

## **Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following information should be read in conjunction with the unaudited interim consolidated financial statements of Ambrilia Biopharma Inc. ("Ambrilia" or the "Company") for the period ended March 31, 2009 and related notes included therein, together with the Company's audited consolidated financial statements for the year ended December 31, 2008 and the related notes, which are prepared in accordance with Canadian generally accepted accounting principles. All amounts shown are stated in Canadian dollars unless otherwise noted. This review was prepared by management from information available to May 1, 2009. Additional information relating to the Company, including the Company's Annual Information Form, can be found on SEDAR at [www.sedar.com](http://www.sedar.com).

### **FORWARD-LOOKING STATEMENTS**

Except for the historical information, matters discussed in this Management's Discussion and Analysis of Financial Condition and Results of Operations of Ambrilia Biopharma Inc. ("Ambrilia") may constitute forward-looking statements that are subject to certain risks and uncertainties that could cause actual results to differ materially from any future results, performance or achievements expressed or implied by such statements. Statements that are not historical facts, including statements preceded by, followed by, or that include words such as "believes", "anticipates", "intends", "plans", "expects", "estimates", "should" or the negative of these words or variations of them or similar terminology may constitute forward-looking statements. There is a significant risk that predictions and other forward-looking statements will not prove to be accurate. Readers are cautioned not to place undue reliance on these forward-looking statements, as they involve risks and uncertainties, which could make actual results differ materially from those currently anticipated. Such risks and uncertainties include the risks disclosed in "Risk Factors" and the effect of misjudgments in the course of preparing forward-looking statements. Such statements are also based on various assumptions, including the successful and timely completion of clinical studies on Ambrilia's products demonstrating efficacy and safety for human use, their successful commercialization within the forecasted timelines and the attainment of the forecasted milestone payments and other revenues. While Ambrilia anticipates that subsequent events and developments may cause Ambrilia's views to change, Ambrilia specifically disclaims any obligation to update these forward-looking statements, unless obliged to do so by applicable securities legislation.

### **OVERVIEW AND OUTLOOK**

Ambrilia Biopharma Inc. ("Ambrilia" or "the Company") is a publicly-traded (TSX:AMB) biotechnology company engaged in the discovery and development of small molecules and peptides to treat infectious diseases and cancer.

As at March 31, 2009, there was substantial doubt as to the Company's ability to continue as a going concern without having access to additional financial resources. (See "Risk Factors" – "Going Concern Uncertainty").

Ambrilia's pipeline includes: C2L octreotide, a proprietary improved and prolonged release formulation of an existing drug to treat acromegaly; a new 3-month release formulation as well as a new 1-month release formulation of goserelin to treat hormone-sensitive prostate cancer; PCK3145, a therapeutic non-toxic peptide for the treatment of hormone-resistant prostate cancer; NGR-Delivery Technology (previously referred to as the TVT Technology), a targeted delivery technology for cancer. Ambrilia also has a novel biomarker for the diagnostic and prognostic of prostate cancer, PSP. The antiviral pipeline is comprised of HIV protease, integrase and entry inhibitors, HCV inhibitors and anti-influenza compounds. On September 29, 2008, Ambrilia announced cost-cutting actions which resulted in a hold on its antiviral research and development activities.

## **Octreotide**

Study 303 involves clinical centers in both Europe and the USA and is proceeding as planned. It is designed to evaluate the 30mg, 20mg and 10mg dosage forms of Ambrilia's octreotide acetate (C2L) in acromegalic patients.

Top line results of Study 302, an open label extension of Study 301 in which all patients were administered C2L, were previously announced. Analysis following the 24-week extension treatment period provided longer term safety data (up to one year on C2L) as well as supportive efficacy data. A decision was recently taken not to collect further data in this group of patients.

The Company depends on its commercial partners to file for marketing authorization. The C2L clinical development program continues to progress and the Company expects some regulatory filings to be initiated during 2009. Ambrilia aims at extracting the maximum value from this asset during 2009.

## **Goserelin**

Ambrilia announced last year that it had initiated a clinical program of its 3-month depot formulation of Goserelin in prostate cancer patients. In parallel, the Company has succeeded in developing a 1-month formulation of Goserelin, intended for the treatment of prostate cancer and several gynaecological indications.

## **Non-core programs**

In December 2008, the Company entered into a 9-month exclusive license option agreement with ZBx Corporation granting ZBx the worldwide rights to develop, manufacture and commercialize the PSP94 technology. At any time during this evaluation period, ZBx is entitled to exercise its option, upon which Ambrilia would be eligible to receive up to a total of US\$ 3.62 million with the achievement of development and commercialization milestones, plus royalties on sales as well as a percentage share from any sublicenses. ZBx is covering all costs associated with the evaluation period and will cover future costs associated with the further development, manufacturing and commercialization if it exercises its option.

PCK3145 is a non-toxic therapeutic peptide for the treatment of advanced metastatic prostate cancer. The mechanism of action suggests that PCK3145 exhibits both anti-metastatic and anti-angiogenic properties. A favorable safety profile and clinically relevant benefits primarily in terms of disease stabilization were observed in several patients. Discussions are being held with potential partners to divest this technology.

NGR- Directed Delivery platform is Ambrilia's means to specifically deliver a therapeutic drug to tumours. The first proof-of-concept was demonstrated with a cytotoxic agent in both in-vitro and in-vivo animal models. Discussions are being held with potential partners to divest this technology.

## **Anti-virals**

Ambrilia's virology research programs have been put on hold, while the Company implements its divestment strategy.

Ambrilia's antiviral portfolio is comprised of small molecules and peptides with activity against HIV integrase, HIV entry, HCV polymerase and HCV entry. In addition, Ambrilia has an early stage program targeting Influenza A.

On December 30, 2008, Ambrilia announced that it had submitted a Request for Arbitration with the International Chamber of Commerce (ICC) to resolve disputes, controversies and claims related to a November 14, 2003 Confidentiality Agreement and an October 12, 2006 Exclusive License Agreement between Ambrilia and Merck & Co., Inc. and Merck Sharpe & Dohme Research Ltd (collectively, "Merck") respectively and certain Ambrilia patent and other rights. Following many attempts at resolution with Merck, Ambrilia came to the conclusion that seeking arbitration was the most efficient way to reach a prompt resolution to the situation.

## **Acquisitions and Divestitures**

At the end of 2008, the Board of Directors approved a strategic review that could have a significant impact on the level of future losses. This review explores all strategic options available to the Company to protect and enhance shareholder value, including the divestment or licensing of the Company's technologies, strategic partnership transactions and the sale or merger of the Company. The Board of Directors has established a committee of independent directors to consider and analyze all possible options. There can be no assurance that the review will result in any specific strategic or financial transactions and no timetable has been set for its completion.

