2008 ANNUAL REPORT

TABLE OF CONTENTS

TSO_3: SIGNIFICANT NEW PROGRESS	3
2008 ANNUAL REVIEW	4
MESSAGE FROM THE PRESIDENT	6
MANAGEMENT, DISCUSSION AND ANALYSIS	9
MANAGEMENT REPORT	27
FINANCIAL STATEMENTS	29
DIRECTORS	56
SCIENTIFIC ADVISORY BOARD	56
INVESTORS' INFORMATION	57
ACKNOWLEDGEMENTS	58

TSO_3: SIGNIFICANT NEW PROGRESS

Company Profile

Since it was founded in 1998, TSO_3 has made its mission the development and commercialization of innovative, high performance solutions with strong commercial potential, designed for the sterilization of medical instruments.

The Company has developed a unique sterilization process that utilizes ozone as the sterilizing agent. Compared to the other methods currently utilized, the ozone sterilization process – developed and patented by TSO_3 – addresses the evolving needs in sterilization: it provides major savings in operating costs, greater security for both users and patients, and "green" technology that is environmentally friendly.

The Company believes this technology constitutes a viable replacement solution for other low-temperature sterilization processes currently utilized in hospital settings.

The TSO_3 STERIZONE® 125L Sterilizer has been cleared for commercialization by both Health Canada and the United States Food and Drug Administration (FDA). In addition, in early 2009 the Company filed new claims with these same organizations in order to expand TSO_3 STERIZONE® Sterilization System's field of application to a wider range of complex surgical instruments. When approved, this will give TSO_3 a new major competitive edge.

More precisely, the TSO_3 STERIZONE® Sterilization System is made for hospital sterile processing centers. It is a large capacity sterilizer designed to be used in all kinds of health care establishments. This reliable and easy-to-use device permits the efficacious sterilization of surgical and diagnostic instruments sensitive to heat and moisture.

TSO_3 currently has approximately 70 employees and became a publicly owned company on August 30, 2001, with an Initial Public Offering of $5 million. The Company has raised an additional $65 million through subsequent rounds of financing and the exercise of warrants. Company shares are now traded on the Toronto Stock Exchange (TSX) TOS symbol.

2008 ANNUAL REVIEW

New additions to the Company's Management Team

During the year 2008, TSO_3 welcomed to its ranks two new executives, including Mr. Richard M. Rumble to the position of President and Chief Executive Officer. Prior to his appointment, Mr. Rumble held the position of President of BERCHTOLD Corporation. He has more than 25 years experience as a manager and senior executive in the North American and global medical devices industry. He has successfully established strategies that resulted in significant growth in profits and revenues for various companies during his career, in addition to creating several business development plans.

Furthermore, Mr. Robert F. Mosher (Executive, non-officer) was appointed Vice President, Marketing of TSO_3. Mr. Mosher has two decades of experience as a senior manager in the international health care and medical sterilization sector. Prior to this appointment, he held the position of Director, Global Product Marketing, Terminal Sterilization for Johnson & Johnson/Advanced Sterilization Products. In his new position, Mr. Mosher is responsible for identifying and developing new growth opportunities for TSO_3' s innovative medical instrument sterilization technology in North America and worldwide.

Operational Changes and Efficiency Gains

Over the last year, TSO_3 has taken various measures to increase its operational efficiency and reduce its operating costs. At the marketing level, the enterprise has re-targeted its US sales team's development efforts toward market segments that offer better short-term sales potential. Furthermore, the sales team is today composed of individuals who have a great deal of experience and whose credibility is renowned in the medical sector.

TSO_3 has exercised tight control over its expenses and made efficiency gains. Cost reduction efforts initiated in 2008 are expected to bring results in 2009. These changes will enable the Company to conserve its liquid assets during a difficult period in the financial markets.

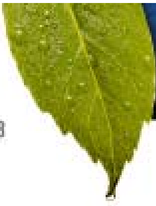
With regard to its R&D operations, TSO_3 has reviewed its methods and its approach to ensure that the Company's technological development efforts are directly aimed at addressing the needs and expectations of targeted potential clients. A hierarchy of these needs has been clearly defined, which has permitted R&D to better orient its work.

Partnership Agreements

In 2008, TSO_3 also established some partnership agreements to support its sales and business development. Notably, the Company was chosen to be a vendor partner by the Mid-Atlantic Group Network of Shared Services (MAGNET), one of the largest and oldest Group Purchasing Organizations in the United States. From its offices on the East Coast, *MAGNET* serves 11,000 health care facilities by providing access to a contract portfolio of high-quality equipment and services.

TSO_3 has also been accredited by the U.S. General Services Administration, which now allows the Company to target a market of about 225 US government health care facilities, such as hospitals and medical centres for military personnel, veterans and aboriginals.

Earlier in 2008, TSO_3 announced the signing of an agreement with Broadlane. This company is a leading US supply chain services company that provides technology-oriented business solutions to improve the financial and operational performance of thousands of acute care hospitals, ambulatory care facilities, physician practices and other healthcare providers throughout the United States.



MESSAGE FROM THE PRESIDENT

A new way forward

Without a doubt, 2008 marked a turning point for TSO_3. We were confronted with challenges, but faced them with determination, which has enabled us to make significant progress at all levels of the Company. These achievements range from our recent Food and Drug Administration (FDA) filing milestone, to strengthening our management and sales teams, to developing a new three-year strategic plan. As we begin the year 2009, we look upon TSO_3's future with renewed confidence, backed by tangible and promising progress.

A team with a vision

To strengthen the Company's leadership and define a clear vision and direction going forward, TSO_3 brought new individuals into key leadership positions, including President and Chief Executive Officer, Vice President, Marketing and a new US sales team leader. Dedicated to serving the best interests of its clients and TSO_3's shareholders – the Company's owners – these individuals together with the Company's Co-founder and members of the leadership team are determined to lead this promising enterprise to success.

As the new President and Chief Executive Officer of TSO_3, a chief priority during my inaugural quarter was to improve communications with the Company's external and internal stakeholders. To further this goal, I have visited clients in the field and am working closely with the R&D team to ensure that technological objectives are directly aligned with client and market needs. Enhanced communications and goal-setting have been established in all areas of the Company through regular meetings with leadership staff. This has positively impacted all operations, as demonstrated by our recent completion of regulatory filings for enhanced claims.

With the lines of communications open and short-term goals set, we set out to develop a three-year strategic plan and tested it for feasibility. The plan's overall objective is to position the Company's technology in the market as the new benchmark in health care sterile processing. This three-year plan was delivered to our Board of Directors and has been approved.

Furthermore, to increase the effectiveness of our business development efforts, we have implemented significant changes to our sales structure, which have resulted in the establishment of an experienced, talented and efficient team of Sales and Clinical Specialists who are marketing TSO_3's sterilization technology to health care facilities across North America.

TSO3

Unrivalled technology: *Dynamic Sterilant Delivery Process*®

TSO_3's strategic plan is centered on the strength of our technology, which is unrivalled by any other new generation low-temperature sterilization system in the market today. TSO_3 is already recognized as providing the most cost effective low temperature sterilization cycles incorporating "Green" technology. Our commitment to develop superior sterilization systems that are commercially and environmentally responsible remain a focus for the Company.

TSO_3 also intends to capitalize on its key competitive edge in the health care sterilization field. This core differentiator lies within our proprietary *Dynamic Sterilant Delivery Process*® that provides a continuous flow of sterilizing ozone gas into the unit's sterilization chamber. This process allows the sterilizing agent to be delivered where and when it is needed.

In contrast, other low-temperature sterilization systems rely on a single dose, diffusion-dependent process that limits the complexity and number of instruments that can be sterilized per load. We firmly believe TSO_3's technology is superior and that, over time, our approach will be recognized as surpassing the limitations of other low-temperature systems, as well as addressing serious safety and other concerns of ethylene oxide – an older generation, low-temperature sterilization method.

To achieve sales growth based on the strength of our proprietary technology, TSO_3 has filed with the FDA to expand claims for our TSO_3 STERIZONE® low temperature Sterilization System. We have collected exhaustive data to document our technology's sterile efficacy across a much broader and deeper range of surgical instruments. For TSO_3, this milestone filing opens many potential avenues for growth and market development that we intend to pursue.

On March 10, 2009 we notified the Medical Devices Bureau (Health Canada) of our intent to begin the commercialization of our process with these expanded claims. These claims include the capability of effectively sterilizing multiple, packaged, multi-lumened flexible endoscopes. It is our intent to continuously document and update data that supports our technology's ability to sterilize the most complex devices in the medical industry.

Customer Needs

In addition to these initiatives, we are also highlighting another important technological advantage. TSO_3's Dynamic Sterilant Delivery Process® allows the Company to modify its cycles to address the compatibility needs of different materials. As a result, we believe that our solution is compatible with a wider range of medical materials than alternative sterilization methods. We believe our proprietary ozone delivery process could provide clients with sterilization cycle options that are unavailable using other low-temperature sterilization systems, such as gentler cycles that could be used to sterilize more delicate instrumentation, yet still offer superior sterile efficacy claims.

Combining sterile efficacy with improved materials compatibility offers the first real option for customers who wish to completely eliminate the use of ethylene oxide in their facilities. This distinctive advantage is another solid pillar on which the Company can build its future. Sterile processing is practiced routinely in three departments within acute care hospitals. Due to the benefits offered by TSO_3's proprietary process, the Company believes that additional markets for low temperature sterilization in the health care sector exist outside of the traditional sterile processing departments. These opportunities are currently being evaluated and will be the subject of future communications.

Our research shows a hierarchy of our clients' and prospective client's low-temperature sterilization needs. These needs, in relative order of importance are: sterile efficacy ensuring patient safety, materials compatibility, timely through-put, cost effectiveness, and users and environmental safety. TSO_3's technology answers all of these needs, plus provides the additional advantages of high reliability and ease-of-use.

