

**NAPIER ENVIRONMENTAL
TECHNOLOGIES INC.
CONSOLIDATED
FINANCIAL STATEMENTS
DECEMBER 31, 2002**

TABLE OF CONTENTS

	PAGE
Auditors' Report	1
Management's Responsibility for Financial Reporting	2
Consolidated Balance Sheets	3
Consolidated Statements of Operations and Deficit	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6
Schedules	18

AUDITORS' REPORT

The Shareholders,
Napier Environmental Technologies Inc.

We have audited the consolidated balance sheets of Napier Environmental Technologies Inc. as at December 31, 2002 and 2001 and the consolidated statements of operations and deficit and cash flows for the years ended December 31, 2002 and December 31, 2001. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles. As required by the Company Act of British Columbia, we report that, in our opinion, these principles have been applied on a basis consistent with that of the preceding periods.

“DELOITTE & TOUCHE LLP”

Chartered Accountants
Vancouver, British Columbia

March 1, 2003

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of Napier Environmental Technologies Inc. are the responsibility of management and have been approved by the Board of Directors.

The financial statements have been prepared by management in conformity with accounting principles generally accepted in Canada. These statements include some amounts that are based on best estimates and judgements. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly, in all material respects.

The Company maintains a system of internal control, which provides management with reasonable assurance that assets are safeguarded and that reliable financial records are maintained.

The Board of Directors carries out its responsibility for the financial statements principally through its Audit Committee, consisting solely of outside directors. The Audit Committee meets periodically with management, as well as the external auditors, to review the financial statements and to satisfy itself that each party is properly discharging its responsibilities.

The external auditors, Deloitte & Touche LLP, have been appointed by the shareholders to render their opinion on the financial statements. The auditors have full and free access to the Audit Committee and their report is included herein.

Frank Dixon
Chief Executive Officer

James G. Grinnell
Chief Financial Officer

March 1, 2003

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

CONSOLIDATED BALANCE SHEETS DECEMBER 31

	2002	2001
ASSETS		
Current		
Cash and cash equivalents	\$ 285,097	\$ 981,798
Accounts receivable	617,166	690,959
Inventory (Note 4)	1,574,303	1,606,710
Prepaid expenses	185,079	163,054
	2,661,645	3,442,521
Investments (Note 5)	161,585	425,545
Capital assets (Note 6)	754,517	897,362
	\$ 3,577,747	\$ 4,765,428
LIABILITIES		
Current		
Bank indebtedness (Note 7)	\$ 353,000	\$ 290,000
Accounts payable	936,999	938,137
Current portion of long term debt	80,033	81,629
	1,370,032	1,309,766
Long term debt (Note 8)	114,313	195,826
	1,484,345	1,505,592
SHAREHOLDERS' EQUITY		
Capital stock (Note 9)	23,335,041	23,270,441
Contributed surplus	39,890	39,890
Deficit	(21,281,529)	(20,050,495)
	2,093,402	3,259,836
	\$ 3,577,747	\$ 4,765,428

Approved by the Directors

"B. Frank Dixon"

"Peter D. Jeffrey"

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

**CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
YEARS ENDED DECEMBER 31**

	2002	2001
Sales	\$ 8,069,430	\$ 7,422,189
Cost of sales	4,745,653	5,380,231
Gross profit	3,323,777	2,041,958
Expenses		
Selling and marketing (Schedule)	2,451,016	3,416,011
General and administrative (Schedule)	1,674,203	1,790,584
Research and product development	197,600	268,178
	4,322,819	5,474,773
Operating loss	(999,042)	(3,432,815)
Other items		
Equity loss in investment	(113,960)	(310,859)
Write down of investment	(150,000)	-
Interest and other income	33,880	91,680
Loss on disposal of capital assets	(1,912)	(58,891)
Amortization and writeoff of goodwill (Note 3)	-	(9,206,811)
	(231,992)	(9,484,881)
Net loss for the year	(1,231,034)	(12,917,696)
Deficit at beginning of the year	(20,050,495)	(7,132,799)
Deficit at end of the year	\$ (21,281,529)	\$ (20,050,495)
Weighted average shares outstanding	47,446,243	47,672,793
Loss per share, basic and fully diluted	\$ (0.03)	\$ (0.27)

