



*Celebrating 30 years of innovation in 2009*

# ANNUAL REPORT | 09



Human Health	Food Safety	Animal Health
<b>Bioniche Therapeutics</b> <ul style="list-style-type: none"> <li>• Drug discovery &amp; development</li> <li>• Products based on proprietary technologies</li> <li>• Development: bladder cancer, peritoneal cancer, other cancers</li> </ul>	<b>Bioniche Food Safety</b> <ul style="list-style-type: none"> <li>• Development of animal vaccines to help enhance food &amp; water safety</li> <li>• <i>E. coli</i> O157 cattle vaccine fully licensed in Canada</li> <li>• Other animal vaccines in pipeline (<i>Salmonella</i>, <i>Campylobacter</i>, <i>Listeria</i>)</li> </ul>	<b>Bioniche Animal Health</b> <ul style="list-style-type: none"> <li>• Largest Canadian-owned animal health company</li> <li>• Foci: reducing reliance on antibiotics (immunology); enhancing reproductive performance; and preventing illness (vaccines)</li> </ul>

Bioniche Life Sciences Inc. is a publicly-traded company, listed on the Toronto Stock Exchange under the symbol "BNC" since 1999. The corporate headquarters are located in Belleville, Ontario, Canada, and the Company owns and operates various offices and manufacturing plants in Canada, the United States, Europe, and Australia. Bioniche employs approximately 187 individuals.

## Fiscal 2009 Financial Highlights

	Year ended June 30, 2009	Year ended June 30, 2008	Year ended June 30, 2007
Revenue	33,281,029	27,468,085	27,479,727
Net loss	(10,500,504)	(16,255,708)	(14,760,994)
Basic and fully diluted net loss per share	(0.15)	(0.26)	(0.32)
Total assets	34,641,440	34,623,010	41,526,774
<b>Long-term Liabilities</b>			
Long-term debt	1,148,706	1,673,853	421,396
Obligations under capital lease	1,224,767	1,424,029	867,387
Government assistance	2,475,975	—	—
Deferred government incentives	3,335,548	3,606,926	2,986,572

## Business Strategy

Bioniche Life Sciences Inc. operates as a fully-integrated business, combining research and development of high potential technologies with business units that generate revenues. Revenue streams have allowed the Company to balance risk, drive innovation, and support corporate growth as its proprietary technologies come through late stage development, ready for commercialization.

The Company's infrastructure is well-developed and experienced, allowing Bioniche to conduct scientific discovery, pre-clinical research, manufacturing, clinical studies, as well as regulatory submissions and product registrations in global jurisdictions.

### GEOGRAPHIC DISTRIBUTION OF CONSOLIDATED REVENUES BY BUSINESS UNITS

*(expressed in millions of Canadian dollars)*

	2009	2008	Growth
For the twelve-months ended June 30	\$	\$	%
Animal Health – Canada	8.5	6.9	23%
Animal Health – USA	18.3	15.4	19%
Animal Health – Australia	3.9	3.1	26%
Animal Health – Europe	2.6	2.1	24%
<b>Total reported revenues</b>	<b>33.3</b>	<b>27.5</b>	<b>21%</b>

Bioniche believes in taking its proprietary technologies to their latest possible stage of development before seeking strategic external partners to assist in marketing the resulting commercialized products.

The Company's goal is to execute its business strategy:

1. Take existing proprietary technologies and continue, through the product development program, to enhance their proven therapeutic value for human and animal use.
2. Work to develop these technologies to the point of commercialization, either alone or with strategic marketing partners.
3. Manufacture as many products emerging from the product development program as possible to increase profit margins, protect the integrity of the Company's products, and enhance long-term shareholder value.

The Company has a pipeline of technologies in each business unit in early stage development to follow its priority projects — Mycobacterial Cell Wall-DNA Complex (MCC) for human bladder cancer treatment and the *E. coli* O157 cattle vaccine — once they are further advanced.



Graeme McRae

**Dear Fellow Shareholders,**

It's hard to believe that Bioniche Life Sciences Inc. has reached its 30<sup>th</sup> year of existence. It's 30 years since the original company — Vetrepharm Animal Health — was founded (1979). At that time, I was the only employee. A number of Canadian veterinarians provided financing to start the company, which was then based in London, Ontario. Our goal was to find alternative livestock therapies that would not result in residues in food and the environment, and would not encourage potential antibiotic resistance.

Since the discovery and development of antibiotic alternatives would take time and money, we identified a range of animal health products that could quickly move through the regulatory system to the marketplace. The cash flow from the sale of these products would help finance the Company's long-term research projects. Thirty years later, the Company's Animal Health business unit continues to generate revenues from product sales. This past year, Animal Health has generated \$33.3 million in revenues, 21% growth over Fiscal 2008.

With the recent announcement of a licensing partnership with Endo Pharmaceuticals, our Human Health division is well equipped to complete the development of *Urocidin*<sup>™</sup> for bladder cancer. Together with our strategic partner, we hope to have our first bladder cancer indication approved for commercial sale by 2012. Our focus now is on expanding our manufacturing facilities to accommodate commercial production of *Urocidin*<sup>™</sup> in anticipation of market launch.

In the Food Safety business unit, our team continues to work with government agencies seeking support for pilot programs to facilitate the use of the *Econiche*<sup>™</sup> vaccine by cattle producers. In the U.S., we are providing all of the required material for a conditional license, which we hope to receive by year-end. Detailed planning for the new vaccine plant in Belleville has been completed, and construction is now beginning.

In its 30-year history, Bioniche has undergone numerous changes and has experienced significant growth. We have faced challenges and overcome them. We have learned how to successfully discover, develop, manufacture, register and market products both close to home and around the world. We have established a reputation — a brand — that sets us apart from many other companies in our industry.

Each of our Bioniche employees — now numbering close to 200 — plays an important role in maintaining and advancing the Bioniche brand. Their loyalty to the Company and commitment to meeting objectives ensures that we deliver high quality products and services.

A strong, clear brand is a promise to our partners, our investors, our communities and, of course, ourselves. It is a promise to make our company something we are proud to be associated with, to conduct ourselves with honour and integrity, to respect and protect the environment, to embody our highest goals and our greatest aspirations and to achieve our Vision and Values:

### Vision

Our strength is **INNOVATION**.

Our commitment is to **IMPROVING THE QUALITY OF LIFE**.

### Core Values

**Integrity** is the foundation for building our credibility and reputation.

It permeates our policies, communications and activities.

**Ethics** are at the core of our being and responsibility.

They are essential to our day-to-day decisions, the commitments we make, and the quality of our products.

**Loyalty** based on mutual respect and a shared vision is an important ingredient in our efforts to achieve essential relationships with all of our clients, partners and stakeholders; and in the development of quality, productive teams.

**Compassion** for our work and the lives that we are trying to improve and save becomes an important component of the organization. It is held by all employees regardless of their duties and responsibilities.

I am proud to say that the original guiding principles of the company have not changed. In both human and animal health, Bioniche is committed to improving the quality of life through innovative research and therapeutics.

Working together, we will continue to make great things happen at Bioniche Life Sciences, in our communities, and around the world. Thank-you for your contribution toward making our first 30 years a success. I look forward to celebrating future corporate achievements with all of you.



**Graeme McRae**

Chairman, President & CEO

Here at Bioniche, we believe that shareholders expect us to act responsibly and do the right thing with their investment in the Company. This brief report details some initiatives we have developed to achieve our mission of improving quality of life through innovation. We take the term 'corporate responsibility' to heart, and are always trying to maintain policies and practices that exceed government regulations. By embodying our core values of integrity, ethics, loyalty and compassion, we hope to create long-term relationships that enhance the well-being of all of our stakeholders.

## Responsible to our patients through our products

Our business model is dependent foremost on the health and well-being of our patients (whether human or animal), so we take steps to protect them from harmful substances and disease. *Urocidin*<sup>™</sup>, our bladder cancer therapy that is currently in Phase III clinical trials, is made from a bacterium that is not disease causing. *Econiche*<sup>™</sup>, our *E. coli* O157 vaccine for cattle, prevents the attachment of a pathogenic bacterium to the intestinal tract of cattle, thus reducing its shed into the environment (food and water supplies) and protecting humans from infection. All of our products must pass stringent testing before being made available to the public, and are designed for maximum effectiveness with minimal impact throughout their life-cycles.

## Responsible to our employees through engagement and empowerment

Our management team has worked hard to design a corporate culture that encourages an inclusive and diverse work environment for our employees, although it hasn't always been easy. Earlier this year, we were forced to cut back on expenses due, in part, to the global credit crisis. Our employees banded together by eliminating overtime and reducing hours without compromising work quality. Although some employees were temporarily laid off during this period, all but one (who found another contract in the meantime) are back working with us full-time.

We are proud to have been ranked #13 in this year's Best Small & Medium Employers in Canada survey performed by the Queen's University School of Business Queen's Centre for Business Venturing and Hewitt Associates. Our employees completed surveys that gauged employee recognition, managing performance, career opportunities and organizational reputation. Building on

this result, our Human Resources department hosted several focus groups with employees to determine our strengths and areas for improvement. Although employees are very happy with a strong sense of community, accessible management, cultural diversity and a Company-wide concern for human and animal health, we recognize that there is still much that can be improved. The valuable information gathered from these focus groups will help inform a "People Strategy" that will further enhance employee engagement and contribute to a stronger corporate culture.

Employee safety is a big priority at Bioniche, and we are proud to report that we have not had a lost-time accident since May, 2002. Furthermore, we have enabled our employees to become stewards of the environment by implementing recycling and composting programs at our head office. In 2008, we saved 88 trees by recycling 4.66 metric tonnes of paper products, and our kitchen food waste is composted on-site and used to fertilize crops at our farm! Every Earth Day for the past five years, our employees worldwide have taken part in the "Bioniche Community Cleanup" to pick up litter around corporate sites and in public areas, and we also gave each of our employees "Going Green" lunch and tote bags that replace disposable plastic bags.

## Responsible to our planet and community through philanthropy

We feel that our commitment to responsibility should extend beyond the walls of our offices and laboratories. That's why we financially support initiatives that contribute to a better planet and community. Species extinction is a big problem in Australia, where endangered animals live in an often harsh environment. To become part of the solution, we've donated supplies and money to the University of Sydney's assisted reproductive technology course that allows researchers to understand and improve breeding techniques for endangered marsupials.

We are also very proud of our partnership with the local Hospice organization that provides palliative care for terminally ill patients. After years of supporting their fundraising efforts at special events, we formalized our partnership with them in May, 2009 by donating a house adjacent to our headquarters and creating the Bioniche Hospice Quinte Centre. The Centre is conveniently close to the local hospital, and provides Hospice Quinte with headquarters, volunteer training and meeting facilities in a home-like setting with easy access for patients and their families.

The following discussion and analysis is the responsibility of management and should be read in conjunction with the Company's audited consolidated financial statements as at June, 2009 and 2008 and related notes thereto, which have been prepared in accordance with Canadian Generally Accepted Accounting Principles ["GAAP"]. It is intended to complement and supplement financial information included in Bioniche Life Sciences Inc.'s [the "Company" or "Bioniche"] interim and annual consolidated financial statements, related notes, other financial information found elsewhere in the Company's annual report and in its annual information form or other documents filed on SEDAR at [www.sedar.com](http://www.sedar.com).

To the extent any statements made in this document contain information that is not historical, these statements are considered forward-looking and are subject to risks and uncertainties. Actual results, levels of activity, performance, or achievements could differ materially from those projected herein and depend on a number of factors, including the successful and timely completion of research and clinical trials, the uncertainties related to the regulatory process, and the commercialization of the Company's therapeutic products thereafter.

The cautionary statements made in this report should be read as applying to all related forward-looking statements wherever they appear in this report. The Company's future results could differ materially from those discussed here. Factors that could cause or contribute to these differences include those discussed under "Risks and Uncertainties". All amounts are in Canadian dollars unless otherwise indicated.

This management's discussion and analysis is current as of September 17, 2009. Where "we", "us", "our", "Bioniche" or the "Company" are utilized, these mean Bioniche Life Sciences Inc. unless otherwise indicated. All percentages reflected herein are calculated on whole amounts as contained in the Company's financial records and financial statements and not on the rounded amounts as disclosed herein.

The Company continued to experience challenges in its financial condition and liquidity throughout Fiscal 2009. These challenges intensified in light of current global economic and financial market conditions. However, subsequent to the year-end, on July 10, 2009, the Company announced the signing of a license, development and supply agreement with a major pharmaceutical company. Under the agreement, the Company received an up-front cash payment of US\$20M along with the potential for up to US\$110M in additional payments linked to the achievement of future clinical, regulatory, and commercial milestones. In addition, Bioniche will manufacture the licensed product and receive a transfer price for supply. Further discussion on both the going concern uncertainty and the partnering agreement are provided in the sections, "Liquidity, Financing, and Capital Resources", "Licensing Development and Supply Agreement with Endo Pharmaceuticals Inc.", and in note [22] of the Financial Statements.

## Global Overview

Bioniche is a research-based, technology-driven Canadian biopharmaceutical company that develops, manufactures, and markets proprietary products for human and animal health markets worldwide. The Company employs 187 people and has three operating business units: Human Health, Animal Health, and Food Safety. Corporate headquarters are located in Belleville, Ontario, Canada.

### Key Assets in the Human Health Business Unit

The human health business unit of the Company operated through Bioniche Therapeutics, which has research and production facilities and a clinical trial group in Montréal, Québec, Canada. This unit develops novel human cancer therapies, with a focus on the research and development of the Company's Mycobacterial Cell Wall-DNA Complex ["MCC"] technology platform for the treatment of bladder and other cancers, and its oligonucleotides, which show pre-clinical promise in the treatment of leukemia and other cancers. The Company's strategy is to develop its therapies through Phase II clinical trials and then to establish alliances to complete final clinical trials and achieve regulatory approvals for marketing.

The MCC technology, trademarked *Urocidin*<sup>TM</sup> for bladder cancer, is currently in Phase III clinical testing in patients with non-muscle-invasive bladder cancer that is refractory (unresponsive) to the standard therapy. A second Phase III study, comparing *Urocidin*<sup>TM</sup> to the standard therapy in patients with non-muscle-invasive bladder cancer as a first-line treatment, is planned.

### Key Assets in the Animal Health Business Unit

The Company's Animal Health business unit develops, manufactures and markets animal health biopharmaceutical products worldwide. The animal health business unit has product development, manufacturing and marketing facilities in Belleville, Ontario, Canada; marketing and production facilities in Athens, Georgia, U.S.A., Pullman, Washington, U.S.A., and Armidale, New South Wales, Australia; and a marketing office in Europe. The Company has progressively grown by using biotechnology to provide the animal health market with innovative solutions to meet the changing needs of the animal health industry.

The revenues from the Animal Health business unit, which has a history of generating positive earnings before interest, taxes, depreciation and amortization ["EBITDA"]<sup>1</sup> before research and development expenditures, have traditionally supported the Company's key research and development projects.

The Company has a product portfolio of more than sixty products, which can be categorized primarily in the following groups: Reproduction and embryo transfer products; products based on hyaluronans; immunostimulant products; polyclonal antibodies; vaccine products; and nutraceuticals. These products are marketed directly to veterinarians in Canada, the United States, Australia and Europe, and through selected distributors in the rest of the world.

### Key Assets in the Food Safety Business Unit

The food safety business unit of the Company — Bioniche Food Safety — was established in July, 2001. The unit is responsible for researching, developing, manufacturing and marketing of veterinary biopharmaceutical products to help improve the safety of food and water supplies. The lead initiative for this unit is the development and commercialization of a cattle vaccine, *Econiche*<sup>™</sup>, used to reduce the spread of the deadly *E. coli* O157 organism. This vaccine was developed to reduce the burden of the pathogenic bacterium *E. coli* O157 in cattle and their manure, thereby reducing contamination of the environment, ground water, and cattle processing plants. The vaccine has proven to reduce the amount of bacteria shed by cattle, and to reduce the number of animals in which the bacteria

colonize. The fewer bacteria reproducing in the cow, the fewer bacteria will be shed in its manure, affecting the environment and the carcass during food processing.

The vaccine is now available in very limited quantities and its first sales were recorded during Fiscal 2008 under a *Permit to Release Veterinary Biologics* granted by the Canadian Food Inspection Agency ["CFIA"] in December, 2006.

On October 27, 2008, the Company announced that *Econiche*<sup>™</sup>, which is the world's first vaccine developed to reduce the shedding by cattle of *Escherichia coli* (*E. coli*) O157, had received full licensing approval from the CFIA for sale in Canada. Sales have been constrained to date, due to limited production capacity and the need to provide vaccine for regulatory purposes and market-related studies.

The Company, in partnership with the Vaccine and Infectious Diseases Organization ["VIDO"] at the University of Saskatchewan and Natural Science and Engineering Research Canada, has sponsored two research positions — *Natural Science and Engineering Research Canada ["NSERC"]/Bioniche Industrial Research Chairs* - in vaccines to reduce food and water contamination. Dr. Andrew Potter (Senior Chair) and Dr. Wolfgang Köster (Associate Chair) were appointed to these positions. The Research Chairs were established to undertake research leading to the development of additional food safety vaccines to fight infectious diseases of animals, including *Salmonella enteritidis* and *Campylobacter jejuni* and *Listeria*.

## Selected Annual Financial Information

	Year ended June 30, 2009	Year ended June 30, 2008	Year ended June 30, 2007
Revenue	33,281,029	27,468,085	27,479,727
Net loss	(10,500,504)	(16,255,708)	(14,760,994)
Basic and fully diluted net loss per share	(0.15)	(0.26)	(0.32)
Total assets	34,641,440	34,623,010	41,526,774
<b>Long-term liabilities</b>			
Long-term debt	1,148,706	1,673,853	421,396
Obligations under capital lease	1,224,767	1,424,029	867,387
Government assistance	2,475,975	—	—
Deferred government incentives	3,335,548	3,606,926	2,986,572

1. Please refer to "Non-GAAP and Other Measures" section

## Corporate Goals and Objectives

The Company's goal is to execute its business strategy:

1. Take existing proprietary technologies and continue, through the product development program, to enhance their proven therapeutic value for human and animal use.
2. Work to develop these technologies to the point of commercialization, either alone or with strategic marketing partners.
3. Manufacture as many products emerging from the product development program as possible to increase profit margins, protect the integrity of the Company's products, and enhance long-term shareholder value.

