



VIRALGENETICS

Inc.

(A DEVELOPMENT STAGE COMPANY)

**CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

(Unaudited)

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Consolidated Financial Statements
Year Ended December 31, 2011

(Unaudited)

The attached consolidated financial statements of Viral Genetics, Inc. (the “Company”) for the years ended December 31, 2010 and 2011 which were originally listed on the OTC Markets website on April 25, 2012 have been modified to correct certain disclosures and incidental clerical errors. These changes included disclosures with respect to the Company’s subsidiary, VG Energy, Inc. included in Note 4 and certain disclosures with respect to a \$100,000 convertible promissory note included in Note 7b. There were no changes to the accompanying consolidated balance sheets, statements of operations, stockholders equity or cashflows from those originally listed on April 25, 2012.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	December 31,	
	2011	2010
ASSETS		
CURRENT ASSETS		
Cash	\$ 5,785	\$ 7,230
Other current assets	3,000	9,130
Total Current Assets	<u>8,785</u>	<u>16,360</u>
PROPERTY AND EQUIPMENT, NET	-	-
OTHER ASSETS		
Intangible assets	2,981,479	2,981,479
Investment in unconsolidated subsidiary	100,000	100,000
Total Other Assets	<u>3,081,479</u>	<u>3,081,479</u>
TOTAL ASSETS	<u>\$ 3,090,264</u>	<u>\$ 3,097,839</u>
LIABILITIES AND STOCKHOLDERS' DEFICIT		
CURRENT LIABILITIES		
Notes payable	\$ 25,000	\$ 175,000
Accounts payable	563,681	543,181
Accrued expenses	689,859	546,966
Convertible debenture-legal settlement	390,947	938,272
Accrued interest	361,580	462,752
Convertible promissory notes	761,397	410,624
Unsecured convertible notes, patents and debt settlements	20,000	61,667
Total Current Liabilities	<u>2,812,465</u>	<u>3,138,463</u>
LONG-TERM LIABILITIES		
Unsecured convertible notes payable - patents	108,108	228,000
Revolving line of credit - related party	711,872	941,087
Convertible debenture - legal settlement	422,222	752,934
Convertible notes payable, net of discount	49,761	49,761
Total Long-term Liabilities	<u>1,291,962</u>	<u>1,971,783</u>
TOTAL LIABILITIES	<u>4,104,427</u>	<u>5,110,246</u>
STOCKHOLDERS' DEFICIT		
Preferred stock, 250,000,000 shares authorized, \$0.0001 par value; 0,000,000 and 4,750,000 issued and outstanding, respectively	475	475
Common stock, 1,500,000,000 shares authorized, \$0.0001 par value; 932,532,478 and 628,853,282 issued and outstanding, respectively	93,253	62,885
Additional paid-in capital	80,142,917	73,795,367
Noncontrolling interests	41,177	2,447
Deficit accumulated during the development stage	(81,282,487)	(75,864,081)
Total stockholders' deficit before deferred costs and subscriptions receivable	(1,004,664)	(2,002,907)
Less: deferred costs and subscription receivable	9,500	9,500
Total Stockholders' Deficit	<u>(1,014,164)</u>	<u>(2,012,407)</u>
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	<u>\$ 3,090,264</u>	<u>\$ 3,097,839</u>

See accompanying notes to unaudited consolidated financial statements

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Years Ended December 31,		July 11, 1995 (Inception) to December 31,
	2011	2010	2011
REVENUES	\$ -	\$ 5,677	\$ 353,427
EXPENSES			
Research and development	738,600	498,606	16,328,621
Management salaries	628,500	219,000	4,776,412
Depreciation and amortization	121,963	90,033	1,573,744
Legal and professional	725,804	542,713	4,219,766
Consulting fees	1,512,000	989,070	18,531,307
General and administrative	339,885	326,497	7,219,713
Total expenses	<u>4,066,752</u>	<u>2,665,920</u>	<u>52,649,563</u>
LOSS FROM OPERATIONS	<u>(4,066,752)</u>	<u>(2,660,243)</u>	<u>(52,296,136)</u>
OTHER INCOME (EXPENSE)			
Sale of distribution rights	-	-	1,309,966
Interest income	-	-	9,392
Settlement - distribution agreement rights	-	(1,668,953)	(1,668,953)
Derivative benefit/(expense)	-	-	(1,500,591)
Interest expense	(1,425,214)	(2,911,237)	(27,209,938)
Total other income (expense)	<u>(1,425,214)</u>	<u>(4,580,190)</u>	<u>(29,060,124)</u>
NET LOSS	<u>(5,491,966)</u>	<u>(7,240,433)</u>	<u>(81,356,260)</u>
NET LOSS ATTRIBUTABLE TO NONCONTROLLING INTEREST	73,560	213	73,773
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	<u>\$ (5,418,406)</u>	<u>\$ (7,240,220)</u>	<u>\$ (81,282,487)</u>
NET LOSS PER COMMON SHARE, BASIC AND DILUTED	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING, BASIC AND DILUTED	<u>737,785,579</u>	<u>555,917,335</u>	

See accompanying notes to unaudited consolidated financial statements

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT
(Unaudited)

	Common Stock		Preferred Stock		Additional Paid-in capital	Noncontrolling Interests	Deficit Accumulated During Development Stage	Deferred Costs and Subscription Receivable	Total Stockholders' (Deficit)
	Shares	Amount	Shares	Amount					
Balance, December 31, 2009 - Restated	481,043,860	\$ 48,104	5,000,000	\$ 500	\$ 67,898,250	\$ -	\$ (68,623,861)	\$ (94,690)	\$ (771,697)
Issuance of common stock and warrants for cash	19,193,333	1,919	-	-	411,948	-	-	-	413,867
Issuance of common stock for cash, net of repricing adjustments - 504 placements	12,000,000	1,200	-	-	63,942	-	-	17,410	82,552
Convertible debentures and accrued interest converted to shares and warrants	2,327,900	233	-	-	65,133	-	-	-	65,365
Revolving line of credit, related party - converted to shares and warrants	33,820,161	3,382	-	-	3,167,124	-	-	-	3,170,506
Satisfaction of liabilities - issuance of common stock	3,627,573	363	-	-	177,137	-	-	-	177,500
Satisfaction of liabilities - issuance of common stock and warrants	500,000	50	-	-	27,950	-	-	-	28,000
Consultants notes and accrued interest converted to shares and warrants	5,052,318	505	-	-	428,541	-	-	-	429,046
Issuance of common shares for services	2,273,333	227	-	-	105,273	-	-	-	105,500
Issuance of common shares and warrants for services	1,000,000	100	-	-	137,900	-	-	-	138,000
Issuance of common shares in connection with debt settlement transactions	55,514,804	5,551	-	-	975,982	-	-	-	981,534
Issuance of common shares for cancellation of marketing rights	7,500,000	750	-	-	224,250	-	-	-	225,000
Cash received and issuance of additional warrants upon exercise of warrants	2,500,000	250	-	-	74,750	-	-	-	75,000
Adjustment of variable common stock purchase options	-	-	-	-	(169,252)	-	-	-	(169,252)
Amortization of fair value of warrants issued for services	-	-	-	-	109,323	-	-	-	109,323
Conversion of preferred shares into common shares	2,500,000	250	(250,000)	(25)	(225)	-	-	-	-
Proceeds - issuance of VGE shares for non-controlling interest	-	-	-	-	100,000	-	-	-	100,000
Noncontrolling interests	-	-	-	-	(2,660)	2,660	-	-	-
Amortization - deferred compensation	-	-	-	-	-	-	-	67,780	67,780
Net Loss attributable to noncontrolling interest year ended December 31, 2010	-	-	-	-	-	(213)	-	-	(213)
Net Loss attributable to controlling interest year ended December 31, 2010	-	-	-	-	-	-	(7,240,220)	-	(7,240,220)
Balance, December 31, 2010	628,853,282	62,885	4,750,000	475	73,795,366	2,447	(75,864,081)	(9,500)	(2,012,407)
Issuance of common stock and warrants for cash	7,300,000	730	-	-	90,270	-	-	-	91,000
Accrued Interest - Convertible notes payable satisfied in shares	9,944,231	994	-	-	93,400	-	-	-	94,395
Issuance of shares to convertible noteholders - antidilution protection	117,521	12	-	-	(12)	-	-	-	-
Convertible promissory notes converted to shares at \$.005 - \$.01 per share	88,438,214	8,844	-	-	521,780	-	-	-	530,624
Revolving line of credit, related party - converted to shares and warrants	2,642,750	264	-	-	116,991	-	-	-	117,255
Satisfaction of liabilities - issuance of common stock	21,775,062	2,178	-	-	554,582	-	-	-	556,760
Consultant's notes and accrued interest converted to shares and warrants	19,762,001	1,976	-	-	702,909	-	-	-	704,885
Issuance of common shares for services	11,600,000	1,160	-	-	323,340	-	-	-	324,500
Issuance of common shares - debt settlement and satisfactions	55,443,726	5,544	-	-	932,292	-	-	-	937,837
Issuance of common shares - T&T legal settlement	81,655,691	8,166	-	-	998,817	-	-	-	1,006,983
Conversion of preferred shares into common shares	5,000,000	500	(500,000)	(50)	(450)	-	-	-	-
Proceeds - issuance of VGE shares for non-controlling interest, net	-	-	-	-	485,000	-	-	-	485,000
Issuance of preferred shares in connection with VGE promissory note	-	-	500,000	50	224,950	-	-	(225,000)	-
Fair value of options granted to employees and consultants earned in period	-	-	-	-	1,126,000	-	-	-	1,126,000
Accrued salaries and consultants fees converted to VGE shares and equity	-	-	-	-	289,250	-	-	-	289,250
Adjustment related to prior years transactions	-	-	-	-	720	-	-	-	720
Amortization of deferred interest expense -VGE preferred 100K note	-	-	-	-	-	-	-	225,000	225,000
Noncontrolling interests allocated to increase in equity	-	-	-	-	(112,290)	112,290	-	-	-
Net Loss attributable to noncontrolling interest year ended December 31, 2011	-	-	-	-	-	(73,560)	-	-	(73,560)
Net Loss attributable to controlling interest year ended December 31, 2011	-	-	-	-	-	-	(5,418,406)	-	(5,418,406)
Balance, December 31, 2011	932,532,478	\$ 93,253	\$ 4,750,000	\$ 475	\$ 80,142,916	\$ 41,177	\$ (81,282,487)	\$ (9,500)	\$ (1,014,164)

