchase of warrants (g)	739	–	–
Balance, end of year	$ 8,525	$ 7,665	$ 6,733

(c) Continuity of stock options

	2007	2006	2005
Balance, beginning of the year	$ 4,525	$ 4,252	$ 2,777
Stock option expense	494	1,205	1,475
Forfeiture of stock options	(121)	(932)	–
Balance, end of year	$ 4,898	$ 4,525	$ 4,252

(d) Alternate compensation plans:

In 2000, the Company established an ACP for directors and officers, which allows the Company, in certain circumstances, to issue common shares to pay directors' fees or performance bonuses of officers in lieu of cash. The number of common shares reserved for issuance under this plan is 2,500,000. Since inception, 121,000 common shares have been issued under this plan. This plan was terminated in September 2005; therefore, for the year ended May 31, 2007, no common shares were issued under this plan (2006 – nil; 2005 – 50,000).

The Company also established a deferred share unit plan that provides directors the option of receiving payment for their services in the form of share units rather than common shares or cash. Share units entitle the director to elect to receive, on termination of their services to the Company, an equivalent number of common shares, or the cash equivalent of the market value of the common shares at that future date. The share units are granted based on the market value of the common shares on the date of issue. During the year ended May 31, 2007, nil deferred share units were issued (2006 – 168,581; 2005 – 99,708), with a cash value of nil (2006 – $64 thousand; 2005 – $71 thousand) being recorded in accrued liabilities.

(e) Share issuance:

On July 13, 2006, the Company entered into an agreement with HighTech Beteiligungen GmbH & Co. KG ("HighTech") to issue 28,800,000 common shares at $0.36 per share for gross proceeds of $10.4 million. The cost of issuance amounted to $450 thousand. The subscription price represented a premium of 7.5% over the closing price of the common shares on the Toronto Stock Exchange on July 13, 2006. The closing of the transaction is subject to certain conditions, including the approval of the Toronto Stock Exchange ("TSX") and the American Stock Exchange ("AMEX") and the filing and clearance of a prospectus in Ontario qualifying the issuance of the common shares. The transaction closed on August 31, 2006. In connection with the transaction, HighTech received demand registration rights that will enable HighTech to request the registration or qualification of the common shares for resale in the United States and Canada, subject to certain restrictions. These demand registration rights expire on June 30, 2012. In addition, HighTech received the right to nominate one nominee to the Board of Directors

of Lorus or, if it does not have a nominee, it will have the right to appoint an observer to the board. Upon completion of the transaction, HighTech held approximately 14% of the issued and outstanding common shares of Lorus.

On July 24, 2006, Lorus entered into an agreement with Technifund Inc. to issue, on a private placement basis, 5,000,000 common shares at $0.36 per share for gross proceeds of $1.8 million. The cost of issuance amounted to $78 thousand. The transaction closed on September 1, 2006.

(f) Employee share purchase plan:

The Company's employee share purchase plan ("ESPP") was established on January 1, 2005. The purpose of the ESPP is to assist the Company in retaining the services of its employees, to secure and retain the services of new employees and to provide incentives for such persons to exert maximum efforts for the success of the Company. The ESPP provides a means by which employees of the Company and its affiliates may purchase common shares of the Company at a discount through accumulated payroll deductions. Generally, each offering is of three months' duration with purchases occurring every month. Participants may authorize payroll deductions of up to 15% of their base compensation for the purchase of common shares under the ESPP. For the year ended May 31, 2007, 69,000 (2006 – 293,000; 2005 – 106,000) common shares have been purchased under the ESPP, and Lorus has recognized an expense of $5 thousand (2006 – $46 thousand; 2005 – $16 thousand) related to this plan in these consolidated financial statements.

(g) Repurchase of warrants:

In May 2007, the Company entered into an agreement with the holder of Lorus $15.0 million secured convertible debenture to the repurchase by New Lorus upon close of the Arrangement of its outstanding 3,000,000 common share purchase warrants at a purchase price of $252 thousand. As discussed in the note 16, the Arrangement closed on July 10, 2007 and, therefore, the conditions were met such that the repurchase amount is set up as a liability and the difference between the carrying value of the warrants and the amount paid has been credited to contributed surplus.