Fiscal 2009 Objectives	Status
<ul style="list-style-type: none"> <li>• Generate cash flow by increasing revenue and productivity, as measured by the consolidated EBITDA* in the Animal Health business unit.</li> </ul>	<ul style="list-style-type: none"> <li>• The Company has met this objective. The Animal Health EBITDA* of \$12.2M for the twelve months ending June 30, 2009 compares to \$7.7M for the same period last year. This represents an increase of 58% year-to-date.</li> <li>• Sales in Animal Health have increased by \$5.8M, or 21%, during Fiscal 2009 as compared to Fiscal 2008.</li> </ul>
<ul style="list-style-type: none"> <li>• Progress to a U.S. conditional license for the <i>Econiche</i>™ cattle vaccine.</li> </ul>	<ul style="list-style-type: none"> <li>• In February, 2008, the <i>E. coli</i> O157 vaccine was granted eligibility for a conditional license in the U.S. In order to be granted this license, several steps had to be undertaken, including the production of three consecutive commercial batches of vaccine that are filled in an approved U.S. manufacturing facility and are proven to meet required specifications.</li> <li>• The Company is in the process of meeting the requirements, and expects that a conditional license may be granted by the end of calendar 2009.</li> </ul>
<ul style="list-style-type: none"> <li>• Successfully conclude a marketing partnership transaction for the Company's bladder cancer technology.</li> </ul>	<ul style="list-style-type: none"> <li>• The Company successfully met this objective, as announced on July 10, 2009.</li> <li>• Further discussions on the License, Development and Supply Agreement are provided in the section, "License, Development and Supply Agreement with Endo Pharmaceuticals Inc."</li> </ul>
<ul style="list-style-type: none"> <li>• Repayment of the existing revolving credit facility.</li> </ul>	<ul style="list-style-type: none"> <li>• In October, 2008, due to financial market conditions, Laurus/Valens informed the Company that it would like the existing revolving credit facility, scheduled to mature on December 9, 2008, replaced with an instrument(s) from an alternative lender(s).</li> <li>• Bioniche and Laurus/Valens agreed to extend this facility past June 30, 2009 in order to give the Company time to find a new banking partner(s) or complete fundraising activities.</li> <li>• Subsequent to the year-end, following the signing of the License, Development and Supply Agreement and receipt of the US\$20M up-front payment, the Company repaid its outstanding credit facility with Valens U.S. and associated fees, a total of C\$6.2M [US\$5.3M]</li> </ul>
<ul style="list-style-type: none"> <li>• Addressing near-term liquidity needs by working on fundraising activities, including potential asset or segment dispositions.</li> </ul>	<ul style="list-style-type: none"> <li>• Given the delays in closing a licensing transaction and the Company's near-term cash needs, the Company decided to retain an agent to provide assistance in this process.</li> <li>• Several strategic options were identified to help the Company maximize its value.</li> <li>• Other than those disclosed already in the subsequent event note [22] and with the conclusion of the License, Development and Supply Agreement, the Company will no longer pursue asset or segment dispositions.</li> </ul>

\* EBITDA means "Earnings Before Interest, Taxes, Depreciation, Amortization and foreign exchange". For more information, please refer to the section, "Non-GAAP & Other Measures" below.

## Liquidity and Going Concern

The Company has incurred significant losses and has an accumulated deficit of \$95,291,503 as at June 30, 2009. The Company's committed cash obligations and expected level of expenditures for Fiscal 2010 exceed its committed sources of funds and funds available as at June 30, 2009.

The Company had a cash position, inclusive of the restricted cash at the end of August, 2009, of \$16.6M. This strong cash position is the net result the closing the License, Development and Supply Agreement as explained above, repaying the revolving credit facility and associated fees of \$6.2M [US\$5.3M], the sale of U.S. licensing rights to an animal health product subsequent to June 30, 2009 for \$0.9M [US\$0.8M], working capital variations, and the repayment of all overdue outstanding payables.

To date, the Company has financed its cash requirements primarily through the issuances of shares, product sales, investment tax credits, the sale of businesses or business units, royalties, government incentives, long-term debt issuances, and a revolving credit facility.

The Company expects to finance its future expenditures by receiving certain payments from its licensing partner on accomplishing milestones related to the conduct of the *Urocidin*<sup>TM</sup> clinical program. Although the Company is confident that it will achieve these milestones, that it will successfully replace its revolving credit facility, and that it will maintain a strong EBITDA\* before research and development expenditures in the Animal Health business unit, these achievements are dependent upon certain factors outside of the Company's control. If not achieved, the Company may be required to obtain additional financing or curtail the Company's development activities and operations.

## License, Development and Supply Agreement with Endo Pharmaceuticals Inc.

On July 10, 2009, Bioniche announced that it had accomplished its goal of securing a strategic partnership to undertake the commercialization of *Urocidin*<sup>TM</sup>. This strategic partnership was struck with Endo Pharmaceuticals Inc. ["Endo"] of Chadds Ford, Pennsylvania, a publicly-listed company (ENDP – NASDAQ). Endo is a speciality pharmaceutical company engaged in the research, development, sale and marketing of branded and generic prescription pharmaceuticals used to treat and manage pain, overactive bladder and prostate cancer, among other categories. The history of Endo can be traced back as far as 1920. Endo re-commenced operations as a division of Dupont Merck in 1994, became independent

via a 1997 management buy-out from the Dupont Merck Pharmaceutical Company, and went public in 2000. Since that time, Endo has increased revenues by ten-fold. Endo markets its branded pharmaceutical products to physicians in pain management, urology, neurology, surgery, oncology, endocrinology and primary care. More information, including past press releases, is available at [www.endo.com](http://www.endo.com).

Under the License, Development and Supply Agreement [the "Agreement"], Endo licensed from Bioniche rights to develop and market *Urocidin*<sup>TM</sup> (now also known as EN3348), for the treatment of non-muscle-invasive bladder cancer. The territories licensed consist of the United States, Mexico and, subject to co-marketing rights, Canada. The Agreement also includes a 12-month option to expand the territory to comprise global marketing rights.

Upon signing the Agreement, Bioniche received an up-front cash payment of US\$20M. The Company also has the potential to receive a further US\$110M in additional payments linked to the achievement of future clinical, regulatory and commercial milestones some of which are near-term. In addition to the above payments, Bioniche has retained exclusive product manufacturing rights and will receive a net-sales-related transfer price for supplying Endo with commercial product, following regulatory approval. Bioniche believes the Agreement will provide overall economics that are superior to most biotech-pharma partnership agreements and that Endo represents an optimal development and commercialization partner due to its market and industry expertise. Endo was also granted a right of first negotiation for other clinical indications of MCC technology, where such clinical indications relate to urology or pelvic disease. Should Endo not elect to enter such negotiations and the parties conclude them to mutual satisfaction within a set period, the Company shall have no further obligations and Endo no further rights.

The Agreement provides that the Company continue to support research and development efforts until December 31, 2009. Subsequent to this date, the Company and Endo will share such costs by an agreed-upon formula until July 10, 2010, by which time Endo must decide whether or not to exercise its option to undertake global marketing rights.

Should Endo exercise its option to global rights at that time, it will then assume responsibility for 100% of external research and development costs. If not, these costs will continue to be shared by formula. If Endo elects to undertake global rights to *Urocidin*<sup>TM</sup>, Bioniche believes the development funding and milestone packages may be adequate to cover its non-capital expenditure costs through to the first approval date of *Urocidin*<sup>TM</sup> in the United States. If Endo does not elect to exercise its global marketing rights option, the Company believes, with the expected

achievement of milestones, it has funds for a sufficient period to enable it to secure other development partners for outside of North America and, thereby, secure additional funding on favourable terms.

In any event, the Company will be seeking third-party, non-equity funding to build-out sufficient commercial production capacity for *Urocidin*<sup>™</sup>.

## Corporate Highlights for Fiscal 2009

The following section is a summary of certain corporate highlights that are not specifically referred to in other sections of this Management Discussion and Analysis. Scientific highlights and other corporate news are presented below under "Segmented Performance".

### Bioniche Repays Revolving Credit Facility

On July 20, 2009, the Company reported that it had repaid its credit facility with Valens U.S. and associated fees, a total of \$6.2M [US\$5.3M]

Valens financed the Company through a challenging time of corporate development, helping the Company to advance its bladder cancer technology to Phase III clinical testing and its *E. coli* O157 vaccine — Econiche<sup>™</sup> — to full Canadian license.

### Bioniche Named One of the Top 50 Best Small and Medium Employers in Canada

On January 14, 2008, the Company was named among the Top 50 Best Small and Medium Employers in Canada. Bioniche was ranked number 13 by its employees. The rankings are primarily determined using the results from employee opinion surveys, where 18 key engagement drivers are detailed and analyzed. The evaluation process also includes the assessment of organization practices and perspectives from the leadership team. This year, more than 250 companies across Canada registered to participate in the study.

## Results of Operations

The following table sets forth, for the periods indicated, the percentage of revenue represented by items in the Bioniche Life Sciences Inc. Consolidated Statements of Loss and Comprehensive Loss.

### CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS

(expressed in millions of Canadian dollars)

For the twelve-months ended June 30	2009		2008	
	\$	%	\$	%
Revenues	33.3	100%	27.5	100%
Cost of Sales	14.4	43%	12.7	46%
Gross Profit	18.9	57%	14.8	54%
<b>Expenses</b>				
Administration	6.1	18%	6.7	24%
Marketing and Selling	6.1	18%	6.7	24%
Other expenses**	0.9	3%	—	0%
EBITDA* before Research and Development	5.8	17%	1.4	5%
Net Research and Development	11.5	35%	14.1	51%
Interest, taxes, depreciation, amortization and others***	4.8	14%	3.6	13%
Net loss and comprehensive loss	(10.5)	-32%	(16.3)	-59%

\* EBITDA means "Earnings before interest, taxes, depreciation and amortization". For more information please refer to the section "Non-GAAP & other measures" below

\*\* other expenses include non-recurrent fees associated with strategic initiatives

\*\*\* other includes foreign exchange losses on financial instruments

### Year-Ended June 30, 2009 as Compared to the Year-Ended June 30, 2008

#### Consolidated Revenue

The Company's consolidated revenues for Fiscal 2009 reached \$33.3M as compared to \$27.5M for Fiscal 2008. This represents a 21% increase and is the result of increased revenues in all markets, as well as favourable exchange rates.

#### Cost of Goods Sold

For the year ended June 30, 2009, gross profit totaled \$18.8M, compared to \$14.8M for the year ended June 30, 2008. For year ended June 30, 2009, gross profit as a percentage of sales totaled 57% compared to 54% in Fiscal 2008.

### GEOGRAPHIC DISTRIBUTION OF CONSOLIDATED REVENUES BY BUSINESS UNITS

(expressed in millions of Canadian dollars)

For the twelve months ended June 30	2009 \$	2008 \$	Growth %
Animal Health – Canada	8.5	6.9	23%
Animal Health – USA	18.3	15.4	19%
Animal Health – Australia	3.9	3.1	26%
Animal Health – Europe	2.6	2.1	24%
<b>Total reported revenues</b>	<b>33.3</b>	<b>27.5</b>	<b>21%</b>

#### Expenses Other than Research and Development

For the year ended June 30, 2009, expenses before research and development totaled \$17.5M, compared to \$16.7M for Fiscal 2008. Importantly, the Company reduced its administration and marketing expenses by 10% from \$13.4M in Fiscal 2008 to \$12.2M in Fiscal 2009, as a result of certain temporary cutbacks necessary during a period of financial challenge.

Management expects administration and marketing costs to increase again during Fiscal 2010 to assure the sustainability of the business. This, combined with a non-cash items increase and other minor variations, resulted in an increase of \$0.8M, or 5%.

### EXPENSES OTHER THAN RESEARCH AND DEVELOPMENT

(expressed in millions of Canadian dollars)

For the twelve months ended June 30	Year to date			
	2009		2008	
	\$	%	\$	%
<b>Revenues</b>	33.3	100%	27.5	100%
<b>Expenses</b>				
Administration	6.1	18%	6.7	24%
Selling and Marketing	6.1	18%	6.7	24%
Other expenses*	0.9	3%	–	0%
<b>Sub-total</b>	<b>13.1</b>	<b>39%</b>	<b>13.4</b>	<b>48%</b>
<b>Non cash and other items</b>				
Amortization	4.0	12%	2.8	10%
Interest	0.7	2%	0.3	2%
Foreign Exchange	(0.3)	–1%	0.2	0%
<b>Sub-total</b>	<b>4.4</b>	<b>13%</b>	<b>3.3</b>	<b>12%</b>
<b>Total Expenses</b>	<b>17.5</b>	<b>53%</b>	<b>16.7</b>	<b>60%</b>

\* Other expenses include non-recurant fees associated with strategic initiatives

## Research and Development

For the year ended June 30, 2009, research and development expenses totaled \$13.3M, compared to \$16.0M for Fiscal 2008. The majority of these costs can be attributed to the ongoing Phase III clinical program for the Company's *Urocidin*<sup>™</sup> bladder cancer treatment and the *E. coli* O157 cattle vaccine development program.

### GROSS RESEARCH & DEVELOPMENT

(expressed in millions of Canadian dollars)

For the twelve months ended June 30 Key Areas	2009		2008	
	\$	%	\$	\$
Animal Health	1.8	14%	1.9	12%
Food Safety	1.6	12%	2.6	16%
Human Health	9.9	74%	11.5	72%
Research and Development, Gross	13.3	100%	16.0	100%

## Consolidated Net Loss and Comprehensive Loss

For the year ended June 30, 2009, the basic and fully-diluted loss per share totaled \$0.15, compared to a loss per share of \$0.26 for the corresponding period in Fiscal 2008. Total common shares outstanding at June 30, 2009 were 71,681,147 as compared to 65,782,510 for the corresponding period in Fiscal 2008.

## EBITDA\* Before Research and Development Expenditures

### CALCULATION OF EBITDA

(expressed in millions of Canadian dollars)

For the twelve months ended June 30	2009 \$	2008 \$
Income (loss) before research and development and other items*	1.3	(1.9)
Add (deduct):		
Amortization	4.0	2.8
Interest and Accreted interest	0.7	0.2
Foreign exchange	(0.3)	0.2
<b>EBITDA before research and development</b>	<b>5.7</b>	<b>1.3</b>

\* other items include unrealized loss (gain) on foreign currency embedded derivative

For the year ended June 30, 2009, EBITDA\* before research and development totaled \$5.7M compared to \$1.3M for Fiscal 2008. This above normal 338% increase is directly attributed to the combined effect of sales growth of 21% and the reduction of administrative expenses by 9%.

\* EBITDA means "Earnings Before Interest, Taxes, Depreciation, Amortization and foreign exchange". For more information please refer to the section, "Non-GAAP & Other Measures" below.

## Q4 Highlights

The Company's consolidated revenues reached \$9.2M for the fourth quarter of Fiscal 2009, as compared to \$7.9M in the same period last year, due primarily to increased sales in the U.S. and Canada.

The profit before research and development and other items of \$0.7M during the fourth quarter of Fiscal 2009 represents a \$0.9M improvement as compared to a loss of \$0.2M for the same period in Fiscal 2008. This reflects increased sales in the fourth quarter of Fiscal 2009 of \$1.3M and improved foreign exchange impact of \$0.3M.

As a result, the total basic and fully-diluted loss per share for the final quarter of Fiscal 2009 was (\$0.03), compared to a basic and fully-diluted loss per share of (\$0.06) for the same period in Fiscal 2008.

## Last Eight (8) Quarters Consolidated Results at a Glance

During the past two years, the Company has been able to consistently reduce its loss per share as a result of stronger sales and reduction of overhead costs, while curtailing and prioritizing certain research expenditures. In addition, the Company issued shares during the period. The Company also increased its accounts payable and credit facility, resulting in deterioration of its working capital position. These practices were essential to support the business and maximize liquidities during recent difficult market conditions. These practices enabled the Company to continue to pursue its primary corporate objective of signing an important partnering transaction, announced on July 10, 2009.

### LAST EIGHT (8) QUARTERS CONSOLIDATED RESULTS AT A GLANCE

(expressed in millions of Canadian dollars)

	2009				2008			
	\$ Q4	\$ Q3	\$ Q2	\$ Q1	\$ Q4	\$ Q3	\$ Q2	\$ Q1
Revenues	9.2	7.4	8.6	8.1	7.9	7.2	6.5	5.9
Income (loss) before research & development and other items	0.7	0.0	0.5	0.1	(0.2)	(0.2)	(0.8)	(0.7)
Net Income (loss)	(1.8)	(3.0)	(2.4)	(3.3)	(3.7)	(4.6)	(4.2)	(3.8)
Basic and fully diluted net income (loss) per share	(0.03)	(0.04)	(0.03)	(0.05)	(0.06)	(0.07)	(0.07)	(0.06)

### WORKING CAPITAL ASSESSMENT

(expressed in millions of Canadian dollars)

	Jun-09	Mar-09	Dec-08	Sep-08	Jun-08	Mar-08	Dec-07	Sep-07
Cash and Cash Equivalents (Unrestricted)	5.9	2.9	5.6	4.3	4.4	8.8	6.6	8.0
Receivables	3.7	6.2	5.8	6.6	6.4	5.5	5.1	5.1
Inventory	5.4	6.6	6.0	4.9	4.7	4.9	5.3	5.5
	15.0	15.8	17.4	15.7	15.5	19.3	17.1	18.6
Less: Payables	(11.6)	(10.5)	(10.1)	(8.0)	(8.3)	(7.9)	(6.9)	(6.5)
Less: Revolver (not net of def. fin. costs)	(4.4)	(5.4)	(5.3)	(3.4)	(3.2)	(5.0)	(3.9)	(3.0)
<b>Net balance</b>	<b>(1.0)</b>	<b>(0.1)</b>	<b>2.0</b>	<b>4.3</b>	<b>4.1</b>	<b>6.4</b>	<b>6.2</b>	<b>9.1</b>

### Fluctuations in Consolidated Operating Results

The Company's consolidated results of operations are likely to fluctuate significantly from period to period in the future. It is anticipated that the quarterly and annual results of operations will be impacted for the foreseeable future by several factors, including the timing of clinical trials, the timing of regulatory approvals to market products, the progress and timing of expenditures related to commercialization efforts, the timing of revenues from product sales and the achievement of milestones. Due to these fluctuations, the Company presently believes that the period-to-period comparisons of its consolidated operating results are not a good indication of future performance, particularly with the closing of the partnership transaction described above.

## Consolidated Balance Sheet Highlights

### Assets

The Company's current assets at June 30, 2009 totaled \$16.9M, as compared to \$16.3M reported at June 30, 2008. The change in assets results primarily from continued losses as the Company invests in advancing its late-stage core technologies. Overall, the Company reduced significantly and maintained an average burn rate\* of approximately \$0.3M per month for the fiscal year ending June 30, 2009, compared to \$1.0M per month in Fiscal 2008. Cash and cash equivalents and short-term investments totaled \$5.9M at June 30, 2009, as compared to \$4.4M at June 30, 2008.

Long-term assets, excluding restricted cash, at June 30, 2009 decreased to \$17.7M, as compared to \$18.3M reported at June 30, 2008. This decrease is attributed to reduced intangible assets, which reflects no new additions and their continued amortization. This is partially offset by capital asset additions during the year ended June 30, 2009 of \$1.5M as compared to \$1.4M during Fiscal 2008 and an increase in long-term accounts receivable representing holdbacks under two government programs.

### Liabilities and Shareholders' Equity

At June 30, 2009, the Company's net working capital totaled (\$0.5M), as compared to \$4.7M at June 30, 2008. This year's negative working capital position was essential to support the business and maximize liquidities during difficult liquidity and market conditions. Shareholders' equity at June 30, 2009 totaled \$9.1M as compared to \$16.4M at June 30, 2008.