See accompanying notes to unaudited consolidated financial statements

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A Development Stage Company)

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Year Ended December 31, 2011	Year Ended December 31, 2010	Cumulative for the Period from July 11, 1995 (Inception) to December 31, 2011
Cash Flows From Operating Activities:			
Net loss attributable to common shareholders	\$ (5,418,406)	\$ (7,240,220)	\$ (81,282,487)
Net loss attributable to noncontrolling interest	(73,560)	(213)	(73,773)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation	-	67,780	1,428,350
Amortization of debt discount	121,963	22,253	511,528
Debt issuance costs	-	-	13,339,211
Services included in accounts payable to be satisfied in shares.	-	200,000	200,000
Issuance of common stock and warrant for services	-	151,000	151,000
Stock based compensation	1,149,906	306,302	3,040,355
Issuance of common stock for services and finders fee	324,500	105,500	7,288,109
Issuance of convertible notes for services	150,000	150,000	660,000
Issuance of common stock for settlement agreement - Latin American market	-	225,000	1,060,000
Settlement - distribution agreement rights	-	1,668,953	1,668,953
Debt Settlement liabilities and common shares in excess of recorded liabilities	45,554	399,530	445,084
Issuance of stock and warrants for interest and financing costs	1,395,462	2,494,103	9,126,237
Non-cash operating expenses	-	-	5,387,663
Non-cash income - gain on settlements	-	-	(384,966)
Options and warrants issued for services and wages	-	-	9,331,836
Options exercised for services	-	-	116,317
Contingently issued stock issued for services	-	-	792,499
Warrants exercised for services	-	-	12,500
Issuance of common stock for expenses paid by third party	-	-	593,947
Notes and issued for expenses	-	-	907,349
Expenses paid with notes payable	-	-	(10,043)
Notes payable converted to accrued wages	-	-	(25,000)
Satisfaction of Syxia - in excess of accrual	-	-	104,577
Change in variable common stock purchase options	-	(169,252)	(22,418)
(Increase) decrease in other current assets	6,130	(6,130)	(94,690)
(Increase) decrease in deposits and other assets	-	-	(45,940)
Increase (decrease) in accrued interest	30,646	51,144	1,223,742
Increase (decrease) in accounts payable	58,120	35,500	1,378,759
Increase (decrease) in accrued expenses	909,455	390,290	1,692,595
Increase (decrease) in accrued wages payable	281,050	137,500	726,245
Increase (decrease) in advances - related parties	-	-	74,283
Increase (decrease) in advances	-	-	136,000
Increase (decrease) in derivative liability	-	-	1,259,265
Net cash used in operating activities	<u>(1,019,180)</u>	<u>(1,010,959)</u>	<u>(19,282,912)</u>
Cash Flows From Investing Activities:			
Increase in leasehold improvements	-	-	(1,039,306)
Acquisition of equipment	-	-	(361,665)
Increase in intangible assets	-	-	(5,206,051)
Net cash used in investing activities	<u>-</u>	<u>-</u>	<u>(6,607,022)</u>
Cash Flows From Financing Activities:			
Proceeds from Revolving line of credit- related party	31,815	506,171	2,949,248
Repayments of Revolving line of credit - related party	(416,100)	(358,929)	(2,110,261)
Proceeds of sale of VGE securities to third parties, net	485,000	100,000	585,000
Proceeds from convertible debentures	825,300	183,758	3,696,075
Proceeds from sale of common stock and warrants, net	91,720	496,419	10,955,924
Proceeds from exercise of options and warrants	-	75,000	173,061
Proceeds from notes payable	-	-	267,000
Proceeds from notes payable - related parties	-	-	9,379,671
Net cash provided by financing activities	<u>1,017,735</u>	<u>1,002,419</u>	<u>25,895,717</u>
Increase (decrease) in Cash	(1,446)	(8,541)	5,783
Cash and cash equivalents, beginning of period	7,230	15,771	-
Cash and cash equivalents, end of period	<u>\$ 5,783</u>	<u>\$ 7,230</u>	<u>\$ 5,783</u>

See accompanying notes to unaudited consolidated financial statements

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A Development Stage Company)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Year Ended December 31, 2011	Year Ended December 31, 2010	Cumulative for the Period from July 11, 1995 (Inception) to December 31, 2011
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid during the period for:			
Interest	\$ -	\$ -	\$ 546,003
Income taxes	\$ -	\$ -	\$ -
NON-CASH TRANSACTIONS			
Issuance of common stock and warrants for convertible notes and interest	\$ 94,395	\$ 297,434	\$ 4,206,626
Refinancing of convertible debt - related party Revolving line of credit	\$ 52,855	\$ 676,403	\$ 3,239,418
Issuance of common shares in various debt settlements and partial satisfactions	\$ 398,000	\$ 629,451	\$ 736,118
Issuance of unsecured convertible debentures for accounts payable	\$ 57,297	\$ 226,866	\$ 534,163
Issuance of common stock in satisfaction of accounts payable/notes	\$ 873,645	\$ 192,500	\$ 942,490
Issuance of common stock for debt repayment - Wonderland	\$ 531,824	\$ -	\$ 439,240
VGE accrued compensation converted to equity in VGE	\$ 276,250	\$ -	\$ 115,625
Noncontrolling interest, net	\$ 112,290	\$ 2,447	\$ 5,890
Issuance of common stock for T&T legal settlement and accrued interest	\$ 1,006,985	\$ -	\$ 1,035,000
Issuance of convertible note to acquire interest in unconsolidated subsidiary	\$ -	\$ -	\$ 782,814
Issuance of common shares, options and warrants - V Clip acquisition	\$ -	\$ -	\$ 1,502,479
Issuance of common shares - repurchase product royalty rights, China Market	\$ -	\$ -	\$ 231,000
Issuance of common shares and warrants - Carcinotek acquisition	\$ -	\$ -	\$ 1,000,000
Restructuring of convertible debentures	\$ -	\$ -	\$ 1,198,167
Issuance of unsecured convertible debentures - patents	\$ -	\$ -	\$ 248,000
Issuance of common stock for debt paid by third party	\$ -	\$ -	\$ 593,947
Issuance of common stock for debt and interest	\$ -	\$ -	\$ 9,086,511
Issuance of common stock for finders fee	\$ -	\$ -	\$ 450,000
Warrants issued with convertible debentures	\$ -	\$ -	\$ 516,800
Transfer from derivative liabilities	\$ -	\$ -	\$ 2,004,423
Issuance of warrant in partial consideration of notes payable	\$ -	\$ -	\$ 100,000
Issuance of note in consideration of White Label acquisition	\$ -	\$ -	\$ 100,000

