

CONJUCHEM®

*Q2 2009*

## LETTER TO SHAREHOLDERS

I am currently attending the American Diabetes Association's 69th Annual Scientific Sessions being held at the New Orleans Convention Center. Thousands of doctors, scientists, dietitians, alongside with drug and device developers and members of the investment community have come to this meeting - the world's largest gathering of experts on diabetes. Much of the discussions are focused on new therapeutics and surgical procedures, the role genetics play in the disease, new ways to diagnose diabetes, and the relationship between diabetes and cardiovascular disease. Underlying it all, one theme stands out: diabetes is becoming ever more present in society and the impact of this epidemic is staggering.

The ADA meeting is the ideal event to showcase our two diabetes drugs, their potential, and the value of our proprietary approach to overcoming the limitations of short-lived therapeutic peptides. At the event we presented two posters:

- The first poster detailed previously disclosed results of our two randomized, double-blind, placebo controlled phase II trials of PC-DAC™:Exendin-4, demonstrating that this long-lasting GLP-1 receptor agonist can significantly and safely reduce HbA1c and body weight in Type 2 diabetes patients with a small volume liquid formulation injected through a fine 31 gauge needle. Consistent with previous studies, PC-DAC™:Exendin-4 was extremely well tolerated, with minimal rates of drug-related nausea, vomiting and diarrhea that decreased over time.
- The second poster describes PC-Insulin, a novel insulin-albumin conjugate we plan to advance into human clinical trials. PC-Insulin showed a prolonged duration of activity in preclinical pharmacodynamic studies, demonstrating it has the potential for advantages over existing basal insulin therapies that may show clinically relevant peak-to-trough ratios and provide insulin coverage for only 24 hours or less.

As you know, our current highest priority is to license our lead product to a partner who will support our efforts to bring PC-DAC™:Exendin-4 to market, and this conference is an important venue for continuing those discussions. As we work toward this goal, during the quarter, we also implemented key decisions that enabled us to reduce spending and extend our resources. Our workforce reduction of 18 employees also included the departure of our long-standing CFO, Mr. Lennie Ryer. On behalf Jacques Lapointe, Chairman of the Board, and everyone at ConjuChem, I would like to thank Lennie for his many years of service and the contributions he has made.

We remain committed and focused on advancing our two products, ultimately to the potential benefit of millions of people with diabetes who are seeking more effective and patient-friendly treatment options. On behalf of the board of directors and management team of ConjuChem, I thank you for your support as we move forward.

Sincerely,



Mark D. Perrin,  
President and CEO

## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Management's discussion and analysis provides a review of the performance of our company and should be read in conjunction with the unaudited interim financial statements as at April 30, 2009, the audited financial statements for the year ended October 31, 2008 and the related notes, which are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). This discussion and analysis compares financial performance for the three- and six-month period ended April 30, 2009, as compared to the three- and six-month period ended April 30, 2008 and discusses issues and risks that may impact future operations. This review was performed by management with information available as at June 10, 2009. Additional information related to the Company, including its Annual Information Form, can be found on SEDAR on [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 essentially forward-looking and are subject to risks and uncertainties, as described in the "Risk factors" section of the Annual Information Form. Forward-looking statements generally can be identified by the use of forward-looking terminology such as "may", "will", "expect", "intend", "estimate", "anticipate", "plan", "foresee", "believe" or "continue" or the negatives of these terms or variations of them or similar terminology. By their nature, forward-looking statements require us to make assumptions and are subject to inherent 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.

Factors that could cause actual results to differ materially include but are not limited to:

- our need for additional financing and our estimates regarding our capital requirements and future revenues and profitability;
- our plans to develop and commercialize product candidates and the timing of these development programs;
- whether we will receive, and the timing and costs of obtaining, regulatory approvals;
- clinical development of our product candidates, including the results of current and future clinical trials;
- the benefits of our drug delivery technologies and product candidates as compared to others;
- our ability to maintain and establish intellectual property rights in our drug delivery technologies and product candidates;
- our estimates of the size of the potential markets for our product candidates;
- our selection and licensing of product candidates;
- our ability to attract distributors and collaborators with acceptable development, regulatory and commercialization expertise and the benefits to be derived from such collaborative efforts;
- sources of revenues and anticipated revenues, including contributions from distributors and collaborators, product sales, license agreements and other collaborative efforts for the development and commercialization of product candidates;
- the rate and degree of market acceptance of our products;
- the timing and amount of reimbursement for our products;
- the success and pricing of other competing therapies that may become available;
- our ability to retain and hire qualified employees;
- the manufacturing capacity of third-party manufacturers for our product candidates; and
- other risk factors discussed herein and listed from time to time in our reports, public disclosure documents and other filings with the securities commissions in Canada.

See "Risk Factors" below.

All amounts are presented in Canadian dollars unless otherwise indicated. Where we say "we", "us", "our" or the "Company" we mean ConjuChem Biotechnologies Inc., unless otherwise indicated.

### **OVERVIEW**

We are a publicly-traded Canadian biotechnology company dedicated to the discovery of novel therapeutics with an initial focus on diabetes. We are currently managing multiple research programs in-house and have one product in development. ConjuChem is focused on discovering and developing new drugs based on our novel technology

platforms called Drug Affinity Complex (“DAC<sup>TM</sup>”) and Pre-formed Drug Affinity Complex (“PC-DAC<sup>TM</sup>”). When applied to a compound, DAC<sup>TM</sup> and PC-DAC<sup>TM</sup> can create new drugs with similar therapeutic activity to the original compound but with a significantly longer duration of activity in the body. One of the greatest opportunities for ConjuChem’s DAC<sup>TM</sup> and PC-DAC<sup>TM</sup> technologies is their ability to harness the therapeutic potential of peptides, which are hindered by a variety of limitations. In particular, peptides have short durations of *in vivo* activity which not only decreases their efficacy, but can also limit their commercialization potential.