## **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. The reported amounts and note disclosures in the consolidated financial statements are determined using management's best estimates based on assumptions that reflect the most probable set of economic conditions and planned courses of action. Actual results, however, may differ from the estimates used in the consolidated financial statements and such differences could be material. Details of our critical accounting estimates were reported in the Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2008 and these continue to apply for the three months ended March 31, 2009.

## **RESULTS OF OPERATIONS**

### **Quarter ended March 31, 2009 compared with the Quarter ended March 31, 2008**

The Company incurred a net loss of \$5,391,691 or \$0.11 per common share for the first quarter of 2009, compared with a net loss of \$7,305,950 or \$0.15 per common share for the same quarter last year. The prior period results were restated to reflect the retrospective application of a new accounting standard relating to goodwill and intangible assets which came into effect on January 1, 2009.

### **Revenues**

Revenues for the first quarter of 2009 were \$18,739, compared with \$260,490 in the corresponding quarter last year. The lower revenues resulted primarily from the reduced level of interest on available cash and short-term investments, due to a combination of lower cash and short-term investments on hand and lower interest rates.

### **Research and Development Expenses**

Research and development expenses amounted to \$2,101,611 in the first quarter of 2009, compared with \$3,098,438 in the same quarter last year. The decrease of \$996,827 resulted primarily from reduced expenditures on the non-core technologies, as well as on goserelin and peptide research, partially offset by higher expenditures on C2L octreotide. Research and development tax credits declined to \$48,000 in the current quarter from \$293,823 in the corresponding quarter last year. The decrease in the current quarter reflects the lower level of spending in Canada and the closure of the Company's operations in France.

Our research and development expenses consist primarily of salaries and related personnel costs, fees paid to external service providers, laboratory supplies and costs for leasing of facilities. In the first quarter of 2009, fees paid to external service providers were primarily related to clinical development of C2L octreotide.

We expect our future research and development expenses to continue to be significant as we continue with the clinical development of C2L and Goserelin. However, the Company is presently reviewing strategic alternatives, including the divestment, strategic partnership transactions or licensing of the company's technologies and the sale or merger of the Company. The result of this review could impact the level of future R&D activities.

In relation to major projects underway at March 31, 2009 discussed in the “Overview and outlook” section, for C2L octreotide, an open-label multicenter study evaluating the safety and efficacy of the 10, 20 and 30 mg doses in acromegaly (Study 303) is ongoing. Spending for clinical development of C2L in the first quarter of 2009 amounted to approximately \$ 1.6 million. For Goserelin, costs incurred in the first quarter of 2009 amounted to approximately \$0.1 million.

The above amounts do not include related salary costs and are expenses expected in a context of a going concern. The projected level of research and development expenditures could be reduced, depending on the outcome of the various projects, the financial situation of the Company and the decisions taken following the strategic review of possible options for the Company.

### **General and Administrative Expenses**

General and administrative expenses amounted to \$1,156,875 in the first quarter of 2009, a decrease of \$549,694 over the total of \$1,706,569 for the same quarter last year. The reduction was primarily due to lower compensation costs, professional fees and occupancy costs, partially offset by higher legal fees.

### **Business Development Expenses**

Business development expenses amounted to \$62,584 in the first quarter of 2009, compared to \$286,944 for the same quarter last year. The decrease of \$224,360 was primarily due to lower compensation costs and consulting fees in the current quarter. The business development expenses incurred in the first quarter of 2008 were included with research and development and general and administrative expenses and have been reclassified for comparative purposes in the financial statements for the first quarter of 2009.

### **Other Expenses**

Amortization expense decreased to \$1,416,010 in the current quarter from \$2,299,318 in the same quarter last year. The decrease resulted primarily from the reduced amortization on intellectual property following the write-down of the carrying value in September and December 2008.

Accretion expense on long-term debt amounted to \$125,895 in the first quarter of 2009 compared to \$113,607 in the same quarter of 2008. This ongoing non-cash accounting charge for imputed interest will increase the carrying value of long-term debt to face value by the maturity date of each item.

Interest on long-term debt was \$197,119 in the first quarter of 2009, compared to \$257,362 in the same quarter last year. The decrease was due to the reduction in interest expense on the Biolevier loan as a result of the lower Canadian prime rate in the current quarter compared to the first quarter of 2008.

Restructuring charges in the first quarter of 2009 amounted to \$378,406, compared to \$608,901 in the same quarter last year. The amount in the current quarter represented the completion of the restructuring process resulting from the decision taken by the Company to close its operations in France. The restructuring charges incurred in the first quarter of 2008 reflected a decision by the Company to streamline its operations, resulting in the departure of the Executive Vice-President, Business Development, Licensing and IP.

As a consequence of the intellectual property arising on the acquisition of Ambrilia France, a future income tax liability of \$9,787,526 was recorded in 2006, with additional amounts of \$315,275 and \$604,356 added in 2008 and 2007, respectively, primarily through the exercise of acquisition warrants to acquire additional shares of Ambrilia France. This future income tax liability is being drawn down over a term of up to the 7-year period during which the intellectual property is being amortized. This resulted in a future income tax recovery on the consolidated statement of operations of \$439,292 for the first quarter of 2008, together with a foreign exchange gain on the future income tax liability of \$189,851. Drawdown of the future income tax liability was completed in the fourth quarter of 2008. Consequently, there is no future income tax recovery in the current quarter.

## **CASH FLOWS**

### **Quarter ended March 31, 2009 compared with the Quarter ended March 31, 2008**

Cash and cash equivalents decreased by \$5,094,687 in the current quarter, compared with an increase of \$392,112 in the same quarter last year. Excluding net amounts realized from maturities and purchases of short-term investments, net cash utilized in the current quarter amounted to \$5,094,687, compared to \$5,400,172 in the first quarter of 2008, a reduced utilization of \$305,485. Operating activities utilized \$188,246 less cash in the quarter, with \$5,101,303 having been utilized in the current quarter, compared to \$5,289,549 in the corresponding quarter last year. Within the operating activities, \$1,255,697 of cash was required due to an increase in working capital, compared to a reduction in working capital of \$28,338 in the same quarter last year. Sales of intellectual property and property, plant and equipment contributed \$6,616 in the current quarter, whereas net purchases of intellectual property and property, plant and equipment amounted to \$110,623 in the same quarter last year. No financing activities occurred in either the current quarter or the same quarter of 2008.

Excluding changes in working capital, operating activities utilized \$3.8 million of cash in the current quarter. The average burn rate in the quarter was \$1.3 million per month, compared with \$1.8 million in the first quarter last year.

## **LIQUIDITY AND CAPITAL RESOURCES**

The Company has financed its operations and its acquisitions of technology and capital assets primarily through private placements and public issues of common shares and convertible debentures, scientific research investment tax credits and other government assistance, interest income and amounts received under licensing agreements for certain of its products.