Equipped with a strengthened team, focused strategic plan, new regulatory filings and unmatched technological edge, I am encouraged and excited about our Company's prospects. I would like to take this opportunity to thank TSO_3's dedicated employees for their enthusiastic response to the Company's new direction. I would also like to express my gratitude to the Company's shareholders for their support as we set the new standard in health care sterilization and continue to grow TSO_3 together.

I would like to extend a special thanks to Mr. Jocelyn Vézina, TSO_3's co-founder, who in 2008 left his position as the Company's President and Chief Executive Officer and as a member of the Board. With his vision, energy and determination, Mr. Vézina played a major role in TSO_3's history, enabling the original project to develop into a structured, innovative and promising Company. He did this while working closely with fellow co-founder Mr. Simon Robitaille and all the Company's employees.

I also wishes to underline the work of Mr. W. Barry McDonald who, for several months during 2008, held the position of Interim President and Chief Executive Officer following Mr. Vézina's departure. Mr. McDonald quickly brought new momentum to the Company.

Richard M. Rumble
President and Chief Executive Officer

MANAGEMENT, DISCUSSION AND ANALYSIS

This management analysis presents information on TSO_3 activities, and compares the operating results and financial situation for the years ended December 31, 2008 and December 31, 2007. The following information must be read in conjunction with the audited financial statements and unless advised otherwise, all figures are in Canadian dollars.

OVERVIEW

Founded in June 1998, TSO_3 (the "Company") has developed a unique new sterilization process that uses ozone as the sterilizing agent. The first device resulting from this technological platform, the TSO_3 STERIZONE® 125L Sterilizer has been designed to sterilize the new generation of surgical and diagnostic instruments made of heat-sensitive polymers. After receiving approval from Health Canada on May 3, 2002, the Company obtained clearance from the United States Food and Drug Administration (FDA) to sell the TSO_3 STERIZONE® 125L Sterilizer and the accompanying Chemical Indicator on September 3, 2003.

INTERNAL SALES FORCE

The Company relies on its direct sales force to support its commercial sales strategy. This team can profit from the contribution of sales professionals predominantly in the United States, who have extensive experience selling capital equipment to both operating rooms and central sterilization departments in hospitals.

TSO3

SUMMARY OF OPERATING RESULTS

Fiscal years ended December 31 (in thousands of dollars, except loss/share)

	2008	2007	2006
Sales	**$2,235**	$1,731	$1,070
Operating	**$2,777**	$1,892	$1,643
Sales and Marketing	**$3,713**	$4,189	$3,185
Research & Development (before tax credits)	**$2,351**	$1,782	$1,682
Administrative	**$3,961**	$3,228	$3,090
Financial Fees	**$23**	$17	$18
Other Revenues	**$956**	$1,465	$1,071
Net Loss	**$9,634**	$7,912	$7,477
Net Loss per Share	**$0.20**	$0.17	$0.20
Weighted Average Number of Shares Outstanding (in thousands)	**47,863**	45,321	36,560

SALES

For the fiscal year ended December 31, 2008, Sales increased $504,084 (29.1%) to reach $2,235,101, compared to $1,731,017 in 2007. During the fiscal year 2008, the Company completed the sale of 13 sterilizers and related accessories, compared to 11 sterilizers and accessories in 2007.

OPERATING

For the fiscal year ended December 31, 2008, Operating Expenses increased $885,147 (46.8%) to reach $2,776,815 $, compared to $1,891,668, in 2007. Operating Expenses are related to the Production and After-Sales Service Department as well as the costs of manufacturing the devices. Having sold more devices during 2008, the variance between the two periods is partially explained by an increase in the cost of goods sold. This variance is also explained by an increase in maintenance, an allowance for inventory obsolescence, and an increase in salaries related to operations and after-sale service. Indeed, these two departments grew from 13 to 15 employees between the two periods.

SALES AND MARKETING

For the fiscal year ended December 31, 2008, sales and marketing expenses decreased $476,811 (11.4%) to reach $3,712,592 compared to an amount of $4,189,403 in 2007. The variance between the two periods is mainly the result of a decrease in salaries, and expenses due to a reorganization of the sales and marketing team implemented in June 2008. The variation can also be explained by a decrease in sales expenses and expenses related to hiring personnel. Conversely, expenses related to the payment of commissions, sales material and professional fees increased during the fiscal year 2008. Also, Sales and Marketing expenses in 2008 include an amount of approximately $240,000 which represents non-recurring exceptional expenses from reorganizations during the year 2008.

RESEARCH AND DEVELOPMENT ACTIVITIES

For the fiscal year 2008, R&D expenses before tax credits increased $568,923 (31.9%) to reach $2,351,176 compared to $1,782,253 in 2007. The increase between these two fiscal years is explained by an increase in material purchases, subcontracting fees and expenses related to work on the inactivation of prions. This variance is also due to an increase in salaries. This department grew from 21 to 28 employees between the two periods. Conversely, expenses related to the Scientific Advisory Board decreased during the fiscal year 2008.

ADMINISTRATION

For the fiscal year ended December 31, 2008, administration expenses increased $732,764 (22.7%) to reach $3,960,970 compared to $3,228,206 in 2007. This variance is attributed to an increase in salary and fringe benefits, lease expenses, and by an increase in professional fees. The variance is also attributed to the payment of severances during the year 2008. Conversely, expenses related to *Stock-based Compensation* and bonuses decreased during the fiscal year 2008. Administration expenses for the last fiscal year include an amount of approximately $780,000 which represents non-recurring exceptional expenses from the reorganization of June 2008.

OTHER REVENUES

For the fiscal year ended December 31, 2008, other revenues decreased $509,406 (34.8%) to reach $955,747 compared to $1,465,153 in 2007. The variance is mainly due to a decrease in investment revenues, grants and R&D tax credits. Conversely, a foreign exchange gain occurred during the fiscal year 2008.

NET LOSS

The Company recorded for the period ended December 31, 2008, a net loss of $9,633,804, or $0.20 per share, compared to a net loss of $7,912,490, or $0.17 per share, in 2007. The loss of 2008 includes an amount of approximately $1,020,000 ($0.02 per share) which represents non-recurring exceptional expenses from reorganizations that took place during the fiscal year 2008.

FINANCIAL SITUATION
As of December 31 (in thousands of dollars)

	2008	2007	2006
Liquid Assets (Cash, Cash Equivalents and Temporary Investments)	**$17,878**	$26,205	$7,309
Accounts Receivable	**$661**	$975	$811
Inventories	**$2,548**	$2,996	$3,388
Property, Plant and Equipment	**$676**	$472	$391
Intangible Assets	**$3,642**	$3,700	$3,712
Deferred Revenues	**$389**	$146	$76
Share Capital and Contributed Surplus	**$81,111**	$80,682	$52,149
Shareholders' Equity	**$23,872**	$33,041	$14,624

LIQUID ASSETS AND FINANCIAL SITUATION

The Company preserved an adequate position of liquidity in 2008. As of December 2008, cash, temporary investments and accounts receivable amounted to $18,538,788 compared to $27,180,185 as of December 31, 2007.

ACCOUNT RECEIVABLES

As of December 31, 2008, accounts receivables amounted to $660,578 compared to $975,011 for the same period in 2007. The difference between the two periods is due to decrease in accounts receivable.

INVENTORIES

As of December 31, 2008, current assets showed inventory valued at $2,548,075 compared to $2,996,409 as of December 31, 2007. These amounts were attributable to the cost of producing sterilizers for the commercial launch. The variance between the two periods is explained by a decrease in the level of inventories between the two periods. Also, during the fiscal year 2008, an allowance for obsolescence in the amount of $298,970 was applied against inventories ($99,357 as of December 31, 2007).

DEFERRED REVENUES

As of December 31, 2008, deferred revenues amounted to $388,958 compared to an amount of $145,878 as of December 31, 2007. The item *Deferred Revenues* reflects financial transactions related to parts, warranties and service contracts not yet recognized as revenues. The variance between the two periods is explained by an increase in amounts received for service contracts.

SHARE CAPITAL AND CONTRIBUTED SURPLUS

As of December 31, 2008, share capital and contributed surplus amounted to $81,111,234 compared to $80,681,660 $ as of December 31, 2007.

REQUIRED CAPITAL PAYMENTS AND CONTRACTUAL COMMITMENTS

Required capital payments and the various contractual commitments in the coming fiscal year are as follows:

	2009	2010	2011	2012	2013
R&D Contracts	**$19,116**	**$ -**	**$ -**	**$ -**	**$ -**
Operating leases and service contracts	**$122,548**	**$68,483**	**$20,130**	**$14,640**	**$1,220**
Total	**$141,664**	**$68,483**	**$20,130**	**$14,640**	**$1,220**

SUMMARY OF QUATERLY RESULTS

($000 except/share)	2008				2007			
	T4	T3	T2	T1	T4	T3	T2	T1
Sales	**382**	**725**	**1,037**	**91**	676	281	575	199
Other Revenues	**247**	**204**	**203**	**302**	399	331	561	174
Net Loss	**2,898**	**1,848**	**2,728**	**2,160**	2,166	2,043	1,634	2,069
Net Loss per share (basic and diluted)	**0.06**	**0.04**	**0.05**	**0.05**	0.04	0.04	0.04	0.05

This figure shows the quarterly evolution of sales and other income as well as losses. Non-recurring expenses associated with reorganizations that took place during the year 2008 accounted for $0.02 per share, one cent in each of Q2 and Q4. Excluding these exceptional charges, the net loss per share has remained somewhat stable over the past eight quarters.

FOURTH QUARTER

Three-month period ended December 31, 2008, compared to the three-month period ended December 31, 2007.