Our diabetes program has focused on the GLP-1 class of peptides for the treatment of Type 2 diabetes. These compounds help lower glucose through multiple mechanisms of actions in the body. We are currently pursuing the development of PC-DAC<sup>TM</sup>:Exendin-4, a GLP-1 homolog combined with our PC-DAC<sup>TM</sup> technology. Phase II multiple-dose clinical trials began in February 2008. Positive preliminary results from three-month multiple dose trials were announced December 3, 2008, final results were released in February 2009 and two posters were presented at the American Diabetes Association's 69th Annual Scientific Sessions.

We have incurred operating losses since our inception due principally to expenditures related to our research and development activities. As at April 30, 2009, we had an accumulated deficit of \$344.3 million and, as of this date, have total liabilities exceeding our total assets. We expect to continue to incur operating losses in the next few fiscal years as we advance other product candidates from our research pipeline into clinical development. To date, we have financed our operations, technology acquisitions and capital expenditures primarily through public equity offerings of common shares, private placements of common shares, issuance of convertible notes and debentures, the receipt of investment tax credits earned on eligible expenditures, interest income, and the proceeds from research collaboration agreements.

Our ability to continue as a going concern is dependent upon our ability to obtain additional financing. We are currently seeking additional capital to finance our operations. Management is considering all financing alternatives, including equity financing, debt arrangement, non-dilutive financing, corporate collaboration and licensing arrangements. There can be no assurance that such financing will materialize on a timely basis or be obtained on favourable terms. If the Company is unable to obtain additional financing, management may be required to curtail the Company’s operations. Please refer to Note 1 – Description of Business and Going Concern Uncertainty - to the unaudited interim financial statements of the Company as of April 30, 2009 and the section “Risk Factors” below for more details. Our success is also dependent on obtaining the necessary regulatory approvals, generating revenue from licensing or sale of therapeutic drugs and achieving future profitable operations.

#### *Consolidation of operations*

During the quarter ended April 30, 2009, we completed a consolidation of our operations, focusing our resources on securing a partner for PC-DAC<sup>TM</sup>:Exendin-4 and the rapid development of PC-Insulin, a long-acting basal insulin in preclinical testing. The restructuring included a workforce reduction of approximately 50% of our personnel. We recorded charges for termination costs of \$582,465, \$296,245 was included in research and development expenses and \$286,220 was included in general and administration expenses during the quarter ended April 30, 2009. As at April 30, 2009, a liability of \$280,148 remains.

#### *Our Goal*

Our goal is to develop next generation medicines from therapeutic peptides based on our proprietary bioconjugation platform technologies. We anticipate applying our systemic PC-DAC Technologies to multiple drug candidates and undertaking the clinical development of said drug candidates until the stage at which we believe we can optimize value for our shareholders by entering into strategic alliances for the further development and eventual marketing of the subject drug candidates.

#### *Revenues*

To date, we have not generated revenues from product sales. Revenue to date has been generated from interest income on cash reserves and research collaboration agreements. To date, we have entered into a number of research collaboration agreements covering a variety of products. Our goal is to enter broader collaboration agreements which generally include up-front fees and milestone payments upon the attainment of specific objectives.

### *Investment Tax Credits (“ITCs”)*

As we are a public company, the federal ITCs for qualified Scientific Research and Experimental Development (“SR&ED”) expenditures are not refundable and are calculated at a rate of 20%. These ITCs can be applied to reduce future income taxes payable with a twenty-year carry-forward period. Eligible SR&ED expenditures incurred in Quebec qualify for Quebec refundable tax credits at a rate of 37.5% for the first \$2 million of eligible expenditures and 17.5% on the remaining eligible expenses and are earned on payments made in Quebec for SR&ED labour and SR&ED contracts, after deducting governmental and non-governmental assistance related to SR&ED. However, only 50% of payments made to arm’s length sub-contractors are eligible for the Quebec tax credit.

### *Research and Development*

Our research and development expenses consist primarily of fees paid to external service providers, manufacturing costs, laboratory supplies and costs for facilities and equipment and related personnel expenses. The majority of our research and development costs incurred in the six-month periods ended April 30, 2009 and 2008 are related to the development of PC-DAC<sup>TM</sup>:Exendin-4. We intend to partner PC-DAC<sup>TM</sup>:Exendin-4 with a third party with sufficient expertise and resources to contribute to its continued development and commercialization. Our research and development expenses have fluctuated significantly from period to period in the past and are likely to do so in the future as they are impacted by the progress related to our development efforts.

We intend to fund the advancement of further drug candidates into preclinical and clinical development.

### *Significant Projects*

Our lead product candidate, PC-DAC<sup>TM</sup>:Exendin-4, is currently in clinical development. This product candidate will have to complete further clinical trials and obtain regulatory approval before significant ongoing revenue streams can be generated. The costs to complete these clinical trials and to attain regulatory approval are significant and, subject to entering into licensing arrangements, the costs associated with this process may increase our research and development expenses over the next few years.

During 2008 we advanced PC-Insulin into preclinical trials and intend to pursue an IND for this compound. PC-Insulin is a basal insulin with potential use in patients with either Type I or Type II diabetes. PC-Insulin is being developed to have advantages over basal insulin therapies that may show clinically relevant peak-to-trough ratios and may also not always provide adequate insulin coverage for the total 24-hour dosing period. Developed with ConjuChem’s proprietary PC-DAC<sup>TM</sup> technology, PC-Insulin is a longer-acting more peakless recombinant insulin that is covalently bound to recombinant human albumin (**Recombunin®**, provided by Novozymes Biopharma).

We also have a number of other discovery programs and preclinical development programs to identify and develop other therapeutic products. The discovery and development of these products is part of our normal ongoing research and development activities and until product candidates are identified, significant expenditures on these projects are not anticipated in the next year.

### *Segment Information*

We operate in a single business segment focused on the discovery and development of novel therapeutics. In addition, we earn interest revenue from our investment of cash resources. We operate out of a single facility in Canada and all our assets are located in Canada.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

In preparing our financial statements, we are required 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 financial statements and the reported amounts of revenue and expenses during the reporting periods. We have identified the following accounting policies that we believe require application of management’s subjective judgments, often

requiring the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Our actual results could differ from these estimates and such differences could be material.