The Company's cash resources are invested in Federal treasury bills and term deposits with a major Canadian bank. Consequently, it has not been impacted by the liquidity crisis in financial markets.

Cash and cash equivalents totalled \$3,240,477 at March 31, 2009, compared with \$8,335,164 at December 31, 2008. The decrease of \$5,094,687 resulted from the utilization of \$5,101,303 to finance operating activities for the first quarter of 2009, including an increase of \$1,255,697 in non-cash working capital. In addition, an amount of \$6,616 was generated in the period from the sale of surplus equipment.

During the second half of 2008, the Company announced a series of cost-cutting actions resulting in reduction in cash consumption and a decrease in headcount to preserve its cash into 2009. The Company is also reviewing strategic alternatives that include the divestment, strategic partnership transactions or licensing of the Company's technologies, and the sale or merger of the Company. There can be no assurance that the review will result in any specific strategic or financial transactions and no timetable has been set for its completion. Depending upon the success of this review, the Company may not have sufficient cash to support its activities for the next 12 months without having access to additional financial resources, which could be difficult to obtain in the short-term due to the ongoing crisis in financial markets. The Company may have to undertake further reductions in its operations.

## **SIGNIFICANT PROJECTS**

Each of our product candidates, which were discussed in the Overview section, will have to complete the necessary phases of clinical trials and obtain regulatory approval before they can generate significant revenues. The costs to complete these clinical trials and to obtain regulatory approval are significant and the costs associated with this process are expected to continue to be significant over the next several years. Part of these costs could be borne by various corporate partners under research collaboration and licensing agreements. The Company is presently reviewing strategic alternatives, including the divestment, strategic partnership transactions or licensing of the company's technologies and the sale or merger of the Company. The result of this review could impact the level of future expenditures to complete these clinical trials and to obtain regulatory approval.

## **CONTRACTUAL OBLIGATIONS AND OFF-BALANCE SHEET ARRANGEMENTS**

A summary of the Company's contractual obligations as at December 31, 2008 was disclosed in the Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended December 31, 2008. The amount of these contractual obligations did not change materially during the three months ended March 31, 2009.

The Company has not entered into any off-balance sheet arrangements during the three months ended March 31, 2009 and does not expect to enter into any, other than in the normal course of business, in the near future.

The Company does not have commitments for capital expenditures as at March 31, 2009.

## **RELATED PARTY TRANSACTIONS**

The outstanding \$100,000 loan under the Company's Employee Share Purchase Loan Program is held by Dr. Chandra Panchal, the former Executive Vice-President, Business Development, Licensing and IP, who left the Company effective February 29, 2008. By mutual agreement between the Company and Dr. Panchal, the settlement of this loan will be deferred until a date to be determined by the Company, which shall be not later than February 28, 2010. The Company has a pre-existing obligation, upon the sale of the underlying common shares of the Company, to forgive any shortfall arising following the application of the proceeds of sale in repayment of the loan, and also to pay to the above former executive an amount sufficient to offset any negative income tax consequences stemming from the forgiveness of the loan balance.

As at March 31, 2009, this loan of \$100,000 was outstanding and the underlying shares had a market value of approximately \$200.

## **PROPOSED TRANSACTIONS**

As noted under section "Significant Projects", the Company is presently reviewing strategic alternatives, including the divestment, strategic partnership transactions or licensing of the company's technologies and the sale or merger of the Company. However, at the present time, the Company has not entered into any agreements involving the acquisition or disposition by the Company of assets or businesses.

## **CHANGES IN ACCOUNTING POLICIES**

Effective January 1, 2009, the Company adopted the following recently-introduced Canadian Institute of Chartered Accountants ["CICA"] Handbook Section, with restatement of prior periods.

Section 3064, Goodwill and intangible assets, replacing Section 3062, Goodwill and other intangible assets and Section 3450, Research and development costs. The new Section, issued in February 2008, is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. As a result of the retrospective application of this new Section, internally-generated patent costs which previously had been capitalized as Intellectual Property and amortized over their useful lives are now expensed as incurred. For the three month period ended March 31, 2008, this resulted in an increase in patent expenditures of \$158,239 and a reduction in amortization of intellectual property of \$36,430 with an increase to the net loss of \$121,809.

## **FUTURE ACCOUNTING CHANGES**

In February 2008, the CICA confirmed that Canadian public companies will be required to adopt International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (IASB), effective January 1, 2011.

The Company is continuing to assess the preliminary differences between IFRS and the Company's current accounting policies, as well as the alternatives available to it upon adoption of IFRS. It has not yet quantified the effect of adopting IFRS on its financial statements, systems and business activities.

## **FINANCIAL INSTRUMENTS**

The Company does not use currency or other hedging instruments.

## **OUTSTANDING SHARE DATA**

As of May 1, 2009, the number of common shares outstanding is 48,580,612, unchanged from December 31, 2008. The number of stock options outstanding at May 1, 2009 is 1,525,391, a decrease of 68,045 from December 31, 2008. The decrease resulted from 66,295 options having been forfeited and 1,750 options having expired. In addition, 15,877,037 warrants are outstanding on May 1, 2009, unchanged from December 31, 2008.

Further, a total of \$4.5 million of convertible debentures were outstanding at May 1, 2009, unchanged from December 31, 2008. This includes \$3.5 million which is convertible into 777,777 common shares at any time prior to June 29, 2010, based on a conversion price of \$4.50 per common share. The balance is convertible into common shares at a price range of 125% to 150% of the market price of the common shares at the date of regulatory approval of a product for which work on the technology has been terminated.

## **RISK FACTORS**

Ambrilia's activities involve a number of risks and uncertainties that are generally experienced by the biotechnology industry. The future viability of Ambrilia depends upon its ability to raise sufficient funds, to successfully develop its technologies and products, to enter into licensing agreements and to obtain the regulatory approvals necessary to allow the products to be marketed.

### **Going Concern Uncertainty**

As at March 31, 2009, there was substantial doubt as to the Company's ability to continue as a going concern without having access to additional financial resources.

The Company has incurred significant operating losses since its inception and its anticipated level of future net annual expenditures exceeds its cash and cash equivalents as at March 31, 2009. Further, based on the Company's current projections, it is unlikely that it will be in compliance with its debt covenants beginning in the second quarter of 2009, which would result in Investissement Quebec ("IQ") having the right to demand immediate repayment of the Biolevier loan facility. Management is actively pursuing initiatives to avoid a breach of the debt covenants and to obtain a waiver from IQ. To-date the Company has financed its cash requirements primarily by issuing common shares and debt instruments, by licensing arrangements and through investment tax credits and interest income. It is currently attempting to monetize its assets through sale or licensing transactions. The Company is also seeking other alternatives, including strategic partnership transactions and the sale or merger of the Company. Ambrilia's ability to continue as a going concern is subject to its ability to successfully implement these plans. There can be no assurance that these plans will materialize on a timely basis or on satisfactory terms. If the Company is unable to obtain additional financial resources, management may be required to further curtail the Company's operations.