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31

	2002	2001
Operating activities		
Net loss for the year	\$ (1,231,034)	\$ (12,917,696)
Items not involving cash		
Amortization and writeoff of goodwill (Note 3)	-	9,206,811
Amortization	164,260	165,020
Equity loss in investment	113,960	310,859
Write down of investment	150,000	-
Loss on disposal of capital assets	1,912	58,891
	(800,902)	(3,176,115)
Change in non-cash operating working capital		
Accounts receivable	73,793	476,202
Inventory	32,407	12,038
Prepaid expenses	(22,025)	(55,707)
Accounts payable	(1,138)	(146,529)
	83,037	286,004
	(717,865)	(2,890,111)
Financing activities		
Bank indebtedness	63,000	290,000
Shares issued for cash	64,600	-
Long-term debt incurred	-	251,582
Repayment of long-term debt	(83,109)	(64,303)
	44,491	477,279
Investing activities		
Purchase of capital assets	(28,127)	(713,683)
Proceeds of disposal of capital assets	4,800	26,808
Purchase of investments	-	(200,000)
	(23,327)	(886,875)
Change in cash during the year	(696,701)	(3,299,707)
Cash and cash equivalents		
at beginning of the year	981,798	4,281,505
Cash and cash equivalents		
at end of the year	\$ 285,097	\$ 981,798
Supplemental information		
Interest paid	\$ 67,873	\$ 34,903

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

1. CONTINUING OPERATIONS

The company is incorporated under the Company Act of British Columbia and is primarily involved in the manufacture and distribution of a wide range of products created through environmentally advanced technology. The product lines include coating removal and wood restoration products.

The company has incurred significant losses over the past fiscal periods and has been reliant on sources of cash from other than operations. Such sources have included bank financing and issuances of equity. The ability of the company to continue as a going concern is dependent upon either achieving cash flow from operations or obtaining an injection of capital.

These financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assume that the company will continue to operate in the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business. If the going concern assumption was not appropriate, then certain adjustments would be necessary to the carrying values of assets and liabilities, the reported costs and expenses and balance sheet classifications used.

Management believes that the actions taken or planned subsequent to the year end will mitigate the conditions and events which raise doubts about the validity of the going concern assumption used in preparing these financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of presentation

These consolidated financial statements include the accounts of the company and its wholly owned subsidiaries. Intercompany balances and transactions are eliminated on consolidation.

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

b) Cash and cash equivalents

Cash and cash equivalents are comprised of highly liquid investments having original terms to maturity of 90 days or less when acquired.

c) Inventory

Raw materials are valued at the lower of cost and replacement cost. Finished goods are valued at the lower of cost and net realizable value.

d) Investments

Investments over which the company exercises significant influence are accounted for using the equity method. Other long-term investments are recorded at the lower of cost and estimated net realizable value.

e) Capital assets and amortization

Capital assets are recorded at cost. Amortization is provided under the straight-line method at annual rates varying from 2 to 10 years.

f) Revenue recognition

Revenue is recognized when goods are shipped and when significant risks and benefits of ownership are transferred.

g) Income taxes

Income taxes are accounted for using the liability method whereby future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of tax losses that are likely to be realized. Future income tax assets and liabilities are measured using enacted tax rates that are expected to be effective when recovered or settled. The net change in recorded future income tax assets and liabilities is recognized in income in the period in which the change occurs including any change in applicable future tax rates.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

h) Stock options

Effective January 1, 2002, the company adopted, on a prospective basis, the new recommendations by the Canadian Institute of Chartered Accountants regarding stock-based compensation. As required under the new recommendations, the company measures certain stock based transactions using the fair value method including stock options granted to non-employees.

The company has elected to use the intrinsic method to value stock options granted to employees whereby no compensation expense is recorded when options are granted. Proceeds received on exercise of employee stock options are recorded as share capital. The new recommendations require that the company provide additional disclosure of the pro forma effect as if accounting for the grant of employee stock options under the fair value method. The fair value method imputes an opportunity cost to the company based on estimates of both when the option will be exercised and what the stock market price will be when exercised (see note 9(d)).

i) Foreign currency translation

The functional currency of the company's operations is the Canadian dollar. Transactions and account balances originally stated in currencies other than the Canadian dollar have been translated into Canadian dollars using the temporal method as follows:

- Revenue and expense items at the rate of exchange in effect on the dates they occur;
- Non-monetary assets and liabilities at historical exchange rates; and
- Monetary assets and liabilities at the exchange rate at the balance sheet dates.