#### *Revenue Recognition*

We recognize revenues from various research agreements as the contracted services are performed or when milestones are achieved, in accordance with the terms of the specific agreements. Upfront payments for the use of technology where further services are to be provided or fees received on the signing of research agreements are recognized over the period of performance of the related activities. The period of performance is based on our expected performance and requires us to make a number of estimates about future events. These estimates could significantly differ from our actual results and require us to change the recognition period. Amounts received in advance of recognition of revenue are included in deferred revenue. Milestone payments are recognized as they are earned.

#### *Impairment of Long-Lived Assets*

Property, plant and equipment and other long-lived assets are regularly reviewed for impairment as well as when 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 with its expected future net undiscounted cash flows from use together with its residual value (net recoverable value). If such assets are considered impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds their fair value. Any impairment results in a write-down of the asset and a charge to income. The determination of expected future cash flows and fair values require estimates which are subject to change. No adjustments to asset values have been required in this six-month period.

#### *Refundable Investment Tax Credits*

We incur research and development expenditures, which are eligible for refundable ITCs. The ITCs recorded are based on our estimates of amounts expected to be recovered and are subject to audit and reassessment by the taxation authorities and, accordingly, these amounts may vary materially.

#### *Valuation Allowance for Future Tax Assets*

We have not recorded a benefit related to future tax assets related to operating losses and research and development expenses incurred. We have assumed that the related tax benefits are not likely to be realized based on our historical results and estimated future taxable income. The implementation of tax planning strategies or the generation of future taxable income could result in the recognition of some portion or all of these benefits, which could result in a material improvement in our results of operations through the recovery of future income taxes.

#### *Stock-Based Compensation*

Assumptions that affect our evaluation of the fair value of stock options include the calculation of volatility factors and the life of the options issued, both of which require us to make assumptions about future events and have a direct impact on the determination of stock-based compensation.

### **CHANGES IN ACCOUNTING POLICIES**

Effective November 1, 2008, the Company adopted the following Handbook Sections recently introduced by the Canadian Institute of Chartered Accountants [“CICA”]:

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 adoption of this section did not have any impact on the Company’s unaudited interim financial statements.

Section 3064, “Goodwill and Intangible Assets”. This section, 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. The adoption of this section did not have any impact on the Company’s unaudited interim financial statements.

*Recent accounting pronouncements*

In January 2009, the CICA issued Handbook Sections 1582 “Business Combinations which replace CICA Handbook Section 1581 “Business Combinations”. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable for the Company’s business combinations with acquisition dates on or after January 1, 2011. Early adoption of this Section is permitted. The Company does not anticipate the adoption of the above standard will have a significant impact on the Company’s financial statements.

In March 2009, the Accounting Standards Board announced that it would improve the information to disclose on financial instruments. Section 3862 of the CICA Handbook, "Financial Instruments - Disclosures" has been amended to clarify the requirements in respect of maturities of financial liabilities and the disclosures about how an entity manages liquidity risk. The Company evaluates the impact on its financial statements.

**RESULTS OF OPERATIONS**

*Fluctuations in Operating Results*

Our results of operations have fluctuated significantly from year to year in the past and are likely to do so in the future.

We anticipate that our quarterly and annual results of operations will be impacted for the foreseeable future by several factors, including the progress and timing of expenditures related to our development programs, our research efforts and the further expansion of facilities and headcount. Due to these fluctuations, we believe that the year to year comparisons of our operating results are not a good indication of our future performance.

*Quarterly Financial Information (unaudited)*

The selected financial information provided below is derived from the Company’s unaudited quarterly financial statements for each of the last eight quarters, all of which cover periods of three months.

	April 30, 2009	Jan. 31, 2009	Oct. 31, 2008	July 31, 2008	April 30, 2008	Jan. 31, 2008	Oct. 31, 2007	July 31, 2007
	(in thousands of dollars, except for earnings per share)							
Revenues								
Contract revenue	15	—	—	9	25	27	45	24
Interest income	.32	106	195	306	376	573	876	950
Net loss	(6,079)	(5,828)	(10,915)	(8,737)	(7,925)	(11,841)	(6,490)	(8,562)
Basic loss per share	(0.02)	(0.02)	(0.04)	(0.04)	(0.03)	(0.05)	(0.03)	(0.04)

Our interest revenue fluctuates from quarter to quarter based on the timing of our financing initiatives while our net loss has fluctuated due to the timing of our clinical trial initiatives and expenditures related to manufacturing. The basic loss per share has decreased from previous periods, due to the completion of our phase II clinical trials in November 2008 for our PC-DAC<sup>TM</sup>:Exendin-4 compound.

## **SIX MONTHS ENDED APRIL 30, 2009 COMPARED TO THE SIX MONTHS ENDED APRIL 30, 2008**

Net loss for the six-month period ended April 30, 2009 amounted to \$11.9 million compared to \$19.8 million for the six-month period ended April 30, 2008. The decrease in the net loss is mainly attributable to a decrease in the accretion in the carrying value of the convertible senior unsecured notes and interest due to the early redemption of the convertible senior unsecured notes during the six-month period of the 2008 fiscal year, a decrease in R&D expenses of \$2.0 million and by the reversal of tax-related reserves following the results of tax audits in the six-month period ended April 30, 2009.

### *Revenues*

For the six-month period ended April 30, 2009, revenues were derived principally from interest income on investments. We recognized income from a research collaboration and generated \$51,904 of revenues in the six-month period ended April 30, 2008, compared to \$15,443 of research collaboration revenues earned for the six-month period ended April 30, 2009. The Company recorded interest income on cash and investments that amounted to \$138,517 for the six-month period ended April 30, 2009, compared to \$948,581 for the six-month period ended April 30, 2008. The decrease in interest income was a result of a reduced investment portfolio base combined with a general decrease in market rates.

### *Research and Development*

Gross research and development expenses amounted to \$7.1 million for the six-month period ended April 30, 2009, compared to \$9.1 million for the six-month period ended April 30, 2008. The decrease is due to the completion of our phase II clinical trials in November 2008 for PC-DAC<sup>TM</sup>:Exendin-4.