8. Stock-based compensation:

Stock option plan:

Under the Company's stock option plan, options may be granted to directors, officers, employees and consultants of the Company to purchase up to a maximum of 15% of the total number of outstanding common shares currently estimated at 31,800,000 options. Options are granted at the fair market value of the common shares on the date immediately preceding the date of the grant. Options vest at various rates (immediate to three years) and have a term of 10 years. Stock option transactions for the three years ended May 31, 2007 are summarized as follows:

	2007		2006		2005	
	Options (In thousands)	Weighted average exercise price	Options (In thousands)	Weighted average exercise price	Options (In thousands)	Weighted average exercise price
Outstanding, beginning of year	10,300	$ 0.70	8,035	$ 0.96	6,372	$ 1.05
Granted	5,318	0.30	6,721	0.58	3,173	0.77
Exercised	(46)	0.30	–	–	(276)	0.40
Forfeited	(2,584)	0.44	(4,456)	0.83	(1,234)	1.05
Outstanding, end of year	12,988	$ 0.59	10,300	$ 0.70	8,035	$ 0.96
Exercisable, end of year	9,796	$ 0.68	6,714	$ 0.79	4,728	$ 1.04

The following table summarizes information about stock options outstanding at May 31, 2007:

	Options outstanding			Options exercisable	
Range of exercise prices	Options (In thousands)	Weighted average remaining contractual life (years)	Weighted average exercise price	Options (In thousands)	Weighted average exercise price
$0.26 to $0.49	$ 7,353	8.13	$ 0.30	$ 4,285	$ 0.29
$0.50 to $0.99	3,766	6.31	0.75	3,642	0.75
$1.00 to $1.99	1,581	5.90	1.23	1,581	1.23
$2.00 to $2.50	288	3.38	2.46	288	2.46
	$ 12,988	7.23	$ 0.59	$ 9,796	$ 0.68

For the year ended May 31, 2007, stock-based compensation expense of $503 thousand (2006 – $1.2 million; 2005 – $1.5 million) was recognized, representing the amortization applicable to the current period of the estimated fair value of options granted since June 1, 2002.

During the year ended May 31, 2006, employees of the Company (excluding directors and officers) were given the opportunity to choose between keeping 100% of their existing options at the existing exercise price or forfeiting 50% of the options held in exchange for having the remaining 50% of the exercise price of the options re-priced to $0.30 per share. Employees holding 2,290,000 stock options opted for re-pricing their options, resulting in the amendment of the exercise price of 1,145,000 stock options and the forfeiture of 1,145,000 stock options. This re-pricing resulted in additional compensation expense of $76 thousand, representing the incremental value conveyed to holders of the options as a result of reducing the exercise price, of which $52 thousand has been included in the stock-based compensation expense during the year ended May 31, 2006. The additional compensation expense of $24 thousand will be recognized as the amended options vest. This increased expense is offset by $113 thousand representing amounts previously expensed on unvested stock options due to the forfeiture of 1,145,000 stock options, which was reversed from the stock-based compensation expense for the year ended May 31, 2006.

For the year ended May 31, 2005, additional stock-based compensation expense of $208 thousand was recorded due to the shareholder approved amendment of the 1993 Stock Option Plan to extend the life of options from 5 years to 10 years. This additional expense represented the incremental value conveyed to holders of the options as a result of extending the life of the options.

For the year ended May 31, 2007, stock option expense of $503 thousand (2006 – $1.2 million; 2005 – $1.5 million) comprised $216 thousand (2006 – $300 thousand; 2005 – $445 thousand) related to research and development and $287 thousand (2006 – $900 thousand; 2005 – $1.0 million) related to general and administrative.

The following assumptions were used in the Black-Scholes option pricing model to determine the fair value of stock options granted during the year:

	2007	2006	2005
Risk-free interest rate	4.50%	2.25%–4.00%	2.25%–3.00%
Expected volatility	75%–80%	70%–81%	70%–90%
Expected life of options	5 years	2.5–5 years	1–5 years
Weighted average fair value of options granted or modified during the year	$ 0.20	$ 0.33	$ 0.54

The Company has assumed no forfeiture rate as adjustments for actual forfeitures are made in the year they occur.