Long-term debt at June 30, 2009 totaled \$8.2M, which compares to \$6.7M reported in the same period in Fiscal 2008. The increase reflects the discounted loan of \$2.5M from the Advanced Manufacturing Investment Strategy and Agri-Opportunities programs, less repayments of capital leases and long-term debt. These loan amounts were advanced to support the capital requirements related to construction of a vaccine facility to manufacture *Econiche*<sup>TM</sup>.

## Cash Flow Statement Highlights

The Company's cash flow used in operations was reduced significantly to approximately \$3.0M during Fiscal 2009, as compared to \$11.6M in Fiscal 2008. This reflects the Company's increased product sales, as well as overall cost reductions, including temporary layoffs of some staff and increased credit line borrowing and management of accounts payable.

The Company's financing activities provided cash of \$5.0M during the fiscal year ending June 30, 2009. This includes \$3.4M borrowing described above and approximately \$3.0M in net borrowing on the revolving credit facility. By comparison, in the fiscal year ending June 30, 2008, \$1.8M was provided under a loan from the Business Development Bank of Canada (BDC) and \$4.1M in net borrowing under the Company's revolving credit facility.

Subsequent to the year-ended June 30, 2009, the Endo Agreement resulted in an up-front payment of US\$20M reported earlier under the section, "License, Development and Supply Agreement with Endo Pharmaceuticals Inc." The financial impact will be reported in the Company's Fiscal 2010 first quarter financial statements.

## Segmented Performance

Segmented financial information analyzes the operations of the Company according to its business segments:

### Human Health Business Unit

During Fiscal 2009, important efforts were made by the Company to advance its first Phase III clinical trial. During the year, the Company reported the following news related to Human Health (all available in the Newsroom section of the Company's website: [www.Bioniche.com](http://www.Bioniche.com)):

#### 24/08/09

Bioniche Phase III Clinical Trial with *Urocidin*<sup>TM</sup> Given Continued Green Light by DMC

\* Burn rate means cash flow used in operations. For more information, please refer to the section, "Non-GAAP & Other Measures".

22/05/09

Bioniche Phase III Clinical Trial with *Urocidin*<sup>TM</sup> Progressing Well

31/03/09

Bioniche Completes Recruitment in First Phase III Clinical Trial with *Urocidin*<sup>TM</sup>

18/02/09

Bioniche Phase II Bladder Cancer Trial Results Published in The Journal of Urology

24/11/08

Bioniche Presents MCC Data at the SIU World Uro-Oncology Update in Santiago, Chile

17/11/08

Update on Bioniche Phase III Clinical Trial in Bladder Cancer

18/08/08

Bioniche Phase III Clinical Trial in Bladder Cancer Progressing Well

Gross research and development expenses for the year ended June 30, 2009 totalled \$9.9M, which compares to \$11.4M reported in the same period in Fiscal 2008. The year-to-date decrease of \$1.5M, or 13.2%, is primarily attributed to Phase III bladder cancer registration trial having reached its enrolment targets and due to a cutback in expenditures to conserve cash.

Government incentives for the year ended June 30, 2009 totaled \$1.5M, which compares to \$1.7M recorded in the same period in Fiscal 2008.

### Animal Health Business Unit

Animal Health product sales increased by \$5.8M, or 21%, to \$33.3M for the year ended June 30, 2009, as compared to \$27.5M recorded in the same period in Fiscal 2008. This reflects increased sales of *Folltropin*<sup>®-V</sup> in the U.S., Canada and global export markets, as well as increase sales of *Cue-Mate*<sup>TM</sup> and *Pregneco*<sup>TM</sup> in Australia.

Gross profit in the Animal Health segment for the year ended June 30, 2009 totalled \$19.3M, or 57.9%, which compares to \$14.8M, or 53.8%, reported in the same period in Fiscal 2008. This primarily reflects increased sales of higher margin products such as *Folltropin*<sup>®-V</sup>, as well as increased sales volumes in the Australian operations.

Expenses incurred in the year ended June 30, 2009 totaled \$7.1M, which is \$0.7M lower than reported in Fiscal 2008. Certain cost reduction measures were put in place during these economic difficulties explain this variation.

Gross research and development expenses in the year ended June 30, 2009 totalled \$1.8M, virtually the same amount reported in Fiscal 2008.

### Food Safety Business Unit

During the year, the Company reported advancements in the Food Safety segment as follows (all news releases available in the Newsroom section of the Company's website: [www.Bioniche.com](http://www.Bioniche.com)):

13/03/09

*Econiche*<sup>TM</sup> Vaccine Shows 92% Reduction in Colonization of *E. coli* O157 in Vaccinated Cattle

27/10/08

World's First Cattle Vaccine to Reduce *E. coli* O157 Threat Receives Full Licensing Approval in Canada

24/09/08

Canadian Regulator Recognizes Efficacy and Safety of Bioniche *E. coli* O157 Cattle Vaccine

25/08/08

Bioniche Animal Health Immunotherapy Now Listed as "Organic" for Use in Cattle

17/07/09

*Econiche*<sup>TM</sup> Vaccine Efficacy Summarized in July Issue of Foodborne Pathogens and Disease

28/05/09

Bioniche Represented at House of Commons Sub-Committee on Food Safety

03/02/09

Bioniche Invited to Participate in Canadian Beef Value Chain Roundtable

17/10/08

*E. coli* O157 Vaccine Efficacy Reinforced by Study Published in Foodborne Pathogens and Disease

10/07/08

Bioniche Presents *E. coli* O157:H7 Vaccine Data to World Buiatrics Congress in Budapest, Hungary

The Company continues its marketing efforts and is receiving strong indications of support, particularly in the Canadian provinces of Ontario and Québec. The Company is continuing with its plans to build a vaccine manufacturing facility to accommodate large-scale manufacturing production of *Econiche*<sup>TM</sup> and other food safety and animal health vaccines. The facility is now expected to be completed by early 2011.

Funding for the vaccine plant expansion comes in part from the Ontario Ministry of Economic Development and Trade's Advanced Manufacturing Investment Strategy program, which is contributing \$10.0M in the form of a loan based on a percentage of eligible expenditures incurred. At June 30, 2009, \$2.9M was advanced under this program. The Department of Agriculture and Agri-Food (Canada)'s Agri-Opportunities Program is also contributing \$5M in the form of a loan based on a percentage of eligible expenditures incurred. At June 30, 2009, \$0.5M was advanced under this program. The Industrial Technologies Office (ITO) of Industry Canada is providing funding of \$5M in the form of a repayable loan. A further \$5M has been secured in the form of a loan from the Business Development Bank of Canada, however, disbursement in excess of \$1.75M will be made only if the Company makes certain qualifying expenditures.

Expenses incurred in the year ended June 30, 2009 totaled \$1.0M, as compared to \$1.7M reported in Fiscal 2008. The Company is continuing its education and awareness program focused on the dangers of *E. coli* O157 and the importance of food and environmental safety. Assistance with funding for market development related to the Company's *E. coli* O157 cattle vaccine continues to come from the Rural Economic Development ["RED"] Program in the form of a \$2.0M grant based on eligible expenditures. As at June 30, 2009, the Company recognized \$1,247,260 of this grant, less a 10% hold-back receivable which has been discounted using a discount rate of 5.69%. The eligible amount less the discount has been netted against the related marketing expenses totaling \$843,415 [2008 – \$394,763] [note 11[iii]].

This segment incurred gross research and development expenses of \$1.6M for the year-ended June 30, 2009, as compared to \$2.6M reported in Fiscal 2008. The Company has continued to pursue its development efforts while awaiting product approval from the relevant regulators in the United States.

## Liquidity, Financing and Capital Resources

### Financial Position and Cash Flow

At June 30, 2009, the Company had approximately \$5.9M in cash and cash equivalents. To date, the Company has financed its expenditures primarily through public and private placements of common shares, the issuance of debt instruments, and the receipt of government incentives earned on eligible scientific expenditures. The operations of the Company's commercial division (Animal Health) have been financed through this unit's own internally generated cash flows, through the use of commercial banking facilities, and through capital leases with equipment vendors.

The Company was able to advance its key development platforms in both Food Safety and Human Health while reducing the average burn rate (cash used in operating activities) to approximately \$0.2M per month during Fiscal 2009, as compared to \$1.0M during Fiscal 2008.

To address the Company's capital needs and to strengthen its financial position during Fiscal 2009 and Fiscal 2008, the Company completed the following transactions:

- On **September 7, 2007**, the Company announced a \$2M grant from the Rural Economic Development (RED) Program of the Ontario Ministry of Agriculture, Food and Rural Affairs. The grant is based on a percentage of eligible expenditures.
- On **December 18, 2007**, the Company announced that it would receive a \$10M loan from the Ontario Ministry of Economic Development and Trade (MEDT)'s Advanced Manufacturing Investment Strategy (AMIS) program. This loan is in support of the Company's vaccine production facility scale-up in Belleville, Ontario, Canada, and is based on a percentage of eligible expenditures.
- On **December 20, 2007**, the Company announced it would receive a \$5M loan from the new Agri-Opportunities Program of the Department of Agriculture and Agri-Food (Canada) (AAFC). The loan is based on a percentage of eligible expenditures.
- On **December 21, 2007**, the Company announced an amendment to its revolving credit facility, resulting in a borrowing limit of US\$5.5M.
- On **February 8, 2008**, the Company entered into a ten-year term loan agreement with the Business Development Bank of Canada (BDC) for up to \$5M to support the scale-up of the Company's vaccine production facility in Belleville, Ontario.
- On **March 27, 2008**, the Company announced the conversion of a portion of its revolving credit facility, issuing 2,671,900 common shares, resulting in additional borrowing capacity of \$1.8M.
- On **June 25, 2008**, the Company amended to a pre-existing \$7.6M contribution agreement with the Industrial Technologies Office of Industry Canada that will support the scale-up of the Company's vaccine production facility in Belleville, Ontario.
- On **September 9, 2008**, the Company announced the conversion of a portion of its revolving credit facility, resulting in the issuance of approximately 4.6M common shares and the availability of up to \$2.0M in additional borrowing capacity.
- On **March 2, 2009**, the Company announced it amended the maturity date of its existing secured revolving credit facility with Valens U.S. This extension was provided to the Company in order to allow it time to

identify new banking partner(s) after Valens decided to withdraw its credit due to recent market conditions. The original revolving credit facility was established in 2005. There were no fees or penalties resulting from this amendment.

- In a subsequent event, on **July 10, 2009**, the Company announced the signing of a strategic partnership agreement to undertake completing the commercialization of *Urocidin*<sup>TM</sup>. Under the agreement, Bioniche has since received a cash payment of US\$20.0M. The Company also has the potential to receive a further US\$110M in additional payments linked to the achievement of future clinical, regulatory and commercial

milestones. In addition to the above payments, Bioniche has retained exclusive product manufacturing rights and will receive a net sales-related transfer price for supplying the partner with commercial product.

- In a subsequent event, on **July 20, 2009**, the Company repaid its credit facility and associated fees with Valens U.S., a total of US\$5.3M.
- In a subsequent event, on **July 23, 2009**, the Company sold its U.S. license for a veterinary anaesthetic product to Bioniche Teoranta for a total price of US\$800,000. The Company received US\$548,639 in cash at closing, along with US\$251,361 in debt forgiveness.

## Contractual Obligations

### CONTRACTUAL OBLIGATIONS AND PAYMENTS DUE BY PERIOD

(expressed in millions of Canadian dollars)

	Total	Less than 1 year	1–3 years	4–5 years	After 5 years
	\$	\$	\$	\$	\$
Long-Term Debt	5.2	0.6	0.9	0.6	3.1
Capital Lease Obligations	1.9	0.4	0.7	0.5	0.3
Operating Leases	0.4	0.3	0.1	0.0	
Purchase Obligations	5.5	5.5			
Other Long-Term Obligations	2.7	0.7	1.3	0.6	
<b>Total Contractual Obligations</b>	<b>15.7</b>	<b>7.5</b>	<b>3.0</b>	<b>1.7</b>	<b>3.4</b>

## Revolving Credit Facility

As at June 30, 2009, \$4,447,836 [2008 – \$3,157,294] was drawn on this Facility [2008 – \$2,593,059 net of unamortized financial expenses].

On September 9, 2008, the Company issued 4,565,049 common shares in lieu of cash principal repayments of the Facility, totaling \$1,966,920 [US \$1,850,000] and 211,429 five-year warrants valued at \$61,315 using the Black-Scholes option pricing model using the following assumptions: A risk-free interest rate of 5.5%, expected dividend yield of 0%, expected volatility of 66%, and expected life of 5.0 years. The value of these warrants was recorded as a reduction of the carrying value of the Facility with a corresponding credit to other paid-in capital and was amortized using the effective interest rate method over the remaining life of the Facility which, at that time, ended December 9, 2008.

In October, 2008, the maturity date was extended to March 2, 2009 and the interest rate became Wall Street Journal prime plus 2.5%, but not less than 10%. A fee of \$0.6M [US\$0.5M] was charged for this amendment, payable in cash or in shares of the Company, at the Company's discretion.

On March 2, 2009, the maturity date was changed to "on demand" status. On April 27, 2009, the maturity date was again amended to June 30, 2009 and a fee of \$0.5M [US\$0.4M] was charged for this amendment, payable in cash.

On July 20, 2009, the Company repaid this Facility in full, as well as electing to pay all fees totalling \$2.2M [US\$1.9 M] in cash, using the proceeds of the upfront payment received on signing the Endo Agreement discussed above.

## Treasury Operations and Restricted Cash

The Company's treasury policy is to invest cash that is not required immediately into short-term instruments that are based on capital preservation. Such investments are primarily made in guaranteed investment certificates (GICs) and Canadian banker's acceptances (BAs), both of which are issued by Canadian chartered banks. There were no short-term investments as at June 30, 2009 or 2008.

The Company had \$1.2M in restricted cash at June 30, 2009. This funding was received in connection with the government assistance loan agreements referred to above. The government agencies in question agreed

to accelerate disbursements under the agreements in advance of claims submitted. The advance disbursements may only be used for expenditures related to the construction of the vaccine facility in Belleville, Ontario.

### **Earnout from the Sale of Bioniche Pharma**

The sale of Bioniche Pharma Group Ltd. to RoundTable Healthcare Partners included an entitlement for the Company to potentially receive contingent receipts associated with the future performance of the new Bioniche Pharma business. This could amount to a maximum of \$11.5M over the next two years. During the year ended June 30, 2009, the third year of five in which these earnout payments are possible, Bioniche Pharma Group Ltd. did not meet the criteria for making such a payment and, therefore, no income has been recorded or accrued in the Company's June 30, 2009 or 2008 Consolidated Financial Statements.

### **Sale of a Product to Bioniche Pharma**

Subsequent to the year end, the Company sold the U.S. rights to one of its generic animal health products for a total price consideration of US\$800,000, for cash consideration of US\$548,639 and forgiveness of US\$251,361 in accounts payable.

### **Related Party Transactions**

On June 3, 2005, the Company entered into a ten-year lease for a facility located at 275 Labrosse Avenue in Pointe-Claire, Québec. The facility is leased to the Company from a company owned and controlled by Graeme McRae, the Company's Chairman, President, Chief Executive Officer and a Director. Under the terms of the lease, the Company had the option to purchase the facility by May 31, 2006 by assuming the balance of the loan outstanding.

This option to purchase was extended effective May 31, 2006 for an additional two years and further extended to May 28, 2010. This transaction was recorded as a capital lease obligation as disclosed in note 10 of the Company's annual consolidated financial statements. The facility consists of 14,000 square feet and is expected to be used for additional manufacturing space in the future. This facility will allow the Company to expand the production capacity of its existing MCC manufacturing to meet the projected eventual demand for *Urocidin*<sup>™</sup> for the North American market.

### **Off-Balance Sheet Arrangements**

To date, the Company has not had any relationships with unconsolidated entities or financial partnerships, such as, entities referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow

or limited purposes. Other than the Company's operating leases and the commitments disclosed therein, the Company has no other off-balance sheet transactions.

### **Outstanding Common Shares**

The Company has total Common Shares outstanding at September 18, 2009 of 71,959,642. In addition, the Company has 1,711,429 outstanding Warrants and 2,964,001 outstanding Options, exchangeable for one Common Share upon exercise. The Series II Preferred Shares with conversion rights are exchangeable for a maximum of 6,521,677 Common Shares.

## **Critical Accounting Estimates**

The Company's discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with Canadian Generally Accepted Accounting Principles (GAAP). The Company has identified the following accounting policies that it believes require application of management's most subjective judgments, often requiring the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. The actual results could differ from these estimates and such differences could be material.

The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, the Company evaluates its estimates, including cash requirements, by assessing planned research and development activities and general and administrative requirements, the retention of key personnel, required clinical trial activity, market need for its drug candidates, and other major business assumptions.

### **Allowance for Doubtful Accounts**

The Company maintains an allowance for doubtful accounts related to its accounts receivable. Accounts receivable are reviewed on a regular basis to determine if any receivables have a high risk of being uncollectible, and include these in the allowance. Based on the information available, the Company believes the allowance for doubtful accounts is appropriate; however, actual write-offs might exceed the recorded allowance.

### **Provision for Inventory Obsolescence**

Provisions for inventory are charged against income when it is determined that specific inventory items do not meet the defined quality and regulatory requirements for sale. The Company does not take general provisions for inventory obsolescence. The Company regularly reviews its inventories for

obsolescence and valuation issues. Should selling prices and demand for inventory decline, additional provisions for obsolescence and valuation may be necessary. Provisions for inventory obsolescence require the Company to make a number of estimates. Inventory is reviewed on a product-by-product basis, and any valuation allowances are written off to cost of sales.

Inventories are valued at the lower of cost and net realizable value, with cost being determined on a weighted average basis. Cost is comprised of direct materials, direct labour and an overhead allocation.

### Refundable Investment Tax Credits

The Company incurs research and development expenditures which are eligible for refundable provincial investment tax credits. The investment tax credits recorded are based on estimates of amounts expected to be recovered and are subject to audit by the taxation authorities. Accordingly, these amounts may vary. The amount of research and development tax credit receivables recorded as at June 30, 2009 is \$0.1 M [2008 – \$1.1 M].

### Valuation Allowance on Future Tax Assets

The Company recorded a valuation allowance on all future tax assets related primarily to operating losses, as well as research and research expense carry-forwards. The related tax benefits are not likely to be realized based upon the Company's historic results and estimated future taxable income and tax planning strategies in the related jurisdictions. However, the implementation of future tax planning strategies or the generation of future taxable income in these jurisdictions could result in the recognition of a portion or all of these carry-forwards, which could result in a material increase in the Company's results of operations through the recovery of future income taxes.

### Stock-Based Compensation

The Company has a stock-based compensation plan for directors, executives, employees and consultants and has applied the fair value method of accounting. The fair value of stock options granted is determined at the measurement date using the Black-Scholes option pricing model, and expensed over the vesting period of the options, with a corresponding increase to additional paid-in capital. Assumptions that affect the application of the fair value method include the determination of the volatility of our share price and the expected life of the options issued.

### Assessment of Impairment of Goodwill and Long-lived Assets

The assessment of the impairment of goodwill and long-lived assets requires the use of careful judgment and significant estimates including

those related to unit sales, gross margins, cost of sales, market size and penetration, sales and marketing costs, etc., and their expected timing. Goodwill is tested annually, and long-lived assets are tested when indicators of impairment are present. During the years ended June 30, 2009 and 2008, the Company did not record any long-lived asset or goodwill impairment losses.