Investment tax credits were estimated at \$1.3 million for the six-month period ended April 30, 2009, compared to \$200,000 in investment tax credits for the six-month period ended April 30, 2008. The increase in 2009 is attributable to the fact that the Company has reversed tax reserves for SR&ED tax credits following the results of tax audits during the six-month period ended April 30, 2009. These investment tax credits are subject to audit by the taxation authorities. The amounts recognized in 2009 have been recorded as a reduction of research and development expenditures.

Research and development expenditures represent the majority of ConjuChem's corporate spending. Through a focused effort to validate our technology, we are targeting, in 2009, to license our lead diabetes compound, PC-DAC<sup>TM</sup>:Exendin-4. We also intend to advance one or more additional compounds during 2009. These research and development initiatives will have a direct effect on our R&D expenditures which are expected to decline in comparison to the 2008 fiscal year in which we conducted multiple Phase II trials for which we announced final results in February 2009.

### *General and Administrative*

General and administrative costs amounted to \$2.5 million for the six-month period ended April 30, 2009, compared to \$2.8 million for the six-month period ended April 30, 2008. The decrease in general and administrative expenses is largely attributable to fees related to the early redemption of the convertible senior unsecured notes in the six-month period ended April 30, 2008.

We reiterate our commitment to maintain the highest standards of corporate governance and continue to allocate resources in this area as we strongly believe that this is mandatory for maintaining shareholders' confidence.

### *Amortization and Debt Service*

Amortization expense decreased to \$87,463 for the six-month period ended April 30, 2009, compared to \$115,024 for the six-month period ended April 30, 2008. The decrease is a function of the decreasing capital base upon which amortization is calculated.

Accretion in the carrying value of the convertible senior unsecured notes and interest amounted to nil for the six-month period ended April 30, 2009, compared to \$5.5 million for the six-month period ended April 30, 2008. The decrease arises due to the early redemption of the convertible senior unsecured notes during the six-month period of the 2008 fiscal year. Accretion, a non-cash item, is a function of the notional allocation of the convertible senior unsecured note between debt and equity components and represents the accelerated accretion in the carrying value of the debt component to its redemption on November 30, 2007. Accretion in the carrying value of the convertible unsecured subordinated debentures and interest amount to \$2.2 million for the six-month period ended April 30, 2009, compared to \$1.6 million for the six-month period ended April 30, 2008. The debentures were issued in December 2007.

#### *Stock-based Compensation*

Stock-based compensation amounted to \$1.4 million for the six-month periods ended April 30, 2009 and April 30, 2008.

#### *Foreign Exchange Loss*

Foreign exchange conversion resulted in a loss of \$117,292 for the six-month period ended April 30, 2009, compared to a loss of \$191,275 for the six-month period ended April 30, 2008. The majority of our clinical trial expenses are incurred in U.S. dollars and some in British pounds, the decrease in the loss in this current period is attributable in part to a decrease in the value of U.S. dollars creating a favorable impact on our expenditures resulting from the need to convert Canadian dollars into foreign currencies at various times during the period.

### **THREE MONTHS ENDED APRIL 30, 2009 COMPARED TO THE THREE MONTHS ENDED APRIL 30, 2008**

Net loss for the quarter ended April 30, 2009 amounted to \$6.1 million compared to \$7.9 million for the quarter ended April 30, 2008. The decrease in the net loss is mainly attributable to a decrease in R&D expenses of \$2.5 million compensated by an increase of \$247,106 in G&A of \$133,097 in Stock-based compensation expenses and of \$57,796 in Accretion in carrying value of convertible unsecured subordinated debentures and interest.

#### *Revenues*

For the quarter ended April 30, 2009, revenues were derived principally from interest income on investments. We recognized income from a research collaboration and generated \$24,557 of revenues in the quarter ended April 30, 2008, compared to \$15,443 of research collaboration revenues earned for the quarter ended April 30, 2009. The Company recorded interest income on cash and investments that amounted to \$32,276 for the quarter ended April 30, 2009, compared to \$375,926 for the quarter ended April 30, 2008. The decrease in interest income was a result of a reduced investment portfolio base combined with a general decrease in market rates.

#### *Research and Development*

Gross research and development expenses amounted to \$2.9 million for the quarter ended April 30, 2009, compared to \$5.4 million for the quarter ended April 30, 2008. The decrease is due to the completion of our Phase II clinical trials in November 2008 for PC-DAC<sup>TM</sup>.Exendin-4.

Investment tax credits were estimated at \$250,000 for the quarter ended April 30, 2009, compared to \$100,000 in investment tax credits for the quarter ended April 30, 2008. The increase in investment tax credits is attributable to the fact that, for 2009, the Company benefits from a higher rate of SR&ED tax credits. These investment tax credits are subject to audit by the taxation authorities. The amounts recognized in 2009 have been recorded as a reduction of research and development expenditures.

Research and development expenditures represent the majority of ConjuChem's corporate spending. Through a focused effort to validate our technology, we are targeting, in 2009, to license our lead diabetes compound, PC-DAC<sup>TM</sup>:Exendin-4. We also intend to advance one or more additional compounds during 2009. These research and development initiatives will have a direct effect on our R&D expenditures which are expected to decline in comparison to the 2008 fiscal year in which we conducted multiple Phase II trials for which we announced final results in February 2009.

#### *General and Administrative*

General and administrative costs amounted to \$1.5 million for the quarter ended April 30, 2009, compared to \$1.2 million for the quarter ended April 30, 2008. The increase in general and administrative expenses in the quarter ended April 30, 2009 is largely attributable to professional fees and to severance costs related to our reduction in headcount.

We reiterate our commitment to maintain the highest standards of corporate governance and continue to allocate resources in this area as we strongly believe that this is mandatory for maintaining shareholders' confidence.

#### *Amortization and Debt Service*

Amortization expense decreased to \$41,960 for the quarter ended April 30, 2009, compared to \$57,422 for the quarter ended April 30, 2008. The decrease is a function of the decreasing capital base upon which amortization is calculated.