### **Product Development**

Ambrilia cannot assure that its products will be developed successfully. Ambrilia's most advanced products are currently in the development stages and its other products are at the research stage. Its first product to market is designed to be a substitute for the drug C2L octreotide in its long-acting formulation. Only the final results from the Phase III study now ongoing will tell whether the potential advantages of Ambrilia's proprietary formulation are confirmed and whether the product has a chance to receive formal approval from regulatory agencies.

Regarding its proprietary products, Ambrilia cannot assure that its research and development programs will result in commercially viable products. To achieve profitable operation, Ambrilia, alone or with others, must successfully develop its products. To obtain regulatory approvals for the products being developed, clinical trials must demonstrate efficacy and that the products are safe for human use. Unsatisfactory results obtained from a particular study relating to a program or changes in business strategies may cause Ambrilia or its collaborators to abandon its commitment to that program. Ambrilia cannot assure that any future animal or human test will yield favourable results.

### **Regulatory Approvals and Clinical Studies**

Ambrilia cannot assure that any of its ongoing or future clinical studies will be successful or that it will receive requisite regulatory approvals. Ambrilia's clinical trials could be delayed or suspended at any time if it is determined at any time that participants are being exposed to unacceptable health risks or that Ambrilia's products are not effective. Obtaining the requisite regulatory approvals will take several years and requires the expenditure of substantial resources. Any failure or delay in obtaining regulatory approvals could adversely affect Ambrilia's ability to commercialize its products.

If regulatory approval of any of Ambrilia's products is obtained, their manufacture, marketing and sale will be subject to ongoing and extensive governmental regulation in the United States, Europe, Canada and other countries in which Ambrilia intends to market its products, which could result in the revocation of previously granted regulatory approvals. The manufacturing facilities for Ambrilia's drug candidates are also subject to continual review and periodic inspection and approval of manufacturing modifications by regulatory authorities. Manufacturing facilities are subject to inspections by the FDA and must comply with the FDA's current good manufacturing practices, or cGMP, regulations. In complying with these regulations, manufacturers must spend funds, time and effort in the areas of production, record keeping, personnel and quality control to ensure full compliance. Regulatory authorities in other countries have similar requirements. Failure to comply with any of these post-approval requirements may, among other things, result in warning letters, product seizures, recalls, fines, injunctions, suspensions or revocations of marketing licenses, operating restrictions and criminal prosecutions. Any of these enforcement actions or any unanticipated changes in existing regulatory requirements or the adoption of new requirements could adversely affect Ambrilia's ability to market products and generate revenues.

Ambrilia has limited experience with regulatory authorities in the United States and Europe and relies on third party licensees for the filing of applications for the approval of its products. The license agreements with such third parties provides for the obligation of Ambrilia to provide licensees with an application file within a prescribed period of time. Failure to provide licensees with a complete application file within the prescribed period of time generally triggers the right to terminate the license agreement, generally, without costs. There can be no assurance that Ambrilia will be able to meet its obligations to provide a complete file within the prescribed period of time and that third party licensees will accept an extension upon the failure by Ambrilia to meet the prescribed time-frame. The exercise of such right of termination by licensees could lead to the failure or delay in obtaining regulatory approvals, which would adversely affect Ambrilia's ability to commercialize its products.

### **Administration of Preclinical Studies and Clinical Trials**

The process of conducting preclinical studies, human clinical trial testing and obtaining required approvals for Ambrilia's products is likely to take a number of years and require the expenditure of substantial resources. The amount and timing of preclinical studies, including animal testing, to be conducted prior to the commencement of human clinical trials is at the discretion of regulators, and may involve significantly more time and money than anticipated.

In addition, human clinical trials may take longer to start and complete than anticipated. In particular, there is competition from various pharmaceutical products for access to a limited number of research clinics and patients in Canada and other countries that are qualified to participate in multi-centre human clinical trials. There can be no assurance that access to such clinics or patients will not be delayed longer than anticipated, or obtained at all.

Animal testing and human clinical trials may result in adverse animal or patient reactions or statistically insignificant results, which may require a cessation or extension of the trials, or an increase in the number of patients enrolled in a given trial or the need to undertake ancillary testing and human trials. This may result in additional delays and expenses and the termination of projects.

### **Reliance on Third Parties to Conduct Clinical Trials**

Ambrilia has only limited experience with clinical trials. It also has limited internal resources and capacity to perform preclinical studies and clinical trials. As a result, Ambrilia hires contract research organizations, or CROs, to perform most of its preclinical and clinical trials for its products being developed without a partner. If the CROs that Ambrilia engages to perform its clinical trials or Ambrilia's partners do not execute their obligations as expected, Ambrilia's clinical trials may be delayed or terminated. If Ambrilia is forced to find a replacement entity to perform clinical trials, it may not be able to find a suitable entity in a timely manner or on favourable terms. Events such as these may result in delays in Ambrilia obtaining regulatory approval for its products or its ability to commercialize its products and could result in increased expenditures.

### **Market Acceptance and Commercialization**

Even if Ambrilia's products are successfully developed and receive regulatory approval, they may not gain market acceptance among physicians, patients, health care payers such as private insurers and other funding parties and the medical community. The degree of market acceptance for any of Ambrilia's products will depend on a number of factors including: demonstration of the clinical efficacy and safety of its products, cost-effectiveness, pricing, potential advantage over alternative treatment methods, superiority of alternative treatment or therapeutics, marketing and distribution support for the products, and reimbursement policies of government and third-party payers. If Ambrilia fails to commercialize products or if its future products do not achieve significant market acceptance, Ambrilia will not likely generate significant revenues or become profitable.

### **Dependence on Collaborative Agreements with Third Parties**

Ambrilia's dependence on collaborative agreements with third parties may not result in marketable products. If any collaborative partner fails to develop or commercialize successfully any product to which it or Ambrilia has rights, Ambrilia may be adversely affected. In addition, while Ambrilia believes that its actual and eventual collaborative partners will have sufficient economic motivation to continue their funding, it cannot assure that any of these collaborations will be continued or result in successfully commercialized products. If one or more of Ambrilia's collaborative partners fails to continue funding any particular program, the development or commercialization of any products arising out of this program could be stopped or delayed.