	FOURTH QUARTER (3 MONTHS)	
	2008	2007
SALES	**$381,517**	$675,616
EXPENSES		
Operating	**902,439**	645,336
Sales & Marketing	**769,510**	1,149,804
Research & Development	**716,584**	514,814
Administrative	**1,132,372**	924,850
Financial	**4,791**	6,082
OPERATING LOSS	**3,144,177**	2,565,269
OTHER REVENUES	**246,795**	398,667
NET LOSS	**$2,897,381**	$2,166,603
BASIC AND DILUTED NET LOSS PER SHARE	**$0.06**	$0.04
AVERAGE NUMBER OF OUTSTANDING SHARES	**47,863,402**	47,790,928

SALES

For the three-month period ended December 31, 2008, Sales amounted to $381,517 compared to $675,616 for the corresponding period in 2007. The Company recognized, during the fourth quarter of 2008, the sale of two sterilizers with accessories compared to the sale of four sterilizers with accessories during the corresponding period in 2007.

OPERATING

For the three-month period ended December 31, 2008, operating expenses were $902,438 compared to $645,336 for the same period in 2007. The variance between these two periods is explained by an increase in the provision for obsolescence of inventories as well as salaries related to operations and after-sale Service. Conversely, the cost of goods sold decreased because fewer devices were sold during the period.

SALES AND MARKETING

Sales and marketing expenses amounted to $769,510 for the three-month period ended December 31, 2008 compared to $1,149,804 for the same period in 2007. The variance between the two periods is explained by a decrease in salaries and sales expenses due to a reduction in the number of regional sales managers following the reorganization of June 2008. The difference is also explained by a decrease in professional fees between the two quarters. Sales and marketing for the three-month period ended December 31, 2008 included an amount of approximately $105,000 which represents non-recurring severance payments.

RESEARCH AND DEVELOPMENT ACTIVITIES

For the three-month period ended December 31, 2008, research and development expenses before tax credits amounted to $716,584 compared to $514,814 for the same period in 2007. The variance between the two periods is mainly explained by an increase in salaries resulting from the addition of employees to the R&D Department. The variance is also explained by an increase in material purchases and expenses related to work on the inactivation of prions. Conversely, expenses related to the Scientific Advisory Board decreased between the two periods.

ADMINISTRATION

Administration expenses for the three-month period ended December 31, 2008, amounted to $1,132,372 compared to $924,850 for the same period in 2007. The variance between the two periods is explained by an increase in professional fees, salaries, and fringe benefits related to administration as well as an increase in capital tax payments. Conversely, expenses related to *Stock-based Compensation* decreased between the two periods. Administration expenses for the three-month period ended December 31, 2008 include an amount of approximately $155,000 which represents non-recurring expenses as a result of continuing reorganization started in June 2008.

OTHER REVENUES

For the last quarter of 2008, the Company realized *Other Revenues* of $246,795 compared to $398,667 for the same period in 2007. The variance is mainly due to a decrease in investment revenues, grants and R&D tax credits. Conversely, a foreign exchange gain occurred during the fourth quarter of 2008.

NET LOSS

The Company recorded, for the fourth quarter of 2008, a net loss of $2,897,381, or $0.06 per share, compared to a net loss of $2,166,603 for the same period in 2007, or $0.04 per share. As previously stated the net loss for the fourth quarter of 2008, includes non-recurring exceptional expenses of approximately $260,000, or $0.01 per share.

CAPITAL RESOURCES

The Company principally uses its capital to finance operating expenses, commercialisation fees, marketing expenses, R&D expenses, administrative expenses, working capital and capital expenditures. Historically, the Company has funded its activities through several rounds of public and private financing, as well as from various government subsidies. Since its inception in June 1998, the Company has raised more than $70,000,000 from the sale of its equity.

For the twelve-month period ended December 31, 2008, the monthly burn-rate was $707,000 or a total of $8,483,969 for the fiscal year 2008. From this amount, approximately $1,020,000 ($76,667 monthly), are non-recurring exceptional expenses from the reorganization of June 2008. The Company believes that its current liquid assets are sufficient to finance its activities through 2010.

The Company has a line of credit with which it can obtain advances up to a maximum of $350,000.

The Company invests its liquidities in different funds and in fixed-income securities offered by governmental, paragovernmental and municipal entities as well as from companies that have high credit ratings. These securities are chosen according to the schedule of foreseen expenses and according to interest rates. Also, the Company does not hold investments in Asset Backed Commercial Paper that are not guaranteed by financial institutions or by the Government.

As of December 31, 2008, the number of outstanding shares was 47,863,402.

STATEMENTS OF CASH FLOW

Fiscal year ended December 31, 2008 compared to fiscal year ended December 31, 2007

Cash flow used for operating activities increased $1,452,946 to reach $7,898,553 for the fiscal year ended December 31, 2008 compared to $6,445,607 for the corresponding period in 2007. This variance is mainly explained by an increase, between the two periods, in the net loss as well as a decrease in the variation in accounts receivable and inventories between the two fiscal years.

For the fiscal year ended December 31, 2008, cash flows used for investment activities amounted to $4,996,972 compared to $4,412,164 for the fiscal year ended December 31, 2007. This variance is mainly explained by an increase of the net difference between the acquisition and liquidation of investments. The variance is also explained by an increase, between the two periods, in the acquisition of property, plant and equipment.

For the fiscal year ended December 31, 2008, Cash Flows from financing activities were zero compared to $25,630,716 in 2007. In fact the Company closed a financing of $23,000,000 from the sale of units during that fiscal year.

FOURTH QUARTER

Cash flows used for operating activities decreased $922,505 to reach $765,827 for the three-month period ended December 31, 2008 compared to $1,688,332 for the corresponding period in 2007. Despite the increase in net loss between the two periods, the decrease is mainly explained by an increase in the variation of accounts receivable.

For the three-month period ended December 31, 2008, cash flows used for investment activities amounted to $8,397,292 mainly due to acquisition of investments. For the corresponding period in 2007, cash flows from investment activities were $1,511,900 also due to the acquisition of investments.

For the three-month periods ended December 31, 2008 and 2007, cash flows from financing activities were zero.

OFF-BALANCE SHEET TRANSACTION

During the fiscal year 2008, the Company made no off-balance sheet transaction.

TRANSACTIONS WITH RELATED PARTIES

The Company leases its premises from a company owned by some of the Company's shareholders. Over the last three complete fiscal years, the Company has made the following related transactions, assessed at fair value:

	2008	2007	2006
Rent	**$61,561**	$59,365	$57,804
Other Rent-Related Expenses	**$71,138**	$67,069	$76,431
	$132,699	$126,434	$134,235

ACCOUNTING POLICIES

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Since the financial reporting process requires the use of estimates, actual results could differ from these estimates.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash, investments, asset-backed commercial paper secured by financial institutions and by the Canadian government, and money market funds. The Company has classified these instruments as held for trading. These investments are highly liquid and are held for the purpose of meeting short-term cash commitments. They are recorded at fair value. Increases and decreases in fair value are recognized as investment income and presented under “Other revenues” in the Statement of Earnings.

INVENTORIES

The cost of inventories is essentially determined using the first in, first out method. The cost of work in progress and finished goods comprises the cost of raw materials and an applicable share of the cost of labour and manufacturing overhead based on normal production capacity. Inventories are valued at the lower of cost and net realizable value.

When an impairment is recognized, a new assessment of net realizable value is performed in each subsequent period. When the circumstances that justified writing down the inventories below cost no longer exist, or when there is a clear indication of an increase in net realizable value due to a change in the economic situation, the amount of the write-down is reversed such that the new carrying amount is the lower of the cost or the revised net realizable value.

INTANGIBLE ASSETS

Intangible assets consist of the acquisition cost of a patent licence, the acquisition cost of a technology and all the related rights, the cost of patents, the costs of trademarks, software and the website.

Amortization of intangible assets is calculated using the straight-line method over the useful lives, as follow:

Patents	*20 years*
Licence	*16 years*
Software and Website	*3 years*
Trademarks	*10 and 15 years*

Technology is amortized using the straight-line method over an estimated useful life of 20 years.

REVENUE RECOGNITION

The Company generates revenue mainly from the sale of ozone sterilization units, parts, supplies and accessories related to these units, and service and maintenance contracts for the units. The Company is generally committed under revenue arrangements with multiple deliverables that include delivery of units, installation, maintenance, customer service and consulting services. The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the price to the buyer is fixed or determinable and collection is reasonably assured.

Revenue from revenue arrangements with multiple deliverables are divided into separate units of accounting when the Company has reliable evidence. Revenue related to service contracts offered to clients is deferred and recognized using the straight-line method over the term of the contract.

Revenue earned on the units sold, the parts and accessories related to these units, and the installation and consulting services, are recognized upon delivery of the service and the client's acceptance of the services received. Maintenance and service contracts are recognized using the straight-line method over the term of the contract.

Conversely, a significant portion of the Company's revenues are received in US dollars. The Company takes advantage of a natural protection. This reality is offset by the fact that approximately 20% of Company expenses are paid out in US dollars.

COMPENSATION AND OTHER STOCK-BASED PAYMENTS

Commencing January 1, 2004, the Company now records stock-based compensation and other stock-based payments according to the fair value method as required by the new Canadian Institute of Chartered Accountants (CICA) regulations. The compensation expense associated with this method of stock-based payment is therefore recognized as earnings. The adoption of this new regulation resulted in an increase of $429,574 in compensation expenses for 2008 ($678,424 in 2007). The stock-options granted for fiscal year 2003 through 2007 will result in additional expenses of $234,626 in 2009, $113,101 in 2010, $48,334 in 2011 and $17,167 in 2012. These costs constitute non-cash operations.