Accretion in the carrying value of the convertible unsecured subordinated debentures and interest amount to \$1.1 million for the quarters ended April 30, 2009 and April 30, 2008. The debentures were issued in December 2007. Accretion, a non-cash item, is a function of the notional allocation of the convertible senior unsecured note between debt and equity components and represents the accelerated accretion in the carrying value of the debt component to its redemption on November 30, 2007.

#### *Stock-based Compensation*

Stock-based compensation for the quarter ended April 30, 2009 amounted to \$791,056 compared to \$657,959 for the quarter ended April 30, 2008. The increase in the quarter ended April 30, 2009 is attributable to the accelerated vesting of certain options offset by the forfeiture of options for terminated employees.

#### *Foreign Exchange Loss*

Foreign exchange conversion resulted in a loss of \$26,829 for the quarter ended April 30, 2009, compared to a loss of \$12,324 for the quarter ended April 30, 2008. The majority of our clinical trial expenses are incurred in U.S. dollars and some British pounds and the loss in this current period is attributable to the unfavorable impact on our expenditures resulting from the need to convert Canadian dollars into foreign currencies at various times during the year.

#### *Liquidity and Capital Resources*

As at April 30, 2009, working capital amounted to \$3.1 million. Funds applied to operating activities in the six-month period of 2009 amounted to \$12.6 million compared to \$11.0 million in the six-month period of 2008. Funds were used primarily to complete the Phase II trials for PC-DAC<sup>TM</sup>:Exendin-4.

Cash flows generated from investing activities for the six-month period ended April 30, 2009 amounted to \$13.1 million compared to \$59.3 million used for in the six-month period ended April 30, 2008, primarily as a result of funds applied to operating activities and in Q1 of 2008, for the repayment of the convertible senior unsecured notes. The net proceeds of cash from acquisitions, disposals and maturities of investments for the six-month period ended April 30, 2009 was \$13.0 million compared to \$59.3 million of proceeds for the comparative period.

Net proceeds from the sale of plant, property and equipment for the six-month period ended April 30, 2009 were \$29,738 compared to capital expenditures of \$10,951 for the six-month period ended April 30, 2008. We do not anticipate making any significant capital acquisitions in fiscal 2009.

Cash flows used from financing activities amounted to nil for the six-month period ended April 30, 2009 compared to \$37.8 million generated for the six-month period ended April 30, 2008. In November 2008, we redeemed the convertible senior unsecured notes amounting to \$45,000,000 plus accrued interest of \$13,006,914 for a total amount of \$58,006,914.

Our receivables totaled \$80,104 as at April 30, 2009 and included commodity tax refunds. Accounts payable and accrued liabilities decreased from \$10.1 million as at October 31, 2008 to \$6.9 million as at April 30, 2009 due to the timing of disbursements relating to clinical development activities and the reversal of tax-related reserves.

As at April 30, 2009, we had cash and cash equivalents and investments totaling \$8.7 million. As at October 31, 2008, cash, cash-equivalents and short-term investments totaled \$21.1 million. ConjuChem's Investment Policy regulates its investment activities relating to cash resources and such Policy is monitored by the Board of Directors. The Company invests strictly in liquid, high-grade investment securities with varying terms to maturity, selected with regard to the expected timing of expenditures for continuing operations and prevailing interest rates. As of April 30, 2009, ConjuChem had invested in six major Canadian companies, all chartered banks, in amounts ranging from approximately \$100,000 to \$2.0 million. As at June 10, 2009, we do not have any investments in non-bank sponsored asset-backed commercial paper (ABCP). We believe that our current cash and cash equivalents, marketable securities and interest income will be sufficient to carry out our current research and development plans and operations into the fourth quarter of 2009. Please refer to Note 1 – Description of Business and Going Concern Uncertainty - to the unaudited interim financial statements of the Company as of April 30, 2009 and the section "Risk Factors" below for more details.

#### *Off-Balance Sheet Arrangements*

Our off-balance sheet arrangements are described below under "Contractual Obligations" and consist of operating leases. Other than these commitments, which are considered to be in the ordinary course of business, we do not have any other off-balance sheet arrangements and do not expect to enter into any other such arrangements outside of the ordinary course of our business in the near future.

#### *Transactions with Related Parties*

Subsequent to the issuance of the Series 1 convertible notes, the managing partner of the investment fund managing the noteholders became a director of the Company and the investment fund is therefore considered to be a related party. This investment fund manages investment partnerships that hold an aggregate of \$3.5 million of the \$22 million principal amount of convertible unsecured subordinated debentures as of April 30, 2009.

#### *Proposed Transactions*

As discussed elsewhere, we expect to strengthen our financial position through various financing initiatives and potential licensing agreements. The Company is not party to any such undertakings at this time.

#### *Financial Instruments*

The Company does not use currency hedging instruments.

#### *Contractual Obligations*

	Payments due by period (\$ '000's)			
	Less than 12 months	12 to 36 months	37 to 60 months	Total
Operating leases	421	20	5	446
Convertible unsecured subordinated debentures	—	20,330	—	20,330
Purchase commitments	609	5,938	2,436	8,983

There were no commitments for capital expenditures as at April 30, 2009.

#### *Outstanding Share Data*

The number of common shares outstanding as of April 30, 2009 and June 10, 2009 is 250,651,168. The number of stock options outstanding as of April 30, 2009 is 23,444,242 and 23,594,242 at June 10, 2009.

Furthermore, as at April 30, 2009, we have 131,201,750 warrants outstanding with prices and expiration dates as described in the following table:

<b># of warrants</b>	<b>Price</b>	<b>Expiration Date</b>
96,826,750	\$1.00	11/28/2009
34,375,000	\$0.25	12/31/2011

#### **Risk Factors**

The results of operations, business prospects and financial condition of the Company are subject to a number of risks and uncertainties, and are affected by a number of factors outside the control of the Company's management. Details are provided in the "Risk Factors" section of the Company's Annual Information Form dated January 29, 2009 (which can be found at [www.sedar.com](http://www.sedar.com)). As at April 30, 2009, we had cash and cash equivalents and investments totaling \$8.7 million. We believe that our current cash and cash equivalents, marketable securities and interest income will be sufficient to carry out our current research and development plans and operations into the fourth quarter of 2009. The Company cannot assure that additional financing will materialize on a timely basis or be obtained on favourable terms, if at all. In particular, given our need to secure further financing in the near future and challenges relating to obtaining financing in the current market conditions, our ability to continue operations as a going concern could be compromised or we could be required to curtail our operations. Please refer to Note 1 – Description of Business and Going Concern Uncertainty - to the unaudited interim financial statements of the Company as of April 30, 2009.