See accompanying notes to unaudited consolidated financial statements

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 1 – ORGANIZATION AND DESCRIPTION OF BUSINESS

Viral Genetics, Inc. (the “Company” or “Viral”) was incorporated in California on July 11, 1995 and is in the development stage. The Company is engaged in the research and development of therapeutic and diagnostic pharmaceutical and medical products as well as compounds that aid in the production of agricultural products and oils refinable into transportation fuels. The Company was acquired by a Delaware corporation and then became a reporting issuer on October 1, 2001. The Company’s fiscal year-end is December 31.

On October 26, 2010, the Company formed VG Energy, Inc. (“VGE”), a Delaware corporation, to conduct research for certain non-pharmaceutical uses of its Metabolic Disruption Technology (“MDT”), as more fully defined in the assignment agreement between the Company and VGE. At December 31, 2011, the Company owns 80.3% of VGE based upon common shares and preferred shares, on an as converted basis, of VGE issued and outstanding. In 2008, the Company acquired 100% of V- Clip Pharmaceuticals and 49% of White Label Generics, Inc., and in 2009 100% of Carcinotek, Inc. In August 2009 the Company established a wholly-owned subsidiary called MetaCytoLytics, Inc., a California corporation, to pursue the development of its Metabolic Disruption Technology. The Company established a subsidiary in South Africa in 2003 that was subsequently sold in May 2004. Certain litigation that arose in connection with this transaction was settled in December 2010 (see Note 10 – Litigation). Viral owns 100% of a Chinese subsidiary, Viral Genetics Beijing, Ltd., which was organized for prospective operations in China. At this time, the office in China is inactive and there is no financial activity.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies is presented to assist in understanding the financial statements. The financial statements and notes are representations of the Company’s management, which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America (“GAAP”), and have been consistently applied in the preparation of these financial statements.

Management believes that the accompanying unaudited consolidated financial statements as of December 31, 2011 and 2010 and for each of the years ended December 31, 2011 and 2010 have been prepared in accordance with GAAP consistently applied; that all material matters necessary for a fair presentation are included and disclosed to the extent necessary and that all material adjustments have been made.

Going Concern

As of December 31, 2011, the Company had a deficit accumulated during the development stage of approximately \$81.3 million and requires substantial additional funds to continue its research and development, support its operations and to achieve its business development goals. The Company has been able to satisfy certain liabilities with convertible indebtedness and common shares and enter into debt settlement arrangements with vendors and creditors for substantial amounts of its accounts payable obligations. Convertible instruments have also been converted into equity. However, substantial indebtedness remains and substantial recurring losses from operations and new additional liabilities continue.

These factors and uncertainties raise substantial doubt about the Company’s ability to continue as a going concern. The financial statements do not include any adjustments relating to the recoverability and classification of recorded assets, or the amounts and classification of liabilities that might be necessary in the event the Company cannot continue in existence. Management has designed plans for sales of the Company’s future pharmaceutical related products and has entered into development of alternative uses for certain of its technologies through its subsidiary, VGE. Management intends to seek additional capital from new equity securities offerings and from debt financing that will provide funds needed to increase liquidity, fund internal growth and fully implement its business plan. However

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

management can give no assurance that these funds will be available in adequate amounts, or if available, on terms that would be satisfactory to the Company.

An amount of approximately \$3,000,000 is believed necessary to continue operations and support planned development through the next twelve month period. The timing and amount of capital requirements will depend on a number of factors, including the need for funds to support research and development and payment requirements to sustain licensing rights, demand for products and services and the availability of opportunities for international expansion through affiliations and other business relationships.

Consolidated Financial Statements

The accompanying financial statements include those of the Company and its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents.

Development Stage Activities

The Company has been in the development stage since its formation on July 11, 1995. It is primarily engaged in pharmaceutical research and development of its Targeted Peptides Technology (“TPT) and non-pharmaceutical uses of its MDT technology.

Impaired Asset Policy

The Company follows generally accepted accounting policies related to Accounting for the Impairment or Disposal of Long-Lived Assets. This provides for a single accounting model for long-lived assets to be disposed of by sale, including discontinued operations. This policy requires that these long-lived assets be measured at the lower of carrying amount or fair value less cost to sell, whether reported in continuing operations or discontinued operations.

Reclassifications and Restatements

Certain amounts from prior periods have been reclassified or restated with respect to the year ended December 31, 2010 to conform to the current period presentation. These reclassifications have not resulted in any material changes to the Company’s accumulated deficit or the net losses presented.

Research and Development

Research and development expenses are charged to operations as incurred.

Use of Estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities,

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

revenues and expenses. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

Basic and Diluted Net Loss Per Share

The Company computes loss per share in accordance with generally accepted accounting principles which requires presentation of both basic and diluted earnings per share on the face of the statement of operations. Basic loss per share is computed by dividing net loss available to common shareholders by the weighted average number of outstanding common shares during the period. Dilutive loss per share excludes all potential common shares if their effect is anti-dilutive.

Fair Value of Financial Instruments

Fair value is defined as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk including the entity's own credit risk.

A fair value hierarchy for valuation inputs is established. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels and which is determined by the lowest level input that is significant to the fair value measurement in its entirety.

These levels are:

Level 1 – inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.

Level 2 – inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques.

The Company's financial instruments consist of cash, notes payable, accounts payable, accrued expenses, and accrued interest, revolving line of credit and various forms of convertible indebtedness. The carrying value of these financial instruments approximates their fair value based on their liquidity, their short-term nature or application of appropriate risk based discount rates to determine fair value. These financial assets and liabilities are valued using level 3 inputs, except for cash which is at level 1. The Company is not exposed to significant interest, exchange or credit risk arising from these financial instruments, except that certain convertible instruments may be satisfied in shares of common stock at the option of the holder, which per share price can fluctuate.

Stock-Based Compensation

The Company records stock-based compensation by using the fair value method. All transactions in which goods or services are the consideration received for the issuance of equity instruments are accounted for based on the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more reliably measurable. Equity instruments issued to employees and the cost of the services received as consideration are measured and recognized based on the fair value of the equity instruments issued.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Income Taxes

The Company accounts for income taxes using the asset and liability method in accordance with ASC 740, Income Taxes. The asset and liability method provides that deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using the currently enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company has recorded a full valuation allowance to reduce the deferred tax asset associated with the accumulated losses of \$81.3 million to the amount that is more likely than not to be realized.

Recent Accounting Pronouncements

In September 2011, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2011-08, “Intangibles – Goodwill and Other (ASC Topic 350): Testing Goodwill for Impairment” (“ASU No. 2011-08”), which amends guidance for goodwill impairment testing. The amendment allows for entities to first assess qualitative factors in determining whether or not the fair value of a reporting unit exceeds its carrying value. If an entity concludes from this qualitative assessment that it is more likely than not that the fair value of a reporting unit exceeds its carrying value, then performing a two-step impairment test is unnecessary. ASU No. 2011-08 will be effective for public companies for fiscal years beginning after December 15, 2011. The Company does not expect that the adoption of ASU 2011-08 will have an impact on its consolidated results of operations, financial condition or cash flows.