FUTURE ACCOUNTING CHANGES

INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February 2008, the Canadian Accounting Standards Board confirmed that publicly-accountable enterprises would be required to use International Financial Reporting Standards (IFRS) in the preparation of financial statements for fiscal years beginning on or after January 1, 2011. In the Company's case, the use of IFRS will be required for the interim and annual financial statements dated after January 1, 2011 with comparative statements restated under IFRS. During the financial period, ended on December 31, 2008, the Company developed an IFRS changeover plan. This plan is comprised of three separate phases:

Phase I

Completed during the last financial period, consisted of a diagnostic designed to identify the main conversion issues for the Company and their potential impact.

Phase II

Should be completed by December 31, 2009. The purpose of this phase is to analyze, calculate the impact of and select the different accounting policies to adopt for the IFRS changeover. During this phase, the Company will put in place the internal processes and policies to collect and compile the required information for the IFRS changeover.

Phase III

Should be completed by March 31, 2011. The purpose of this phase is to prepare the opening balance sheets, the financial statements (current and comparative period), the conciliation notes and the supplementary notes required for the IFRS and its initial adoption.

Further to the work done, management created a summary list of the potential consequences to the Company of the IFRS changeover:

- **Accounting policies**: According to the Company's management, the IFRS will have little impact on the accounting policies of the Company because these policies are currently consistent with the IFRS. According to the Company's management, the biggest impact of the IFRS changeover for the Company should be at the level of supplementary information as disclosed in the notes of the Financial Statements and at the level of accounting terminology used. The IFRS could have a moderate impact on the recognition and presentation of financial instruments and shareholder's equity of the Company.
- **Information technology (IT)**: Company's management believes that the IFRS changeover will have a limited impact on internal controls and procedures because they are currently able to produce complete and reliable financial and non financial information to management in accordance to the IFRS.
- **Control mechanisms and internal procedures:** Company's management estimates that the adoption of the IFRS will have a limited impact on mechanisms of control and internal procedures because the majority of these procedures and mechanisms currently allow the management to obtain exhaustive and reliable information to present financial and non-financial information in accordance with the IFRS.
- **Financial information expertise**: Company's management ensures that employees receive necessary training related to IFRS, either from an external firm or professional organization.
- **Commercial activities**: Company's management believes that IFRS should not have material impact on the Company's commercial activities.

The next management reports will provide updates on the IFRS plan and on recommend changes, if any.

PERSPECTIVES

The Company competes in an industry characterized by both multinational and regional companies that market low temperature sterilization technologies. The most commonly utilized technologies today use Ethylene Oxide Gas, Hydrogen Peroxide Vapour, Liquid Peroxides and Ozone as their primary sterilizing agent. Low temperature sterilization is performed in three distinct areas within acute care hospitals. These areas include the Central Sterilization Department, Operating Room Sterile Processing areas, and Gastrointestinal (GI) Departments. The Company's primary target market for its first product, the TSO_3 STERIZONE® Sterilization System, is the Central Sterilization Department found in acute care hospitals. This targeted customer group, by nature, is conservative so sales cycles can be long as a result of administrative and budgeting procedures. These customers require a low temperature sterilization process that is efficacious, materials compatible, provides timely throughput, is cost effective in use, safe for users and environmentally responsible. Prior to the introduction of the TSO_3 STERIZONE® Sterilization System, no single competitor or technology had been able to meet all these stated customer requirements. As a result, end-users had to employ multiple products and technologies to meet their sterilization needs. To address this issue, the Company entered the market with a proprietary sterilization process that provided unmatched efficacy, economy and safety.

On March 10, 2009 the Company filed for enhanced claims which, when cleared, will increase the indications for use of the sterilizer offering customers increased product utility further lowering their operating costs. The Company believes that its patented technology can be used to create a number of additional cycles, each having the superior efficacy of the existing product while tuning the cycle to optimize compatibility with today's increasingly delicate diagnostic and surgical instruments. The Company expects that many of these cycles will be configured as part of the current product as well as completely new cycles that address different requirements for different locations in the hospital. As such the Company is focusing on delivering increased value to the central sterile department while developing new equipment focused on the needs of the Operating Room. Longer term the company believes that its technology will prove itself as a viable, efficacious, compatible and cost effective replacement for a significant portion of current sterilization cycles using steam to process surgical instruments.

The Company is currently focused on commercializing its first product within North America and relies on its own sales force, comprised of sales professionals who have extensive experience selling capital equipment to hospitals. The requirements for market entry and prioritization of international markets are ongoing and plans to enter these markets are under development.

RISK FACTORS

Risks related to operating activities

The Company's activities entail certain risks and uncertainties inherent to the industry in which it operates. However, management has implemented a risk-reduction strategy that addresses:

Risks associated with international operations

TSO_3 must carry out the majority of its sales outside of Quebec and Canada, primarily in the United States. The necessity of marketing on an international scale puts the Company in a position of direct competition with firms that possess networks and resources greater than its own. Nothing guarantees that the marketing campaigns implemented by the Company for international markets, alone or with strategic alliances, will be successful. The operations of TSO_3 at an international level could be negatively affected by factors such as Canadian and United States foreign trade policies, investments and taxes, foreign exchange rate controls and fluctuations, political instability and increased payment periods. One or more of these factors could have a significantly negative effect on the financial situation and results of the Company.

TSO3

Compatibility, Biocompatibility and Research and Development Projects

All sterilization processes can affect medical instruments or alter their key properties over a period of time. Taking into consideration the nature of the devices to be sterilized and the oxidative effects on devices in contact with ozone, TSO_3 limits to a minimum the frequency and duration that the devices are exposed to ozone. Nevertheless, oxidization can produce several effects, depending on the material. In order to fully establish the true commercial value of its sterilization process, the Company must demonstrate the compatibility of its technology with a wide range of medical instruments. Even though the tests and studies undertaken to date by TSO_3 have shown that its ozone sterilization process is compatible with the majority of medical instruments currently used in the hospital environment, the Company must maintain ongoing studies in this respect. Conversely, the Company can not guarantee the success of its different research and development projects.

Dependency on key personnel

TSO_3 believes that its success will continue to depend on its ability to attract and retain qualified managers and other key personnel. Losing a key employee could have a major negative impact on TSO_3. The Management expects to review the Succession Plan in 2009 of all senior level management.

Management of Business Growth

Achieving its short-term objectives could launch the Company into a phase of significant and rapid growth and force it to considerably increase its personnel, the number of partners, cash flow and operating capacity.

Intellectual Property and Counterfeiting Risks

The success of the Company is based on its unique technology. TSO_3 relies on a combination of patents, trade secrets, non-disclosure agreements and various contractual provisions in order to protect its technology. Nothing guarantees that these measures will be sufficient to protect any illegal appropriation or infringement of its technology by a third party.

Competition Risks

The Company's products face intense competition. Many of our competitors have greater financial resources and marketing capabilities than our own. TSO_3's competitors and potential competitors may succeed in developing products and processes that are more effective and less expensive to use than any products or processes the Company may develop or licence, or that may render TSO_3's products or processes obsolete. The high level of competition in the sterilization industry could force the Company to reduce the price at which it sells its products or require TSO_3 to spend more time and money to market its products.

Product Liability Issues

In the health sector, lawsuits, often claiming substantial damages, are becoming increasingly common. In particular, in the United States, lawsuits are filed by patients, employees or beneficiaries against healthcare providers, as well as authorities operating and managing hospitals in the private and public sectors. During these proceedings, claimants could allege and blame the non-sterility of certain instruments or defective functioning of products sold, installed or derived from TSO_3's technology. To address the problems associated with such lawsuits, the Company is of the opinion that it has the necessary insurance coverage.

Cash equivalents and temporary investments

The Company is exposed to various risks, including the risks related to holding financial instruments. To manage the risk related to the use of financial instruments contained in the various investments that make up cash equivalents and temporary investments, controls have been implemented, in particular the cash and risk management policy. The measures aim primarily to optimize returns from cash flow while reducing the Company's main risk exposures, which are described below:

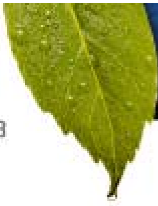
Market risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in the parameters underlying its measurement, particularly interest rates and market prices.

Interest rate risk

Interest rate risk exists when interest rate fluctuations modify the cash flows of the Company's investments.

At December 31, 2008, if the base rate at that date had been 0.5% lower, all other variables held constant, the after-tax loss for the year would have been $25,221 lower, arising mainly as a result of an increase in the fair value of fixed rate financial assets classified as held for trading. If the base rates at that date had been 0.5% higher, all other variables held constant, the after-tax loss for the year would have been $25,044 higher, arising mainly as a result of a decrease in the fair value of fixed rate financial assets classified as held for trading. The net loss therefore has a similar sensitivity to interest rate increases and interest rate decreases because of investments with capped interest rates.



Credit risk

The use of financial instruments can create a credit risk in which there is a risk of financial loss resulting from a counterparty's inability or refusal to fully meet its contractual obligations. The Company's credit risk management policies include the authorization to perform investment transactions with recognized financial institutions, either in bonds, money market funds or guaranteed investment certificates. Therefore, the Company manages credit risk by complying with the established investment policies.

Concentration risk

Concentration risk exists when investments are made with multiple entities that share similar characteristics or when a large investment is made with a single entity. At December 31, 2008, there was no concentration.

Liquidity risk

Liquidity risk represents the possibility of the Company not being able to raise the funds needed to meet financial commitments at the appropriate time and under reasonable conditions. The Company manages this risk by maintaining permanent and sufficient liquidity to meet current and future financial obligations, under both normal and exceptional circumstances. The funding strategies used to manage this risk include turning to capital markets to carry out issues of equity and debt securities. The Company can not guarantee that it will be able to put in place such financing.

Currency risk

The risk related to the exchange rate on financial instruments exists when monetary assets or liabilities are denominated in foreign currencies.