#### **Disclosure Controls and Procedures**

In accordance with the Canadian Securities Administrators Multilateral Instrument 52-109, the Company has filed certificates signed by the President and Chief Executive Officer and the Vice-President, Finance, that among other things, report on the design and effectiveness of disclosure controls and procedures and the design of internal control over financial reporting.

Also at April 30, 2009, an evaluation of the design and effectiveness of disclosure controls and procedures, and the design of internal controls over financial reporting, as defined in the Canadian Securities Administrators Multilateral Instrument 52-109, was carried out to provide reasonable assurance regarding the reliability of financial reporting and financial statement compliance with GAAP. Based on that evaluation, the President and Chief Executive Officer and the Vice-President, Finance will certify that the design of internal controls over financial reporting was effective.

Controls systems have limitations, no matter how well designed, including the possibility of human error and the circumvention or overriding of the controls or procedures. As a result, there is no certainty that our disclosure controls and procedures or internal control over financial reporting will prevent all errors or all fraud.

There were no changes in our internal controls over financial reporting during the six-month period ended April 30, 2009, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

**ConjuChem Biotechnologies Inc.**

**UNAUDITED INTERIM BALANCE SHEETS**

[See Description of Business and Going Concern Uncertainty - *note 1* ]

As at

	April 30, 2009	October 31, 2008
	\$	\$
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	2,689,621	2,187,423
Investments	5,972,581	18,934,737
Accounts receivable	80,104	160,644
Investment tax credits receivable	1,022,000	542,000
Prepaid expenses	146,236	229,006
<b>Total current assets</b>	<b>9,910,542</b>	<b>22,053,810</b>
Property, plant and equipment	732,514	841,685
Intangible assets	8,331	11,108
	<b>10,651,387</b>	<b>22,906,603</b>
<b>LIABILITIES AND SHAREHOLDERS' DEFICIENCY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities <i>[note 1]</i>	6,858,482	10,080,463
<b>Total current liabilities</b>	<b>6,858,482</b>	<b>10,080,463</b>
Convertible unsecured subordinated debentures <i>[note 4]</i>	15,018,184	13,634,906
	<b>21,876,666</b>	<b>23,715,369</b>
<b>Shareholders' deficiency</b>		
Capital stock <i>[note 5]</i>	266,858,635	266,823,735
Warrants <i>[note 5]</i>	10,817,394	10,817,394
Equity portion of convertible unsecured subordinated debentures	5,184,867	5,193,793
Contributed surplus <i>[note 5]</i>	50,211,587	48,818,826
Deficit	(344,298,290)	(332,390,857)
Accumulated other comprehensive income (loss)	528	(71,657)
<b>Total shareholders' deficiency</b>	<b>(11,225,279)</b>	<b>(808,766)</b>
	<b>10,651,387</b>	<b>22,906,603</b>

*See accompanying notes*

On behalf of the Board:



Director



Director

## ConjuChem Biotechnologies Inc.

### UNAUDITED INTERIM STATEMENTS OF DEFICIT

[See Description of Business and Going Concern Uncertainty - *note 1* ]

	Three-months ended		Six-months ended	
	April 30,	April 30,	April 30,	April 30,
	2009	2008	2009	2008
	\$	\$	\$	\$
<b>Deficit, beginning of period</b>	<b>(338,219,066)</b>	(304,814,216)	<b>(332,390,857)</b>	(292,973,699)
Net loss for the period	<b>(6,079,224)</b>	(7,925,350)	<b>(11,907,433)</b>	(19,765,867)
<b>Deficit, end of period</b>	<b>(344,298,290)</b>	(312,739,566)	<b>(344,298,290)</b>	(312,739,566)

*See accompanying notes*

**ConjuChem Biotechnologies Inc.**

**UNAUDITED INTERIM STATEMENTS OF  
OPERATIONS AND COMPREHENSIVE LOSS**

[See Description of Business and Going Concern Uncertainty - *note 1* ]

	Three-months ended		Six-months ended	
	April 30, 2009	April 30, 2008	April 30, 2009	April 30, 2008
	\$	\$	\$	\$
<b>REVENUES</b>				
Contract revenues	15,443	24,557	15,443	51,904
Interest income	32,276	375,926	138,517	948,581
	<b>47,719</b>	<b>400,483</b>	<b>153,960</b>	<b>1,000,485</b>
<b>EXPENSES</b>				
Research and development <i>[note 1]</i>	2,937,049	5,422,425	7,064,280	9,080,282
Investment tax credits <i>[note 6]</i>	(250,000)	(100,000)	(1,330,000)	(200,000)
Net research and development expenses	2,687,049	5,322,425	5,734,280	8,880,282
General and administrative expenses <i>[note 1]</i>	1,458,416	1,211,310	2,511,160	2,797,951
Amortization of property, plant and equipment	40,572	54,979	84,686	110,100
Amortization of intangible assets	1,388	2,443	2,777	4,924
Stock-based compensation	791,056	657,959	1,392,761	1,372,838
Financial charges	5,545	6,101	8,897	10,307
Foreign exchange loss	26,829	12,324	117,292	191,275
Accretion in carrying value of convertible senior unsecured notes and interest	—	—	—	5,504,427
Accretion in carrying value of convertible unsecured subordinated debentures and interest	1,116,088	1,058,292	2,209,540	1,626,809
Loss on redemption of long-term investments	—	—	—	267,439
	<b>6,126,943</b>	<b>8,325,833</b>	<b>12,061,393</b>	<b>20,766,352</b>
<b>Net loss</b>	<b>(6,079,224)</b>	<b>(7,925,350)</b>	<b>(11,907,433)</b>	<b>(19,765,867)</b>
<b>OTHER COMPREHENSIVE INCOME</b>				
Unrealized gain/(loss) on investments	(63)	405	72,185	2,732
<b>Comprehensive loss</b>	<b>(6,079,287)</b>	<b>(7,924,945)</b>	<b>(11,835,248)</b>	<b>(19,763,135)</b>
<b>Basic and diluted loss per share</b>	<b>(0.02)</b>	<b>(0.03)</b>	<b>(0.05)</b>	<b>(0.08)</b>
<b>Weighted average number of common shares outstanding during the period</b>	<b>250,456,997</b>	<b>240,213,668</b>	<b>250,444,504</b>	<b>240,213,668</b>