9. Income taxes:

Income tax recoveries attributable to losses from operations differ from the amounts computed by applying the combined Canadian federal and provincial income tax rates to pretax income from operations primarily as a result of the provision of a valuation allowance on net future income tax benefits.

Significant components of the Company's future tax assets are as follows:

	2007	2006
Non-capital loss carryforwards	$ 24,459	$ 25,174
Research and development expenditures	20,156	22,089
Book over tax depreciation	1,904	1,995
Other	309	738
Future tax assets	46,828	49,996
Valuation allowance	(46,828)	(49,996)
	$ –	$ –

In assessing the realizable benefit from future tax assets, management considers whether it is more likely than not that some portion or all of the future tax assets will not be realized. The ultimate realization of future tax assets is dependent on the generation of future taxable income during the years in which those temporary differences become deductible. Management considers projected future taxable income, uncertainties related to the industry in which the Company operates and tax planning strategies in making this assessment. Due to the Company's stage of development and operations, and uncertainties related to the industry in which the Company operates, the tax benefit of the above amounts has been completely offset by a valuation allowance.

The Company has undeducted research and development expenditures, totalling $62.5 million for federal purposes and $59.2 million for provincial purposes and these can be carried forward indefinitely. In addition, the Company has non-capital loss carryforwards of $73.6 million for federal purposes and $74.8 million for provincial purposes. To the extent that the non-capital loss carryforwards are not used, they expire as follows:

2008	$ 4,985
2009	6,658
2010	8,660
2011	1,131
2014	22,029
2015	13,340
2026	9,712
2027	7,126
	$ 73,641

Income tax rate reconciliation:

	2007	2006	2005
Recovery of income taxes based on statutory rates	$ (3,481)	$ (6,469)	$ (7,971)
Expiry of losses	1,311	1,252	780
Change in valuation allowance	(3,168)	3,861	6,124
Non-deductible accretion and stock-based compensation expense	519	721	687
Change in enacted tax rates	4,437	–	–
Other	382	635	380
	$ –	$ –	$ –

10. Research and development programs:

The Company's cancer drug research and development programs focus primarily on the following technology platforms:

(a) Immunotherapy:

This clinical approach stimulates the body's natural defenses against cancer. The Company's lead immunotherapeutic drug, Virulizin®, completed a global Phase III clinical trial for the treatment of pancreatic cancer during 2005.

(b) Antisense:

Antisense drugs are genetic molecules that inhibit the production of disease-causing proteins. GTI-2040 and GTI-2501, the Company's lead antisense drugs, have shown preclinical anticancer activity across a broad range of cancers and are currently in various Phase II trials.

(c) Small molecules:

Anticancer activity was discovered with an antifungal agent, Clotrimazole ("CLT"). Based on the structural feature found to be responsible for the anticancer effect of CLT, chemical analogues of CLT have been designed and tested. Our library of CLT analogues has been licensed to Cyclacel Limited under a licensing agreement.

Lorus scientists have discovered novel low molecular weight compounds with anticancer and anti-bacterial activity in preclinical investigations. Of particular interest to the Company are compounds that inhibit the growth of human tumor cell lines, including hepatocellular carcinoma, pancreatic carcinoma, ovarian carcinoma, breast adenocarcinoma and metastatic melanoma.

In addition to the above, Lorus has a number of other technologies under preclinical development, including a tumor suppressor or gene therapy approach to inhibiting the growth of tumors.

	Years ended May 31			Period from inception September 5, 1986
	2007	2006	2005	to May 31, 2007
Immunotherapy:				
Expensed	$ 87	$ 6,202	$ 11,891	$ 75,046
Acquired	–	–	–	–
Antisense:				
Expensed	1,676	2,550	2,384	31,485
Acquired	–	–	–	11,000
Small molecules:				
Expensed	1,621	1,485	119	7,328
Acquired	–	–	–	1,228
Total expensed	$ 3,384	$ 10,237	$ 14,394	$ 113,859
Total acquired	$ –	$ –	$ –	$ 12,228

Amortization of the acquired patents and licenses is included in the 'Expensed' line of the table.