If conflicts arise between Ambrilia and its collaborators or its scientific advisors, the other party may act in its self-interest and not in the interest of Ambrilia's shareholders. Additionally, Ambrilia cannot assure that its collaborative partners will not pursue alternative technologies or develop alternative products either on their own or in collaboration with others, including Ambrilia's competitors, as a means for developing treatments for the diseases targeted by Ambrilia's programs. Disputes may arise with respect to the payment of milestones or the ownership of intellectual property rights to any technology or products ultimately developed with any current or future collaborative partner. Lengthy negotiations with potential new collaborative partners or disagreements between Ambrilia and its current collaborative partners may lead to delays in, or termination of, the research, development or commercialization of any products Ambrilia develops or result in time-consuming and costly litigation or arbitration.

### **Manufacturing Risks**

Ambrilia has not yet introduced any products and has limited manufacturing experience. To be successful, Ambrilia's products will have to be scalable, stable and safely manufactured in clinical trial quantities and commercial quantities in compliance with current good manufacturing practices, or cGMPs, and other regulatory requirements and at acceptable costs. In order to manufacture its products in commercial quantities Ambrilia or its partners will need to develop or expand current manufacturing facilities or contract with third parties to manufacture its products. No assurance can be given that Ambrilia, or its partners or its third party contractors will be able to make the transition to commercial production or that current manufacturing facilities will be adequate or sufficient or will continue to be available to Ambrilia following the termination date of the lease on its premises. Should any of its suppliers or its partners be unable or delayed in supplying Ambrilia with

sufficient supplies, no assurance can be given that Ambrilia will be able to find alternative means of supply in a short period of time and key new raw materials could become scarce or unavailable. There may be a limited number of third parties who may manufacture Ambrilia's products. Should such parties' operations suffer a material adverse effect, the manufacturing of Ambrilia's products would also be adversely affected.

### **Price Controls**

In some countries, particularly the countries of the European Union, the pricing of prescription drugs is subject to governmental control. In these countries, pricing negotiations with governmental authorities can take considerable time and delay the marketing of a product. In some countries, it may be necessary, in order to obtain reimbursement or pricing approval, to conduct clinical trials to compare the cost effectiveness of Ambrilia's product candidate to other available therapies. If reimbursement of Ambrilia's products is unavailable or limited in scope or amount, or if pricing is set at unsatisfactory levels, Ambrilia could be adversely affected.

### **Capital Requirements**

To develop its products, Ambrilia requires significant investment of financial resources. Consequently, the ability of Ambrilia to obtain the cash needed to finance its operations is fundamental to its future success and therefore constitutes a business risk. Ambrilia's planned cash requirements may vary materially in response to a number of factors, including continued scientific progress in its products discovery and development program, progress in its preclinical evaluation of products and product candidates, time and expenses associated with filing, prosecuting and enforcing its patent claims, and costs associated with obtaining regulatory approvals. In order to meet such capital requirements, Ambrilia will consider collaborative research and development arrangements, and additional public or private financing (including the issuance of additional equity securities) to fund all or a part of particular programs. Ambrilia's ability to arrange such financing in the future will depend in part upon prevailing capital-market conditions as well as its business performance. There can be no assurance that Ambrilia will be successful in its efforts to arrange additional financing, if needed, on terms satisfactory to it. Such financing, if available, may result in dilution to existing Ambrilia shareholders. If adequate funds are not available, Ambrilia may have to substantially reduce or eliminate expenditures for research and development, testing, production and marketing of its proposed products, or obtain funds through arrangements with corporate partners that require it to relinquish rights to certain of its technologies or products.

With regards to the concentration of credit risk, investment tax credits recoverable are due from the Québec and French governments. The cash and cash equivalents are held with two Canadian chartered banks and one French bank and in Government of Canada treasury bills and term deposits. No short-term investments were held at March 31, 2009.

Since the beginning of its operations, Ambrilia has incurred significant losses and expects to continue to incur losses in the near future.

### **Share Price Volatility**

The market price of Ambrilia's Common Shares is subject to volatility. General market conditions as well as differences between Ambrilia's financial, scientific and clinical results and the expectations of investors as well as securities analysts can have a significant impact on the trading price of the Common Shares. In recent years, the stocks of many biopharmaceutical companies have experienced extreme price fluctuations, unrelated to the operating performance of the affected companies. There can be no assurance that the market price of the Common Shares will not continue to experience significant fluctuations in the future, including fluctuations that are unrelated to Ambrilia's performance. The occurrence of any of the risks and uncertainties described in this management discussion and analysis could have a material adverse effect on the price of the Common Shares.

### **Personnel**

Ambrilia requires sophisticated management, research and development, marketing and sales, regulatory and clinical development personnel to develop its products. Success depends on Ambrilia's ability to attract, train and retain such personnel. The market for highly-trained personnel is very competitive due to the limited number of people available with the necessary technical skills and understanding of Ambrilia's products and technologies. If Ambrilia fails to attract and retain qualified personnel, its business operations and product development efforts could suffer.

## **Intellectual Property Matters**

Ambrilia relies on patent, copyright, trade secret and trade-mark laws to limit the ability of others to compete with it using the same or similar technologies. However, these laws afford only limited protection and may not adequately protect Ambrilia's rights to the extent necessary to sustain any competitive advantage.

Third parties may claim that Ambrilia's products infringe upon their intellectual property rights. This risk is exacerbated by the fact that the validity and breadth of medical technology patents involve complex legal and factual questions for which important legal principles remain unresolved.

In addition, because patents are not published until 18 months post-filing and can take many years to issue, there may be currently pending applications of which Ambrilia is unaware or which issue with an unexpected scope, such applications may later result in issued patents that Ambrilia's products infringe upon. There could also be existing patents of which Ambrilia is not aware that its products may infringe upon.

Furthermore, competitors may independently develop similar products or copy Ambrilia's products by circumventing its patents.

Patent applications relating to or affecting Ambrilia's business have been filed by a number of healthcare and biopharmaceutical companies. Some of these applications have been received. A number of technologies, applications or patents may conflict with its technologies or patent applications and such conflict could reduce the scope of patent protection that it could otherwise obtain or even lead to refusal of its patent applications.

Ambrilia may not enter into licensing arrangements at a reasonable cost, or develop or obtain alternative technology in respect of patents issued to third parties that incidentally cover its products. Any liability to secure licenses or alternative technology could result in delays in the introduction of some of its products or even lead to prohibition of the development, manufacture or sale of certain products. Moreover, Ambrilia could potentially incur substantial legal costs in defending legal actions that allege patent infringement or by instituting patent infringement suits against others.

Ambrilia cannot be certain that it is the creator of inventions covered by pending patent applications or that it was the first to file patent applications for any such inventions. No assurance can be given that its patents, once issued, would be declared by a court to be valid or enforceable, or that a competitor's technology or product would be found to infringe its patents.