*See accompanying notes*

**ConjuChem Biotechnologies Inc.**

**UNAUDITED INTERIM STATEMENTS OF CASH FLOWS**

[See Description of Business and Going Concern Uncertainty - *note 1* ]

	Three-months ended		Six-months ended	
	April 30, 2009	April 30, 2008	April 30, 2009	April 30, 2008
	\$	\$	\$	\$
<b>OPERATING ACTIVITIES</b>				
Net loss	(6,079,224)	(7,925,350)	(11,907,433)	(19,765,867)
Items not affecting cash:				
Amortization of property, plant and equipment	40,572	54,979	84,686	110,100
Amortization of intangible assets	1,388	2,443	2,777	4,924
Amortization of premium on long-term investments	—	—	—	(8,436)
Stock-based compensation	791,056	657,959	1,392,761	1,372,838
Accretion in carrying value of convertible senior unsecured notes and interest	—	—	—	5,504,427
Accretion in carrying value of convertible unsecured subordinated debentures	719,752	389,639	1,409,252	958,156
Gain on proceeds for sales of property, plant and equipment	(5,253)	—	(5,253)	—
Loss on redemption of long-term investments	—	—	—	267,439
	<b>(4,531,709)</b>	<b>(6,820,330)</b>	<b>(9,023,210)</b>	<b>(11,556,419)</b>
Net changes in non-cash working capital balances relating to operations	(390,402)	2,102,413	(3,538,671)	526,257
<b>Cash flows relating to operating activities</b>	<b>(4,922,111)</b>	<b>(4,717,917)</b>	<b>(12,561,881)</b>	<b>(11,030,162)</b>
<b>INVESTING ACTIVITIES</b>				
Acquisition of investments	(4,236,904)	(8,784,180)	(9,043,104)	(21,694,881)
Proceeds on maturities of investments	7,331,130	11,115,581	22,077,445	21,515,408
Acquisition long-term investments	—	—	—	(167,037)
Proceeds on redemption of long-term investments	—	—	—	59,644,132
Acquisition of property, plant and equipment	(958)	—	(11,652)	(9,772)
Proceeds for sales of property, plant and equipment	41,390	—	41,390	—
Acquisition of intangible assets	—	—	—	(1,179)
<b>Cash flows relating to investing activities</b>	<b>3,134,658</b>	<b>2,331,401</b>	<b>13,064,079</b>	<b>59,286,671</b>
<b>FINANCING ACTIVITIES</b>				
Repayment of convertible senior unsecured notes	—	—	—	(58,006,914)
Issuance of convertible unsecured subordinated debentures	—	—	—	22,000,000
Issuance costs paid in cash	—	—	—	(1,764,414)
<b>Cash flows relating to financing activities</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>(37,771,328)</b>
<b>Net change in cash and cash equivalents during the period</b>	<b>(1,787,453)</b>	<b>(2,386,516)</b>	<b>502,198</b>	<b>10,485,181</b>
Cash and cash equivalents, beginning of period	4,477,074	14,107,401	2,187,423	1,235,704
<b>Cash and cash equivalents, end of period</b>	<b>2,689,621</b>	<b>11,720,885</b>	<b>2,689,621</b>	<b>11,720,885</b>
<b>Supplemental cash flow information:</b>				
Interest paid	52	—	814,661	13,006,914

See accompanying notes

## **ConjuChem Biotechnologies Inc.**

# **NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS**

April 30, 2009

## **1. DESCRIPTION OF BUSINESS AND GOING CONCERN UNCERTAINTY**

### **Description of business**

ConjuChem Biotechnologies Inc. ["ConjuChem" or the "Company"] is a biotechnology company operating in a single business segment out of its Canadian facility and its primary business purpose is the development and use of its bioconjugation technologies to develop therapeutic drugs. The Company enters into contracts with companies for the exclusive right to use certain of its technologies and to jointly develop specific drugs. All of the Company's contract revenues were derived from clients in the United States in 2008 and 2009. The Company's assets are all located in Canada.

### **Going concern uncertainty**

These financial statements have been prepared by management on a going concern basis, which assumes the Company will continue its 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. The use of these principles may not be appropriate because as of April 30, 2009, there was substantial doubt that the Company will be able to continue as a going concern without raising additional financial resources.

The Company has incurred significant operating losses since inception, has accumulated a deficit of \$344,298,290 as at April 30, 2009 and, as of this date, has total liabilities exceeding its total assets. Also, the Company's anticipated level of annual expenditures exceeds the committed sources of funds and the Company's cash, cash equivalents, and investments on hand as of April 30, 2009. To date the Company has financed its cash requirements primarily through the issuance of common shares, convertible unsecured notes, debenture issuances, and investment tax credits. The Company's ability to continue as a going concern is dependent upon its ability to obtain additional financing. The Company is currently seeking additional capital to finance its operations. Management is considering all financing alternatives, including equity financing, debt arrangement, non-dilutive financing, corporate collaboration and licensing arrangements. There can be no assurance that such financing will materialize on a timely basis or be obtained on favourable terms. If the Company is unable to obtain additional financing, management may be required to curtail the Company's operations.

These financial statements do not give effect to any adjustments to the amounts and classification for assets and liabilities that may be necessary should the Company be unable to continue as a going concern. Such adjustments could be material.