11. Supplemental cash flow information:

Cash and cash equivalents consists of:

	2007	2006
Cash on hand	$ 495	$ 74
Term deposits and guaranteed investment certificates	910	2,618
	$ 1,405	$ 2,692

Change in non-cash operating working capital is summarized as follows:

	Years ended May 31			Period from inception September 5, 1986
	2007	2006	2005	to May 31, 2007
Prepaid expenses and other assets	$ 180	$ 611	$ 571	$ 241
Accounts payable	549	(514)	(1,360)	(140)
Accrued liabilities	(1,039)	(559)	(377)	1,181
	$ (310)	$ (462)	$ (1,166)	$ 1,282

During the year ended May 31, 2007, the Company received interest of $767 thousand (2006 – $627 thousand; 2005 – $679 thousand).

Supplementary disclosure relating to non-cash financing activities consists of $252 thousand related to the liability to repurchase warrants.

12. Convertible debentures:

On October 6, 2004, the Company entered into a Subscription Agreement (the "Agreement") to issue an aggregate of $15.0 million of secured convertible debentures (the "debentures"). The debentures are secured by a first charge over all of the assets of the Company.

The Company received $4.4 million on October 6, 2004 (representing a $5.0 million debenture less an investor fee representing 4% of the $15.0 million to be received under the Agreement), and $5.0 million on each of January 14 and April 15, 2005. All debentures issued under this Agreement are due on October 6, 2009 and are subject to interest payable monthly at a rate of prime plus 1% until such time as the Company's share price reaches $1.75 for 60 consecutive trading days, at which time, interest will no longer be charged. Interest is payable in common shares of Lorus until Lorus' shares trade at a price of $1.00 or more after which interest will be payable in cash or common shares at the option of the debenture holder. Common shares issued in payment of interest will be issued at a price equal to the weighted average trading price of such shares for the 10 trading days immediately preceding their issue in respect of each interest payment. For the year ended May 31, 2007, the Company issued 3,726,000 (2006 – 2,153,000; 2005 – 425,000) shares in settlement of approximately $1.0 million (2006 – $882 thousand; 2005 – $300 thousand) in interest.

The $15.0 million principal amount of debentures issued on October 6, 2004, January 14 and April 15, 2005 is convertible at the holder's option at any time into common shares of the Company with a conversion price per share of $1.00.

With the issuance of each $5.0 million debenture, the Company issued to the debenture holder from escrow 1,000,000 purchase warrants expiring October 6, 2009 to buy common shares of the Company at a price per share equal to $1.00.

The debentures contain both a liability and an equity element, represented by the conversion option and, therefore, under Canadian GAAP, these two elements must be split and classified separately as debt and equity. In addition, as noted above, the debenture holder received 1,000,000 purchase warrants on the issuance of each tranche of convertible debt. The Company allocated the total proceeds received from the issuance of the debentures to these three elements based on their relative fair values. The fair value of the purchase warrants has been determined based on an option pricing model. The fair value of the debt has been based on the discounted cash flows using an estimated cost of borrowing of 15% to represent an estimate of what the Company may borrow secured debt without a conversion option or purchase warrant. The debentures conversion option was valued using a trinomial model. The resulting allocation based on relative fair values resulted in the allocation of $9.8 million to the debt instrument, $4.1 million to the conversion option and $1.1 million to the purchase warrants. The financing fees totalling $1.1 million related to the issuance of the convertible debentures have been allocated pro-rata between deferred financing charges of $652 thousand, against the equity portion of the convertible debentures of $322 thousand and against the purchase warrants of $87 thousand. This allocation resulted in net amounts allocated to the equity portion of the debentures and warrants of $3.8 million and $991 thousand respectively. The financing charges are being amortized over the five-year life of the Agreement. For the year ended May 31, 2007, the Company has recognized $110 thousand (2006 – $87 thousand; 2005 – $84 thousand) in amortization expense. This amortization expense has reduced the value of the deferred financing charges to $371 thousand at May 31, 2007 (2006 – $481 thousand).