## Recent Accounting Pronouncements/Transition to IFRS

In February 2008, the CICA issued Section 3064, *Goodwill and Intangible Assets*. Section 3064, which replaces Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*, establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This standard is effective for the Company's interim and annual financial statements beginning on January 1, 2009. The Company is currently determining the impact of the application of this new section on its consolidated financial statements.

The CICA will converge Canadian GAAP with International Financial Reporting Standards ["IFRS"] over a transition period to end in 2011. The Company is currently in the diagnostic phase of the conversion of its consolidated financial statements to IFRS. This phase includes identifying the differences between existing Canadian GAAP and IFRS standards and evaluating their impact on business processes and information systems, as well as assessing resource requirements for the conversion. The Company has provided, and will continue to provide, training to its staff. The Company expects to complete its analysis over the next two quarters.

By December 31, 2009, when the diagnostic phase is complete, the Company will prepare a detailed conversion plan in the third quarter of Fiscal 2010 and thereafter begin execution of this plan. It is currently not possible to fully determine the impact of conversion to IFRS on the consolidated financial statements and any potential business impacts, as the diagnostic phase is not complete and accounting standards and related interpretations continue to change.

## Non-GAAP & Other Measures

The following measures included in the MD&A do not have a standardized meaning under Canadian Generally Accepted Accounting Principles (GAAP) and, therefore, are unlikely to be comparable to similar measures presented by other companies:

**EBITDA:** Means "Earnings before Interest, Taxes, Depreciation, Amortization and foreign exchange". The Company considers EBITDA to be an effective measure of each segment's contribution to the Company on an operational basis. It is management's view that this measure is used by analysts and shareholders to evaluate the financial performance of the Company's operations.

**Burn Rate:** Means consolidated cash flow used in operations. This information can be found in the Consolidated Statements of Cash Flows, under Operating Activities. It shows the cash flow used in operations (before change in non-cash working capital balances related to operations).

## Risks and Uncertainties

Before making an investment decision with respect to the Company's Common Shares, investors should carefully consider the following risk factors, in addition to the other information included or incorporated by reference into this report and the annual report for the fiscal year ended June 30, 2008. The risks as set out in the annual report remain unchanged. The primary risks that may affect the Company during this fiscal year are summarized below. If any of the risks and uncertainties occurs, the business, financial condition, prospects, or results of operations for the Company would likely suffer.

**Cash Flow and Financial Resources:** The current burn rate, excluding revenues from licensing milestone payments, of approximately \$0.5M per month on average is expected to remain and grow during Fiscal 2010, contingent upon the start of the of the second Phase III clinical trial with *Urocidin*<sup>TM</sup> in first-line treatment of non-muscle-invasive bladder cancer. In the near-term, the Company will require cash to fund operations. The Company believes that it will be able to obtain long-term capital to support its corporate objectives. The Company could pursue many opportunities to raise financial resources. However, it is impossible to guarantee the availability of additional financial resources or that these will be available under acceptable terms and conditions. If the Company does not obtain adequate funds or funds on reasonable terms, it may need to:

- Terminate or delay clinical trials of product candidates;
- Delay the build-out of manufacturing capabilities;
- Curtail significant product development programs;
- Sell or assign rights to our technologies, existing products, or product candidates; and/or
- Undertake a corporate reorganization.

**The Company may be unable to achieve certain milestones associated with external partnerships, which could curtail future development and negatively impact the Company's share price.**

The Company's product candidates require significant funding to reach regulatory approval upon positive clinical results. Such funding, in particular for *Urocidin*<sup>TM</sup> in bladder cancer, may be very difficult, or impossible to raise in the capital markets without significant dilution. If the near term milestones contemplated in the current partnership agreement with Endo Pharmaceuticals are not attainable, the development of *Urocidin*<sup>TM</sup> may be significantly delayed or stopped altogether. The announcement of such delay or discontinuation of development may have a negative impact on the Company's share price. The Company cannot assure that parties will perform their obligations as expected or devote adequate resources to programs. In addition, the Company could become involved in disputes with its partner(s), which could result in a delay or termination of the related development programs or result in litigation.

**Clinical trials are long, expensive and uncertain processes, and Health Canada or the FDA may ultimately not approve any of the Company's product candidates. The Company may never develop any further commercial drugs or other products that generate revenues.** The products under research have not yet received regulatory approval. The Company cannot market a pharmaceutical product in any jurisdiction until it has completed thorough pre-clinical testing and clinical trials, in addition to that jurisdiction's extensive regulatory approval process. In general, significant research and development and clinical studies are required to demonstrate the safety and effectiveness of products before the Company can submit any regulatory applications. Clinical trials are long, expensive and uncertain processes. Clinical trials may not be commenced or completed on schedule, and Health Canada or the FDA may not ultimately approve the Company's product candidates for commercial sale. Further, even if the results of the Company's pre-clinical studies or clinical trials are initially positive, it is possible that the Company will obtain different results in the later stages of drug development or that results seen in clinical trials will not continue with longer term treatment. Drugs in late stages of clinical development may fail to show the desired safety and efficacy traits despite having progressed through initial clinical testing. For example, positive results in early Phase I or Phase II clinical trials may not be repeated in larger Phase II or Phase III clinical trials. The results of the Company's Phase III clinical trials with *Urocidin*<sup>TM</sup> in bladder cancer may not meet the primary endpoint of the studies, despite promising preclinical and early stage clinical data.

In addition, unacceptable toxicities or adverse side effects may occur at any time in the course of clinical trials or, if any products are successfully developed and approved for marketing, during commercial use of any approved products. The appearance of any such unacceptable toxicities or adverse side effects could interrupt, limit, delay or abort the development of any of the Company's product candidates or, if previously approved, necessitate their withdrawal from the market. Furthermore, disease resistance or other unforeseen factors may limit the effectiveness of the Company's potential products. The clinical trials of any of the Company's drug candidates could be unsuccessful, which would prevent it from advancing, commercializing or partnering the drug. The Company's failure to develop safe, commercially viable drugs would substantially impair its ability to generate revenues and sustain its operations and would materially harm its business and adversely affect its share price.

**Early Stage Development:** Several of the Company's products or processes are at an early stage of development. Significant additional investment in research and development and clinical trials of such product and process candidates is required prior to commercialization. A commitment of substantial time and resources is required to conduct research and clinical trials if the Company is to complete the development of any product or process. It is not known whether any of these product or process candidates will meet applicable health regulatory standards and obtain required regulatory approvals, whether such products or processes can be produced in commercial quantities at reasonable costs and be successfully marketed, or if the Company's investment in any such product or process candidate will be recovered through sales or royalties.

**Manufacturing Facilities:** The Company relies on having properly validated, fully functioning, manufacturing facilities of sufficient size in which to produce its products for market. Should systems fail, or a disaster strike, the ability to produce products would be negatively affected which, in turn, would affect revenue generation. The Company does not currently have backup manufacturing capacity for some of its key products. As a result, it would be forced to turn to external manufacturers should an unexpected event as described above occur.

**Government Regulations:** The manufacture and sale of animal and human therapeutic products is governed by numerous statutes and regulations in the United States, Canada, Ireland, and other countries where the Company intends to market its products. The subject matter of such legislation includes approval of manufacturing facilities, controlled research and testing procedures, review and approval of manufacturing,

pre-clinical, and clinical data prior to marketing approval, adherence to good manufacturing practices (GMP) during production and storage, and regulation of marketing activities, notably advertising and labeling. The Company's products and processes will require significant development, pre-clinical and clinical testing, and investment of significant funds prior to their commercialization. There can be no assurance that any such products will actually be developed. The process of completing clinical testing and obtaining required approvals is likely to take several years and require the expenditure of substantial resources. Furthermore, there can be no assurance that the regulators will not require modification to submissions, which may result in delays or failure to obtain regulatory approval. Any delay or failure to obtain regulatory approvals could adversely affect the ability of the Company to utilize its technology, thereby adversely affecting operations. Further, there can be no assurance that the Company's product candidates will prove to be safe and effective in clinical trials, nor that they will receive the requisite regulatory approval. Foreign markets, other than the United States and Canada, impose similar restrictions.

**Key Personnel:** The Company's success is also dependent upon its ability to attract and retain a highly-qualified work force, and to establish and maintain close relations with research centres. Competition is intense and the Company's success will depend, to a great extent, on its senior executives, scientific staff, and collaborators. The loss of key personnel could compromise the rhythm and success of product development.

**Foreign Currency Risks:** The Company is exposed to foreign currency risks as a result of the sales of products, purchases of materials, and costs of manufacturing operations in currencies other than the Canadian dollar.

**Volatility of Share Prices:** Share prices are subject to change because of numerous different factors related to Company activity, including reports of new information, changes in the Company's financial situation, the sale of shares in the market, the Company's failure to obtain results in line with the expectations of analysts, an announcement by the Company or any of its competitors concerning technological innovation, etc. During the past few years, shares of Bioniche Life Sciences Inc., other biopharmaceutical companies, and the capital market in general have been subjected to extreme fluctuations that were unrelated to the operational results of the companies affected. There is no guarantee that the market price of Company shares will be protected from any such fluctuations in the future.

**Intellectual Property Infringement Claims:** Third parties may claim that we infringe upon their intellectual property. Any such claims, with or without merit, could materially harm our business and operating results.

**Suppliers:** The Company is dependent on certain third parties for the supply involved in the manufacturing of certain key products. Although the Company seeks to secure alternative suppliers, an interruption in the availability of certain raw material sources could have a material adverse effect on the Company's business and financial condition.

### OTHER RISKS AND UNCERTAINTIES

If any of the following risks occur, the Company's business, results of operations or financial condition could be materially adversely affected.

- The Company expects to continue to experience losses. It is also difficult to estimate timing and future costs of its research and development programs.
- The Company is indirectly subject to price regulation in certain countries and this could affect its gross margin.
- The Company may not achieve its projected development goals in the timeframes it announces and expects.
- Rapid technological change could make the Company's products obsolete.
- The Company faces uncertainties related to regulatory approval which could result in delays in product commercialization in certain territories.
- Even if the Company obtains marketing approval, its products will be subject to ongoing regulatory review.
- The Company's products, if approved, may fail to achieve market acceptance.
- Development of drugs can be costly and require years of research and development activities.
- If the Company cannot raise additional capital on acceptable terms, it may delay or be unable to pursue further development of its product portfolio, obtain regulatory approvals or commercialize its product candidates.
- If the Company is unable to protect its intellectual property rights, its competitors may develop and market products with similar features that may reduce demand for its products and the effective commercialization of its products may be inhibited.
- The Company may become involved in lawsuits to protect or enforce its patents that would be expensive and time consuming.
- If third-party manufacturers of the Company's products fail to devote sufficient time and resources to its concerns, or if their performance is substandard, clinical trials and product introductions may be delayed and its costs may rise.
- The Company may not be able to manufacture its products in commercial quantities, which would prevent it from marketing its products.
- The Company may not be able to successfully achieve its goals.
- The Company has international operations that expose it to additional business risks.
- The Company may incur losses associated with foreign currency fluctuations.
- The Company is subject to the risk of product liability claims, for which it may not have, or be able to obtain, adequate insurance coverage.
- Some of the Company's products involve may use hazardous materials and, as a result, it is exposed to potential liability claims and to costs associated with complying with laws regulating hazardous waste.
- Future sales of Common Shares by the Company or its existing lenders or shareholders may cause its share price to fall.
- The Company has never paid dividends on its Common Shares, and it does not anticipate paying any cash dividends in the foreseeable future.
- The Company has international operations that expose it to additional business risks.

## Effectiveness of Disclosure Controls

In accordance with National Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings ["National Instrument 52-109"], the Company is responsible for establishing and maintaining internal control over financial reporting of the Company, which is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's consolidated financial statements in accordance with Canadian GAAP. Due to the inherent limitations in any control system, internal control over financial reporting may not prevent or detect all material misstatements. Also, any conclusions on the effectiveness of a system of internal control in the future are subject to risk as the system may be or become inadequate for many reasons, including due to changes in business conditions, personnel changes and/or the impact of other risks and uncertainties on internal controls.

Management has used the framework of the Committee of Sponsoring Organizations of the Treadway Commission ["COSO"] to evaluate the effectiveness of the Company's internal control over financial reporting.

The Chairman, President and Chief Executive Officer and the Chief Financial Officer, together with management, have not completed the evaluation of the effectiveness of the Company's disclosure controls and procedures

["DCP"] and internal controls over financial reporting ["ICFR"] as of June 30, 2009. During this challenging year, due to the circumstances faced by the Company as a result of its financial condition, the Company had to limit the resources available for the evaluation in favour of those dedicated to improving its financial condition through efforts to raise financing. As a result, the evaluations could not be completed.

Based on the work completed to date, the Company has identified a material weakness in its DCP and ICFR which it believes arose as a result of the aforementioned challenges and the resulting resource and workload constraints. Consequently, the Company's review and approval process could not be carried out as normal. Because of the pervasive nature of this deficiency, and its impact on the financial statement close process, it is a material weakness such that there is a reasonable possibility that a material misstatement of the Company's financial statements will not be prevented or detected on a timely basis. In the year ended June 30, 2009, there were certain adjustments to the amounts or disclosures of the following items: Inventories and liabilities.

Following the identification of this deficiency, appropriate adjustments were made, and management believes that the consolidated financial statements and notes included in this report present fairly the financial results of the Company for the year ended June 30, 2009.

The Company plans to continue to review and make the necessary changes to its ICFR policies and procedures to remediate this deficiency, including the hiring of additional resources in the accounting and finance department. These new resources, combined with changes in the Company's financial condition, should result in improvements in its review and approval process, particularly the financial statement close process. The Company expects to complete the evaluation of its ICFR in the next six months and will keep investors apprised of the continued progress on this evaluation and in its remediation efforts in its future interim reports.

## Forward-Looking Statements

This discussion and analysis contains certain forward-looking statements that are subject to risks and uncertainties that may cause the results or events predicted in this document to differ materially from actual results or events. No assurance can be given that results, performance or achievement expressed in, or implied by, forward-looking statements within this disclosure will occur or, if they do, that any benefit may be derived from them.

## Other Information About the Company

Additional information relating to the Company, including the Annual Information Form (AIF), is available on SEDAR at [www.sedar.com](http://www.sedar.com).



Patrick Montpetit, CA, CF

Vice-President, Finance and Chief Financial Officer

September 17, 2009

To the Shareholders of

**Bioniche Life Sciences Inc.**

We have audited the consolidated balance sheets of Bioniche Life Sciences Inc. [the "Company"] as at June 30, 2009 and 2008 and the consolidated statements of loss and comprehensive loss, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at June 30, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Montreal, Canada

September 3, 2009

(except for Note 9, which is as of September 10, 2009)

*Ernst & Young s.r.l.*

Chartered Accountants

**Bioniche Life Sciences Inc.**

Amalgamated under the laws of Ontario

## CONSOLIDATED BALANCE SHEETS

[see going concern uncertainty — note 1]

As at June 30	2009 \$	2008 \$
<b>ASSETS</b> [notes 8 and 9]		
<b>Current</b>		
Cash and cash equivalents	5,949,617	4,399,065
Accounts receivable [note 4[a]]	3,720,123	6,443,299
Inventories [note 5]	5,407,624	4,738,765
Prepaid expenses and deposits	569,605	640,326
Restricted cash [note 11[c]]	1,227,374	—
Foreign currency embedded derivatives	—	59,693
	<b>16,874,343</b>	<b>16,281,148</b>
<b>Long-term</b>		
Property, plant and equipment [note 6]	9,494,013	9,718,157
Intangible assets [note 7]	6,791,777	7,688,698
Goodwill	456,155	456,155
Long-term accounts receivable [note 4[b]]	1,025,152	478,852
	<b>34,641,440</b>	<b>34,623,010</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current</b>		
Revolving credit facility [note 8]	4,447,836	2,593,059
Accounts payable and accrued liabilities	11,607,217	8,341,398
Income and other taxes payable	321,166	104,592
Deferred government assistance [note 11[c]]	342,269	—
Current portion of long-term debt and obligations under capital leases [notes 9 and 10]	634,427	458,713
	<b>17,352,915</b>	<b>11,497,762</b>
<b>Long-term</b>		
Long-term debt [note 9]	1,148,706	1,673,853
Obligations under capital leases [note 10]	1,224,767	1,424,029
Government assistance loans [note 11[c]]	2,475,975	—
Deferred government incentives [note 11]	3,335,548	3,606,926
	<b>25,537,911</b>	<b>18,202,570</b>
<b>Shareholders' equity</b>		
Share capital [note 12]	95,855,503	92,941,966
Special warrants [note 12]	—	2,174,008
Other paid-in capital [note 12]	8,539,529	6,056,115
Deficit	(95,291,503)	(84,751,649)
	<b>9,103,529</b>	<b>16,420,440</b>
	<b>34,641,440</b>	<b>34,623,010</b>

Commitments and contingencies [note 19]  
See accompanying notes

On behalf of the Board:

  
Director

  
Director

## Bioniche Life Sciences Inc.

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY***[see going concern uncertainty — note 1]*

	Common shares		Preferred shares — Series 1		Preferred shares — Series II		Special warrants	Other paid-in capital	Deficit	Total
	#	\$	#	\$	#	\$	\$	\$	\$	
Balance, June 30, 2007	61,711,867	81,078,737	167	161,000	9,000,000	8,798,787	2,174,008	5,528,059	(68,630,615)	29,109,976
Transition adjustment	—	—	—	—	—	—	—	—	134,674	134,674
Net loss for the year	—	—	—	—	—	—	—	—	(16,255,708)	(16,255,708)
Issued under employee share ownership plan [note 12(c)(iii)]	808,291	638,500	—	—	—	—	—	—	—	638,500
Fair value of stock options vested [note 12(e)]	—	—	—	—	—	—	—	388,731	—	388,731
Directors' remuneration	73,560	76,502	—	—	—	—	—	—	—	76,502
Share bonus [note 12(c)(iii)]	516,886	408,340	—	—	—	—	—	—	—	408,340
Warrants issued in connection with the revolving credit facility [note 8]	—	—	—	—	—	—	—	112,000	—	112,000
Revolving credit facility principal payments made in shares [note 12(c)(ii)]	2,671,900	1,780,100	—	—	—	—	—	—	—	1,780,100
Warrants issued to a consultant	—	—	—	—	—	—	—	27,325	—	27,325
Adjustment for conversion of fractional shares	6	—	—	—	—	—	—	—	—	—
<b>Balance, June 30, 2008</b>	<b>65,782,510</b>	<b>83,982,179</b>	<b>167</b>	<b>161,000</b>	<b>9,000,000</b>	<b>8,798,787</b>	<b>2,174,008</b>	<b>6,056,115</b>	<b>(84,751,649)</b>	<b>16,420,440</b>

See accompanying notes

Bioniche Life Sciences Inc.