Moreover, much of Ambrilia's know-how technology, which is not patentable, may constitute trade secrets. Therefore, Ambrilia requires its employees, consultants, advisors and collaborators to enter into confidentiality agreements. However, no assurance can be given that such agreements will provide for a meaningful protection of its trade secrets, know-how or other proprietary information in the event of any unauthorized use or disclosure of information.

## **Product Liability Claims**

The testing and marketing of medical products, even after regulatory approval, has an inherent risk of product liability. Ambrilia obtains product liability insurance coverage in the total amount of \$5,000,000 relating to Phases I, II, and III clinical trials as required. It also maintains coverage for any claims arising from its previous clinical trials. However, these insurance coverages are limited and a product liability claim could potentially be greater than these coverages. Ambrilia would be adversely affected by a successful product liability claim in excess of its insurance coverage.

## **Fluctuations in Short-Term Revenues**

The revenues of Ambrilia in the foreseeable future will be derived primarily from products licensed to pharmaceutical and biotechnology companies. Ambrilia expects fluctuation in such short-term revenues. Accordingly, these revenues will depend in large part upon the success of these companies and Ambrilia's operating results may fluctuate substantially due to reductions and delays in their research, development and marketing expenditures. These reductions and delays may result from factors that are not within Ambrilia's control, including changes in economic conditions, changes in the regulatory environment, including governmental pricing controls affecting health care and health care providers, pricing pressures and other factors affecting research and development spending.

### **Intense Competition and Rapid Technological Changes**

The biotechnology and pharmaceutical industries are highly competitive. There are a number of pharmaceutical companies, biopharmaceutical companies, universities and research organizations actively engaged in research and development and conducting clinical trials of products or medical treatment that may be similar to, or compete with, Ambrilia's products. Increased competition and technological advancement could diminish Ambrilia's ability to become profitable or affect its profitability in the future. Some of Ambrilia's competitors have substantially greater financial and technical resources, including more extensive research and development capabilities and greater marketing, distribution, production and human resources. A number of Ambrilia's largest competitors are pursuing the development or marketing of pharmaceuticals that target the same diseases or viral infections that Ambrilia is targeting, and it is possible that the number of companies seeking to develop such products and therapies will increase. In addition, many of these competitors have significantly greater experience in undertaking pre-clinical testing and human clinical trials of new pharmaceutical products and in obtaining regulatory approvals of human therapeutic products. Accordingly, Ambrilia's existing and potential competitors may develop products sooner, or obtain regulatory approval for their products more rapidly. They may also develop superior products or technology rendering Ambrilia's products or technology non-competitive or obsolete.

### **Unproven Market**

Ambrilia believes that there will be applications for products successfully derived from its core technologies and that the anticipated markets for products under development will continue to expand. However, no assurance can be given that these beliefs will prove to be correct owing, in particular, to competition from existing or new products and the yet to be established commercial validity of Ambrilia's products.

### **Government Regulation**

The procedure involved in obtaining regulatory approval from government regulators in Canada, Europe and the United States to market therapeutic products is long, costly, time-consuming and uncertain and may delay product development. The approval to market a product may be given to a limited extent only or it may be refused. Such limitations or refusals could be detrimental to Ambrilia's sales.

### **Hazardous Material and Environmental Matters**

Ambrilia's activities involve the controlled use of hazardous materials. Ambrilia is subject to federal, provincial and local laws and regulations governing the use, manufacturing, storage, handling and disposal of such materials and certain waste products. Although Ambrilia believes that its safety procedures for handling and disposing of such materials comply with the standards prescribed by those laws and regulations, the risk of accidental contamination or injury from these materials cannot be completely eliminated. Should this occur, Ambrilia could be held liable for any damages that result, and any such liability could exceed its resources. Although Ambrilia believes that it is in compliance with environmental laws and regulations, and currently does not expect to make material capital expenditures for environmental control facilities in the near-term, there can be no assurance that it will not be required to incur significant costs to comply with environmental laws and regulations in the future, or that it will not be materially adversely affected by current or future environmental laws or regulations.

### **Foreign Currency Exchange**

Ambrilia operates and intends to generate revenue and expenses internationally, which are likely to be denominated in U.S. dollars, in euros and other foreign currencies. Ambrilia's international business is subject to risks typical of an international business including differing tax structures, myriad regulations and restrictions and general foreign exchange rate volatility. A decrease in the value of such foreign currencies relative to the Canadian dollar could result in downward price pressure for Ambrilia's products or losses from currency exchange rate fluctuations. Ambrilia cannot assure that any hedging techniques will be successful or that it will not be materially adversely affected by exchange rate fluctuations.

## **Value of Intangible Assets**

Ambrilia is required to review the carrying value of its intangible assets for impairment annually or when events change. Intangible assets include net book value of product rights and process know-how covered by certain patented and non-patented information. Management reviews the carrying value based on projected future results. If events such as generic competition or inability to manufacture or obtain supply of product occur that may cause sales of the related products to decline, Ambrilia adjusts the projected results accordingly. Any impairment in the carrying value results in a write-down of the intangible asset that is charged to income during the period in which the impairment is determined. The write-down of intangible assets may have a material adverse effect on the results of operations in the period in which the write-down occurs.

## **DISCLOSURE CONTROLS AND PROCEDURES**

The President and Chief Executive Officer and the Executive Vice-President, Finance and Chief Financial Officer are responsible for establishing and maintaining Ambrilia's disclosure controls and procedures. They are required to be fully apprised of any material information affecting the Company, so that they may review and evaluate this information in order to determine the appropriateness and timing of public releases.

The President and Chief Executive Officer and the Executive Vice-President, Finance and Chief Financial Officer, having evaluated the effectiveness of the Company's disclosure controls and procedures as at March 31, 2009, have concluded that these disclosure controls and procedures are adequate and effective and thus would have ensured that material information relating to the Company would have been known to them.

## **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

Internal controls over financial reporting ("ICFRs") are designed to provide reasonable assurance regarding the reliability of the Company's financial reporting and its compliance with GAAP in its consolidated financial statements. The President and Chief Executive Officer and the Executive Vice-President, Finance and Chief Financial Officer, together with other members of management, have designed ICFRs in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with Canadian GAAP.

The President and Chief Executive Officer and the Executive Vice-President, Finance and Chief Financial Officer have evaluated the design and effectiveness of the Company's internal controls over financial reporting as of the end of the period covered by the annual filings and believe the design and effectiveness to be adequate to provide such reasonable assurance using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control – Integrated Framework.