Each reporting period, the Company is required to accrete the carrying value of the convertible debentures such that at maturity on October 6, 2009, the carrying value of the debentures will be their face value of $15.0 million. For the year ended May 31, 2007, the Company has recognized $935 thousand (2006 – $790 thousand; 2005 – $426 thousand) in accretion expense. This accretion expense has increased the carrying value of the convertible debentures to $11.9 million at May 31, 2007 (2006 – $11.0 million).

The lender has the option to demand repayment in the event of default, including the failure to maintain certain subjective covenants, representations and warranties. Management assesses on a quarterly basis whether or not events during the quarter could be considered an event of default. This assessment was performed and management believes that there has not been an event of default and that, at May 31, 2007, the term of the debt remains unchanged.

13. Commitments and guarantees:

(a) Operating lease commitments:

The Company has entered into operating leases for premises and equipment under which it is obligated to make minimum annual payments of approximately $118 thousand in 2008, $8 thousand in 2009.

During the year ended May 31, 2007, operating lease expenses were $139 thousand (2006 – $130 thousand; 2005 – $136 thousand).

(b) Other contractual commitments:

In December 1997, the Company acquired certain patent rights and a sub-license to develop and commercialize the anticancer application of certain compounds in exchange for:

(i) A 20% share interest in NuChem;

(ii) A payment of U.S. $350 thousand in shares of Lorus; and

(ii) Up to U.S. $3.5 million in cash.

To date, the Company has made cash payments of U.S. $500 thousand. The remaining balance of up to U.S. $3.0 million remains payable upon the achievement of certain milestones based on the commencement and completion of clinical trials. Additional amounts paid will be classified as acquired patents and licenses and will be amortized over the estimated useful life of the licensed asset.

The Company does not currently expect to achieve any of the above milestones in fiscal years ended May 31, 2008 or 2009 and cannot reasonably predict when such milestones will be achieved, if at all.

The Company holds an exclusive worldwide license from the University of Manitoba (the "University") and Cancer Care Manitoba ("CCM") to certain patent rights to develop and sub-license certain oligonucleotide technologies. In consideration for the exclusive license of the patent rights, the University and CCM are entitled to an aggregate of 1.67% of the net sales received by the Company from the sale of products or processes derived from the patent rights and 1.67% of all monies received by the Company from sub-licenses of the patent rights. Any and all improvements to any of the patent rights derived in whole or in part by the Company after the date of the license agreement, being June 20, 1997, are not included within the scope of the agreement and do not trigger any payment of royalties.

The Company has not yet earned any revenue from the products covered under this agreement and, therefore, has not paid any royalties thereunder and cannot reasonably predict the timing and amount of any future payment. The Company does not expect to make any royalty payments under this agreement in fiscal years ended May 31, 2008 or 2009, and cannot reasonably predict when such royalties will become payable, if at all.

(c) Guarantees:

The Company has entered into various contracts, in which contractors agree to perform certain services for the Company. The Company indemnifies the contractors against costs, charges and expenses in respect of legal actions or proceedings against the contractors in their capacity of servicing the Company. The maximum amounts payable from these guarantees cannot be reasonably estimated. Historically, the Company has not made significant payments related to these guarantees.

14. Financial instruments:

The carrying values of cash and cash equivalents, short-term marketable securities and other investments, amounts receivable, other assets, accounts payable and accrued liabilities approximate their fair values due to the short-term nature of these financial instruments. Long-term marketable securities and other investments are valued at carrying value that, by virtue of the nature of the investments, primarily interest-bearing instruments, approximates their quoted market value.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Financial instruments potentially exposing the Company to a concentration of credit risk consist principally of cash equivalents and short-term investments. The Company mitigates this risk by investing in high grade fixed income securities.

The Company is exposed to interest rate risk due to the convertible debentures that require interest payments at a variable rate of interest.

The fair value of the convertible debentures at May 31, 2007 is $13.6 million.