Exchange gains and losses are included in the determination of income in the period in which they occur.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

j) Loss per share

Loss per share is calculated based on the weighted average number of shares outstanding during the period. Potentially dilutive items are described in Note 9. Fully diluted loss per share is the same as basic loss per share as the exercise of options and warrants would reduce the loss per share.

k) Comparative figures

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

3. WRITEOFF OF GOODWILL

During the year ended December 31, 2001 the company, as part of its review of financial results, performed an assessment of the carrying value of the company's long-lived assets, including goodwill. Goodwill previously arose on the acquisition of Bio-Wash Products (Canada) Inc. on November 30, 1999. Management determined there was an impairment in goodwill based on a number of factors, including the contribution to operating results over the prior two years and expected contribution in the future. As the original benefits identified at the time of the acquisition were not expected to be realized with sufficient certainty nor within the time frame previously anticipated, the company wrote off the entire balance during the 2001 year, resulting in a charge to operations of \$9,206,811.

4. INVENTORY

Inventory is comprised of:

	<u>2002</u>	<u>2001</u>
Raw materials	\$ 786,639	\$ 819,424
Finished goods	787,664	787,286
	<u>\$ 1,574,303</u>	<u>\$ 1,606,710</u>

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

5. INVESTMENTS

The company has investments in the common shares of two public companies as follows:

	<u>2002</u>	<u>2001</u>
Investment in Ecoprogress, beginning of the year	\$ 225,545	\$ 536,404
Equity share of losses	(150,110)	(448,626)
Gain on dilution of equity interest	36,150	137,767
Investment in Ecoprogress, end of the year	<u>111,585</u>	<u>225,545</u>
Investment in Radical Elastomers Inc. at written down cost	50,000	200,000
Total investments, end of the year	<u>\$ 161,585</u>	<u>\$ 425,545</u>

The company's investment in Consolidated Ecoprogress Technology Inc. ("Ecoprogress") represents a 21% interest (2001 - 23%). The excess purchase price of the company's investment over the fair value of the underlying net assets has been allocated to product licenses owned by Ecoprogress and is amortized on a straight-line basis over the estimated life of the product licenses.

During the year the company wrote down its investment in Radical Elastomers Inc. by \$150,000 to estimated net realizable value.

6. CAPITAL ASSETS

	<u>2002</u>			<u>2001</u>
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>	<u>Net Book Value</u>
Machinery and equipment	\$ 889,944	\$ 511,579	\$ 378,365	\$471,324
Furniture and fixtures	209,147	55,651	153,496	172,827
Leasehold improvements	277,544	54,888	222,656	253,211
	<u>\$ 1,376,635</u>	<u>\$ 622,118</u>	<u>\$ 754,517</u>	<u>\$ 897,362</u>

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

7. BANK INDEBTEDNESS

Bank indebtedness consists of an operating line of credit bearing interest at prime plus 1% and secured by a general security agreement over the assets of the company. At December 31, 2002 the company was not in compliance with all covenant requirements and obtained a temporary waiver from the bank. Subsequent to the year end the company renegotiated the terms of the operating line and eliminated the restrictive covenants.

8. LONG TERM DEBT

	<u>2002</u>	<u>2001</u>
Capital lease obligations repayable in aggregate monthly instalments of \$9,187 including interest averaging 11.19% per annum due until January, 2005.	\$ 194,346	\$ 277,455
Less current portion	<u>80,033</u>	<u>81,629</u>
	<u>\$ 114,313</u>	<u>\$ 195,826</u>

Principal repayments required are as follows: 2003 - \$80,033; 2004 - \$70,000; 2005 - \$44,313.