Management have concluded that no changes were made to ICFRs during the three months ended March 31, 2009, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

**AMBRILIA BIOPHARMA INC.**  
**CONSOLIDATED BALANCE SHEETS**

(unaudited)  
[*note 2*]

As at

	<b>March 31, 2009</b>	December 31, 2008
	\$	\$
		Restated [ <i>note 3</i> ]
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	3,240,477	8,335,164
Accounts receivable	153,468	238,846
Investment tax credits recoverable	2,367,278	2,418,663
Prepaid expenses	320,308	182,973
	<b>6,081,531</b>	11,175,646
Property, plant and equipment	1,626,818	1,751,157
Intellectual property	20,956,563	22,254,850
Other long-term assets	400,000	400,000
	<b>29,064,912</b>	35,581,653
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	3,957,877	5,207,076
Deferred license revenues	1,107,190	1,113,116
	<b>5,065,067</b>	6,320,192
Biolevier loan facility [ <i>note 4</i> ]	8,352,646	8,322,914
Convertible debentures	3,018,690	2,922,527
	<b>16,436,403</b>	17,565,633
<b>Shareholders' equity [<i>note 5</i>]</b>		
Share capital	139,508,548	139,508,548
Warrants	8,610,715	8,610,715
Contributed surplus	8,922,754	8,918,574
Equity component of convertible debentures	1,920,914	1,920,914
Deficit	(146,334,422)	(140,942,731)
	<b>12,628,509</b>	18,016,020
	<b>29,064,912</b>	35,581,653

See accompanying notes

**AMBRILIA BIOPHARMA INC.**  
**CONSOLIDATED STATEMENTS OF**  
**OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT**

(unaudited)  
[*note 2*]

	Three months ended March 31,	
	2009	2008
	\$	\$
		Restated [ <i>note 3</i> ]
<b>REVENUES</b>		
License revenue	5,926	10,946
Interest revenue on cash, cash equivalents and short-term investments	12,813	246,544
Other income	-	3,000
	<b>18,739</b>	<b>260,490</b>
<b>EXPENSES</b>		
Research and development	2,101,611	3,098,438
Research and development tax credits	(48,000)	(293,823)
Net research and development	2,053,611	2,804,615
General and administrative	1,156,875	1,706,569
Business development	62,584	286,944
Patent expenditures	51,276	174,063
Amortization of property, plant and equipment	117,723	137,886
Amortization of intellectual property	1,298,287	2,161,432
Accretion on Biolevier loan facility	29,732	29,312
Accretion on convertible debentures	96,163	84,295
Interest on Biolevier loan facility	135,869	196,112
Interest on convertible debentures	61,250	61,250
Financial charges	11,431	2,694
Restructuring charges [ <i>note 7</i> ]	378,406	608,901
Foreign exchange gains	(42,777)	(58,490)
	<b>5,410,430</b>	<b>8,195,583</b>
<b>Loss before income taxes</b>	<b>(5,391,691)</b>	<b>(7,935,093)</b>
Future income tax recovery	-	439,292
Foreign exchange gain on future income tax liability	-	189,851
	-	629,143
<b>Net loss and comprehensive loss for the period</b>	<b>(5,391,691)</b>	<b>(7,305,950)</b>
Deficit, beginning of period – as previously reported	(140,548,785)	(100,741,754)
Adjustment on implementation of new accounting standard [ <i>note 3</i> ]	(393,946)	(1,242,978)
Deficit, beginning of period as amended	(140,942,731)	(101,984,732)
<b>Deficit, end of period</b>	<b>(146,334,422)</b>	<b>(109,290,682)</b>
<b>Basic and diluted loss per share</b>	<b>(0.11)</b>	<b>(0.15)</b>
<b>Weighted average number of common shares outstanding</b>	<b>48,576,796</b>	<b>47,650,555</b>

See accompanying notes

**AMBRILIA BIOPHARMA INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(unaudited)  
[*note 2*]

	<b>Three months ended</b>	
	<b>March 31,</b>	
	<b>2009</b>	2008
	\$	\$
		Restated
		[ <i>note 3</i> ]
<b>OPERATING ACTIVITIES</b>		
Net loss for the period	(5,391,691)	(7,305,950)
Items not affecting cash		
Amortization of property, plant and equipment	117,723	137,886
Amortization of intellectual property	1,298,287	2,161,432
Accretion on Biolevier loan facility	29,732	29,312
Accretion on convertible debentures	96,163	84,295
Future income tax recovery and related exchange gain	-	(629,143)
Services paid by issuance of stock options [ <i>note 5</i> ]	4,180	204,281
	<b>(3,845,606)</b>	<b>(5,317,887)</b>
Net change in non-cash balances relating to operations	<b>(1,255,697)</b>	28,338
<b>Cash flows related to operating activities</b>	<b>(5,101,303)</b>	<b>(5,289,549)</b>
<b>INVESTING ACTIVITIES</b>		
Acquisition of property, plant and equipment	-	(110,893)
Proceeds from disposal of property, plant and equipment	6,616	270
Maturities of short-term investments	-	5,792,284
<b>Cash flows related to investing activities</b>	<b>6,616</b>	<b>5,681,661</b>
<b>FINANCING ACTIVITIES</b>		
<b>Cash flows related to financing activities</b>	-	-
Net increase (decrease) in cash and cash equivalents	<b>(5,094,687)</b>	392,112
Cash and cash equivalents, beginning of period	<b>8,335,164</b>	10,795,297
<b>Cash and cash equivalents, end of period</b>	<b>3,240,477</b>	<b>11,187,409</b>
<b>Supplemental cash flow information</b>		
Cash paid during the period for:		
Interest	<b>141,984</b>	200,466
See accompanying notes		

## **Ambrilia Biopharma Inc.**

# **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 31, 2009

(unaudited)

### **1. Description of business**

Ambrilia Biopharma Inc. [the "Company"] is a biopharmaceutical company engaged in the development and commercialization of diagnostics and therapeutic drugs. It was incorporated under the laws of the province of Ontario in 1986 and was continued under the Canada Business Corporations Act in 2001.

### **2. Basis of presentation and going concern uncertainty**

#### **Going concern uncertainty**

These unaudited interim consolidated financial statements have been prepared by management on a going concern basis, which assumes that the Company will continue to operate and be able to realize its assets and discharge its liabilities and commitments in the ordinary course of business for the foreseeable future. The use of these principles may not be appropriate because, as at March 31, 2009, there was substantial doubt as to the Company's ability to continue as a going concern without having access to additional financial resources.

The Company has incurred significant operating losses since its inception and has accumulated a deficit of \$146,334,422 as at March 31, 2009. Its anticipated level of future net annual expenditures exceeds its cash and cash equivalents as at March 31, 2009. Further, based on the Company's current projections, it is unlikely that it will be in compliance with its debt covenants beginning in the second quarter of 2009. To-date the Company has financed its cash requirements primarily by issuing common shares and debt instruments, by licensing arrangements and through investment tax credits and interest income. It is currently attempting to monetize its assets through the sale or licensing of these assets to third parties. The Company is also seeking other alternatives, including strategic partnership transactions and the sale or merger of the Company. Ambrilia's ability to continue as a going concern is subject to its ability to successfully implement these plans. There can be no assurance that these plans will materialize on a timely basis or on satisfactory terms. If the Company is unable to obtain additional financial resources, management may be required to further curtail the Company's operations.