**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (CONTINUED)**

[see going concern uncertainty — note 1]

	Common shares	Preferred shares — Series 1	Preferred shares — Series II	Special warrants	Other paid-in capital	Deficit	Total
	#	#	#	\$	\$	\$	\$
Balance, June 30, 2008	65,782,510	167	9,000,000	2,174,008	6,056,115	(84,751,649)	16,420,440
Transition adjustment [note 3]	—	—	—	—	—	(39,350)	(39,350)
Net loss for the year	—	—	—	—	—	(10,500,504)	(10,500,504)
Issued under employee share ownership plan [note 12[c][iii]]	1,171,916	—	—	—	—	—	593,447
Fair value of stock options vested [note 12[e]]	—	—	—	—	247,391	—	247,391
Directors' remuneration	161,672	—	—	—	—	—	113,170
Warrants issued in connection with the revolving credit facility [note 8]	—	—	—	—	61,315	—	61,315
Revolving credit facility principal payments made in shares [note 12[c][ii]]	4,565,049	—	—	—	—	—	1,966,920
Special warrants expired	—	—	—	(2,174,008)	2,174,008	—	—
Options issued to a consultant	—	—	—	—	700	—	700
Write-off of employee share purchase loan [note 12[c][iv]]	—	—	—	—	—	—	240,000
<b>Balance, June 30, 2009</b>	<b>71,681,147</b>	<b>167</b>	<b>9,000,000</b>	<b>8,798,787</b>	<b>8,539,529</b>	<b>(95,291,503)</b>	<b>9,103,529</b>

See accompanying notes

## Bioniche Life Sciences Inc.

**CONSOLIDATED STATEMENTS OF LOSS  
AND COMPREHENSIVE LOSS***[see going concern uncertainty — note 1]*

Years ended June 30	2009 \$	2008 \$
<b>REVENUE</b>		
Sales	33,281,029	27,468,085
Cost of sales (excluding amortization) <i>[note 5]</i>	14,431,868	12,695,925
Gross profit	18,849,161	14,772,160
<b>EXPENSES</b>		
Administration	6,108,984	6,710,565
Marketing and selling	6,096,518	6,703,929
Other expenses <i>[note 17]</i>	863,257	—
Interest on long-term debt	323,645	203,210
Other interest, net	357,776	(1,450)
Accreted interest on discounted receivables and interest free loans	(3,995)	(13,819)
Amortization of property, plant and equipment	1,342,918	1,202,328
Amortization and write-down of intangible assets	896,921	856,517
Amortization of financial expenses	1,787,104	767,921
Foreign exchange loss (gain)	(250,876)	232,822
	17,522,252	16,662,023
Income (loss) before research and development expenses and other items	1,326,909	(1,889,863)
Research and development expenses, gross	13,314,889	15,972,660
Less: government incentives, net <i>[note 11]</i>	(1,861,730)	(1,918,380)
Change in unrealized loss on foreign currency embedded derivatives	59,693	126,988
Loss before income taxes	(10,185,943)	(16,071,131)
Provision for income taxes <i>[note 16]</i>	314,561	184,577
<b>Net loss and comprehensive loss for the year</b>	<b>(10,500,504)</b>	<b>(16,255,708)</b>
<b>Basic and fully diluted net loss per share</b>	<b>(0.15)</b>	<b>(0.26)</b>
<b>Weighted average number of common shares outstanding</b>	<b>70,313,509</b>	<b>63,104,876</b>

*See accompanying notes*

**Bioniche Life Sciences Inc.**

### CONSOLIDATED STATEMENTS OF CASH FLOWS

*[see going concern uncertainty — note 1]*

Years ended June 30	2009 \$	2008 \$
<b>OPERATING ACTIVITIES</b>		
Net loss for the year	(10,500,504)	(16,255,708)
Add (deduct) non cash items:		
Amortization	3,926,943	2,826,766
Amortization of deferred government incentives <i>[note 11]</i>	(311,266)	—
Change in unrealized loss on foreign currency embedded derivatives	59,693	126,988
Accreted interest on discounted receivables and interest-free loans	(3,995)	(13,819)
Write-off of intangible assets	100,000	—
Unrealized foreign exchange loss (gain)	184,798	(34,680)
Deemed government assistance	(283,734)	—
Stock-based compensation	487,391	388,731
Warrants issued to consultants	700	27,325
Share bonus and shares issued to directors	—	544,507
Employee share ownership plan	532,827	684,556
	(5,807,147)	(11,705,334)
Increase in restricted cash	(1,227,374)	—
Net change in non-cash working capital balances <i>[note 20]</i>	4,068,689	62,188
<b>Cash used in operating activities</b>	<b>(2,965,832)</b>	<b>(11,643,146)</b>
<b>INVESTING ACTIVITIES</b>		
Proceeds from maturity of short-term investments	—	9,500,000
Government incentives received on account of property, plant and equipment	79,798	4,641
Purchases of property, plant and equipment	(1,404,799)	(584,573)
<b>Cash provided by (used in) investing activities</b>	<b>(1,325,001)</b>	<b>8,920,068</b>
<b>FINANCING ACTIVITIES</b>		
Proceeds from term note <i>[note 9]</i>	—	1,750,000
Proceeds from government assistance <i>[note 11[c]]</i>	3,408,936	—
Payment of financing fees – debt	(11,036)	(88,010)
Proceeds from deferred government incentives	121,360	49,965
Proceeds from revolving credit facility	31,474,720	26,759,247
Repayment of revolving credit facility	(28,447,761)	(22,635,316)
Repayment of capital lease obligations	(297,771)	(217,232)
Repayment of long-term debt	(407,063)	(20,108)
<b>Cash provided by financing activities</b>	<b>5,841,385</b>	<b>5,598,546</b>
<b>Net increase in cash and cash equivalents during the year</b>	<b>1,550,552</b>	<b>2,875,468</b>
Cash and cash equivalents, beginning of year	4,399,065	1,523,597
<b>Cash and cash equivalents, end of year</b>	<b>5,949,617</b>	<b>4,399,065</b>

*See accompanying notes*

June 30, 2009 and 2008

## 1. Nature of the Business and Going Concern Uncertainty

### NATURE OF THE BUSINESS

Bioniche Life Sciences Inc. [the "Company"], is a Canadian biopharmaceutical company engaged in the research, development, manufacturing and commercialization of human and animal health products and technologies worldwide. The Company's common stock is traded on the Toronto Stock Exchange ["TSX" symbol "BNC"].

Headquartered in Belleville, Ontario, the Company has offices and manufacturing facilities in Canada, the United States, Europe, and Australia.

The Company has three business units: **Human Health**, **Animal Health**, and **Food Safety**.

- The **Human Health business unit** is responsible for research, discovery and clinical development of human health products. Its revenues are generated from sales of proprietary products, royalties and licensing arrangements.
- The **Animal Health business unit** is responsible for the research, development, manufacturing and marketing of animal health products worldwide. Established in 1979, Bioniche Animal Health develops technologies to replace antibiotics in live-stock, among other activities. The Animal Health unit has operations in Canada, the United States, Europe and Australia.
- The **Food Safety business unit** is responsible for research, development, manufacturing and marketing of biopharmaceutical animal health products to help prevent disease in humans and improve the safety of food and water supplies worldwide. The current leading initiative for the unit is the development and commercialization of a cattle vaccination to help reduce the spread of the *E.coli* O157 bacteria.

### GOING CONCERN UNCERTAINTY

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ["GAAP"] on a going concern basis, which presumes the Company will continue in operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the ordinary course of business for the foreseeable future. The use of these principles may not be appropriate. As of June 30, 2009, there was uncertainty that the Company will be able to continue as a going concern without obtaining additional financial resources.

The Company has incurred significant losses and has an accumulated deficit of \$95,291,503 as at June 30, 2009. The Company's committed cash obligations and expected level of expenditures for fiscal 2010 exceed its committed sources of funds which include the US\$20 million upfront payment received subsequent to June 30, 2009 upon signature of the license, development and supply agreement less the repayment of its revolving credit facility and related fees [note 22] and funds available as at June 30, 2009. The Company expects to finance its future expenditures, by receiving certain payments on accomplishing milestones along with receiving reimbursements for certain costs associated with the conduct of the *Urocidin*<sup>TM</sup> clinical programs, from its licensing partner. If the Company is unable to accomplish the milestones on a timely basis, which is outside of management's control, the Company may be required to obtain additional financing and curtail the Company's development activities and operations.

These consolidated financial statements do not give effect to any adjustments to the amounts and classifications of assets and liabilities that may be necessary should the Company be unable to continue as a going concern, and such adjustments could be material.

June 30, 2009 and 2008

## 2. Summary of Significant Accounting Policies

### BASIS OF CONSOLIDATION

The consolidated financial statements reflect the consolidated financial position and results of operations of the Company and its active subsidiaries, Bioniche Animal Health Canada Inc., Bioniche Animal Health USA, Inc., Bioniche Animal Health (Europe) Limited., Bioniche Animal Health (A/Asia) Pty. Ltd., and Bioniche Therapeutics.

### USE OF ESTIMATES

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant estimates include, but are not limited to, the measure of allowance for doubtful accounts, impairment assessments, tax credits, as well as stock-based compensation. The reported amounts and note disclosures are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. Actual results, however, may differ from the estimates used in these consolidated financial statements and such differences may be material.

### CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash and highly liquid short-term investments with maturities of less than three months from the date of acquisition that are readily convertible to known amounts of cash at any time and that are subject to an insignificant risk of change in value. Due to the liquid nature of these financial assets, the Company has elected to classify them as held for trading and changes in fair value are recorded in the consolidated statement of loss and comprehensive loss. As at June 30, 2009, cash and cash equivalents consisted entirely of cash [2008 – \$2,491,964 cash and \$1,907,101 cash equivalents].

### SHORT-TERM INVESTMENTS

Short-term investments are recorded at fair value, based on published price quotations.

### INVENTORIES

Inventories are valued at the lower of cost and net realizable value, with cost being determined on a weighted average basis. Cost is comprised of direct materials, direct labour and an overhead allocation.

### PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are carried at cost less any applicable government assistance.

Assets acquired under capital leases are carried at cost, being the present value of the minimum lease payments after the deduction of any executory costs.

Amortization of property, plant and equipment is calculated over their estimated useful lives using the following methods and rates:

Buildings	5% declining balance
Building under capital lease	straight-line basis over ten years
Equipment	20% declining balance
Equipment under capital lease	20% declining balance
Computer equipment	straight-line basis over five years
Automobiles	straight-line basis over five years
Automobiles under capital lease	straight-line basis over five years
Leasehold improvements	straight-line basis over the lease term

June 30, 2009 and 2008

## 2. Summary of Significant Accounting Policies [Cont'd]

Construction in progress comprises construction and engineering costs. No amortization is recorded until construction is substantially complete and the assets are ready for productive use. Interest costs relating to funds borrowed for construction in progress are expensed as incurred.

### INTANGIBLE ASSETS

Intangible assets represent technology costs, patents and trademarks and the costs to acquire licenses.

Amortization of intangible assets are calculated over their estimated useful lives using the straight-line methods over the following periods:

Technology	over twenty years
License agreements	over a period not more than five years
Patents and trademarks	over the remaining life of the patent

If a license agreement is terminated, the unamortized costs relating to the agreement are charged to income. All costs related to the development of patents and trademarks are expensed as incurred.

### IMPAIRMENT OF LONG-LIVED ASSETS

Property, plant and equipment and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Impairment is assessed by comparing the carrying amount of an asset to be held and used with the total of the undiscounted cash flows expected from its use and disposal. If such assets are considered impaired, the impairment loss to be recognized is measured by the amount by which the carrying amount of the assets exceeds its fair value generally determined on a discounted cash flow basis. Any impairment results in a write-down of the asset and a charge to income during the year.

### GOODWILL

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the tangible and intangible assets acquired, less liabilities assumed, based on their fair values. When the Company enters into a business combination, the purchase method of accounting is used. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test is carried out in two steps. In the first step, the carrying amount of the reporting unit, including goodwill, is compared with its fair value. When the fair value of the reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step of the impairment test is unnecessary. The second step is carried out when the carrying amount of the reporting unit exceeds its fair value, in which case the implied fair value of the goodwill, determined in the same manner as the value of goodwill is determined in a business combination, is compared with its carrying amount to measure the amount of the impairment loss, if any.

### GOVERNMENT INCENTIVES

Government incentives with respect to property, plant and equipment are netted against the related asset cost when earned. Incentives related to research and development are deferred until the respective costs are incurred and all conditions related to the government incentives have been met at which time they are recorded as a reduction of research and development expenses.

June 30, 2009 and 2008

## 2. Summary of Significant Accounting Policies [Cont'd]

### REVENUE RECOGNITION

Product revenue is recognized when the product is shipped to the Company's customers, provided the Company has not retained any significant risks of ownership or future obligations with respect to the product shipped, prices are fixed or determinable, and collection is reasonably assured.

Royalty revenue is recognized on an accrual basis in accordance with the contractual agreements.

Interest income is accrued as it is earned.

Revenue arrangements from research and development collaborations, and licensing arrangements with multiple elements are reviewed in order to determine whether the multiple elements can be divided into separate units of accounting, if certain criteria are met. If separable, the consideration received is allocated among the separate units of accounting based on their respective fair values, and the applicable revenue recognition criteria are applied to each of the separate units. Otherwise, the applicable revenue recognition criteria are applied to combined elements as a single unit of accounting.

Licensing revenue — For up-front non-refundable licensing payments, revenue is deferred and recognized on a straight-line basis during the term over which the Company maintains substantive contractual obligations. For any portion of an up-front licensing payment that is subject to a refund, the revenue is deferred. Once the refund condition lapses, revenue is recognized on a straight-line basis during the term over which the Company maintains substantive contractual obligations. Milestone payments are immediately recognized as licensing revenue when the underlying condition is met, the milestone is not a condition to future deliverables, and collectibility is reasonably assured. Amounts received in advance of recognition are included in deferred revenue.

### RESEARCH AND DEVELOPMENT COSTS

Research costs, which include a share of administration expenses, are charged to income as incurred net of government incentives and tax credits earned. Development costs are charged against income in the period of the expenditure unless a development project meets the criteria under GAAP for capitalization and amortization. At June 30, 2009 and 2008, no development costs have been capitalized.

### FOREIGN CURRENCY TRANSLATION

The Company's foreign subsidiaries are considered to be integrated foreign entities and are accounted for in accordance with the temporal method, as are transactions in foreign currencies entered into by the Company. Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the year-end exchange rate, non-monetary assets and liabilities are translated at the historical exchange rate, and revenue and expense items are translated into Canadian dollars at rates of exchange in effect at the related transaction dates. Exchange gains and losses arising from these transactions are included in income.

### INCOME TAXES

Future tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities, and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future tax assets are recognized only to the extent that it is more likely than not that future tax assets will be realized. A valuation allowance is provided to the extent that tax assets are not expected to be realized.

June 30, 2009 and 2008

## 2. Summary of Significant Accounting Policies [Cont'd]

### EARNINGS (LOSS) PER SHARE

Earnings (loss) per share is calculated using the weighted average number of Common Shares outstanding during the year. Diluted earnings (loss) per share is calculated using the treasury stock method, giving effect to the exercise of all dilutive factors. The treasury stock method assumes that any proceeds that could be obtained upon the exercise of Options would be used to purchase Common Shares at the average market price during the year.

### SHARE ISSUE COSTS

Share issue costs are recorded as a reduction of share capital.

### FINANCING AND TRANSACTION COSTS

Financing costs associated with the issuance of debt are deferred, recorded as a reduction of the carrying value of the related debt and amortized over the term of the related debt using the effective interest rate method. Transaction costs, such as legal fees, that are directly attributable to the acquisition or issuance of financial assets or liabilities follow the same accounting treatment as financing costs.

### STOCK-BASED COMPENSATION AND OTHER STOCK-BASED PAYMENTS

The Company has a stock-based compensation plan and has applied the fair value method of accounting. The fair value of Stock Options granted is determined at the measurement date using the Black-Scholes Option pricing model, and expensed over the vesting period of the Options, with a corresponding increase to other paid-in capital. Any consideration paid on the exercise of Stock Options is credited to share capital.

## 3. Changes in Accounting Policies

The following Handbook Sections, released by the Canadian Institute of Chartered Accountants ["CICA"], were adopted by the Company on July 1, 2008. The impact of the adoption of these sections on the Company's consolidated financial statements is presented below.

Section 3031, *Inventories*, replaces the existing standard for inventories, Section 3030. The main features of the new section are as follows:

- Measurement of inventories at the lower of cost and net realizable value;
- Consistent use of either first-in, first-out or a weighted average cost formula to measure cost; and
- Reversal of previous write-downs to net realizable value when there is a subsequent increase to the value of inventories.

The transitional provisions of the Section require that the standard be applied to the opening inventory of the period, with any resulting adjustment recorded in the opening deficit. The adoption of this Section resulted in a decrease of \$39,350 to the opening inventory as at July 1, 2008 and consequently the opening balance of deficit was increased by \$39,350. Prior periods were not restated. The adoption of this Section had no other impacts on the Company's consolidated financial statements.

Section 3862, *Financial Instruments – Disclosure*, describes the required disclosure for the assessment of the significance of financial instruments for an entity's financial position and performance and of the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. Disclosure requirements pertaining to Section 3862 are contained in note 14.

June 30, 2009 and 2008

### 3. Changes in Accounting Policies [Cont'd]

Section 3863, *Financial Instruments – Presentation*, establishes standards for presentation of the financial instruments and non-financial derivatives. It carries forward the presentation related requirements of Section 3861, *Financial Instruments – Disclosure and Presentation*. The adoption of this section had no impact on the Company's consolidated financial statements.

Section 1535, *Capital Disclosures*, establishes standards for disclosing information about an entity's capital and how it is managed. It describes the disclosure of the entity's objectives, policies and processes for managing capital, the quantitative data about what the entity regards as capital, whether the entity has complied with any capital requirements, and, if it has not complied, the consequences of such non-compliance. Disclosure requirements pertaining to Section 1535 are contained in note 13.

Section 1400, *General Standards of Financial Statement Presentation*. This section has been amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The main features of the changes are as follows:

- Management is required to make an assessment of an entity's ability to continue as a going concern;
- In making its assessment, management takes into account all available information about the future, which is at least, but is not limited to, twelve months from the balance sheet date;
- Financial statements must be prepared on a going concern basis unless management intends to liquidate the entity, to cease trading or cease operations, or has no realistic alternative but to do so;
- Disclosure is required of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern; and
- When financial statements are not prepared on a going concern basis, that fact should be disclosed, together with the basis on which the financial statements are prepared and the reasons the entity is not regarded as a going concern.

#### RECENT ACCOUNTING PRONOUNCEMENTS

Section 3064, *Goodwill and Intangible Assets*. Section 3064, which replaces Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*, establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This standard is effective for the Company's interim and annual financial statements beginning on July 1, 2009. The Company is currently assessing the impact of the adoption of this new section on its consolidated financial statements.