At December 31, 2008, if the Canadian dollar had weakened 10 percent against the US dollar with all other variables held constant, the after-tax loss and other comprehensive loss for the year would have been $13,900 lower. Conversely, if the Canadian dollar had strengthened 10 percent against the US dollar with all other variables held constant, the after-tax loss and comprehensive loss for the year would have been $13,900 higher.

In 2008, 53% of the Company's sales were made in Canadian dollars compared to 29% in 2007.

DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer and the Chief Financial Officer of the Company are responsible for establishing and maintaining the Company's Disclosure Controls and Procedures and the Company's Internal control over financial reporting. As required by Securities Legislation, the Chief Executive Officer and the Chief Financial Officer have evaluated, or caused to be evaluated under their supervision, the controls and procedures regarding information disclosure and have concluded that these controls and procedures are effective.

STATEMENT

This document contains certain prospective statements that reflect the Company's current expectations concerning future activities. These prospective statements include risks and uncertainties. Actual results can differ considerably from the results, as previously described in this report, expected by the Company. Investors are advised to consult the Company's quarterly and annual reports, as well as the filing of the Company's annual information form for more details on the risks and uncertainties related to these prospective statements. The reader must not unduly rely upon the Company's prospective statements. The Company is not obliged to update these prospective statements.

This Management Report has been prepared as of March 12, 2009. Additional information on the Company is available through regular filing of press releases, annual reports, quarterly financial statements and the Annual Information Form on the SEDAR website (www.sedar.com).

Marc Boisjoli, M.Sc.
Vice President, Finances and Chief Financial Officer

March 12, 2009

MANAGEMENT REPORT

RESPONSIBILITY OF THE FINANCIAL STATEMENTS

The financial statements of TSO_3 Inc., which have been approved by the Board of Directors, were prepared by Management in accordance with Canadian Generally Accepted Accounting Principles and contain certain amounts based on best judgment and estimates as their final determination is dependent upon subsequent events. It is the opinion of Management that the accounting policies utilized are appropriate in the circumstances and are adequate to reflect the financial position and the results of operations within reasonable limits of materiality. The financial information presented elsewhere in this annual report is consistent with the information contained in the financial statements.

In order to carry out its responsibilities with regard to the financial statements, Management maintains internal control systems that aim to provide a reasonable degree of certainty that transactions are duly authorized, that the assets are well protected, and that adequate records are kept.

The Board of Directors' Audit and Risk Management Committee, comprised solely of board members who are neither managers nor employees of the Company, ensures that Management assumes its responsibility in terms of financial statements.

The functions of the Audit and Risk Management Committee are to:

- Review the financial statements and recommend them for approval by the Board of Directors;
- Review the systems of internal control and security;
- Recommend the appointment of the external auditors and their fee arrangements to the Board of Directors;
- Review other accounting, financial, and security matters as required.

This committee meets regularly with Management and the external auditors. The latter may, as they see fit, meet with the Audit and Risk Management Committee, with or without Management, to discuss matters affecting the audit and financial information.

The external auditors are appointed to report to the shareholders regarding the fairness of presentation of the Company's financial statements. The auditors fulfil this responsibility by carrying out an independent examination of these statements in accordance with Canadian Generally Accepted Auditing Standards.

On behalf of Management,

Richard M. Rumble
President and CEO

Marc Boisjoli
Vice President, Finances and
Chief Financial Officer

March 12, 2009

![Deloitte.]

FINANCIAL STATEMENTS

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Auditors' Report

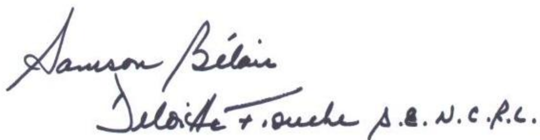
To the Shareholders of TSO_3 Inc.,

We have audited the balance sheets of TSO_3 Inc. as at December 31, 2008 and 2007 and the statements of earnings and comprehensive loss, contributed surplus, deficit 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 financial statements present fairly, in all material respects, the financial position of TSO_3 Inc. as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants



Quebec City, February 23, 2009

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Chartered Accountant auditor permit n° 16162

Statements of Earnings and Comprehensive Loss
Years ended December 31

	2008	2007
SALES	**$ 2,235,101**	$ 1,731,017
EXPENSES		
Operating	**2,776,815**	1,891,668
Marketing	**3,712,592**	4,189,403
Research and development	**2,351,176**	1,782,253
Administrative	**3,960,970**	3,228,206
Financial	**23,099**	17,130
	12,824,652	11,108,660
OPERATING LOSS	**10,589,551**	9,377,643
OTHER INCOME (Note 18)	**955,747**	1,465,153
NET LOSS AND COMPREHENSIVE LOSS	**$ 9,633,804**	$ 7,912,490
Basic and diluted net loss per share (Note 17)	**$0.20**	$0.17

References:

Amortization of property, plant and equipment and intangible assets (Notes 7 and 8)
Interest (Note 12)
Research and development tax credits (Note 15)
Foreign exchange gain (loss) (Note 18)

The accompanying notes are an integral part of these financial statements.

Statements of Contributed Surplus
Years ended December 31

	2008	2007
Balance at beginning	**$ 7,471,369**	$ 4,999,850
Options exercised (Note 10)	**-**	(34,743)
Warrants exercised (Note 10)	**-**	(1,272,733)
Warrants (Note 10)	**-**	2,819,051
Compensation options (Note 10)	**-**	281,520
Stock-based compensation (Note 10)	**429,574**	678,424
Balance at end	**$ 7,900,943**	$ 7,471,369

Statements of Deficit
Years ended December 31

	2008	2007
Balance at beginning	**$ 47,640,464**	$ 37,524,647
Changes in accounting policies (Note 3)	**(34,943)**	(20,216)
Restated deficit	**47,605,521**	37,504,431
Share issue expenses	**-**	1,942,023
Compensation options (Note 10)	**-**	281,520
Net loss	**9,633,804**	7,912,490
Balance at end	**$ 57,239,325**	$ 47,640,464

The accompanying notes are an integral part of these financial statements.

Balance Sheets
as at December 31

	2008	2007
CURRENT ASSETS		
Cash and cash equivalents (Note 4)	**$ 9,186,202**	$ 22,081,727
Temporary investments (Note 4)	**8,692,008**	4,123,447
Accounts receivable (Note 5)	**660,578**	975,011
Inventories (Note 6)	**2,548,075**	2,996,409
Prepaid expenses	**114,848**	139,410
	21,201,711	30,316,004
PROPERTY, PLANT AND EQUIPMENT (Note 7)	**675,810**	471,651
INTANGIBLE ASSETS (Note 8)	**3,642,126**	3,700,296
	$ 25,519,647	$ 34,487,951
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	**$ 1,258,780**	$ 1,300,877
Deferred revenues	**388,958**	145,878
	1,647,738	1,446,755
SHAREHOLDERS' EQUITY		
Share capital (Note 10)	**73,210,291**	73,210,291
Contributed surplus	**7,900,943**	7,471,369
Deficit	**(57,239,325)**	(47,640,464)
	23,871,909	33,041,196
	$ 25,519,647	$ 34,487,951

The accompanying notes are an integral part of these financial statements.

Approved by the Board,

Director

Director

Statements of Cash Flows
Years ended December 31

	2008	2007
OPERATING ACTIVITIES		
Net loss	**$ (9,633,804)**	$ (7,912,490)
Adjustments for:		
Amortization of property, plant and equipment (Note 7)	**154,144**	109,985
Amortization of intangible assets (Note 8)	**285,008**	262,663
Change in the value of temporary investments (Note 18)	**(56,884)**	(122,594)
Stock-based compensation (Note 10)	**429,574**	678,424
Gain on disposal of investments	**(91,722)**	-
Gain on disposal of property, plant and equipment (Note 18)	**(8,124)**	(10,718)
	(8,921,808)	(6,994,730)
Change in non-cash operating working capital items (Note 12)	**1,023,255**	549,123
Cash flows applied to operating activities	**(7,898,553)**	(6,445,607)
INVESTING ACTIVITIES		
Acquisition of temporary investments	**(21,143,577)**	(13,523,110)
Disposal of temporary investments	**16,723,622**	9,542,473
Acquisition of property, plant and equipment	**(356,040)**	(250,158)
Acquisition of intangible assets	**(229,406)**	(192,544)
Disposal of property, plant and equipment	**8,429**	11,175
Cash flows applied to investing activities	**(4,996,972)**	(4,412,164)
FINANCING ACTIVITIES		
Options exercised (Note 10)	**-**	50,764
Warrants exercised (Note 10)	**-**	4,521,975
Share issue expenses	**-**	(1,942,023)
Share issue (Note 10)	**-**	23,000,000
Cash flows from financing activities	**-**	25,630,716
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(12,895,525)**	14,772,945
CASH AND CASH EQUIVALENTS AT BEGINNING	**22,081,727**	7,308,782
CASH AND CASH EQUIVALENTS AT END	**$ 9,186,202**	$ 22,081,727

The accompanying notes are an integral part of these financial statements.

1. Description of business

The Company was incorporated on June 10, 1998 under Part 1A of the *Companies Act* (Québec). Its activities consist of developing and marketing a sterilization process for heat-sensitive medical instruments using ozone as a sterilizing agent.

2. Accounting policies

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) and reflect the following significant accounting policies:

Use of estimates

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Since the financial reporting process requires the use of estimates, actual results could differ from these estimates.

Financial instruments

Financial assets and financial liabilities are initially recognized at fair value and subsequent measurement depends on how they are classified, which is described below. Their classification depends on the purpose for which the financial instruments were acquired or issued, their characteristics, and the designation made by the Company. Settlement date accounting is used.