In June 2011, the FASB issued ASU No. 2011-05, “Comprehensive Income (ASC Topic 220): Presentation of Comprehensive Income” (“ASU No. 2011-05”), which amends current comprehensive income guidance. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of stockholders’ equity. Instead, the Company must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. ASU 2011-05 will be effective for public companies for fiscal years beginning after December 15, 2011, with early adoption permitted. In December 2011, the FASB issued an update to ASU No. 2011-05. The update, ASU No. 2011-12, “Deferral of the Effective Date for Amendments to the Presentation of Reclassification of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05” (“ASU No. 2011-12”), defers the effective date of certain presentation requirements within ASU No. 2011-05. The Company does not expect that the adoption of ASU 2011-05 will have an impact on its consolidated results of operations, financial condition or cash flows as it only requires a change in the format of the Company’s current presentation.

Subsequent Events

The Company evaluates subsequent events through the date when financial statements are issued. The Company, which files its financial statements on the OTC Markets, Inc. website, considers its consolidated financial statements issued when they are made available there.

NOTE 3 – PATENTS

Effective in December 2009, the Company agreed to reimburse the University of Vermont and the University of Colorado (together the “Universities”) for certain prior patent costs they incurred for a Metabolic Disruption portfolio totaling approximately \$248,000. On December 3, 2009, the Company issued two 5% Unsecured Convertible Notes to the Universities evidencing these obligations pursuant to the Company’s licensing agreements with these institutions. This amount is included in intangible assets on the accompanying balance sheets. Under the terms of each of the notes, the Company is obligated to pay \$5,000 every quarter in cash or in shares of its common stock at the lower of the then-current

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 3 – PATENTS, continued

market price or \$0.054. The Company also has the right at its election to require the holders to accept prepayment of the entire balance of the notes in cash or shares. Other royalties and milestone payments are payable by the Company upon completion of certain milestones, including FDA clinical trial approval and commercialization, as well as upon sublicensing of the rights. The Company now holds exclusive direct licenses to the underlying patents, patents rights, patent applications and other rights.

In March and April, 2011, the Company and a third party entered into Note Purchase Agreements (the “NPA’s”) and Release and Settlement Agreements (the “RSA’s”) with each University, pursuant to which each University agreed to assign its 5% Debenture, upon satisfaction of all required tranche payments by a third party (“DMBM, Inc.”) to each respective University. The third party simultaneously entered into a Release and Settlement Agreements for each debenture with the Company whereby the debenture plus accrued interest will be completely satisfied with the issuance of shares valued at \$0.01 per share of the Company’s common stock. These shares are issuable to the third party to the extent and in proportion to the third party’s payments stipulated under the NPA. As of the date these agreements were consummated, an aggregate of \$266,547, including accrued interest through the agreement date, was due under these debentures. Assuming complete satisfaction of these debentures by the third party at the original terms, the Company will be required to issue 26,654,700 common shares based upon original terms, plus additional shares for accrued interest through the payment dates. These payments are scheduled to be made in agreed upon monthly installments from April 2011 through September 2011. This schedule has been modified by mutual consent of the parties. In the three months ended June 30, 2011, \$65,000 in payments on the NPA’s were made by the third party for which the Company issued 6,500,000 common shares based upon the original terms. Subsequently the value of the Viral common shares to be issued in satisfaction was reduced. In November 2011 an additional \$55,000 in payments were made under this arrangement resulting in the issuance of 22,000,000 shares. Based upon the current terms, an additional 58.6 million common shares would need to be issued to satisfy the remaining principal balance of \$128,100 outstanding as of December 31, 2011. These payments have been accounted for as a reduction of Convertible notes –patents in the accompanying balance sheet. Interest expense includes a non-cash charge in of \$580,200 representing the excess of the fair value of the shares issued over the cost ascribed in these transactions. Additional non-cash interest expense will be recorded for each future cash payment for the difference between the fair value per share and the agreed upon modified issuance price per share of \$0.0025.

NOTE 4 - ACQUISITIONS/BUSINESS FORMATION

VG Energy, Inc.

On October 26, 2010, the Company formed VGE to exploit opportunities related to applications of its Metabolic Disruption technology. Through manipulation of a metabolic pathway in algae and other plant cells the Company believes it can further develop and commercialize augmentation of the production of certain oils including refinable algae-oils for biofuels and high-value oils used in cosmetics, food and nutraceuticals such as omega-3 fatty acids, corn oil and palm oil.

VGE’s articles of incorporation authorize 130,000,000 shares, par value \$0.001 per share, of any class of stock. On formation VGE issued to the Company 30,000,000 shares of its common stock and 3,000,000 shares of its Series A Preferred Stock for consideration of \$33,000 (par value). The Company granted to VGE an exclusive worldwide royalty-free license to research, develop, market and commercialize related Company patent and patent rights as specified in the agreement (“Metabolic Exclusive License Agreement”), provided that the license shall be restricted to applications in agriculture, energy generation and yield enhancements of plants and oils. This license shall automatically include any new inventions, patents or know-how acquired by the Company or VGE that are within the scope of this license.

In November 2010, the Company sold four VGE Units at \$25,000 per Unit to investors and received \$100,000 in proceeds. These investors received an aggregate of 600,000 VGE common shares, 60,000 VGE preferred shares and warrants to purchase 600,000 VGE common shares for 5 years at exercise price of \$0.25 per share. Further, the Company issued these VGE investors warrants to purchase an aggregate of 1,833,333 shares of common stock of the Company for

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 4 - ACQUISITIONS/BUSINESS FORMATION, continued

five years at \$0.05 per share with respect to 1,000,000 shares and \$0.06 per share with respect to 833,333 shares. The fair value of the Company warrants of \$38,500, determined using the Black-Scholes option pricing model, is reflected as an allocation of additional paid-in capital. The arrangement extended certain antidilution protection to the initial investors for each class of VGE stock such that their percentage ownership of VGE will not be diluted up to the issuance of 25% of the shares of each class of VGE stock. Consequently the initial 7.5 million VGE common shares and 750,000 VGE preferred shares issued to investors will reduce the shares held by the Company by an equal number of shares in order to maintain that percentage. In the periods presented, the issuances to VGE investors reduced directly the Company's holdings in VGE.

In the year ended December 31, 2011, the Company received \$500,000 in proceeds (\$485,000 after cash commissions) for the sale of additional VGE Units. These investors received an aggregate of 3,000,000 VGE common shares; 300,000 VGE preferred shares; warrants to purchase 3,000,000 VGE common shares for 5 years at exercise price of \$0.25 per share; and warrants to purchase 300,000 preferred shares at \$2.50 per share. Further, the Company issued certain of these VGE investors warrants to purchase an aggregate of 3,333,333 shares of common stock of the Company for five years at \$0.06 per share. The fair value of the Company warrants of \$90,000, determined using the Black-Scholes option pricing model, is reflected as an allocation of additional paid-in capital. The Company also incurred commissions of \$15,000, included in accrued expenses, and \$40,000, satisfied by the issuance of 240,000 VGE shares and 24,000 preferred VGE shares.

An investor that purchased 9 of these units, upon becoming a member of the Board of Directors, will also receive an option to purchase 1,500,000 shares of VGE common stock exercisable at \$0.083 per share and an option to purchase 150,000 shares of VGE preferred stock exercisable at \$0.83 per share. These options have a five year life from the date of grant and, upon becoming a member of the Board of Advisors, will begin to vest over a three year period with respect to half of these options and upon receipt of additional financing in the first year for the remainder.

At December 31, 2011 and 2010, the aforementioned issuances directly reduced the Company's holdings in VGE as a result of anti-dilution protection rights extended to investors in the VGE Units.

After the effect of these antidilution provisions included in these transactions, the Company effectively owns 22,831,693 shares of VGE common stock and 2,616,000 shares of VGE Series A Preferred Stock, representing 81.65% of the equity and 81.68% of the voting rights in VGE, assuming the preferred shares were converted into common stock. In accordance with the agreements, related warrants are not considered in this determination.