### 4. Accounts Receivable and Long-Term Accounts Receivable

<b>[a] ACCOUNTS RECEIVABLE</b>	<b>2009</b>	<b>2008</b>
	<b>\$</b>	<b>\$</b>
Trade	3,169,547	4,435,985
Government incentives receivable	307,601	1,696,068
Other	242,975	311,246
	<b>3,720,123</b>	<b>6,443,299</b>
<b>[b] LONG-TERM ACCOUNTS RECEIVABLE</b>		
Loans receivable	128,203	128,203
Government incentive holdbacks	1,084,726	495,116
	<b>1,212,929</b>	<b>623,319</b>
Less: Discount to reflect receivables at amortized cost	<b>(187,777)</b>	<b>(144,467)</b>
	<b>1,025,152</b>	<b>478,852</b>

June 30, 2009 and 2008

#### 4. Accounts Receivable and Long-Term Accounts Receivable [Cont'd]

Loans receivable includes \$100,000 at June 30, 2009 and 2008 outstanding from a former director. This amount is collateralized by shares in Bioniche Pharma Holdings Limited, a former subsidiary of the Company and earn-out payments to which the former director may be entitled to over the next two years. The loan is due on December 30, 2011. Loans receivable also includes \$28,203 at June 30, 2009 and 2008 outstanding from the Chairman, President & CEO, who is also a director. The loan is payable in annual installments of \$5,000 per year. Both of these interest free loans have been discounted at 12% and reflect their amortized cost.

Government incentive holdbacks of 10% are being applied on two government programs [note 11]. The Industrial Technology Office ["ITO"] holdback is being discounted at 7.5% with an expected receipt date of September 30, 2011. The Rural Economic Development ["RED"] holdback is being discounted at 5.69% with an expected receipt date of August 31, 2010 [note 11].

#### 5. Inventories

	2009 \$	2008 \$
Raw materials	1,001,449	996,202
Work-in-process	1,875,430	1,060,445
Finished goods	2,530,745	2,682,118
	5,407,624	4,738,765

During the year ended June 30, 2009, inventories in the amount of \$13,731,430 were recognized as cost of goods sold, including provisions for write-downs to net realizable value of \$27,891, and a reversal of previously recorded write-downs of \$44,497 primarily as a result of a change in estimate of unsalable inventory due to short dating, based on current estimates. As at June 30, 2009 inventories in the amount of \$38,158 are carried at their net realizable value.

#### 6. Property, Plant and Equipment

	Cost \$	Accumulated amortization \$	Net book value \$
<b>2009</b>			
Land	1,266,486	—	1,266,486
Buildings	4,616,541	1,368,078	3,248,463
Building under capital lease	1,255,265	186,276	1,068,989
Equipment	7,080,223	5,446,767	1,633,456
Equipment under capital lease	230,376	59,563	170,813
Computer equipment	2,695,572	2,271,864	423,708
Automobiles	304,635	227,718	76,917
Automobiles under capital lease	676,614	179,240	497,374
Leasehold improvements	83,758	81,112	2,646
Construction in progress	1,105,161	—	1,105,161
	19,314,631	9,820,618	9,494,013

June 30, 2009 and 2008

## 6. Property, Plant and Equipment [Cont'd]

	Cost \$	Accumulated amortization \$	Net book value \$
<b>2008</b>			
Land	1,266,486	—	1,266,486
Buildings	4,616,541	1,195,492	3,421,049
Building under capital lease	1,255,265	147,198	1,108,067
Equipment	6,936,453	5,064,826	1,871,627
Equipment under capital lease	230,376	16,861	213,515
Computer equipment	2,618,205	1,721,406	896,799
Automobiles	257,934	204,275	53,659
Automobiles under capital lease	551,933	47,240	504,693
Leasehold improvements	84,158	80,402	3,756
Construction in progress	378,506	—	378,506
	18,195,857	8,477,700	9,718,157

The Company leases a building from an officer and director of the Company. This building is included in building under capital lease and the corresponding capital lease obligation is included in obligations under capital leases [note 10]. The transaction was recorded at its exchange amount.

Amortization of assets under capital leases during the year ended June 30, 2009 amounted to \$213,780 [2008 – \$106,119].

At June 30, 2009, the Company had \$1,105,161 [2008 – \$378,506] in construction in progress relating to the scale up of a vaccine production facility in Belleville, Ontario.

## 7. Intangible Assets

	Cost \$	Accumulated amortization \$	Net carrying amount \$
<b>2009</b>			
Technology	11,974,171	5,623,378	6,350,793
Patents and trademarks	1,032,924	723,940	308,984
License agreements	511,516	379,516	132,000
	13,518,611	6,726,834	6,791,777
<b>2008</b>			
Technology	11,974,171	4,951,296	7,022,875
Patents and trademarks	1,032,924	633,400	399,524
License agreements	611,516	345,217	266,299
	13,618,611	5,929,913	7,688,698

During the year ended June 30, 2009, the Company wrote off a license valued at \$100,000 for a product it will not be pursuing to market.

June 30, 2009 and 2008

### 8. Revolving Credit Facility

	2009 \$	2008 \$
Revolving credit facility [2009 – US \$3,868,374, 2008 – US \$3,097,208]	4,447,836	3,157,294
Less: unamortized financial expenses	—	(564,235)
	<b>4,447,836</b>	<b>2,593,059</b>

On December 19, 2007, the Company's three-year revolving credit facility [the "Facility"] was amended to a maximum available amount of US \$5,500,000 from the previous maximum of US \$4,000,000. Amounts drawn are based on 90% of eligible accounts receivable and 35% of eligible North American inventory, capped at US \$2,500,000 plus an additional US \$3,000,000. A fee of US \$1,000,000 was charged by the lender for this amendment, payable in cash or in shares of the Company, at the discretion of the Company.

On October 31, 2008, the Facility was amended to extend the maturity date to March 2, 2009 and the interest rate became Wall Street Journal (WSJ) prime plus 2.5%, but not less than 10%. A fee of \$601,950 [US \$500,000] was charged by the lender for this amendment, payable in cash or in shares of the Company, at the discretion of the Company.

On March 2, 2009, the Facility became repayable on demand of the lender, and on April 27, 2009 the maturity date was again amended to June 30, 2009. A fee of \$502,800 [US \$400,000] was charged by the lender for this amendment, payable in cash. On June 22, 2009, the maturity date was again amended and the Facility again became repayable on demand.

All fees were recorded as a reduction in the carrying value of the Facility and were amortized over the remaining life of the Facility.

On March 27, 2008, the Company issued 2,671,900 Common Shares in lieu of cash principal repayments of the Facility, totalling \$1,780,100 [US \$1,750,000] and 200,000 five-year warrants valued at \$112,000 using the Black-Scholes Option pricing model using the following assumptions: a risk-free interest rate of 5.5%, expected dividend yield of 0%, expected volatility of 66% and expected life of 5.0 years.

On September 9, 2008, the Company issued 4,565,049 Common Shares in lieu of cash principal repayments of the Facility, totalling \$1,966,920 [US \$1,850,000] and 211,429 five-year Warrants valued at \$61,315 using the Black-Scholes option pricing model using the following assumptions: a risk-free interest rate of 5.5%, expected dividend yield of 0%, expected volatility of 66% and expected life of 5.0 years.

The value of these Warrants was recorded as a reduction of the carrying value of the Facility with a corresponding credit to other paid-in capital and was amortized over the remaining life of the Facility, which at that time ended December 9, 2008, using the effective interest rate method.

The Company had given a first charge over all of its North American assets except for certain intellectual property which is subject to a negative pledge pursuant to an agreement with the Government of Canada. On July 17, 2007, the lender released the mortgage that it had held on the manufacturing facility in Belleville, Ontario.

On July 20, 2009, the Company repaid the Facility in full, as well as electing to pay all outstanding fees, totalling \$2,196,000 [US \$1,900,000], in cash [note 22].

June 30, 2009 and 2008

**9. Long-Term Debt**

	2009 \$	2008 \$
<b>North American Operations</b>		
[a] Business Development Bank of Canada	1,370,000	1,750,000
<b>Australian Operations</b>		
[b] ANZ Bank [2009 – A\$439,907; 2008 – \$470,610]	409,245	458,562
Total senior debt	1,779,245	2,208,562
Less: unamortized financial expenses	64,851	85,118
Less: current portion	565,688	449,591
<b>Total long-term debt</b>	<b>1,148,706</b>	<b>1,673,853</b>

[a] On February 7, 2008, the Company entered into a ten-year, \$5,000,000 commercial loan facility with the Business Development Bank of Canada ["BDC"] repayable in monthly instalments of \$44,000. This loan facility is collateralized by certain property, plant and equipment at the Company's Belleville, Ontario facility and is subject to certain annual financial and non-financial covenants. The loan bears interest, payable monthly, at the BDC floating base rate [at June 30, 2009 – 4.25%; 2008 – 6.75%] plus 2%, but the rate may be fixed at the Company's option at the then current BDC base rate. At June 30, 2009, the effective interest rate on the amount borrowed to date was 8.94% [2008 – 10.53%]. Principal repayments commenced September 1, 2008 with a payment of \$28,000 followed by monthly payments of \$44,000 until repaid. BDC agreed to the payment of interest only for the month of June 2009. Additional drawdowns on this loan facility will only be made if the Company makes certain qualifying expenditures. The proceeds must be used to finance the project to create an animal health and food safety vaccine manufacturing centre in Belleville, Ontario. Financing fees of \$87,338 have been recorded as a reduction of the carrying value of the loan facility and are being amortized over the life of this loan facility using the effective interest rate method.

At June 30, 2009, the Company was in breach of two of its financial covenants. A waiver of the breaches was granted by BDC on September 10, 2009.

As at June 30, 2009, \$1,370,000 [2008 – \$1,750,000] has been drawn on this loan facility [\$528,000 current and \$842,000 long-term, [2008 – \$424,000 current and \$1,326,000]. Commencing October 24, 2008, the Company began to pay a monthly fee equal to 1.5% per annum on the undrawn portion of the loan facility. After January 24, 2009, the BDC may cancel the undrawn portion of the loan facility. The undrawn portion of the loan facility remained available to the Company, however the Company must provide a guaranteed irrevocable letter of credit to draw the last \$500,000 of the loan facility.

[b] The Company entered into a A\$547,185 loan facility with ANZ Bank as of September 30, 2004 repayable over a 15 year term bearing interest at the bank's fluctuating mortgage index rate [2009 – 6.44%; 2008 – 8.94%] plus 1.03%. Principal and interest payments of \$5,582 [A\$6,000] [2008 – \$5,846; A\$6,000] are payable monthly. The Company has provided a first charge over real estate and certain property in Australia with a carrying value of \$633,632 [A\$697,811] [2008 – \$697,951; A\$716,288] as collateral for this facility.

June 30, 2009 and 2008

### 9. Long-Term Debt [Cont'd]

Principal repayments on the Company's long-term debt or the next five years and thereafter are as follows:

	\$
2010	565,688
2011	568,602
2012	357,741
2013	47,122
2014	50,766
Thereafter	189,326
	1,779,245

### 10. Obligations Under Capital Leases

	2009 \$	2008 \$
Building, repayable in monthly instalments of \$16,667 until October 2015, including interest calculated at 10.1% [a]	1,266,666	1,433,334
Leases for equipment, repayable in variable monthly instalments until July 2013, at interest rates ranging from 4.75% to 19.40%	677,852	744,358
	1,944,518	2,177,692
Interest included in minimum lease payments	400,997	496,749
Advances netted against building lease obligations	250,015	247,792
	1,293,506	1,433,151
Less: current portion	68,739	9,122
<b>Total long-term obligations under capital leases</b>	<b>1,224,767</b>	<b>1,424,029</b>

[a] In May 2005, the Company entered into a capital lease with an officer and director to lease a building for a ten-year period. Minimum lease payments are \$16,667 per month. Effective with April 2008's lease payment, the Company had an agreement to reduce its monthly payments for a six-month period to the payment of interest only. The obligation is calculated as the net present value of the future lease payments calculated at 10.1%. In addition, the Company has made non-interest bearing advances repayable on demand during the year related to the leased property in the amount of \$2,223 [2008 – \$20,503] which have been offset against the obligations under this capital lease.

Future annual minimum lease payments for the next five years and thereafter are as follows:

	\$
2010	441,286
2011	387,484
2012	356,680
2013	291,244
2014	201,158
Thereafter	266,666
	1,944,518

June 30, 2009 and 2008

## 11. Deferred Government Incentives and Government Assistance

### [A] INDUSTRIAL TECHNOLOGY OFFICE

Under the federal contribution program with Industry Canada's Industrial Technology Office ["ITO"], the Company is entitled to a reimbursement of 18.3% and 21.6% of the eligible operating and capital expenses incurred in the development and commercialization of *Urocidin*<sup>TM</sup> and the *E. coli* O157 cattle vaccine to a maximum of \$9,600,000 and \$7,600,000, respectively. At the Company's discretion, it can claim reimbursements at accelerated rates of 35% for *Urocidin*<sup>TM</sup> and 28% for the *E. coli* O157 cattle vaccine to the maximum as noted above. Under the agreements, if the Company does not reach certain expenditure levels for *Urocidin*<sup>TM</sup> and the *E. coli* O157 cattle vaccine by September 30, 2011 and March 31, 2013, respectively, the portion of reimbursements received in excess of 18.3% and 21.6% of eligible expenditures become repayable to the ITO. These accelerated reimbursements are recorded as deferred government incentives. Once the maximum eligible reimbursement under each program have been received, claims for additional eligible expenditures will be applied against these deferred government incentive balances and the deferred balances will be recorded as government assistance.

At June 30, 2009, accelerated reimbursements of \$2,675,306 associated with the *Urocidin*<sup>TM</sup> project [2008 – \$2,986,572] and \$660,242 associated with the *E. coli* O157 cattle vaccine project [2008 – \$620,354] are included in long-term liabilities for a total of \$3,335,548 [2008 – \$3,606,926]. The *Urocidin*<sup>TM</sup> project reached the maximum eligible reimbursement under the program during the year ended June 30, 2009. Claims for additional eligible expenditures are being applied against the deferred government incentive balance resulting in \$311,266 recorded as government assistance.

In the event that either *Urocidin*<sup>TM</sup> or the *E. coli* O157 cattle vaccine become commercially available prior to the required expenditure levels being reached, any amounts received under the accelerated claims are not repayable. Total contributions claimed for both projects in Fiscal 2009 were \$679,409 [2008 – \$1,217,871] of which \$39,889 was included in deferred government incentives [2008 – \$79,072] and \$79,798 [2008 – \$84,826] has been netted against the related cost of property, plant and equipment. The remaining amount of \$559,722 [2008 – \$1,053,973], has been presented as a reduction in research and development expense.

#### [i] *Urocidin*<sup>TM</sup>

Under the current terms of the *Urocidin*<sup>TM</sup> agreement with ITO, the maturity date for the project was extended to September 30, 2011; royalties potentially payable to ITO, commencing upon regulatory approval for commercialization, are 6% of gross project revenues, to a cap of \$11,278,115, and annual cash payments of \$960,000 for five years, commencing with the occurrence of either regulatory approval for commercialization or by an agreement with a partner for either funding of the clinical development of the product or for the commercialization of the product, but no earlier than June 2010. On July 10, 2009, the Company signed a licencing agreement for the development and marketing of *Urocidin*<sup>TM</sup> in the US [note 22].

ITO has exercised its option to withhold the last 10% of the funding for the *Urocidin*<sup>TM</sup> project until the project is completed, currently estimated to be September 30, 2011. As a result of the long-term nature of this asset, the Company has discounted the amounts withheld [2009 – \$960,000], [2008 - \$455,106] to its estimated fair value of \$812,200 [2008 – \$357,466] using a discount rate of 7.5% and classified it as a long-term accounts receivable [note 4[b]]. The discount has been reflected as a reduction in government incentives and will be amortized over the term that each claim amount is outstanding, using the effective interest rate method.

June 30, 2009 and 2008

## 11. Deferred Government Incentives and Government Assistance [Cont'd]

### [ii] *E. coli* 0157 Cattle Vaccine

During Fiscal 2008, the Company reached an agreement with ITO to amend the existing agreement supporting the *E. coli* 0157 cattle vaccine project. Under the terms of the new agreement, the maturity date for the project was extended to March 31, 2013; royalties potentially payable to ITO related to gross project revenues, commencing no earlier than July 1, 2010 and no later than July 1, 2014 or the first day of the fiscal year where gross revenue exceeds \$500,000, increased to 2.5% from 1.49% with the cap on ITO's royalties increasing from \$6,763,000 to \$13,638,000, and the requirement to issue Warrants to purchase Common Shares was removed.

### [B] RURAL ECONOMIC DEVELOPMENT PROGRAM

On September 7, 2007, the Company announced an agreement for a government grant from the Rural Economic Development Program ["RED"] in the amount of \$2,000,000 based on eligible expenditures for market development related to its *E. coli* 0157 cattle vaccine. During the year, the RED program agreed to accelerate funding from 50% of eligible expenditures to 70%, with the maximum total funding remaining unchanged. As at June 30, 2009, the Company has recognized \$1,247,260 [2008 – \$400,116] of this grant related to eligible expenditures incurred since August 16, 2007. As a result of a 10% holdback clause in this agreement, the Company has discounted its holdback receivable of \$124,726 [2008 - \$40,010] to its estimated fair value of \$116,221 [2008 – \$35,234] using a discount rate of 5.69% and reclassified it to long-term accounts receivable [note 4[b]]. This discount will be amortized over the term that each claim amount is outstanding, using the effective interest rate method. The eligible amount less the discount has been netted against the related marketing expenses totaling \$843,415 [2008 – \$394,763].

### [C] MINISTRY OF ECONOMIC DEVELOPMENT AND TRADE AND AGRI-OPPORTUNITIES PROGRAM

	2009		
	MEDT \$	Agri-Ops \$	Total \$
Government assistance loans received	2,931,815	477,121	3,408,936
Less: interest-free discount	(729,911)	(258,396)	(988,307)
Accretion of interest	50,817	4,529	55,346
<b>Government assistance loan</b>	<b>2,252,721</b>	<b>223,254</b>	<b>2,475,975</b>
Government assistance related to interest-free discount	729,911	258,396	988,307
Government assistance netted against research and development expenses	(238,846)	(44,888)	(283,734)
Government assistance netted against property, plant and equipment	(207,727)	(154,577)	(362,304)
<b>Deferred government assistance</b>	<b>283,338</b>	<b>58,931</b>	<b>342,269</b>

June 30, 2009 and 2008

### 11. Deferred Government Incentives and Government Assistance [Cont'd]

On December 18, 2007, the Company announced that it was eligible to receive up to \$10,000,000 in Ontario government financing in the form of a loan from the Ontario Ministry of Economic Development and Trade's 'Advance Manufacturing Investment Strategy' program ["MEDT"] to fund eligible expenditures made by the Company since April 12, 2007, to scale up a vaccine production facility in Belleville, Ontario. During the incentive period, which runs until August 22, 2013, the loan is interest-free provided the Company meets certain targets by the end of the incentive period. To reflect the benefit of the interest-free period, the loan is discounted to its estimated fair value using a discount rate equal to the rate charged on the BDC loan described in note 9[a] plus 0.25% [at June 30, 2009 – 6.50%] with the discount shown as a government grant. The discount will be amortized over the interest-free portion of the term of the loan, using the effective interest rate method. No principal payments are due during the incentive period. Interest at 5.69% begins to accrue on the first day following the incentive period. Beginning August 22, 2014 an annual payment of 20% of the principal balance plus accrued interest to that date becomes due. The loan is collateralized by a second charge on certain property and equipment at the Company's Belleville, Ontario facility. An advance received under this program to expedite the scale-up of the vaccine production facility is being held as restricted cash.