Classification

Cash and cash equivalents	Held for trading
Temporary investments	Held for trading
Accounts receivable	Loans and receivables
Accounts payable and accrued liabilities	Other liabilities

Temporary investments

Temporary investments are designated as instruments held for trading, effective as of the recognition date. These investments are recorded at fair value. Increases and decreases in fair value are recognized as investment income and presented under “Other revenues” in the Statement of Earnings.

Cash and cash equivalents

Cash and cash equivalents include cash, investments, asset-backed commercial paper secured by financial institutions and by the Canadian government, and money market funds. The Company has classified these instruments as held for trading. These investments are highly liquid and are held for the purpose of meeting short-term cash commitments. They are recorded at fair value. Increases and decreases in fair value are recognized as investment income and presented under "Other revenues" in the Statement of Earnings.

Loans and receivables

Loans and receivables are accounted for at amortized cost using the effective interest method.

Other liabilities

Other liabilities are recorded at amortized cost using the effective interest method and include all financial liabilities other than derivative instruments.

Transaction costs

Transaction costs related to held-for-trading financial assets are expensed as incurred. Transaction costs related to other liabilities and to loans and receivables are added to the carrying value of the asset or are netted against the carrying value of the liability and are then recognized over the expected life of the instrument using the effective interest method.

Effective interest method

The Company uses the effective interest method to recognize interest income or expense, which includes transaction costs as well as the fees, premiums or discounts earned or incurred for financial instruments.

Fair value

The fair value of a financial instrument is equal to the amount at which this instrument could be traded knowingly and willingly between the parties involved. Fair value is based on the published prices (buy/ask prices) in an active market. If this is not the case, fair value is based on the prevailing market prices for instruments with similar risk profiles or characteristics or on internal or external valuation models that use observable market data.

The fair value of cash, accounts receivable, accounts payable and accrued liabilities approximates their carrying values due to the short-term maturities of these items.

Inventories

The cost of inventories is essentially determined using the first in, first out method. The cost of work in progress and finished goods comprises the cost of raw materials and an applicable share of the cost of labour and manufacturing overhead based on normal production capacity. Inventories are valued at the lower of cost and net realizable value.

When an impairment is recognized, a new assessment of net realizable value is performed in each subsequent period. When the circumstances that justified writing down the inventories below cost no longer exist, or when there is a clear indication of an increase in net realizable value due to a change in the economic situation, the amount of the write-down is reversed such that the new carrying amount is the lower of the cost or the revised net realizable value.

Property, plant and equipment

Property, plant and equipment are recorded at cost. Amortization is calculated using the declining balance method except for leasehold improvements, which are amortized using the straight-line method at the following annual rates or useful life:

Office furniture, stand, equipment and tools	*20%*
Computer equipment and lift truck	*30%*
Leasehold improvements	*Lease term*

Intangible assets

Intangible assets consist of the acquisition cost of a patent licence, the acquisition cost of a technology and all the related rights, the cost of patents, the costs of trademarks, software and the website.

Amortization of intangible assets is calculated using the straight-line method over their estimated useful lives, as follows:

Patents	*20 years*
Licence	*16 years*
Software and website	*3 years*
Trademarks	*10 and 15 years*

Technology is amortized using the straight-line method over an estimated useful life of 20 years.

Impairment of long-lived assets

Long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognized when their carrying value exceeds the total undiscounted cash flows expected from their use and eventual disposition. The amount of the impairment loss is determined as the excess of the carrying value of the asset over its fair value.

Foreign currency translation

Foreign currency transactions are translated into Canadian dollars as follows: monetary assets and liabilities are translated at the exchange rates in effect at the balance sheet date, and revenues and expenses are translated at the exchange rates in effect at the time of the transaction. Non-monetary assets and liabilities are translated at historical rates. Exchange gains or losses resulting from translation are carried to earnings under the item "Other revenues."

Government assistance and research and development tax credits

Government assistance is recorded in the financial statements when there is reasonable assurance that the Company has complied with, and will continue to comply with, all of the conditions necessary to obtain the assistance.

The Company incurs research and development expenses that are eligible for tax credits. The recorded tax credits are based on management's estimates of amounts expected to be recovered and are subject to audit by taxation authorities.

Government assistance, including the tax credits for scientific research and experimental development costs, is presented in "Other revenues."

Income taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income taxes are recognized based on the expected future tax consequences of differences between the carrying amount of balance sheet items and their corresponding tax basis, using the enacted and substantively enacted income tax rates for the years in which the differences are expected to reverse. Future income tax assets are recognized in earnings only if their realization is considered more likely than not.

Revenue recognition

The Company generates revenue mainly from the sale of ozone sterilization units, parts, supplies and accessories related to these units, and service and maintenance contracts for the units. The Company is generally committed under revenue arrangements with multiple deliverables that include delivery of units, installation, maintenance, customer service and consulting services. The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the price to the buyer is fixed or determinable and collection is reasonably assured.

Revenue from revenue arrangements with multiple deliverables are divided into separate units of accounting when the Company has reliable evidence. Revenue related to service contracts offered to clients is deferred and recognized using the straight-line method over the term of the contract.

Revenue earned on the units sold, the parts and accessories related to these units, and the installation and consulting services are recognized upon delivery of the service and the client's acceptance of the services received. Maintenance and service contracts are recognized using the straight-line method over the term of the contract.

Provision for warranties

The Company offers a standard 12-month warranty to its clients. Warranty income is deferred and recognized on a straight-line basis over a 12-month period. The estimated cost of the warranty is based on the following: the Company's history with defective ozone sterilization units and the parts and accessories for these units; the probability that these defects will arise; and the costs to repair them.

Stock-based compensation

The Company uses the fair value method to measure compensation expense at the date of grant of stock options to employees. Fair value is determined using the Black-Scholes option pricing model and is amortized to earnings over the vesting period with an offset to contributed surplus. When options are exercised, the corresponding contributed surplus and the proceeds received by the Company are credited to share capital.

3. Changes in accounting policies

Accounting changes

On January 1, 2008, the Company adopted the new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA): Section 1535, "Capital Disclosures," Section 3031, "Inventories," Section 3862, "Financial Instruments – Disclosures," and Section 3863, "Financial Instruments – Presentation." These new standards were applied without restatement of comparative financial statements.

a) Capital disclosures

Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. An entity must disclose information about the objectives, policies and procedures for managing capital, quantitative data about what the Company regards as capital, whether the Company has complied with capital requirements and the consequences of non-compliance with such capital requirements.

Since this standard came into effect, the Company has been presenting relevant information related to its capital management in Note 11 "Capital management."

b) Inventories

Section 3031 replaces Section 3030, "Inventories." It indicates that inventories are valued at the lower of cost and realizable value. It provides guidance on determining cost and requires previous write-downs to be reversed when the value of inventories increases.

Since this standard came into effect, the Company has been recognizing raw materials inventories according to the lower of cost and net realizable value. In the past, the Company recorded raw materials inventories according to the lower of cost and replacement cost.

c) Financial instruments

Sections 3862 and 3863 have replaced Section 3861, "Financial Instruments – Disclosure and Presentation." They place heightened importance on disclosure, enabling financial statement users to assess the nature and extent of the risks associated with the financial instruments to which the Company is exposed and the manner in which it manages these risks. Information on risk is presented in Note 4 "Financial instruments."

Accounting changes from the previous year

On January 1, 2007, the Company adopted the CICA's new financial instrument accounting standards (Section 3855): Section 3251, "Equity," Section 3861, "Financial Instruments – Disclosure and Presentation," and Section 1530, "Other Comprehensive Income." Figures from periods prior to January 1, 2007 have not been restated.

Impact of adopting the new accounting standards

On January 1, 2008 and 2007, the Company made the following adjustments to its balance sheet in order to comply with the new accounting standards:

	2008	2007
Increase (decrease)		
Balance sheet		
Temporary investments	**$ -**	$ 20,216
Inventories	**34,943**	-
Statement of deficit		
Accounting changes	**$(34,943)**	$(20,216)

Future accounting changes

In February 2008, the CICA issued a new Section 3064, "Goodwill and Intangible Assets" which will replace Section 3062 "Goodwill and Other Intangible Assets" as well as Section 3450 "Research and Development Costs." The new Section 3064 states that upon initial identification, intangible assets are to be recognized as assets only if they meet the definition of an intangible asset and the asset recognition criteria. Section 3064 also provides further information on the recognition of internally generated intangible assets (including research and development costs). As for subsequent measurement of intangible assets, goodwill and disclosure, Section 3064 essentially carries forward unchanged the recommendations of former Section 3062. This section will apply to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2009. Management is currently evaluating the impact of this new section on its financial statements.

Section 1400, "General Standards of Financial Statement Presentation," will apply to interim periods beginning on or after January 1, 2009. This section sets out the conditions for assessing and presenting the Company's ability to continue as a going concern. The adoption of this new section will not have a significant impact on the Company's financial statements.

In February 2008, the Canadian Accounting Standards Board confirmed that publicly accountable enterprises would be required to adopt International Financial Reporting Standards (IFRS) when preparing financial statements for years beginning on or after January 1, 2011. The Company will therefore be required to transition to IFRS for its interim and annual financial statements beginning on or after January 1, 2011 and provide a restated comparative statement in accordance with IFRS. As of the year ended December 31, 2008, the Company had developed an IFRS conversion plan allowing it to evaluate the impact of IFRS on its financial statements.

4. Financial instruments

Cash equivalents and temporary investments

	2008	2007
Commercial paper and various bonds, maturing at various dates through July 2009 and having an average yield of 3.9%	**$12,060,599**	$4,623,057
Money market funds and fixed income securities	**1,918,236**	20,772,886
	$13,978,835	$25,395,943
Distributed as follows:		
Cash equivalents	**$5,286,827**	$21,272,496
Temporary investments	**8,692,008**	4,123,447
	$13,978,835	$25,395,943

Cash equivalents are presented on the balance sheet under line item "Cash and cash equivalents". This item consists of $3,899,375 in cash ($809,231 in 2007) and $5,286,827 ($21,272,496 in 2007) in cash equivalents, for a total amount of $9,186,202 ($22,081,727 in 2007).