The amount attributable to the equity in the assets of the noncontrolling interests of the investors as of December 31, 2011 was \$114,950, reduced by an allocated share of net losses of \$73,773 since the inception in 2010 in VGE. This results in a noncontrolling interests having net equity of \$41,177 at December 31, 2011.

Among other things, the Certificate of Designation for the VGE Series A Preferred Shares provides that each share is exchangeable into shares of common stock at the rate of ten (10) shares of common stock for each share of Series A preferred stock. The Series A Preferred Shares have an aggregate liquidation preference of \$1,000,000 such that in the event of the dissolution, winding-down, or other liquidation of the Company the Series A Preferred Shares holders shall receive the first \$1,000,000 of net proceeds after payment of debts. Following the payment of this liquidation preference, the holders of common stock would receive the next \$1,000,000 of net proceeds. All other remaining net proceeds would then be split ratably between the Series A preferred stockholders and common stockholders on an as-converted basis. The effect of the liquidation preference is to subordinate the claims of the common stockholders on residual net proceeds after such a winding down, liquidation or dissolution, and to reduce by \$1,000,000 the overall claims common stockholders hold on residual assets after payment of debts. The Series A Preferred Shares are not redeemable by VGE, and rank on par with Company common stock in the payment of dividends of any kind being declared on common stock. There is no sinking fund provision for the Series A Preferred Shares. The issued Series A Preferred Shares vote as common stock in all matters presented to stockholders for approval, but have special voting rights such that the aggregate of all then issued, outstanding

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 4- ACQUISITIONS/BUSINESS FORMATION, continued

and unconverted Series A Preferred Shares possesses a number of votes equal to all of the then issued and outstanding common shares of VGE multiplied by 1.01. The effect of the voting rights is that the holders of common stock by definition possess fewer aggregate votes than the aggregate votes of the then issued, outstanding and unconverted Series A Preferred Shares stockholders. The holders of a majority of the then issued and outstanding Series A Preferred Shares have the authority to require all holders of Series A Preferred Shares to exercise the conversion feature described above. Other than when transferred for estate planning purposes, the Series A Preferred Shares automatically convert to common shares upon a transfer outside of the control of the original investor.

NOTE 5 – COMMITMENTS AND CONTINGENCIES

Employment and Consulting Agreements

In the year ended December 31, 2011, a former officer and now a consultant to the Company agreed to the satisfaction of \$300,000 of convertible notes issued for compensation and \$29,885 in accrued interest in exchange for an aggregate of 19,762,001 shares of common stock and a five year warrant to purchase 9,071,071 common shares of common stock of the Company at \$0.036 per share expiring February 1, 2016. The excess of the fair value of these warrants (determined utilizing the Black-Scholes option pricing model) over the consideration paid in the amount of \$375,000 was included in non cash interest expense for the year ended December 31, 2011. At December 31, 2011, the balance outstanding under this arrangement approximated \$29,500, including accrued interest.

In January 2011:

- a. The Company entered into employment and consulting agreements with its President and CEO and various consultants requiring annual base salaries and fees aggregating \$744,000 in each year from 2011 through 2015 aggregating \$3,720,000; aggregate options to purchase 42 million common shares in 2011 and 11,500,00 in each year for the period 2012 to 2015 aggregating 88 million shares. The options are issuable annually. Their exercise price will be the VWAP based upon the 20 days after the grant date and will be fully vested on grant and expire in December 2018. The options also include cashless exercise rights. The agreements are generally cancellable by the Company with a one year severance provision in the event of termination without cause by the Company, or no severance if terminated by the Company in the event of “good reason” as defined in the agreements. Otherwise, no severance is due. The options granted for 2011 have an exercise price \$0.042 per share. Results of operations for the year ended December 31, 2011 includes stock based compensation of \$1,092,000. This represents the fair value of the options vesting in the year ended December 31, 2011 determined using the Black-Scholes option pricing model. The consulting agreements with M. Karen Newell-Rogers (“Newell”), Chief Scientist, and one other consultant provide for royalties based on sales. Each party also entered into a non-interest bearing Unsecured Revolving Credit Note with the Company, which provides for the conversion of unpaid compensation under these employment and consulting into shares of the Company based upon 80% of the VWAP as of the date of any conversion. The holder can elect to convert at any time, to the extent not paid or previously converted. At maturity, any unpaid or unconverted balance shall automatically convert without action by either the Company or the holder. Under her agreement, Newell received 5 million common shares of the Company as a signing bonus in consideration of past service and for entering into this agreement. The fair market value of these shares of \$147,000 is included in research and development expense for the year ended December 31, 2011; and
- b. VGE entered into employment and consulting agreements with its president and CEO and consultants requiring annual base salaries and fees aggregating \$360,000 in each year from 2011 through 2015 aggregating \$1,800,000; aggregate options to purchase 4.1 million shares in 2011

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 5 – COMMITMENTS AND CONTINGENCIES, continued

and 1,025,000 in each year for the period 2012 to 2015 aggregating 8,200,000. The options are issuable annually. Their exercise price will be at the VWAP based upon the 20 days after the grant date and will be fully vested on grant and expire in December 2018. The options also include cashless exercise rights. The agreements are generally cancellable by the Company with a one year severance provision in the event of termination without cause by the Company, or no severance if terminated by the Company in the event of “good reason” as defined in the agreements. Otherwise, no severance is due. The consulting agreement with Newell provides for royalties based on sales. Each party also entered into a non-interest bearing Unsecured Revolving Credit Note with the Company, which provides for the conversion of unpaid compensation into shares of the Company based upon 80% of the VWAP as of the date of any conversion. The holder can elect to convert at any time, to the extent not paid or previously converted. At maturity, any unpaid or unconverted balance shall automatically convert without action by either the Company or the holder. Further, under these agreements, an aggregate of \$276,250 in accrued compensation was converted into 4,123,130 common shares of VGE in the year ended December 31, 2011.

Other

Under an Assignment of Patent agreement between the Company and Therapeutic Genetics, Inc. (“TGI”), the Company, among other things, is obligated to pay a royalty of 5% of the gross sales of any products derived directly from an early technology studied by the Company. Subsequently, that royalty was assigned to Therapeutic Genetics, LLC. The royalty is payable for a period equal to the life of the patent underlying the products being sold. The owners of Therapeutic Genetics LLC are substantially the same as the original founders of the Company.

The Company and Imperial Consulting Network, Inc. (“ICN”) entered into an agreement effective on January 1, 2010 and expiring December 31, 2010 with comparable terms and conditions related to the preceding investor relations agreement between the parties. Under the 2010 agreement, ICN was entitled to receive 4 million common shares. The fair market value of these shares of \$200,000 as of that date was included in accrued expenses at December 31, 2010. The 4,000,000 million shares were issued in January 2011 in satisfaction of this accrual. Additional common shares and three year warrants to purchase additional shares were not issuable since contractually stipulated stock price milestones were not met in the period. Effective in January 2011, the Company and Imperial Consulting Network, Inc. (“ICN”) terminated their Marketing Advertising and Financial Agreement originally intended to be effective for the period from December 1, 2010 through November 30, 2011. The Company accrued \$160,000 in connection with this termination as of December 31, 2011. The amount was satisfied with the issuance of 8 million shares of common stock of the Company.