On December 20, 2007, the Company announced that it was eligible to receive up to \$5,000,000 in federal government financing in the form of a loan from the Department of Agriculture and Agri-Food (Canada) 'Agri-Opportunities' Program ["Agri-Ops"] to fund eligible expenditures made by the Company since September 21, 2007, and to scale-up the aforementioned vaccine production facility. The loan is interest free. To reflect the benefit of the interest-free status of the loan, the loan is discounted to its estimated fair value using a discount rate equal to two times the rate charged on the BDC loan described in note 9[a] plus 1% [at June 30, 2009 – 13.50%] with the discount shown as a government grant. The discount will be amortized over the term of the loan using the effective interest rate method. Principal repayment begins July 1, 2013, with payments of \$83,333 per month. An advance received under this program to expedite the scale-up of the vaccine production facility is being held as restricted cash.

As at June 30, 2009, \$1,227,374 of the funds advanced under these two programs was restricted to use for future eligible expenses associated with the vaccine manufacturing facility and are therefore shown separately as restricted cash.

#### [D] NON-REFUNDABLE INVESTMENT TAX CREDITS

The Company has available non-refundable investment tax credits of \$7,228,000 as at June 30, 2009 related to research and development expenditures which may be utilized to reduce federal income taxes payable in future years and expire as follows:

	\$
2020	395,000
2021	301,000
2022	532,000
2023	594,000
2024	679,000
2025	1,000,000
2026	1,018,000
2027	1,031,000
2028	790,000
2029	888,000
	7,228,000

The benefits of these non-refundable investment tax credits have not been recognized in the consolidated financial statements.

June 30, 2009 and 2008

### 11. Deferred Government Incentives and Government Assistance [Cont'd]

The government incentives recorded as a reduction of research and development expenses is as follows:

	2009 \$	2008 \$
ITO	559,722	1,053,973
Less: discount to fair value on portion held back	(95,476)	(96,443)
MEDT interest-free discount	238,846	—
Agri-Ops interest-free discount	44,888	—
Amortization of deferred government incentives	311,266	—
Investment tax credits	802,484	960,850
	<b>1,861,730</b>	<b>1,918,380</b>

### 12. Shareholders' Equity

#### SHARE CAPITAL

##### Authorized and Issued

The authorized capital of the Company is as follows:

- unlimited number of Common Shares; and
- unlimited number of Preferred Shares issuable in series with no par value

Share capital at June 30 consists of the following:

	2009 \$	2008 \$
[a] Series I Preferred Shares	161,000	161,000
[b] Series II Preferred Shares	8,798,787	8,798,787
[c] Common Shares	86,895,716	83,982,179
	<b>95,855,503</b>	<b>92,941,966</b>

#### [a] SERIES I PREFERRED SHARES

The Series I shares are redeemable at the Company's option at \$1,000 each plus dividends, if any, which have been declared but not paid. The Series I shares are non-voting and are entitled to a fixed non-cumulative preferential dividend at the rate of 12% per annum. As at June 30, 2009 and 2008, no dividends have been declared or paid.

#### [b] SERIES II PREFERRED SHARES

On November 3, 2004 the Company issued 12,000,000 shares of Series II convertible preferred stock for gross consideration of \$12,000,000. The Series II Preferred Shares are convertible at the option of the holder into Common Shares for five years plus one day at a conversion ratio which is obtained by dividing the fully-accreted value by the applicable conversion price as follows: 25% at \$1.45; 50% at \$2.50; and 25% at \$3.75. The fully accreted value is calculated as the aggregate subscription price of the preferred shares plus 6% per annum until the earlier of conversion or five years from the date of issuance. Issue costs for this private placement totaling \$268,284 were netted against the share capital of the Series II Preferred Shares.

June 30, 2009 and 2008

## 12. Shareholders' Equity [Cont'd]

On June 4, 2007, the holder converted 3,000,000 shares or 25% of their Series II convertible preferred stock at its accreted value for conversion purposes of \$3,463,068 to Common Shares at a conversion price of \$1.45. As a result, 2,388,323 Common Shares were issued.

After the initial five-year plus one-day term, any Series II Preferred Shares outstanding are convertible, at the option of the holder, into Common Shares at the fully accreted value divided by the average market price of the Common Shares less the greater of 5% or the maximum discount permitted by the TSX [subject to the issuance of a maximum of 6,521,677 [2008 – 6,521,677] Common Shares in the aggregate on conversion of all Series II Preferred Shares].

If the trading price of the Common Shares exceeds \$13.50 for 60 consecutive days, the Company may require the holders to convert the Preferred Shares into Common Shares at the conversion ratio applicable on the date of conversion.

The Preferred Shares have voting rights on the basis of the number of Common Shares that the holder would have if the Preferred Shares were converted into Common Shares on the date of the applicable shareholders' meeting.

### [c] COMMON SHARES

#### [i] Revolving debt principal payments made in shares

During the year ended June 30, 2009, the Company made Facility repayments of \$1,966,920 [US \$1,850,000] through the issuance of 4,565,049 Common Shares [2008 - US \$1,750,000 repaid resulting in the issuance of 2,671,900 Common Shares and \$1,780,100 added to share capital].

#### [ii] Share bonus

During the year ended June 30, 2009, the Company did not pay out a share bonus. During the year ended June 30, 2008, the Company issued 516,886 Common Shares as a bonus, resulting in \$408,340 added to share capital.

During the year ended June 30, 2008, the Company accrued a bonus for all eligible employees which it expected to settle by issuing Common Shares of the Company's stock with a fair value of approximately \$504,000. This accrual was reversed during the year ended June 30, 2009.

#### [iii] Employee share ownership plan

The Company has an employee share ownership plan in Canada whereby the Company matches contributions made by employees for the purpose of purchasing the Company's stock. In April this year, issued shares reached the maximum shares available under the plan at which time, the plan was suspended. The Company's portion of this plan is recorded as a stock-based compensation expense in the period incurred and totaled \$532,827 for the year ended June 30, 2009 [2008 – \$684,556]. At June 30, 2009, no Common Shares under this plan remain to be issued [2008 – 86,600 Common Shares remained to be issued and an amount of \$60,620 was recorded in current liabilities].

#### [iv] Employee share purchase loan

During 1995, the Company loaned \$240,000 to a former officer and current director to purchase 40,000 Common Shares, on a non-interest bearing basis with no set terms of repayment. During the year ended June 30, 2009, this loan was forgiven and the corresponding stock-based compensation expense has been included in administration expenses on the statement of loss and comprehensive loss with a corresponding increase to share capital.

June 30, 2009 and 2008

## 12. Shareholders' Equity [Cont'd]

### [d] WARRANTS AND SPECIAL WARRANTS

A summary of the Company's warrants outstanding as at June 30, 2009 is presented below:

Range of exercise prices	Warrants outstanding and exercisable		
	Number Outstanding #	Weighted average remaining contractual life [years] #	Weighted average exercise price \$
\$0.49 to \$1.10	1,711,429	2.20	0.96

The following table summarizes information about the warrants outstanding at June 30:

	2009		2008	
	Warrants #	Weighted average exercise price \$	Warrants #	Weighted average exercise price \$
Outstanding, beginning of year	10,903,861	1.37	10,633,861	1.39
Granted to revolving credit facility holder [note 8]	211,429	0.49	200,000	0.77
Issued to consultant	—	—	70,000	1.04
Expired	(9,403,861)	1.43	—	—
<b>Outstanding, end of year</b>	<b>1,711,429</b>	<b>0.96</b>	<b>10,903,861</b>	<b>1.37</b>

On March 13, 2009, all special warrants and compensation warrants issued under a unit offering completed in March 2007 were delisted, then extended as unlisted warrants to May 12, 2009. The value of this modification was not significant. They have all subsequently expired.

On June 7, 2008, the Company issued 70,000 fully vested warrants with an exercise price of \$1.04 to a consultant as previously approved at the November 8, 2007 Annual Shareholders' Meeting. The fair value of these warrants has been determined using the Black-Scholes option pricing model with the following assumptions: a risk-free interest rate of 5.50%, an expected dividend yield of 0%, an expected volatility of 80% and an expected life of 3.0 years. As the options were fully vested at the grant date, the entire estimated fair value of \$27,325 was recorded as an administration expense, with an offset to other paid-in capital.

### [e] STOCK OPTION PLAN

The Company has a Stock Option Plan for the benefit of employees, officers, directors and consultants such that the maximum number of Common Shares available to be issued under the plan shall not exceed 6,000,000. Under this plan, the Company has issued 3,336,501 [2008 – 3,456,501] Stock Options. In addition, outside of the Stock Option Plan ["Additional Options"], 2,000 Options were issued to a consultant, 780,000 options were granted in fiscal 2006 as an employment inducement and 50,000 Options were issued in fiscal 2004 related to an acquisition expired this year, bringing total outstanding Options to 4,118,501 at June 30, 2009 [2008 – 4,286,501].

June 30, 2009 and 2008

## 12. Shareholders' Equity [Cont'd]

The exercise price of each Option equals no less than the market rate at the date immediately preceding the date of the grant. In general, Options issued under the plan vest and are exercisable in equal amounts over five years at the anniversary date of the grant. The Additional Options have the same terms as the Company's Stock Option Plan except that they will not be issued until target per share prices are attained, at which time the issued Options will vest in equal amounts over five years. The Additional Options have a ten-year contractual life.

During the year ended June 30, 2009, the Company issued 2,000 fully vested Options with an exercise price of \$0.70 to a consultant as previously approved at the November 8, 2007 Annual Shareholders' Meeting. The Company also elected to modify Options previously granted to a member of the Board of Directors, now deceased. The value of this modification of \$4,709 was recorded as an administration expense, with an offset to other paid-in capital.

A summary of the status of the Company's Stock Option Plan as at June 30, 2009 is presented below:

Range of exercise price	Options outstanding			Options exercisable	
	Number outstanding #	Weighted average remaining contractual life [years] #	Weighted average exercise price \$	Number exercisable #	Weighted average exercise price \$
\$0.70 to \$0.93	1,780,000	2.3	0.89	928,000	0.89
\$1.10 to \$1.60	655,000	1.0	1.54	430,000	1.55
\$1.68 to \$2.40	415,000	6.7	2.18	12,000	1.68
\$2.80 to \$3.20	509,001	6.1	3.03	109,001	3.15
\$4.40	759,500	0.2	4.40	627,600	4.40
	4,118,501	2.6	2.04	2,106,601	2.19

The following table summarizes information about stock options outstanding at June 30:

	2009		2008	
	Options \$	Weighted average exercise price \$	Options \$	Weighted average exercise price \$
Outstanding, beginning of year	4,286,501	2.06	3,861,501	2.19
Granted	2,000	0.70	450,000	0.93
Expired	(170,000)	2.06	(25,000)	2.95
Outstanding, end of year	4,118,501	2.04	4,286,501	2.06

Stock-based compensation is recorded as a compensation expense related to the expense category for the service provided by the optionee.

June 30, 2009 and 2008

## 12. Shareholders' Equity [Cont'd]

The fair value of options granted during the year was estimated at the grant date using the Black-Scholes option pricing model, resulting in the following weighted average assumptions:

	2009	2008
Risk-free interest rate	5.50%	5.78%
Expected volatility	81.9%	57.3%
Expected option life	3.0 years	5.0 years
Dividend yield	0%	0%
<b>Weighted-average fair value of options granted</b>	<b>\$0.35</b>	<b>\$0.49</b>

## 13. Management of Capital

The Company's capital management objectives are to safeguard its ability to continue as a going concern and to fund its research and development activities, to pursue its commercialization efforts and to maintain its ongoing operations. To secure the additional capital necessary to pursue these plans, the Company may attempt to raise additional funds through the issuance of debt or equity, and by entering into strategic partnerships which will generate funds to finance its operations.

In the management of capital, the Company includes the revolving credit facility, shareholders' equity, the Business Development Bank of Canada loan ["BDC"] facility and ANZ Bank mortgage included in long-term debt, and government assistance in the form of interest free loans from the Ministry of Economic Development and Trade and the Department of Agriculture and Agri-Food (Canada).

All future advances on the BDC loan facility, the two government assistance loans and advances from the Industrial Technology Office are capital resources targeted for the scale up of the vaccine production facility in Belleville, Ontario.

	2009	2008
	\$	\$
Revolving credit facility	4,447,836	2,593,059
Shareholders' equity	9,103,529	16,420,440
Long-term debt (including current portion)	1,714,394	2,123,444
Government assistance loans	2,475,975	—
	<b>17,741,734</b>	<b>21,136,943</b>

June 30, 2009 and 2008

**14. Financial Instruments****CLASSIFICATION OF FINANCIAL INSTRUMENTS**

Financial assets and financial liabilities are measured on an ongoing basis at fair value or amortized cost. As at June 30, 2009, the classification of the financial instruments, as well as their carrying values and fair values, are shown in the table below:

June 30, 2009	Held for trading	Loans and receivables	Other financial liabilities	Total carrying value	Fair value
	\$	\$	\$	\$	\$
<b>Financial assets</b>					
Cash and cash equivalents	5,949,617	—	—	5,949,617	5,949,617
Restricted cash	1,227,374			1,227,374	1,227,374
Accounts receivable <sup>1</sup>	—	3,538,613	—	3,538,613	3,538,613
Long-term accounts receivable	—	1,025,152	—	1,025,152	1,025,152
	7,176,991	4,563,765	—	11,740,756	11,740,756
<b>Financial liabilities</b>					
Revolving credit facility <sup>2</sup>	—	—	4,447,836	4,447,836	4,447,836
Accounts payable and accrued <sup>3</sup> liabilities	—	—	9,527,101	9,527,101	9,527,101
Long-term debt <sup>4</sup>	—	—	1,779,245	1,779,245	1,779,245
Government assistance loans	—	—	2,475,975	2,475,975	2,475,975
	—	—	18,230,157	18,230,157	18,230,157
<b>June 30, 2008</b>					
	Held for trading	Loans and receivables	Other financial liabilities	Total carrying value	Fair value
	\$	\$	\$	\$	\$
<b>Financial assets</b>					
Cash and cash equivalents	4,399,065	—	—	4,399,065	4,399,065
Accounts receivable <sup>1</sup>	—	5,007,203	—	5,007,203	5,007,203
Long-term accounts receivable	—	478,852	—	478,852	478,852
	4,399,065	5,486,055	—	9,885,120	9,885,120
<b>Financial liabilities</b>					
Revolving credit facility <sup>2</sup>	—	—	3,157,294	3,157,294	3,157,294
Accounts payable and accrued <sup>3</sup> liabilities	—	—	6,252,215	6,252,215	6,252,215
Long-term debt <sup>4</sup>	—	—	2,208,562	2,208,562	2,208,562
	—	—	11,618,071	11,618,071	11,618,071

<sup>1</sup> Excluding non-financial assets comprised of provincial and federal sales taxes and tax credits receivable totaling \$181,510 [2008 – \$1,291,463].

<sup>2</sup> Excluding financing expenses recorded as a reduction of the loan balance totaling nil [2008 – \$564,235].

<sup>3</sup> Excluding non-financial liabilities comprised of provincial and federal sales and capital taxes, accruals that are not contractual obligations and amounts that will be settled in shares totaling \$2,080,116 [2008 – \$2,089,183].

<sup>4</sup> Excluding financing expenses recorded as a reduction of the loan balance totaling \$64,851 [2008 – \$85,118].

June 30, 2009 and 2008

#### 14. Financial Instruments [Cont'd]

##### FAIR VALUES

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies; however, considerable judgment is required to develop these estimates. Accordingly, the estimated fair values are not necessarily indicative of the amounts the Company could realize in a current market exchange. The estimated fair value amounts can be materially affected by the use of different assumptions or methodologies. The methods and assumptions used to estimate the fair value of financial instruments are described below:

- Given their short-term maturity, the fair value of cash and cash equivalents, restricted cash, accounts receivable, the revolving credit facility and accounts payable and accrued liabilities approximate their carrying values.
- Long-term receivables are carried at amortized cost. As each component has been discounted at a rate the Company would expect for similar receivables, the amortized cost approximates fair value.
- The fair value of long-term debt is approximately equal to the carrying value due to the variable rates of interest charged on these loans.
- Government assistance loans are carried at their amortized cost, which approximates fair value due to the use of discount rates the Company would expect for similar loans.

##### FOREIGN CURRENCY RISK

The Company operates internationally and a substantial portion of its revenue from product sales is denominated in US dollars, Euros and Australian dollars. This results in financial risk due to fluctuations in the value of the Canadian dollar relative to these currencies. The Company has a natural hedge for a portion of this risk, in that many of its expenditures are in US dollars, Euros and Australian dollars. Fluctuations in payments made for the Company's products could cause unanticipated fluctuations in the Company's consolidated operating results. At June 30, 2009, the Company has not entered into any currency hedging contracts to manage foreign currency risk.

The significant balances in foreign currencies at June 30 are as follows:

	U.S. dollars		Euros	
	2009 \$	2008 \$	2009 €	2008 €
Cash and cash equivalents	3,051,041	940,058	228,042	397,574
Accounts receivable	1,676,283	2,549,626	461,605	636,146
Revolving credit facility	(3,868,374)	(3,125,522)	—	—
Accounts payable and accrued liabilities	(3,812,228)	(2,522,494)	(230,654)	(460,792)
	(2,953,278)	(2,158,332)	458,993	572,928
	AUS dollars		NZL dollars	
	2009 \$	2008 \$	2009 \$	2008 \$
Cash and cash equivalents	486,467	133,844	—	—
Accounts receivable	318,129	481,113	22,936	—
Accounts payable and accrued liabilities	(508,028)	(331,072)	(120,605)	(62,692)
Long-term debt	(462,733)	(470,610)	—	—
	(166,165)	(186,725)	(97,669)	(62,692)

June 30, 2009 and 2008

#### 14. Financial Instruments [Cont'd]

Based on the above net exposure as at June 30, 2009, and assuming that all other variables remain constant, a 10% appreciation or depreciation of the Canadian dollar against the other currencies would have resulted in the following impact on net loss and comprehensive loss as follows:

	Canadian Dollar	
	Appreciate 10%	Depreciate 10%
	\$	\$
Against the US dollar	341,399	(341,399)
Against the Euro	(74,540)	74,540
Against the AUS dollar	15,458	(15,458)
Against the NZL dollar	7,307	(7,307)
Decrease (increase)	289,624	(289,624)

#### CREDIT RISK

Credit risk is the risk of an unexpected loss if a counterparty to a financial instrument fails to meet its contractual obligations.

The Company monitors the credit risk and credit standing of counterparties on a regular basis. Concentrations of credit risk with respect to trade accounts receivable are limited due to the large number of customers and their dispersion across many geographic areas. Of total trade receivables as at June 30, 2009 of \$3.2 million, 59% are aged as current, 23% are aged between one and thirty days past due, 13% are aged between thirty-one and sixty days past due and 5% are aged sixty-one or more days past due. The Company did not have an allowance for doubtful accounts as at June 30, 2009 and 2008. As at June 30, 2009, accounts receivable with respect to government incentives represented 2% of current assets [2008 – 10%]. At June 30, 2009, two customers comprised 25% of trade receivables [2008 – one customer, 10%].