The Company is exposed to various risks, including the risks related to holding financial instruments. To manage the risk related to the use of financial instruments contained in the various investments that make up cash equivalents and temporary investments, controls have been implemented, in particular the cash and risk management policy. The measures aim primarily to optimize returns from cash flow while reducing the Company's main risk exposures, which are described below.

Market risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in the parameters underlying its measurement, particularly interest rates and market prices.

Interest rate risk

Interest rate risk exists when interest rate fluctuations modify the cash flows of the Company's investments.

At December 31, 2008, if the base rate at that date had been 0.5% lower, all other variables held constant, the after-tax loss for the year would have been $25,221 lower, arising mainly as a result of an increase in the fair value of fixed rate financial assets classified as held for trading. If the base rates at that date had been 0.5% higher, all other variables held constant, the after-tax loss for the year would have been $25,044 higher, arising mainly as a result of a decrease in the fair value of fixed rate financial assets classified as held for trading. The net loss therefore has a similar sensitivity to interest rate increases and interest rate decreases because of investments with capped interest rates.

Credit risk

The use of financial instruments can create a credit risk in which there is a risk of financial loss resulting from a counterparty's inability or refusal to fully meet its contractual obligations. The Company's credit risk management policies include the authorization to perform investment transactions with recognized financial institutions, either in bonds, money market funds or guaranteed investment certificates. Therefore, the Company manages credit risk by complying with its established investment policies.

Concentration risk

Concentration risk exists when investments are made with multiple entities that share similar characteristics or when a large investment is made with a single entity. At December 31, 2008, there was no concentration.

Liquidity risk

Liquidity risk represents the possibility of the Company not being able to raise the funds needed to meet financial commitments at the appropriate time and under reasonable conditions. The Company manages this risk by maintaining permanent and sufficient liquidity to meet current and future financial obligations, under both normal and exceptional circumstances. The funding strategies used to manage this risk include turning to capital markets to carry out issues of equity and debt securities.

Currency risk

The risk related to the exchange rate on financial instruments exists when monetary assets or liabilities are denominated in foreign currencies.

At December 31, 2008, if the Canadian dollar had weakened 10 percent against the US dollar with all other variables held constant, the after-tax loss and other comprehensive loss for the year would have been $13,900 lower. Conversely, if the Canadian dollar had strengthened 10 percent against the US dollar with all other variables held constant, the after-tax loss and comprehensive loss for the year would have been $13,900 higher.

In 2008, 53% of the Company's sales were made in Canadian dollars compared to 29% in 2007.

5. Accounts receivable

	2008	2007
Accounts receivable	**$ 319,806**	$ 647,104
Tax credits receivable	**285,052**	269,000
Other	**55,720**	58,907
	$ 660,578	$ 975,011

6. Inventories

	2008	2007
Raw materials	**$1,013,681**	$1,015,204
Work in progress	**61,952**	437,945
Finished goods and goods on consignment	**1,472,442**	1,543,260
	$2,548,075	$2,996,409

Operating expenses include a cost of inventory charge of $1,222,474, including a write-down of $298,970.

7. Property, plant and equipment

	Cost	Accumulated amortization	Net book value 2008	Net book value 2007
Equipment and tools	$ 787,588	$ 428,703	$ 358,885	$ 301,993
Computer equipment	483,363	322,426	160,937	116,812
Office furniture	185,970	84,987	100,983	39,784
Lift truck	14,115	12,703	1,412	2,016
Stand	18,259	10,905	7,354	9,192
Leasehold improvements	228,378	182,139	46,239	1,854
	$ 1,717,673	$ 1,041,863	$ 675,810	$ 471,651

Amortization of property, plant and equipment for the year totalled $154,144 ($109,985 in 2007).

8. Intangible assets

	Cost	Accumulated amortization	Net book value 2008	Net book value 2007
Technology	$ 2,978,874	$ 595,775	$ 2,383,099	$ 2,532,043
Licence	991,063	309,707	681,356	743,297
Patents	438,716	50,861	387,855	358,547
Trademarks	35,276	4,629	30,647	29,942
Software	472,410	313,241	159,169	33,901
Website	44,077	44,077	-	2,566
	$ 4,960,416	$ 1,318,290	$ 3,642,126	$ 3,700,296

Amortization of intangible assets for the year totalled $285,008 ($262,663 in 2007).

9. Credit facilities

The Company has a line of credit with which it can obtain advances up to a maximum of $350,000. This line of credit, which is renewable on an annual basis, bears interest at prime rate plus 1%. The Company's accounts receivable and inventories are pledged as security on this line of credit, and the Company must comply with certain financial ratios usually found in this type of loan. This line of credit was undrawn as at December 31, 2008.

10. Share capital

Authorized

An unlimited number of shares

Common, voting, participating, without par value

Class A, voting, participating, with a par value of $1.00 each

Class B, voting, participating, without par value

	2008		2007	
Issued and paid	**Number**		Number	
Balance at beginning	**47,863,402**	**$ 73,210,291**	36,800,853	$ 47,149,127
New issue	**-**	**-**	9,200,000	20,180,949
Options exercised	**-**	**-**	27,999	85,507
Warrants exercised	**-**	**-**	1,834,550	5,794,708
Balance at end	**47,863,402**	**$ 73,210,291**	47,863,402	$ 73,210,291

In 2008, no options or warrants were exercised. In 2007, holders exercised certain options and warrants; they subscribed for 1,862,549 shares for a total cash consideration received of $4,572,739.

On March 8, 2007, the Company completed a private financing of $23,000,000 through the issue of 9,200,000 units distributed as follows: $20,180,949 for 9,200,000 shares and $2,819,051 for 4,600,000 warrants. Each unit consisted of one common share and a half-warrant, with the warrant allowing for the purchase of one common share at a price of $3.00 until March 8, 2009.

The proceeds from this issuance of units was divided proportionally between share capital and contributed surplus according to the respective fair values of the shares and the warrants issued.

Stock-based compensation and other stock-based payments

a) Employee stock purchasing plan

On May 2, 2007, the Company set up an employee stock purchasing plan for employees and executives. Eligible participants may contribute, in the form of payroll deductions, up to 5% of their basic salary. The Company contributes an amount equal to 50% of the participant's total monthly contribution.

Every month the participant and Company contributions are remitted to a brokerage firm that uses the entire balance of the contributions to purchase, on the open market and on the last day of the month, shares to the nearest whole number.

b) Stock option plan

The Company's Board of Directors adopted a stock option plan solely for directors, executives, employees and service providers of the Company, which was approved by its shareholders. The total number of common shares from the Company's share capital that can be issued under this plan is 4,553,573. The total number of common shares reserved for the exercise of stock options in favour of a holder cannot, at any time, represent more than 5% of the Company's common shares issued and outstanding at the time of granting less the total number of options already exercised by this person from any other stock options. The options granted pursuant to this plan, which vest over a three-year period, may be exercised within a maximum of 10 years of the grant date.

During 2008, the Company awarded 2,116,224 stock options to its employees, directors and suppliers at a weighted average exercise price of $0.51. The weighted average fair value of these stock options was $0.27 per option.

The stock-based compensation expense pertaining to the options granted has been amortized using the graded vesting method, giving rise to a stock-based compensation expense of $429,574 in 2008 ($678,424 in 2007) presented in "Administrative expenses." Stock options granted from 2004 to 2008 will also involve additional compensation expenses of $234,626 in 2009, $113,101 in 2010, and $48,334 in 2011, and $17,167 in 2012.

The fair value of the stock options granted in 2008 is estimated using the Black-Scholes option pricing model under the following weighted average assumptions:

Risk free interest rate	*3.48%*
Expected volatility	*62%*
Life	*9.4 years*
Expected dividend yield	0%

*The weighted average fair value of the stock options granted was $0.27 per option.

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable, a practice significantly different from how stock options are granted by the Company. In addition, option pricing models require highly subjective valuations and include the expected stock price volatility of the underlying shares. Any changes in the assumptions can materially affect the fair value estimates.

The following table summarizes the stock option activity:

	2008		2007	
	Number	**Weighted average exercise price**	Number	Weighted average exercise price
Outstanding at beginning	**2,494,430**	**$ 2.18**	2,292,066	$ 2.16
Granted	**2,116,224**	**0.51**	282,523	2.44
Exercised	**-**	**-**	(27,999)	1.81
Forfeited	**(384,868)**	**2.37**	(52,160)	2.47
Outstanding at end	**4,225,786**	**$ 1.33**	2,494,430	$ 2.18
Exercisable at end	**2,077,624**	**$ 1.98**	1,843,698	$ 2.02

The following table summarizes certain information regarding the stock options of the Company as at December 31, 2008:

	Outstanding options		Exercisable options	
Exercise price	Number	Average remaining contractual life (years)	Number	Average remaining contractual life (years)
$0.24 to $1.85	3,462,370	6.71	1,599,870	3.12
$2.16 to $2.99	463,571	7.78	240,857	6.98
$3.10 to $3.45	299,845	6.34	236,897	6.10
	4,225,786	6.80	2,077,624	3.91

c) Warrants and compensation options

Upon the issuance of 9,200,000 units on March 8, 2007, 4,600,000 warrants were granted. Each warrant can be used to purchase one common share of the Company at a price of $3.00 through March 8, 2009.

Also, as additional consideration for the issuance of these units, the Company granted 460,000 compensation options to the underwriters valued at $281,520. Each compensation option can be used to subscribe to one common share of the Company at a price of $2.50 each through September 8, 2008.