Effective October 1, 2009, the Company entered into a fifteen month financial consulting agreement expiring December 31, 2010 with JTL Enterprises, Inc. (“JTL”) to provide SEC accounting and financial reporting services. Compensation is comprised of 2 million shares of restricted common stock of the Company, warrants (5 year life) to purchase an additional 2 million shares of common stock at prices ranging from \$0.03 to \$0.06 per share and the payment of \$3,000 per month commencing on November 1, 2009 through December 31, 2010. The fair value of this stock based compensation was expensed ratably over the period of service, approximately \$177,000 expensed in the year ended December 31, 2010. In accordance with the terms of the agreement, an additional 500,000 restricted common shares and warrants to purchase 500,000 restricted common shares expiring in December 2015 were issued in satisfaction of unpaid fees of \$15,000. The fair value of these warrants of \$13,000 (determined using the Black-Scholes option pricing model) is included in results of operations for the year ended December 31, 2010. For the year ending December 31, 2011, JTL and the Company have entered into an agreement for similar services, with compensation comprised of 2 million shares of restricted common stock of the Company, warrants (5 year life) to purchase an additional 2 million shares of common stock at prices ranging from \$0.02 to \$0.05 per share and a monthly fee \$3,000 per month commencing January 2011.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 5 – COMMITMENTS AND CONTINGENCIES, continued

Total expense for the year ended December 31, 2011 approximated \$148,000, including \$112,000 in stock based compensation. For the year ending December 31, 2011, JTL and the VGE have entered into an agreement for similar services, with compensation comprised of 1 million shares of restricted common stock of the Company, warrants (5 year life) to purchase an additional 1 million shares of common stock at prices ranging from \$0.02 to \$0.05 per share and the payment of \$1,500 per month commencing January 2011. Total VGE expense for the year ended December 31, 2011 approximated \$74,000, including \$56,000 in stock based compensation. At December 31, 2011, \$41,000 in accrued fees under these agreements is included in accounts payable. The parties are currently negotiating satisfying certain amounts of these fees in common shares of the Company.

In 2009 the Company entered into an investor relations agreement with Institutional Analyst, Inc. (“IA”) for a six month period. Compensation for these services included the issuance of 1 million shares of common stock at \$0.01 per share valued at \$10,000 and warrants exercisable at an average of \$0.075 per share for 5 years to buy 2 million shares of common stock, valued at \$13,000. In February 2010 the Company again retained IA for a renewable six month period. Compensation for these services included the issuance of 1 million shares of common stock valued at \$0.02 per share valued at \$50,000 and warrants exercisable at an average of \$0.075 per share for 5 years to buy 2 million shares of common stock, valued at \$88,000. An additional 1 million shares were issued for services in the year ended December 31, 2011 with a fair value of \$40,000, which was expensed in the period.

On August 5, 2010, the Company entered into an agreement with Patton Capital Corp. (“Patton”), a Canadian company, which provides for Patton to make introductions for the purpose of securing a transaction on a non-exclusive basis or listing either through direct or indirect introductions on an exclusive basis. A transaction, which would be at the discretion of the Company, would result in any business development opportunity or cash funding, including licensing, research funding, grants, partnerships, joint ventures, and public or private financings whether by debt or equity or a combination of both. The initial term of the agreement is for a 12 month period, renewable at the option of the Company. On October 28, 2010, the agreement was amended to include origination of financing for any subsidiary of the Company, including VGE and MetaCytoLytics. Patton shall receive a monthly fee of \$8,000, payable in cash or shares of the Company as mutually agreed. In June 2011, Patton elected to convert \$61,500 in accrued monthly fees and received 1,762,062 shares of Company common stock. Subsequent to December 31, 2011, the parties agreed to the issuance of 3,681,536 shares of Company common stock to satisfy \$72,000 outstanding as of year end. Upon the occurrence of any form of transaction or listing initiated by Patton, Patton would be entitled to a warrant to purchase 11 million common shares of the Company at the lower of \$0.041 per share or the valuation of the Company’s common shares in any transaction or listing. As more fully described in Note 4 – VGE, Patton arranged certain equity financing in that transaction. As a result, the Company issued Patton a warrant to purchase 11 million common shares exercisable at \$0.025 per share through November 16, 2015. The fair value of this warrant of \$242,000 was determined using the Black-Scholes option pricing model with the following assumptions: expected life of 5 years, risk free interest rate of 1.49%, a dividend and forfeiture rate of 0% and a volatility of 143%. This amount is reflected as a component of Additional paid-in capital. The agreement was subsequently amended to include transactions relating to the Company and its subsidiaries.

NOTE 6- REVOLVING LINE OF CREDIT – Related Party

In October 2007, Soh Teck Toh, an affiliate of the Company’s President, exchanged debts totaling \$348,000 owed to him by the Company for cash advances made by him to the Company for 5,800,000 shares of common stock and 11,600,000 warrants to acquire common stock. Effective in March 2008, it was agreed that the indebtedness of the Company to Soh Tech Toh would be included as part of the revolving line of credit arrangement with Best and Best is considered an entity affiliated with Mr. Toh, and Haig Keledjian, CEO, President and a principal shareholder of the Company.

On March 5, 2008, Best Investments, Inc. (“Best”), entered into a Debt Restructuring Agreement with the Company whereby the Company and Best agreed to restructure \$1,508,302 in outstanding indebtedness and accrued

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 6- REVOLVING LINE OF CREDIT – Related Party, continued

interest. The original convertible indebtedness, which had previously been extended, matured on March 29, 2008. The Restructuring Agreement converted the existing indebtedness to a secured revolving line of credit (“RLC”) that is collateralized by substantially all of assets of the Company. The revolving line of credit matures December 31, 2013, bears interest at the rate of 5% per annum, payable at the maturity date. The obligations under the revolving line of credit may be prepaid at any time and may be exchanged for common stock and warrants. The conversion price is equal to the volume-weighted closing price of common stock of the Company for the 20 trading days preceding notice of conversion by Best. For each share of stock issued for conversion of obligations, Best will receive a warrant to purchase a share of common stock for 150% of the price at which obligations under the revolving line of credit were converted. The warrant expires five years from the date of issuance. The amount Best agreed to lend under the revolving line of credit was not limited. The obligations of the Company under the revolving line of credit are guaranteed by Viral Genetics, Inc., a California corporation and wholly-owned subsidiary.

The outstanding principal balances of the RLC and related accrued interest as of December 31, 2011 and December 31, 2010 were \$711,872 and \$941,087, respectively. In the year ended December 31, 2011, \$52,855 in principal under the RLC was satisfied with the issuance of 2,642,750 shares of common stock and the issuance of warrants to purchase 5,285,500 shares of common stock of the Company for a two year period at \$0.03 per share. The fair market value of these warrants, determined using the Black-Scholes option pricing model, of \$64,400 was charged to interest expense – non-cash in the year ended December 31, 2011.

In January 2010, \$373,007 in principal was satisfied by the issuance of 18,700,659 shares of common stock and warrants to purchase 40,167,385 shares of common stock at \$0.03 expiring in January 2012. The fair value of these warrants determined using the Black-Scholes option pricing model of \$1,687,030 is included in interest expense for the year ended December 31, 2010. Of these shares and warrants, 50,000 shares and warrants to purchase 100,000 common shares for two years at \$0.03 per share were acquired by Soh Teck Toh for approximately \$1,000.

In July, 2010, an aggregate of \$154,568 in principal of the RLC was satisfied by the issuance of 7,728,067 shares of common stock and warrants to purchase 15,456,734 shares of common stock at \$0.03 per share, expiring in July 2012. The fair value of these warrants determined using the Black-Scholes option pricing model of \$479,159 is included in interest expense for the period.

On October 12, 2010, \$112,453 in principal of the RLC was satisfied by the issuance of 5,622,668 shares of common stock and warrants to purchase 11,245,336 shares of common stock at \$0.03 per share expiring through October 12, 2014. The fair value of these warrants determined using the Black-Scholes option pricing model of \$269,888 is included in interest expense for the period.

On November 11, 2010, \$10,562 in principal of the RLC was satisfied by the issuance of 528,100 shares of common stock and warrants to purchase 1,056,200 shares of common stock at \$0.03 per share expiring through November 10, 2014. The fair value of these warrants determined using the Black-Scholes option pricing model of \$15,843 is included in interest expense for the period.

On December 8, 2010, \$24,813 in principal of the RLC was satisfied by the issuance of 1,240,667 shares of common stock and warrants to purchase 2,481,334 shares of common stock at \$0.03 per share expiring through December 8, 2014. The fair value of these warrants determined using the Black-Scholes option pricing model of \$42,183 is included in interest expense for the period.