Cash is held with one Canadian chartered bank, two US banks, one Irish bank and one Australian bank.

The maximum extent of the Company's exposure to credit risk is the aggregate carrying value of the Company's financial assets.

#### LIQUIDITY RISK

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's objective is to provide for expected cash requirements and accommodate for changes in liquidity needs. The Company manages this risk by managing its capital structure, through continuous monitoring of its actual and projected cash flows.

June 30, 2009 and 2008

#### 14. Financial Instruments [Cont'd]

The following are the undiscounted contractual maturities of financial liabilities at June 30, 2009:

	Total \$	Less than 1 year \$	1-3 years \$	4-5 years \$	More than 5 years \$
Revolving credit facility	4,447,836	4,447,836	—	—	—
Accounts payable and accrued liabilities	9,527,101	9,527,101	—	—	—
Long-term debt	1,779,245	565,688	926,343	97,888	189,326
Government assistance loans	3,408,936	—	—	477,121	2,931,815
	19,163,118	14,540,625	926,343	575,009	3,121,141

#### INTEREST RATE RISK

Financial instruments that potentially subject the Company to cash flow interest rate risk are those assets and liabilities with a variable interest rate. Accounts receivable, accounts payable and accrued liabilities bear no interest. The revolving credit facility and both the BDC and ANZ loan facilities which are included in long-term debt have variable interest rates. Based on the carrying value of these variable interest-bearing liabilities as of June 30, 2009, an assumed 25 basis point increase or decrease in interest rates during the year ended June 30, 2009 would have resulted in increases (decreases) in net loss and comprehensive loss as follows:

	Interest rate	
	Increase 25 pts. \$	Decrease 25 pts. \$
Decrease (increase) in net loss and comprehensive loss	(16,705)	16,705

Financial assets and financial liabilities that bear interest at fixed rates are subject to fair value interest rate risk. Certain cash equivalents bear interest at a fixed rate but are not deemed significant due to the short term of the investment. Long-term accounts receivable bear no interest but are carried at amortized cost, calculated using discount rates appropriate to each component. The Company's obligations under capital leases are at fixed rates of interest. The Company's government assistance loans are interest-free as described in note 11[c]. They are carried at amortized cost, calculated using discount rates appropriate to each component.

June 30, 2009 and 2008

### 15. Segmented Financial Information

The Company's three reportable business units, Animal Health, Human Health and Food Safety are strategic entities that offer different products and require different technology and marketing strategies.

	2009				
	Human Health \$	Animal Health \$	Food Safety \$	Corporate \$	Total \$
Sales	—	33,276,208	4,821	—	33,281,029
Cost of sales	—	13,996,997	434,871	—	14,431,868
Expenses	—	7,063,893	1,036,456	4,968,410	13,068,759
<b>EBITDA before research and development</b>	—	12,215,318	(1,466,506)	(4,968,410)	5,780,402
Research and development expenses	9,928,224	1,773,400	1,613,265	—	13,314,889
Less: Government incentives	(1,516,657)	—	(345,073)	—	(1,861,730)
<b>Net research and development expenses</b>	8,411,567	1,773,400	1,268,192	—	11,453,159
Interest expense, net	—	47,613	—	629,813	677,426
Amortization and write-off of property, plant, equipment and intangible assets	1,173,305	838,715	49,729	178,090	2,239,839
Amortization of financial expenses	—	—	—	1,787,104	1,787,104
Foreign exchange gain	—	—	—	(250,876)	(250,876)
Change in unrealized loss on foreign currency embedded derivatives	—	—	—	59,693	59,693
<b>Segment income (loss) before income taxes</b>	<b>(9,584,872)</b>	<b>9,555,590</b>	<b>(2,784,427)</b>	<b>(7,372,234)</b>	<b>(10,185,943)</b>
Provision for income taxes	—	314,561	—	—	314,561
Segment assets	9,558,437	14,225,739	2,363,810	8,493,454	34,641,440
Goodwill	—	456,155	—	—	456,155
Purchases of property, plant and equipment	82,217	126,482	1,138,505	133,874	1,481,078

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**15. Segmented Financial Information [Cont'd]**

	2008				
	Human Health \$	Animal Health \$	Food Safety \$	Corporate \$	Total \$
Sales	—	27,450,435	17,650	—	27,468,085
Cost of sales	—	12,687,599	8,326	—	12,695,925
Expenses	—	7,021,216	1,733,448	4,659,830	13,414,494
<b>EBITDA before research and development</b>	—	7,741,620	(1,724,124)	(4,659,830)	1,357,666
Research and development expenses	11,464,430	1,939,977	2,568,253	—	15,972,660
Less: Government incentives	(1,698,349)	—	(220,031)	—	(1,918,380)
<b>Net research and development expenses</b>	9,766,081	1,939,977	2,348,222	—	14,054,280
Interest expense, net	—	94,558	—	93,383	187,941
Amortization of property, plant and equipment and intangible assets	1,118,345	764,525	60,231	115,744	2,058,845
Amortization of financial expenses	—	—	—	767,921	767,921
Foreign exchange loss	—	—	—	232,822	232,822
Change in unrealized loss on foreign currency embedded derivatives	—	—	—	126,988	126,988
<b>Segment income (loss) before income taxes</b>	<b>(10,884,426)</b>	<b>4,942,560</b>	<b>(4,132,577)</b>	<b>(5,996,688)</b>	<b>(16,071,131)</b>
Provision for income taxes	—	184,577	—	—	184,577
Segment assets	11,422,459	15,971,852	1,472,934	5,755,765	34,623,010
Goodwill	—	456,155	—	—	456,155
Purchases of property, plant and equipment	548,824	442,646	16,179	355,474	1,363,123

The Company uses EBITDA [earnings before interest, taxes, depreciation, and amortization] before research and development as a measure of each segment's contribution to the Company on an operational basis.

June 30, 2009 and 2008

### 15. Segmented Financial Information [Cont'd]

Segmented financial information analyzes the operations of the Company by the following geographic locations, based on the location of its customers:

	2009 \$	2008 \$
<b>Revenue</b>		
Canada	6,512,289	5,562,175
Europe*	1,277,458	1,276,964
United States	18,306,759	15,373,732
Australia	3,674,754	2,954,607
Other**	3,509,769	2,300,607
<b>Total revenue</b>	<b>33,281,029</b>	<b>27,468,085</b>

\* Europe primarily includes Switzerland, Germany, Spain, the Netherlands, Ireland and the United Kingdom.

\*\* Other primarily includes countries in Asia, South America and the Middle East.

	2009 \$	2008 \$
<b>Total assets</b>		
Canada	27,485,323	26,382,719
Ireland	1,337,003	1,720,602
United States	3,059,670	4,085,995
Australia	2,759,444	2,433,694
<b>Total assets</b>	<b>34,641,440</b>	<b>34,623,010</b>
<b>Property, plant and equipment and goodwill</b>		
Canada	8,987,749	9,165,396
Other	962,419	1,008,916
<b>Total property, plant and equipment and goodwill</b>	<b>9,950,168</b>	<b>10,174,312</b>

### 16. Income Taxes

The reconciliation of income tax computed at the statutory tax rates to the provision for income taxes is as follows:

	2009 \$	2008 \$
Loss before income taxes	(10,185,943)	(16,071,131)
Basic income tax rate	32.87%	34.34%
Computed income tax recovery (expenses)	3,348,119	5,518,827
Effect on income tax rate resulting from:		
Foreign jurisdictions rate differential	8,169	(201,551)
Unrecorded potential tax benefits of current period losses	(3,537,072)	(4,889,051)
Benefit of losses not previously recognized	212,155	—
Accounting charges not deductible for tax purposes	(345,932)	(612,802)
	<b>(314,561)</b>	<b>(184,577)</b>

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### 16. Income Taxes [Cont'd]

As at June 30, 2009, the Company has non-capital losses of approximately \$35,940,000 for Canadian Federal and Ontario purposes and \$31,160,000 for Québec purposes that are available to offset future taxable income. These losses expire as follows:

	Federal and Ontario \$	Quebec \$
2010	4,505,000	4,165,000
2014	4,085,000	3,660,000
2015	4,500,000	4,445,000
2026	3,765,000	2,045,000
2027	7,205,000	6,480,000
2028	7,280,000	5,765,000
2029	4,600,000	4,600,000
	\$35,940,000	\$31,160,000

The Company has Scientific Research and Experimental Development ["SRED"] expenditures of approximately \$39,000,000 [2008 – \$34,500,000] for Federal and Ontario income tax purposes and \$49,000,000 [2008 – \$43,000,000] for Québec income tax purposes, which have not been deducted. These expenditures are available to reduce future taxable income and have an unlimited carryforward period. Research and development tax credits and expenditures are subject to verification by the tax authorities and, accordingly, these amounts may vary.

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future tax assets and liabilities are as follows:

	2009 \$	2008 \$
<b>Future tax assets</b>		
Net operating loss carryforwards	10,296,000	8,550,000
Tax basis of capital assets and intangibles in excess of carrying values	2,341,000	1,981,000
Research and development expenditures	11,331,000	10,069,000
Deferred revenue	849,000	1,034,000
Other	60,000	—
Financing fees	807,000	672,000
Total gross future tax assets	25,684,000	22,306,000
Less: valuation allowance	(23,919,000)	(20,293,000)
<b>Net future tax assets</b>	1,765,000	2,013,000
<b>Future tax liabilities</b>		
Carrying value of intangibles in excess of tax basis	1,765,000	2,013,000
Total future tax liabilities	1,765,000	2,013,000
<b>Net future tax liabilities</b>	—	—

June 30, 2009 and 2008

## 16. Income Taxes [Cont'd]

The income tax benefits relating to the future tax assets have been recognized to the extent of the future tax liabilities under the liability method of tax allocation.

Significant components of the provision for income taxes are as follows:

	2009 \$	2008 \$
Current tax expense	526,716	184,577
Future income tax benefit resulting from recognition of loss carryforwards	(212,155)	—
	<b>314,561</b>	<b>184,577</b>

## 17. Other Expenses

As a result of the Company's financial condition during the year ended June 30, 2009, a number of strategic initiatives were undertaken prior to the signing of the collaboration agreement described in note 22 and none of these initiatives were concluded. Costs incurred of \$863,257 consist primarily of professional fees.

## 18. Employee Benefit Plans

The Company has two defined contribution pension plans for its US and Canadian employees. Contributions to these plans are expensed as incurred. The Company funded and charged to expense during the year ended June 30, 2009, for the defined contribution plans, an amount of \$587,219 of which \$532,827 was paid in shares [2008 – \$736,370 of which \$684,556 was paid in shares] [note 12[c][iii]].

## 19. Commitments and Contingencies

### [i] COMMITMENTS

The Company is committed under various operating leases for buildings and equipment to total future minimum lease payments as follows:

	\$
2010	295,157
2011	73,868
2012	35,744
2013	14,624
2014	10,450
	<b>429,843</b>

In addition to the royalties described in note 11[a], the Company is committed to paying royalties ranging from 1% – 5% as a result of certain license agreements on the sales of certain products on the commercialization of specific technologies or products.

On July 2, 2004, the Company initiated the funding of two Industrial Research Chairs at the Vaccine & Infectious Disease Organization, jointly with Natural Science and Engineering Research Canada. Under this agreement, the Company receives the first commercial rights to new food safety vaccines to fight infectious diseases of animals, including *Salmonella enteritidis*, *Campylobacter* and *Cryptosporidium parvum*. The Company's financial commitment is up to \$400,000 per year payable semi-annually over five years. The Company has expensed \$376,454 in research and development related to this funding during the year ended June 30, 2009, [2008 – \$378,555].

June 30, 2009 and 2008

## 19. Commitments and Contingencies [Cont'd]

### [ii] CONTINGENCIES

The Company is involved from time to time in litigation, which arises in the normal course of business. In respect of these claims the Company believes it has valid defenses and/or has made adequate provision for such claims. The Company believes that no material exposure exists on the eventual settlement of such litigation.

The Company participates in research and development funding arrangements, some of which, based on management's best estimates, are recorded as a reduction in the related cost and some as a deferred government incentives obligation. The funding arrangements are subject to audit by the contributors. Any adjustments which could be material will be made in the period in which they are known.

The Company periodically enters into research agreements with third parties that include indemnification provisions that are customary in the industry. These guarantees generally require the Company to compensate the other party for certain damages and costs incurred as a result of damages arising from these transactions. In some cases, the maximum potential amount of future payments that could be required under these indemnification provisions is unlimited. These indemnification provisions generally survive termination of the underlying agreement. The nature of the indemnification obligations prevents the Company from making a reasonable estimate of the maximum potential amount it could be required to pay. Historically, the Company has not made any indemnification payments under such agreements and no amount has been accrued in the accompanying consolidated financial statements with respect to these indemnification obligations.

Under an employment agreement, the Company is committed to pay royalties on net sales of MCC formulation which includes *Urocidin* at a rate 1.5% for the first \$10,000,000 of net sales and 1% for the next \$20,000,000 of net sales.

## 20. Consolidated Statements of Cash Flows

	2009 \$	2008 \$
<b>Net change in non-cash working capital balances:</b>		
Accounts receivable	2,154,743	(1,335,395)
Inventories	(708,209)	741,402
Prepaid expenses and deposits	70,721	18,541
Accounts payable and accrued liabilities	2,334,860	816,893
Income and other taxes payable	216,574	(179,253)
	<b>4,068,689</b>	<b>62,188</b>

Included in accounts payable and accrued liabilities are liabilities in the amount of \$1,837,042 which the Company has the option to settle through the issuance of shares [2008 – \$1,637,209].

### Supplemental cash flow information:

	2009 \$	2008 \$
<b>Cash paid for</b>		
Income taxes	108,576	70,219
Interest	651,347	127,236
	<b>759,923</b>	<b>197,455</b>
<b>Non-cash investing and financing activities</b>		
Capital leases	156,077	783,191

June 30, 2009 and 2008

## 21. Related Party Transactions

In addition to related party transactions disclosed elsewhere the consolidated financial statements, the Company paid a director \$69,800 [2008 – \$35,200] in consulting fees.

## 22. Subsequent Event

[a] On July 10, 2009, the Company signed a strategic partnership to undertake completing the commercialization of *Urocidin*<sup>TM</sup>. Under this agreement the Company received a cash payment of US\$20 million. This cash payment will be recognized over the period that the Company has substantive obligations under the strategic partnership which we expect to be approximately 15 years. The Company also has the potential to receive a further US\$110 million in additional payments linked to the achievement of future clinical, regulatory and commercial milestones. The Company will also receive a reimbursement of certain external development costs commencing in calendar 2010. The magnitude of the reimbursement will be based on budgets agreed to by the joint development committee and the extension of the agreement to consider markets outside of North America.

In addition to the above payments, the Company has retained exclusive product manufacturing rights and will receive a net-sales related transfer-price for supplying the partner, with commercial product.

[b] On July 20, 2009, the Company repaid its Facility and associated fees, for a total of US\$5.3 million.

[c] On July 23, 2009, the Company sold its interest in a regulatory registration in the United States for a veterinary anesthetic product, *Ketamine*, to Bioniche Teoranta for US\$800,000. The Company received US\$548,639 in cash at closing and debt was forgiven in the amount of US\$251,361.

[d] A former financial advisor has requested payment of 6% of the funds received under the strategic partnership disclosed in [a] above. Management believes that this demand is frivolous and without merit.

## 23. Comparative Consolidated Financial Statements

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the 2009 consolidated financial statements.

**BOARD OF DIRECTORS****GRAEME McRAE** <sup>(3) (4) (6)</sup>Chairman, President and CEO  
Bioniche Life Sciences Inc.**STANLEY ALKEMADE, D.V.M.** <sup>(4) (5) (6)</sup>

President, BioMedEx Inc.

**ARMEN APRIKIAN, M.D., F.R.C.S.  
(C) (OBSERVER)** <sup>(4)</sup>Head, Division of Urology, Department of  
Surgery, McGill University & Interim Chief,  
Department of Oncology, McGill University  
Health Centre**ALBERT BERALDO** <sup>(1) (2) (6)</sup>

President, Alveda Pharmaceuticals Inc.

**MARGARET CUNNINGHAM, PH.D.** <sup>(1) (6)</sup>Director of the School of Business, Associate  
Dean, and R. A. Jodrey Chair, Faculty of  
Management, Dalhousie University, Halifax,  
Nova Scotia**PIERRE-YVES DESBIENS, C.A., MBA** <sup>(1) (2) (6)</sup>

Vice-President, Finance, PureCell Technologies Inc.

**JAMES JOHNSON PH.D.** <sup>(4) (6)</sup>

Partner, King &amp; Spalding LLP

**NICK PHOTIADES** <sup>(3)</sup>Management and Strategic  
Planning Consultant**LYLE VANCLIEF** <sup>(3) (6)</sup>

Agricultural and Agri-Food Consultant

<sup>1</sup> Member of the Audit Committee<sup>2</sup> Member of the Compensation Committee<sup>3</sup> Member of the Corporate Governance and  
Nominating Committee<sup>4</sup> Member of the Scientific Audit Committee<sup>5</sup> Member of the Risk Management Committee<sup>6</sup> Each Director has been elected to hold office  
until the date of the Company's next Annual  
Meeting of Shareholders**EXECUTIVE MANAGEMENT****Graeme McRae**

Chairman, President and CEO

**Cindy Benning**Vice-President, Operations, Corporate Quality  
and Regulatory Affairs**François Charette, M.D., MBA**

Senior Vice-President and Chief Medical Officer

**Rick Culbert**

President, Bioniche Food Safety

**Mohamed Elrafih**

Vice-President, Manufacturing Operations

**Brian Ford, BA, CA**

Chief Financial Officer

**Andrew Grant**Divisional President, Bioniche Animal  
Health Export Sales, Europe & Australia**Cameron Groome**Executive Vice-President, Corporate &  
Strategic Development**Bruce McLeod**

Vice-President, Human Resources

**Jim Phillips**

President, Bioniche Global Animal Health

**Nigel C. Phillips, Ph.D.**Senior Vice-President, Scientific Affairs and  
Chief Scientific Officer**Dragan Rogan, Ph.D.**Vice-President, Research & Development  
Animal Health**Jennifer Shea**Vice-President, Communications,  
Investor & Government Relations**Rick Sutin**

Corporate Secretary (interim)

**Dr. Gary Weber**

President, Bioniche Food Safety, U.S.A.

**STOCK LISTING:**

Toronto Stock Exchange

Symbol: BNC

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**AUDITORS:**

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**SHAREHOLDER INQUIRIES:**

Inquiries related to stock transfer or lost certificates and notices of address change should be directed to the Transfer Agent noted above. General information regarding the Company, recent news releases, and SEDAR filings are available via our Internet website at [www.Bioniche.com](http://www.Bioniche.com), through our Corporate Communications & Investor Relations office at (613) 966-8058, or by e-mail at [info@Bioniche.com](mailto:info@Bioniche.com).

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