The fair value of the warrants, on the grant date in 2007, is estimated using the Black-Scholes option pricing model under the following weighted average assumptions:

Risk-free interest rate	*3.98*	*%*
Expected volatility	*53.6*	*%*
Life	*1.9*	*years*
Expected dividend yield	*0*	*%*

* The weighted average fair value of the warrants granted was $0.71 per warrant.

Warrants and compensation options varied as follows:

	2 0 0 8		2 0 0 7	
	Number	**Weighted average exercise price**	Number	Weighted average exercise price
Outstanding at beginning	**5,060,000**	**$ 2.95**	2,621,100	$ 2.48
Granted	**-**	**-**	5,060,000	2.95
Exercised	**-**	**-**	(1,834,550)	2.46
Expired	**(460,000)**	**2.50**	(786,550)	2.50
Outstanding at end	**4,600,000**	**$ 3.00**	5,060,000	$ 2.95
Exercisable at end	**4,600,000**	**$ 3.00**	5,060,000	$ 2.95

The following table summarizes certain information regarding warrants and compensation options as at December 31, 2008:

	Outstanding warrants and compensation options		**Exercisable warrants and compensation options**	
		Average remaining contractual life		**Average remaining contractual life**
Exercise price	**Number**	**(years)**	**Number**	**(years)**
$3.00	4,600,000	0.18	4,600,000	0.18
	4,600,000	0.18	4,600,000	0.18

11. Capital management

The Company needs capital primarily to finance its research and development activity, its operating, administrative and marketing expenses, its working capital and its capital expenditures. In the past, the Company has financed its activities through various rounds of public and private financing as well as through government grants.

Depending on its capacities and prevailing market conditions, the Company could finance all or a portion of its long-term assets through long-term debt.

The monthly burn rate was approximately $707,000 at December 31, 2008 ($572,000 at December 31, 2007). The Company attributes this increase primarily to non-recurring reorganization expenses.

The Company has a line of credit that it can use to obtain advances up to a maximum of $350,000. To maintain this credit line, the Company must comply with two financial ratios: the working capital ratio and the net worth ratio. Although the credit line has not been drawn, the Company reviews these ratios every month. At December 31, 2008, the Company was in compliance with these ratios.

The Company reviews its loss-per-share ratio quarterly. Its goal is to improve this ratio.

12. Additional information relating to the statements of cash flows

	2 0 0 8	2 0 0 7
Change in non-cash operating working capital items		
Decrease (increase) in current assets		
Accounts receivable	**$ 330,485**	$ (191,892)
Tax credits receivable	**(16,052)**	28,000
Inventories[1]	**483,277**	391,428
Prepaid expenses	**24,562**	(5,759)
Increase (decrease) in current liabilities		
Accounts payable and accrued liabilities	**(42,097)**	257,177
Deferred revenues	**243,080**	70,169
	$ 1,023,255	$ 549,123
Interest		
Received	**$ 89,127**	$ 173,769
Research and development tax credits		
Received	**$ 283,817**	$ 324,811

(1) *Non-cash item*

To reflect the accounting change impact of presenting inventories at realizable value, i.e., an impact of $34,943, the Company adjusted the retained earnings and inventories balances at the beginning of 2008 (Note 3).

13. Related party transactions

During the year, the Company carried out the following transactions, measured at the exchange amount, with a company held by certain shareholders of the Company:

	2 0 0 8	2007
Rent	**$ 61,561**	$ 59,365
Other rent-related expenses	**71,138**	67,069
	$ 132,699	$ 126,434

At December 31, 2008, no amount was included in accounts payable with respect to the related party ($3,897 in 2007).

14. Income taxes

For tax purposes, the operations of each year result in a loss that can be applied against future taxable income.

As at December 31, 2008, the accumulated tax losses that can be carried forward are as follows:

Expiry	Loss carry-forwards	
date	Federal	Provincial
2028	$8,053,000	$8,042,000
2027	6,898,000	6,413,000
2026	5,885,000	5,820,000
2015	5,009,000	4,961,000
2014	4,601,000	4,591,000
2010	4,188,000	4,128,000
2009	2,793,000	2,610,000
	$37,427,000	$36,565,000

As at December 31, 2008, in addition to these tax losses carried forward, the Company has unclaimed research and development expenses ($7,831,000 at the federal level and $10,912,000 at the provincial level) and $1,450,000 in financing costs that can be carried forward to reduce future taxable income. The unrealized tax benefit, estimated at $12,829,000, and related to these losses carried forward and unclaimed expenses, has not been recorded.

With respect to property, plant and equipment, the Company has a future income tax asset related to the tax cost that is higher than the net book value of these capital assets, estimated at $626,000, which has not been recorded.

In addition, as at December 31, 2008, the Company has $1,894,000 in additional tax credits, representing the outstanding and unrecorded portion of the federal tax credit receivable.

Furthermore, the cost of intangible assets for tax purposes was $605,000 (net book value of $3,843,000) resulting from the Company taking advantage of provisions in the federal and provincial income tax laws with respect to rollovers. Future income taxes estimated at $541,000 and resulting from the difference between the carrying value and the tax value of intangible assets have not been recorded.

Future income tax assets related to tax losses and unclaimed expenses will be recorded in the financial statements, resulting in an increase in earnings and shareholders' equity, once the Company concludes that these losses likely will be realized. At the same time, the future income tax liability related to the cost of the intangible assets for tax purposes will be recorded, and the amount of intangible assets will be increased accordingly.

15. Research and development tax credits

For tax credit purposes, research and development expenses incurred during the year totalled $1,210,237 ($1,217,670 in 2007); of these research and development expenses, an amount of $51,325 as at December 31, 2008 ($195,297 in 2007) is related to property, plant and equipment.

Some of these expenses qualify for refundable scientific research tax credits amounting to $270,000 as at December 31, 2008.

The tax credit received for the year ended December 31, 2007 has not been reviewed by the tax authorities. Consequently, the amount of tax credits that will be awarded could differ from the one already recorded.

16. Segmented information

Operating revenues according to geographic region are as follows:

	2008	2007
Canada	**$1,192,921**	$502,017
United States	**1,042,180**	1,229,000
	$2,235,101	$1,731,017

Operating revenues are assigned to geographic area based on the location of the client.

17. Earnings per share

The following table reconciles the basic and the diluted earnings per share:

	2008	2007
Net loss		
Basic and diluted	**$ 9,633,804**	$ 7,912,490
Number of shares		
Weighted average number of outstanding shares[1]	**47,863,402**	45,321,048
Loss per share		
Basic	**$ 0.20**	$ 0.17
Diluted[1]	**$ 0.20**	$ 0.17

[1] The weighted average number of outstanding shares is calculated using the number of common shares according to a weighted average based on the fraction of the period during which they were outstanding.

The weighted average number of outstanding shares remains unchanged for the calculation of the diluted loss per share given that the inclusion of potential common shares in computing the diluted earnings (loss) per share still had an anti-dilutive effect.

18. Other revenues

	2008	2007
Investment income	**$ 89,128**	$ 173,769
Change in the value of investments held as cash and cash equivalents	**427,500**	658,374
Change in the value of temporary investments	**56,884**	122,594
Research and development tax credits	**252,465**	296,811
Foreign exchange gain (loss)	**24,609**	(57,991)
Gain on disposal of investments	**91,722**	-
Gain on disposal of property, plant and equipment	**8,124**	10,718
Grants	**3,955**	256,861
Other	**1,360**	4,017
	$955,747	$ 1,465,153

19. Commitments and guarantees

Under its operating leases and service contracts, the Company is committed to pay $122,548 in 2009, $68,483 in 2010, $20,130 in 2011, $14,640 in 2012 and $1,220 in 2013.

The Company is committed under a research contract to pay a total amount of $127,440 (75,000 €). At December 31, 2008, an amount of $108,324 (63,750 €) had been paid. The Company expects to make a payment of $19,116 (11,250 €) during 2009.

20. Comparative figures

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

DIRECTORS

Richard M. Rumble
President and Chief Executive Officer
TSO_3 Inc.

Simon Robitaille
Vice President, Operations / R&D,
Chief Scientific Officer and Co-Founder
TSO_3 Inc.

Christian Bélisle
Vice President Finance
Targanta Therapeutics

André Boulanger
Engineer
Project Manager

Germain Carrière
President and Chief Operating Officer
Desjardins Securities

André de Villers
President
CEMA

Pierre Désy
Corporate Director

Serge Lapointe
Investment Director
Fonds de solidarité FTQ

Jacques Marcotte
President
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Corporate Solicitors
Lavery, de Billy, LLP

Bank
National Bank of Canada

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Thursday, April 30, 2009 at 9:30 a.m.
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ACKNOWLEDGEMENTS

Each year, TSO_3's accomplishments and progress are due to the contribution of a diversity of talents and expertise, in particular from its employees whose dedication has never failed over the years. Thank you very much to everyone for the indispensable contribution that you have made to the Company and its development.

TSO_3 would like to extend a special thanks to Mr. Jocelyn Vézina, TSO_3's co-founder, who in 2008 left his positions as the Company's President and Chief Executive Officer and as a member of the Board. With his vision, energy and determination, Mr. Vézina played a major role in TSO_3's history, enabling the original project to develop into a structured, innovative and promising Company. He did this while working closely with fellow co-founder Mr. Simon Robitaille and all the Company's employees.

TSO_3 also wishes to underline the work of Mr. W. Barry McDonald who, for several months during 2008, held the position of Interim President and Chief Executive Officer following Mr. Vézina's departure. Mr. McDonald quickly brought new momentum to the Company during which, the Board of Directors recruited Mr. Richard M. Rumble, the new permanent President and Chief Executive Officer.

Finally, we would like to express our gratitude to all the Company's shareholders for their support and confidence during the last year.

Germain Carrière
Chairman of the Board

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Ticker Symbol: **TOS (TSX)**

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