15. Comparative figures:

Certain of the comparative figures have been reclassified to conform to the current year's method of presentation.

16. Subsequent events:

On July 10, 2007 (the "Effective Date"), the Company completed a corporate reorganization by way of a plan of arrangement (the "Reorganization") with unrelated parties, 6707157 Canada Inc. ("Investor") and its affiliate, Pinnacle International Lands Inc., to reorganize Lorus' business. The Reorganization was effected pursuant to an arrangement agreement dated as of May 1, 2007 and was approved by Lorus' shareholders on June 25, 2007.

Pursuant to the Reorganization, Lorus transferred all of its assets (with the exception of certain future tax assets) and liabilities to New Lorus and/or one of its wholly-owned subsidiaries, and New Lorus assumed those liabilities. Under the Reorganization, the share capital of Lorus was reorganized into voting common shares and non-voting common shares and securityholders of Lorus exchanged their securities in Lorus for equivalent securities in New Lorus (the "Exchange"). As part of the Reorganization, Lorus changed its name to 4325231 Canada Inc. and New Lorus changed its name from 6650309 Canada Inc. to Lorus Therapeutics Inc. The common shares of Lorus were de-listed from both the Toronto Stock Exchange and the American Stock Exchange. As a result of the Reorganization, Lorus ceased carrying on the business of the research and development of pharmaceutical products and technologies that was previously carried on by Lorus. As part of and upon the completion of the Reorganization, the nature of Lorus' business underwent a fundamental change and, since the Effective Date, has been focused entirely on real estate development. After completion of the Reorganization, New Lorus was not related to Lorus.

As part of the Reorganization, the Investor acquired from New Lorus and the Selling Shareholders (as defined below) approximately 41% of the voting common shares and all of the non-voting common shares of Lorus for cash consideration of approximately $8.5 million less an escrowed amount of $600 thousand, subject to certain post-closing adjustments before transaction costs. The remaining 59% of the voting common shares of Lorus were distributed on a pro-rata basis to the New Lorus shareholders who were not residents of the United States, and the New Lorus shareholders who were residents of the United States received a nominal cash payment instead of voting common shares. As part of the Reorganization, High Tech Beteiligungen GmbH & Co. KG and certain other shareholders of Lorus (the "Selling Shareholders") sold to the Investor the voting common shares of Lorus received under the Reorganization at the same price per share as was paid to shareholders who are residents of the United States. The proceeds received by the Selling Shareholders were nominal.

New Lorus and its subsidiaries have agreed to indemnify Lorus and its directors, officers and employees from and against all damages, losses, expenses (including fines and penalties), other third party costs and legal expenses, to which any of them may be subject arising out of any matter occurring (i) prior to, at or after the effective time of the Reorganization (the "Effective Time") and directly or indirectly relating to any of the assets of Lorus transferred to New Lorus pursuant to the Reorganization (including losses for income, sales, excise and other taxes arising in connection with

the transfer of any such asset) or the conduct of the business of Lorus prior to the Effective Time; (ii) prior to, at or after the Effective Time as a result of any and all interests, rights, liabilities and other matters relating to the assets transferred by Lorus to New Lorus pursuant to the Reorganization; and (iii) prior to or at the Effective Time and directly or indirectly relating to, with certain exceptions, any of the activities of Lorus or the Reorganization.

Certain of the transactions associated with the Reorganization are taxable and would result in income taxes otherwise payable of approximately $4.1 million. Lorus will utilize tax loss carryforwards of $11.5 million to offset income taxes otherwise payable. Accordingly, the future tax assets would be reduced by $4.1 million. There would be a corresponding reduction of the valuation allowance. Future tax assets relating to income tax attributes of Lorus Therapeutics Inc. (but not those of its subsidiaries) of $39.8 million will not be available to New Lorus in the future. These future tax assets have been fully reserved through the valuation allowance and will not otherwise impact the Company's loss.

During the year ended May 31, 2007, the Company incurred approximately $1.3 million in deferred arrangement costs associated with negotiating the above arrangement, consisting primarily of professional fees. These costs were transferred to New Lorus as part of the arrangement and will be offset against proceeds from the transaction in the first quarter of 2008 in the New Lorus consolidated financial statements.