9. CAPITAL STOCK

a) Authorized
145,635,962 common shares

	<u>2002</u>		<u>2001</u>	
	Number of shares	\$	Number of shares	\$
Beginning of the year	47,248,042	23,270,441	48,097,544	23,278,936
Shares cancelled	-	-	(849,502)	(8,495)
Issued for cash	380,000	64,600	-	-
End of the year	<u>47,628,042</u>	<u>23,335,041</u>	47,248,042	23,270,441

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

9. CAPITAL STOCK (continued)

b) Issued (continued)

During the year ended December 31, 2002, 380,000 stock options were exercised at \$0.17 per share for proceeds of \$64,600.

During the year ended December 31, 2001, 849,502 shares previously held in escrow were cancelled as a result of the expiry of an old outstanding escrow agreement. Accordingly, both the authorized and issued shares have been reduced and, contributed surplus has been increased by \$8,495.

c) Stock options

Under the terms of the company's incentive stock option plan, options are granted upon approval by the Board of Directors and the exercise price of each option is determined by reference to the market price of the company's stock. Options are normally exercisable within 10 years from the date of grant or a lesser period as determined by the Board and within 30 days of termination of employment. Options generally vest upon grant date, however the Board reserves the right to attach vesting periods to stock options granted.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

9. CAPITAL STOCK (continued)

c) Stock options (continued)

The following table summarizes the status and changes in stock options outstanding at December 31, 2002 and 2001:

	2002		2001	
	Number	Weighted average price	Number	Weighted average price
Beginning of the year	4,087,000	\$ 0.98	2,607,500	\$ 1.74
Granted/issued	895,000	0.30	2,886,000	0.67
Exercised	(380,000)	0.17	-	-
Cancelled/expired	(963,000)	0.98	(1,406,500)	1.94
End of the year	3,639,000	0.90	4,087,000	0.98
Exercisable, end of the year	3,339,000	\$ 0.95	4,087,000	\$ 0.98
Weighted average fair value of options granted during the year	\$ 4.18			
Options remaining for issuance under stock option plan	981,000		913,000	

The following table summarizes information about stock options outstanding at December 31, 2002:

Range of exercise prices	Number of options	Weighted average remaining contractual life	Weighted average exercise price
Vested			
\$.17 - \$.24	1,205,000	3.1 years	\$ 0.18
\$.40	215,000	4.3 years	\$ 0.40
\$.85 - \$1.15	1,299,000	2.3 years	\$ 1.02
\$2.18 - \$2.56	620,000	1.6 years	\$ 2.50
	3,339,000	2.6 years	\$ 0.95
Non-vested			
\$.28	300,000	4.9 years	\$ 0.28
	3,639,000	2.8 years	\$ 0.90

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

9. CAPITAL STOCK (continued)

d) Pro forma stock-based compensation

Under new accounting recommendations (see note 2(h)), the company is required to disclose an estimate of the pro forma effect as if the fair value method of accounting had been used for stock options granted to employees.

During the year the company issued 895,000 stock options. The estimated fair value of these options has been calculated using the Black Scholes model; stock price volatility ranging from 115% to 123%, no dividend yield, and a 5% risk free interest rate for the expected option life of 5 years.

Year ended December 31, 2002

Net loss, as reported	\$	(1,231,034)
Net loss, pro forma	\$	(1,391,710)
Loss per share, as reported	\$	(0.03)
Loss per share, pro forma	\$	(0.03)

e) Warrants

	<u>2002</u>	<u>2001</u>
Beginning of the year	\$ 3,967,120	\$ 4,967,120
Expired	(50,000)	(1,000,000)
End of the year	<u>\$ 3,917,120</u>	<u>\$ 3,967,120</u>

During the year ended December 31, 2002 the company obtained approval to re-price the outstanding warrants from \$2.40 to \$0.41 per share and to extend the expiry date to September 11, 2003. The re-priced warrants have a thirty day accelerated expiry date should the market price of the company's shares exceed \$0.52.