These securities issued to Mr. Toh were issued under Regulation S.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 7 – CONVERTIBLE PROMISSORY NOTES PAYABLE AND OTHER INDEBTEDNESS

- a. In the period from October 1, 2007 through December 31, 2010, the Company received services from Wonderland Capital Corp (“Wonderland”) related to meetings and/or conferences to meet with potential investors, potential joint venture and strategic partners, potential board members and other third parties. Effective on March 10, 2010, the Company issued its Promissory Note for these services to that date, bearing interest at 6% per annum and due on demand, in the amount of \$226,866. This represents the amounts due to Wonderland for services rendered to March 10, 2010 comprised of management fees of \$180,000 and unreimbursed expenses paid by Wonderland of \$46,866. Pursuant to the terms of the Promissory Note and upon election by Wonderland, in March, 2011 the Company issued 22,686,614 of its common shares at \$0.01 per share in full satisfaction. Accrued interest related to this note was waived based on terms of the Promissory Note since the principal was satisfied with Company shares. For the period March 10, 2010 through December 31, 2010 an additional \$57,297 was incurred and included in accrued expenses on December 31, 2010. Services were comprised of management fees of \$45,000 and unreimbursed expenses of \$12,297 paid by Wonderland. In April 2011, upon election by Wonderland, the Company issued its Promissory note bearing interest at 6% per annum and due on demand, in the amount of \$57,297 to evidence its obligations for these services. This note is convertible into 5,729,697 common shares at the option of Wonderland. Effective May 21, 2010, the Company issued a convertible debenture to Wonderland in the amount of \$183,758 for cash advances received from Wonderland and another entity affiliated with Wonderland (DMBM), pursuant to an agreement between those parties. This debenture is due on December 31, 2011 and bears interest at 0.35% per annum. The Company, at its sole option, can satisfy this obligation on maturity in cash or in shares of its common stock at the conversion price. Alternatively, Wonderland may at its option at any time convert the minimum principal amount of \$25,000 and integral multiples of \$5,000 thereafter at the conversion price. The conversion price shall be the lower of \$0.02 per share or the lowest price per share at which the Company issues shares of its common stock while this debenture is outstanding, but in no event less than \$0.005 per share. In April 2011, Wonderland elected to convert \$177,160 of this note and received 35,432,000 shares of common stock of the Company. In August 2011, Wonderland converted \$20,000 of this amount and received 4,000,000 restricted shares of common stock of the Company. In October 2011, Wonderland converted \$15,000 of this amount and received 3,000,000 restricted shares of the Company. The amount remaining outstanding as of December 31, 2011 on these arrangements with Wonderland was \$28,895.

Pursuant to a letter agreement dated March 25, 2011, the Company entered into an arrangement with Wonderland to borrow \$100,000. DMBM, as a consequence of providing funds to Wonderland, entered into an agreement effective March 25, 2011 whereby Wonderland assigned all of its rights title and interest to the benefits of the arrangement as described to DMBM. The funds were received in March 2011, and are included in convertible promissory notes in the accompanying unaudited balance sheet as of December 31, 2011. Proceeds are intended to be used by the Company to pay all costs necessary to fund a “fast track” test of algae oil production-increasing additives by the Company’s subsidiary, VG Energy, Inc. and the remainder for general corporate purposes. The loan is evidenced by a convertible promissory note due (for which the Company substituted a Promissory Note dated March 25, 2011) March 25, 2012 with interest at 5% per annum. Upon maturity DMBM elected to convert the principal balance into shares of Company common stock and received 40 million shares. In consideration of making the loan, the Company also agreed to issue to DMBM 500,000 shares of the Company’s Series A Preferred Stock (see Note 8) and an option to purchase 10 VGE Units at \$25,000 per VGE Unit originally expiring March 25, 2012. The parties are currently negotiating extending this expiration date. Each VGE Unit is comprised of the following: (i) one hundred fifty thousand (150,000) shares of VGE common stock; (ii) fifteen thousand (15,000) shares of VGE Series A Preferred Stock; and (iii) a five year warrants to acquire one hundred fifty thousand (150,000) shares of VGE common stock at an exercise price of \$0.25 per share (the “VGE Warrants”). The fair value of the Series A Preferred Stock of the Company issued in this transaction was deemed to be the market value of the 5 million common shares of the Company on March 25, 2011, into which these preferred shares were convertible, or \$225,000. This amount was initially accounted for as deferred interest expense and was

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 7 – CONVERTIBLE PROMISSORY NOTES PAYABLE AND OTHER INDEBTEDNESS, continued

reflected as a reduction of equity. This amount was expensed in the year ended December 31, 2011 as non-cash interest expense.

- b. As part of a December 29, 2010 Release and Settlement Agreement between the Company and Timothy & Thomas, LLC ("T&T") the Company is obligated to T&T for a total of \$1,900,000 payable over the course of three years, as follows: \$1,000,000 by November 1, 2011; \$450,000 by November 1, 2012; and \$450,000 by November 1, 2013. These obligations are evidenced by a Convertible Debenture (the "Debenture") bearing interest at the stated rate of 0.35% per annum. Subject to certain terms and conditions of the Debenture, the Company may elect to make these installment payments in cash or in shares of Company common stock. The conversion price for a payment in shares on a due date is equal to the 20-trading day volume-weighted average closing price ("VWAP") of the shares for the period ending the day prior to each installment due date, not to exceed \$0.15. Further, if the VWAP of the Company's common shares with respect to a due date is at or above \$0.20, the option to receive payment in shares or cash is to be at T&T's discretion. All or any part of the Debenture may be prepaid in cash or stock at any time without penalty, provided that the shares used for prepayment are either registered for resale or may be sold under an exemption from registration. The Company can also direct T&T to assign all or any part of the Debenture to a third party for cash payment at any time. The Debenture ranks junior in security to the note held by Best Investments, Inc. (controlled by Haig Keledjian, Company President) (see Note 6), but will rank senior to any subsequent debt issued by the Company. Unpaid principal and interest under the Debenture is accelerated under certain terms and conditions. Payment would be accelerated in the event of a Change in Control, as defined in the agreement, prior to the maturity date of the Debenture and if the Debenture has not otherwise been paid in full.

On November 8, 2011, the Company issued 81,655,691 of its common shares in satisfaction of a \$1,000,000 principal payment, plus \$6,982 of accrued interest, due under the settlement agreement.

For financial reporting purposes, the series of future payments in the gross amount of \$1,900,000 were initially recorded at their fair value of \$1,668,953 (of which \$925,926 net of discount was current as of the transaction date) determined utilizing a discount rate of 8% per annum in excess of the stated rate of the Debenture, which resulted in a discount of \$231,047. Interest expense for the year ended December 31, 2011 includes accretion of \$122,000 of this debt discount. This results in a remaining net balance of these future payments as of December 31, 2011 of \$813,169 of which \$390,947 is included in current liabilities and \$422,222 is included in noncurrent. An additional \$6,100 of interest expense based upon the stated interest rate of the Debenture is included in the results of operations for the year ended December 31, 2011.

- c. In the year ended December 31, 2010, the Company satisfied approximately \$65,000 in accrued interest relating to convertible debentures as well as other indebtedness with the issuance of 2,327,900 common shares and warrants to purchase 208,333 common shares at \$0.15 per share through August 5, 2011. Accrued interest remaining to be paid in the future is included in the accompanying December 31, 2010 balance sheet. In the year ended December 31, 2011, the Company satisfied approximately \$94,395 in accrued interest and interest dilution adjustments relating to convertible debentures with the issuance of 9,974,231 common shares. Further, an additional 117,521 common shares of the Company were issued pursuant to certain cashless exercise and ratchet protection provisions.
- d. In the year ended December 31, 2011, the Company received proceeds of a convertible debenture dated November 3, 2011 and December 31, 2011 of \$616,700 and \$103,000, respectively DMBM. The Company issued convertible debentures evidencing these obligation with the following terms and conditions: (i) debenture bears interest at the rate of 1% per annum from the date of each loan (ii) principal and accrued interest is due in one year (iii) payments due may be made in cash or in shares of its common stock at the

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 7 – CONVERTIBLE PROMISSORY NOTES PAYABLE AND OTHER INDEBTEDNESS, continued

sole discretion of the Company iv) indebtedness under this debenture shall be senior to future indebtedness and obligations of the Company and (v) all or any portion of the debenture may be converted into common shares of the Company at the option of DMBM. The price per share for purposes of (ii) and (v) shall be the lower of \$0.02 per share or the lowest price at which the Company issues shares of its common stock while any of the indebtedness under these debentures is outstanding, but in no event less than \$0.0025 per share (\$.005 for conversions prior to the November 3, 2011). The Company is also obligated to promptly file a Regulation A Offering Statement with the SEC and use its best efforts to cause the Offering to be reviewed and approved by the SEC as soon as possible. The Offering Statement is to be available to be used for shares of Company common stock issued upon any conversion of this debenture or any common shares used by the Company to pay any debenture outstanding principal and accrued interest. In the year ended December 31, 2011, DMBM elected to convert a total of \$91,598 in principal and received 23,319,600 common shares of the Company. The principal amount outstanding under these debentures \$632,502 at December 31, 2011, was included in Convertible promissory notes in the accompanying balance sheet.