As part of the Reorganization, on July 10, 2007, the following transactions ensued:

(i) Lorus issued 294,296,851 additional non-voting common shares to the Investor for gross proceeds of $1.2 million; and

(ii) Lorus acquired all of the limited partnership units (the "LP Units") in Pinnacle Centre Three Limited Partnership and Pinnacle Centre Four Limited Partnership ("Pinnacle Partnerships"), each of which has an interest in a real estate development project located in downtown Toronto, Ontario, for a total purchase price of $1.2 million (the "Purchase Price") from an entity related to the Investor. The Purchase Price was satisfied by the issuance of interest-bearing demand promissory notes aggregating to $500,000, and the balance of $700,000 will be paid in cash. These transactions have occurred between two commonly controlled entities. Since these transactions do not result in a substantive change in ownership, the transactions will be accounted for at carrying value.

As at the date of the acquisition, the Pinnacle Partnerships had the following combined assets and liabilities:

	Combined Pinnacle Partnerships (Unaudited)
Assets	
Property under development	$ 11,368
Cash held in trust	3,430
Other current assets	226
Due from related party	1,934
	$ 16,958
Liabilities and partners' equity	
Due to related parties	$ 13,547
Sales deposits	3,397
Accrued liabilities	12
	$ 16,956
Partners' equity	2
	$ 16,958

Prior to the acquisition of the LP Units, the Pinnacle Partnerships each entered into a revolving demand loan agreement with Pinnacle International Realty Group Inc., an entity with common ownership to the Investor, whereby each of the Pinnacle Partnerships may borrow up to $60 million with interest at prime plus 2% in order to finance construction costs until conventional construction financing is secured.

Management Team

Aiping Young, M.D., Ph.D.
President and Chief Executive Officer

Elizabeth Williams, C.A.
Director of Finance
(Acting Chief Financial Officer)

Saeid Babaei, Ph.D., MBA
Director, Corporate Development

Yoon Lee, Ph.D.
Director, Research

Peter Murray
Director, Clinical Development

Board of Directors

Herbert Abramson
Chairman, CEO and Portfolio Manager,
Trapeze Capital Corp.,
Ontario, Canada

J. Kevin Buchi
Executive Vice President and
Chief Financial Officer,
Cephalon Inc.,
Pennsylvania, USA

Georg Ludwig
Managing Director
ConPharm Anstalt,
Eschen, Liechtenstein

Michael Moore, Ph.D., DSC,
Chief Executive Officer,
Piramed Limited,
Surrey, United Kingdom

Donald W. Paterson
President,
Cavandale Corporation,
Ontario, Canada

Alan Steigrod
Managing Director,
Newport HealthCare Ventures,
Florida, USA

Graham Strachan, (Chairman)
President,
GLS Business Development Inc.,
Ontario, Canada

Jim A. Wright, Ph.D.
Chief Executive Officer,
NuQuest Bio Inc.,
Ontario, Canada

Aiping Young, M.D., Ph.D.
President and Chief Executive Officer,
Lorus Therapeutics Inc.,
Ontario, Canada

Medical and Scientific Advisory Board (MSAB)

Dr. Donald Braun, Ph.D.
Professor/Administrative Director
of The Cancer Institute,
Medical College of Ohio

Dr. Gregory Curt, M.D.
Medical Director, Field Medical Group
AstraZeneca PLC,
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and Cellular Biology Research,
Canada Research Chair in
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Chairman,
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Marusyk Miller & Swain LLP, Ottawa

Auditors

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Transfer Agent and Registrar

Inquiries regarding transfer requirements, lost certificates and changes of address should be directed to the transfer agent.

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Inquiries, Annual and Quarterly Reports

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with questions or requests for
additional information.
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email: ir@lorusthera.com
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Annual Meeting

The 2007 Annual and Special Meeting of Shareholders will be held on Wednesday September 19, 2007 at 10:00 a.m. at:

The Trading Floor
The Design Exchange
234 Bay Street,
Toronto, Ontario

CORPORATE DIRECTORY

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