## **ConjuChem Biotechnologies Inc.**

# **NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS**

April 30, 2009

### **Consolidation of operations**

During the quarter ended April 30, 2009, the Company completed a consolidation of its operations, focusing its resources on securing a partner for PC-DAC<sup>TM</sup>:Exendin-4 and the rapid development of PC-Insulin, a long-acting basal insulin in preclinical testing. The restructuring included a workforce reduction of approximately 50% of the Company's personnel. The Company recorded charges for termination costs of \$582,465, \$296,245 was included in research and development expenses and \$286,220 was included in general and administration expenses during the quarter ended April 30, 2009. As at April 30, 2009, a liability of \$280,148 remains.

### **2. BASIS OF PRESENTATION**

The unaudited interim financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles applicable to interim financial statements. Accordingly, they do not include all the information and disclosures required according to Canadian generally accepted accounting principles for audited annual financial statements and should be read in conjunction with the Company's audited financial statements and notes thereto for the year ended October 31, 2008.

Information with respect to the October 31, 2008 balance sheet is derived from the Company's audited financial statements. The accounting policies underlying these interim financial statements are those set forth in notes 2 and 3 of the audited financial statements for the year ended October 31, 2008 and those mentioned in note 3 to the interim financial statements.

### **3. CHANGE IN ACCOUNTING POLICIES**

Effective November 1, 2008, the Company adopted the following Handbook Sections recently introduced by the Canadian Institute of Chartered Accountants ["CICA"]:

Section 1400, "General Standards of Financial Statement Presentation". This section has been amended to include requirements for management to assess and disclose an entity's ability to continue as a going concern. The adoption of this section did not have any impact on the Company's unaudited interim financial statements.

Section 3064, "Goodwill and Intangible Assets". This section, 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. The adoption of this section did not have any impact on the Company's unaudited interim financial statements.

## ConjuChem Biotechnologies Inc.

### NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS

April 30, 2009

#### Recent accounting pronouncements

In January 2009, the CICA issued Handbook Sections 1582 "Business Combinations which replace CICA Handbook Section 1581 "Business Combinations". Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable for the Company's business combinations with acquisition dates on or after January 1, 2011. Early adoption of this Section is permitted. The Company does not anticipate the adoption of the above standard will have a significant impact on the Company's financial statements.

In March 2009, the Accounting Standards Board announced that it would improve the information to disclose on financial instruments. Section 3862 of the CICA Handbook, "Financial Instruments - Disclosures" has been amended to clarify the requirements in respect of maturities of financial liabilities and the disclosures about how an entity manages liquidity risk. The Company evaluates the impact on its financial statements.

#### 4. CONVERTIBLE UNSECURED SUBORDINATED DEBENTURES

The carrying value of the convertible unsecured subordinated debentures is detailed as follows as at April 30, 2009:

	\$
Fair value upon issuance	13,500,000
Accumulated accretion expense	3,122,330
Less: Unamortized portion of deferred financing costs	(579,373)
Less: Portion of the carrying value attributable to the 1,670 units converted into common stock	(1,024,773)
<b>Balance as at April 30, 2009</b>	<b><u>15,018,184</u></b>

The debentures bear interest at an accrual rate of 8.0% payable semi-annually and mature on December 31, 2010.

#### 5. SHAREHOLDERS' DEFICIENCY

##### Authorized

An unlimited number of common shares.

**ConjuChem Biotechnologies Inc.**

**NOTES TO UNAUDITED INTERIM  
FINANCIAL STATEMENTS**

April 30, 2009

**5. SHAREHOLDERS' DEFICIENCY [Cont'd]**

**Issued and outstanding**

	Number of common shares #	Capital Stock \$
<b>Balance as at October 31, 2008</b>	250,432,418	266,823,735
Issued upon conversion of 35 units of convertible unsecured subordinated debentures	218,750	34,900
<b>Balance as at April 30, 2009</b>	<b>250,651,168</b>	<b>266,858,635</b>

**Contributed surplus**

	\$
<b>Balance as at October 31, 2008</b>	48,818,826
Stock-based compensation charge for the six-month period	1,392,761
<b>Balance as at April 30, 2009</b>	<b>50,211,587</b>

**Warrants**

Warrants outstanding as at April 30, 2009 are as follows:

Exercise price (\$)	Number outstanding	Weighted average months to expiry
1.00	96,826,750	7
0.25	34,375,000	32
	<b>131,201,750</b>	

**Stock option plan**

The changes to the number of stock options granted by the Company and their weighted-average exercise price, for the six-month period ended April 30, 2009, are as follows:

	#	\$
<b>Balance as at October 31, 2008</b>	<b>23,848,443</b>	0.69
Forfeited	(404,201)	0.90
<b>Balance as at April 30, 2009</b>	<b>23,444,242</b>	0.67
Options exercisable, end of period	13,399,576	0.94

**ConjuChem Biotechnologies Inc.**

**NOTES TO UNAUDITED INTERIM  
FINANCIAL STATEMENTS**

April 30, 2009

**5. SHAREHOLDERS' DEFICIENCY [Cont'd]**

Compensation expense of \$1,392,761 [2008 – \$1,372,838] has been recorded in the six-month period ended April 30, 2009 for stock options granted with a corresponding credit to contributed surplus. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions:

	<b>2009</b>	<b>2008</b>
	\$	\$
Expected dividend	—	0.0%
Volatility	—	131.4%
Risk-free interest rate	—	3.2%
Expected option life in years	—	5
Weighted-average fair value of options on date of grant	—	\$0.09

No options were granted in the six-month period ended April 30, 2009.

**Diluted earnings per share**

No options or warrants outstanding at April 30, 2009 and 2008 were included in the calculation of diluted earnings per share, as all such securities would be anti-dilutive.

**6. INVESTMENT TAX CREDITS**

Following the results of tax audits during the six month period ended April 30, 2009, the Company reversed tax reserves for investment tax credits in the amount of \$850,000.

## **CONJUCHEM<sup>®</sup>**

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