At December 31, 2002, 2,597,120 warrants are exercisable at \$0.41 per share and 320,000 warrants are exercisable at \$2.40 per share.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

10. INCOME TAXES

The approximate tax effect of temporary differences and tax loss carry forwards that give rise to the company's future income tax assets are as follows:

	<u>2002</u>	<u>2001</u>
Capital assets	\$ 1,270,000	\$ 1,220,000
Investments and other	243,000	220,000
Tax loss carryforwards	<u>2,770,000</u>	<u>2,600,000</u>
	4,283,000	4,040,000
Less valuation allowance	<u>4,283,000</u>	<u>4,040,000</u>
	<u>\$ -</u>	<u>\$ -</u>

The income tax recovery and change in valuation allowance differs from the amounts computed by applying Canadian statutory rates to loss before income taxes as follows:

	<u>2002</u>	<u>2001</u>
Income tax recovery at statutory rate of 39.6% (2001 - 42.6%)	\$ (490,000)	\$ (5,500,000)
Manufacturing and processing allowance	50,000	200,000
Amortization of goodwill	-	3,920,000
Amortization of tangible assets	65,000	70,000
Investments	105,000	130,000
Other	(10,000)	80,000
Valuation allowance	<u>280,000</u>	<u>1,100,000</u>
Income tax recovery	<u>\$ -</u>	<u>\$ -</u>

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

10. INCOME TAXES (continued)

The company has loss carryforwards available for tax purposes as follows:

<u>Expiry date</u>	<u>Amount</u>
December 31, 2003	\$ 550,000
December 31, 2004	830,000
December 31, 2005	180,000
December 31, 2006	210,000
December 31, 2007	1,995,000
December 31, 2008	3,000,000
December 31, 2009	1,015,000
	<u>\$ 7,780,000</u>

11. SEGMENTED INFORMATION

The company operates in one industry segment, which is the manufacture and distribution of coatings removal products and wood restoration products in Canada and internationally. Within this general industry segment the company distributes to both retail and industrial sectors. Sales of the company's Biowash products are distributed through retail outlets and the company's SARA/RemovAll products are predominantly distributed via industrial/commercial relationships. All of the company's capital assets are located in Canada.

	<u>2002</u>	<u>2001</u>
Sales by region		
Canadian	\$ 2,872,000	\$ 2,455,000
International	5,197,000	4,967,000
Total Sales	<u>\$ 8,069,000</u>	<u>\$ 7,422,000</u>
Sales by product line		
Biowash products	4,103,000	3,680,000
SARA/RemovAll products	3,966,000	3,742,000
	<u>\$ 8,069,000</u>	<u>\$ 7,422,000</u>

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2002

12. COMMITMENTS

The company leases its premises and certain office equipment under operating leases. The aggregate minimum rental payments under these leases over the next five years are approximately 2003 - \$347,000; 2004 - \$319,000; 2005 - \$345,000; 2006 - \$347,000; 2007 - \$204,000.

13. FINANCIAL INSTRUMENTS

The company is exposed to financial risk resulting from fluctuations in foreign exchange rates and the degree of volatility of these rates. The company does not use derivative financial instruments to reduce its exposure to rate changes.

The carrying values of cash, accounts receivable, bank indebtedness, accounts payable and capital lease obligations approximate their fair value based on their liquidity and short-term nature.

The quoted market prices of the company's investments aggregate \$477,176 at December 31, 2002. The market value of the company's investments may differ from net realizable value due to the number of shares held and the liquidity of these shares.

NAPIER ENVIRONMENTAL TECHNOLOGIES INC.

CONSOLIDATED SCHEDULES SELLING AND MARKETING EXPENSES YEARS ENDED DECEMBER 31

	2002	2001
Advertising	\$ 162,204	\$ 228,164
Bad debt recovery	(78,800)	-
Commissions	291,600	325,113
Consulting and other	22,206	35,703
Promotional materials	269,540	327,371
Retail service fees	123,128	-
Salaries and wages	1,136,489	1,731,698
Telecommunications	66,336	109,586
Travel, training and tradeshow	458,313	658,376
	\$ 2,451,016	\$ 3,416,011

GENERAL AND ADMINISTRATIVE EXPENSES YEARS ENDED DECEMBER 31

	2002	2001
Amortization	\$ 105,523	\$ 92,976
Capital tax	-	8,669
Consulting	23,164	44,474
Insurance	195,253	128,947
Interest on long term debt	32,528	27,545
Occupancy	108,454	195,803
Other	156,821	27,813
Professional fees	246,258	242,146
Regulatory and filing fees	14,082	27,919
Salaries and wages	678,456	842,280
Telecommunications	28,047	52,012
Travel and corporate relations	85,617	100,000
	\$ 1,674,203	\$ 1,790,584