NOTE 8 – PREFERRED STOCK

The Series A Preferred Shares are not redeemable by the Company, and rank on par with Company common stock in the payment of dividends of any kind being declared on common stock. There is no sinking fund provision for the Series A Preferred Shares. The issued Series A Preferred Shares vote as common stock in all matters presented to stockholders for approval, but have special voting rights such that the aggregate of all then issued, outstanding and unconverted Series A Preferred Shares possesses a number of votes equal to all of the then issued and outstanding common shares of the Company multiplied by 1.01. The effect of the voting rights is that the holders of common stock by definition possess fewer aggregate votes than the aggregate of the then issued, outstanding and unconverted Series A Preferred Shares stockholders. Series A Preferred Shares are exchangeable into shares of common stock at the rate of ten (10) shares of common stock for each share of Series A preferred stock. The Series A Preferred Shares have an aggregate liquidation preference of \$1,000,000 such that in the event of the dissolution, winding-down, or other liquidation of the Company the Series A Preferred Shares holders shall receive the first \$1,000,000 of net proceeds after payment of debts. Following the payment of this liquidation preference, the holders of common stock would receive the next \$1,000,000 of net proceeds. All other remaining net proceeds would then be split ratably between the Series A preferred stockholders and common stockholders on an as-converted basis. The effect of the liquidation preference is to subordinate the claims of the common stockholders on residual net proceeds after such a winding down, liquidation or dissolution, and to reduce by \$1,000,000 the overall claims common stockholders hold on residual assets after payment of debts

The holders of any majority of the then issued and outstanding Series A Preferred Shares have the authority to require all holders of Series A Preferred Shares to exercise the conversion feature described above. Other than where transferred for estate planning purposes, the Series A Preferred Shares automatically convert to common shares upon any transfer.

NOTE 9 – COMMON STOCK

Effective January 3, 2011 the Company amended its Articles of Incorporation in Delaware increasing its authorized share capital to a total of 1,750,000,000 of which 1,500,000,000 are common shares and 250,000,000 are preferred shares. This modification in the share capital has been given retroactive effect in the accompanying balance sheets.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 9 – COMMON STOCK, continued

The Company has reserved the following shares for issuance or conversions related to outstanding stock options, warrants and convertible securities based upon transactions consummated through December 31, 2011:

Conversion of 4.75 million Series A Preferred Shares	47,500,000
Revolving Line of Credit and accrued interest – related party	35,594,000
Unsecured Convertible Debenture – patents, (DMBM satisfaction arrangement)	51,243,000
Convertible debenture – TT legal settlement (\$0.015 per share VWAP assumed)	54,211,000
Convertible promissory notes	300,456,000
Consultant Notes and accrued interest	5,000,000
Employee/consultant common stock purchase options (a)	65,100,000
Common stock purchase warrants	232,658,000
Reserved for accounts payable and other	<u>10,000,000</u>
	<u>801,762,000</u>

(a) These option agreements provided for an additional 11.5 million options be granted for each of the next four years to all of these grantees so long as each remains employed, or an aggregate of 46 million options. The grant price shall be the 20-day VWAP determined on the grant date in each year.

Substantially all warrants and conversion rights were exercisable at December 31, 2011, certain of which had exercise prices in excess of the closing market price per share of the Company's common stock. Employee and consultant warrants vest over a four year term. If all holders with the right to exercise elected to exercise as of December 31, 2011, the Company would not have enough authorized shares of Common Stock and would be required to amend its Articles of Incorporation.

On November 8, 2010, the holder of 250,000 shares of the Company's Series a Preferred Shares received in the Carcinotek transaction elected to convert those shares into 2,500,000 shares of common stock. On January 18, 2011, a consultant to the Company converted 500,000 shares of the Company's Series A Preferred Shares received in the Carcinotek transaction into 5,000,000 shares of common stock.

In the year ended December 31, 2010 the Company sold 12 million common shares for net proceeds of \$82,552, after giving effect to a reduction in the price per share with respect shares originally sold in this offering pursuant to SEC Rule 504 of the Securities Act of 1933. An amount of \$9,500 remains due to the Company and is included in Deferred costs and subscriptions receivable, principally related to the reconciliation of discrepancies. This is reflected as an increase of Stockholders Deficit in the accompanying balance sheet as of December 31, 2011.

In the year ended December 31, 2011, the Company received \$91,000 in proceeds and issued 7,300,000 common shares and warrants to purchase 11,500,000 common shares at prices ranging from \$0.05-\$0.08 per share. The warrants expire at various dates through April 2014. The fair value of these warrants of \$97,600 based upon the Black-Scholes option pricing model is reflected as an allocation of Additional paid-in capital since these warrants are associated with the sale of common shares.

VIRAL GENETICS, INC. AND SUBSIDIARIES
(A DEVELOPMENT STAGE COMPANY)
Notes to Consolidated Financial Statements
Years Ended December 31, 2011 and 2010

(Unaudited)

NOTE 9 – COMMON STOCK, continued

In the year ended December 31, 2011, the Company entered into the following additional transactions not described elsewhere herein:

- (i) In February 2011 a final payment in the amount of \$41,667 made by a third party (DMBM, Inc.) in a debt settlement transaction (included in unsecured convertible notes at December 31, 2010), for which the company issued the third party 4,166,667 common shares. The Company recorded a charge to interest expense – non-cash of \$150,416 representing the excess of the fair value of the shares issued as compared to the liability settled.; in April and June 2011, the Company issued to a third party (DMBM, Inc.) 6.5 million common shares for payments aggregating \$65,000. Interest expense – non cash of
- (ii) \$142,200 representing the excess of the fair value of the shares issued over the cost ascribed to the debt satisfied was recorded. Refer to Note 3.
- (iii) An aggregate of 8,050,000 common shares with a fair value of \$253,500 were issued for services in the year ended December 31, 2011 – 2,050,000 shares to consultants; 1,000,000 to an investor relations consultant; and 5,000,000 shares pursuant to an employment agreement as described in Note 5a.

NOTE 10 – LITIGATION

Lawsuit Relating to Harry Zhabilov, Jr. and Jordanka Zhabilov

On February 9, 2012, the Company entered into a Settlement Agreement and Mutual Release of Claims with Harry H. Zhabilov and related parties (“Zhabilov Parties”) effectively ending litigation and outstanding claims and complaints brought by them, and vice versa. As part of this settlement, the Zhabilov Parties agreed to return to the Company all shares, ownership interests, royalties and other value in the Company, its technology, and related entities. In addition, the Company entered into a Non-License Commission Agreement with some of the Zhabilov Parties that will pay the Company a commission on any sales of a product currently being developed by them; and, similarly, the Company agreed to pay to the Zhabilov Parties a commission on any sales of a product based on an older patent which are not currently in development or expecting any revenue from.

NOTE 11 - SUBSEQUENT EVENTS

In January 2012, a termination payment of 8,000,000 common shares of the Company was paid to Wonderland Capital.

In February 2012, the Company agreed to issue 6,923,070 of its common shares in satisfaction of \$90,000 in outstanding fees to a legal advisor. Of this amount, \$72,500 was accrued at December 31, 2011.