These interim consolidated financial statements do not include any adjustments to the amounts and classification of assets and liabilities that might be necessary if the Company is unable to continue as a going concern. Such adjustments could be material.

#### **Basis of presentation**

The interim consolidated financial statements include the accounts of the Company, those of its wholly-owned French subsidiary, Ambrilia Biopharma France S.A. ["Ambrilia France"], those of its wholly-owned U.S. subsidiary, Oncologic Biopharmaceuticals Corporation ["Oncologic"], and those of its wholly-owned Canadian subsidiary, Cellpep Pharma Inc. ["Cellpep"]. All significant intercompany transactions and balances have been eliminated upon consolidation.

The interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles applicable to interim financial statements and, except for the change reported in note 3 below, follow the same accounting policies and methods of application as the most recent annual consolidated financial statements. The interim consolidated financial statements do not include all disclosures required for annual financial statements and should be read in conjunction with the most recent annual consolidated financial statements as at and for the year ended December 31, 2008.

## Ambrilia Biopharma Inc.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2009

(unaudited)

#### 3. Change in accounting policy

Effective January 1, 2009, the Company adopted the following recently introduced Canadian Institute of Chartered Accountants ["CICA"] Handbook Section retroactively with restatement of prior periods.

Section 3064, Goodwill and intangible assets, replacing Section 3062, Goodwill and other intangible assets and Section 3450, Research and development costs. The new Section, issued in February 2008, is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. As a result of the retrospective application of this new Section, internally-generated patent costs which previously had been capitalized as Intellectual Property and amortized over their useful lives are now expensed as incurred. The adoption of this new standard resulted in a \$1,242,978 increase in deficit on January 1, 2008, with a corresponding decrease of intellectual property and a \$393,946 increase in deficit on January 1, 2009, with a corresponding decrease of intellectual property. For the three month period ended March 31, 2008, this resulted in an increase in patent expenditures of \$158,239 and a reduction in amortization of intellectual property of \$36,430, with an increase to the net loss of \$121,809.

#### 4. Biolevier loan facility

	March 31, 2009	December 31, 2008
	\$	\$
Biolevier loan facility	8,927,466	8,927,466
Less: Deferred financing fees	(574,820)	(604,552)
	<b>8,352,646</b>	8,322,914

Amongst other conditions, the Company is subject to a working capital ratio of 1.2, which was respected at March 31, 2009. Based on the Company's current projections, it is unlikely that it will be in compliance with the existing quarterly financial covenants beginning in the second quarter of 2009. Failure to comply with this debt covenant would result in Investissement Quebec ("IQ") having the right to demand repayment of the loan immediately. In this event, should the Company be unable to obtain a waiver from IQ to avoid repayment of the loan for a period of more than one year from the consolidated balance sheet date, the Biolevier loan facility balance would be reclassified as a current liability and the unamortized deferred financing fees would be written off. Management is actively pursuing initiatives to avoid a breach of the IQ covenant and to obtain a waiver from IQ.

#### 5. Shareholders' equity

##### Share capital

The Company is authorized to issue an unlimited number of common shares.

	Number of common shares	Share capital \$
<b>Issued and outstanding</b>		
<b>Balance as at March 31, 2009 and December 31, 2008</b>	<b>48,580,612</b>	<b>139,508,548</b>

**Ambrilia Biopharma Inc.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

March 31, 2009

(unaudited)

**5. Shareholders' equity [cont'd]**

**Warrants**

	Number of common shares reserved for issuance	\$
<b>Balance as at March 31, 2009 and December 31, 2008</b>	<b>15,877,037</b>	<b>8,610,715</b>

**Stock option plan**

As at March 31, 2009, there were 1,525,391 stock options outstanding, compared to 1,593,436 at December 31, 2008.

	Number	Three months ended March 31,		
		2009	2008	
		Weighted average exercise price \$	Number	Weighted average exercise price \$
<b>Options outstanding, beginning of period</b>	<b>1,593,436</b>	<b>2.13</b>	1,023,267	3.28
Granted	-	-	326,250	0.84
Forfeited	(66,295)	2.23	(8,000)	4.26
Expired	(1,750)	7.20	-	-
<b>Options outstanding, end of period</b>	<b>1,525,391</b>	<b>2.12</b>	1,341,517	2.68
<b>Exercisable</b>	<b>1,288,253</b>	<b>2.32</b>	726,256	3.47

All options granted were with exercise prices equal to or higher than the market price of the Company's shares at the date of grant. Stock-based compensation expense of \$4,180 has been recognized in the first quarter of 2009 for stock options granted to employees and directors. [ 2008 - \$204,281]. Based on the Black-Scholes option pricing model, the weighted average stock option fair value of the options granted during the quarter ended March 31, 2008 was \$0.84. In addition to the options shown above, grants of 424,219 options to employees on August 11, 2008 and of 767,141 to employees and directors on February 9, 2009 are conditional upon obtaining shareholders' approval.

Black-Scholes option pricing model assumptions:

	Three months ended March 31,	
	2009	2008
Expected dividend	-	Nil
Expected volatility	-	68%
Risk-free interest rate	-	3.7%
Expected option life	-	7 years

## Ambrilia Biopharma Inc.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2009

(unaudited)

#### 5. Shareholders' equity [cont'd]

##### Contributed surplus

	\$
<b>Balance as at December 31, 2008</b>	<b>8,918,574</b>
Options granted to employees and directors	4,180
<b>Balance as at March 31, 2009</b>	<b>8,922,754</b>

#### 6. Government assistance

Under an agreement with the National Research Council Canada Industrial Research Assistance Program to provide a contribution of up to \$980,000 to help fund the clinical development of one of the Company's technologies, the Company recorded, for the year ended December 31, 2006, \$883,334 of government assistance as a reduction of research and development expenses.

Repayment of the contribution is subject to certain terms and conditions based on gross revenues as defined by the agreement, but will not commence before January 1, 2009 and will continue up to January 1, 2019, or until a maximum of 150% of the total amount advanced under the agreement is repaid, if earlier. Repayments, if any, will be accounted for as part of research and development expense.

During the first quarter of 2009, the Company made the initial repayment required under the agreement in the amount of \$37,018, based on gross revenues for the year 2008. This amount is included in research and development expense.

#### 7. Restructuring charges

	<b>Three months ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
	<b>\$</b>	<b>\$</b>
Severance payments	<b>378,406</b>	608,901

On February 4, 2009, the Company completed the major reduction of its activities in France, resulting in the layoff of all the permanent employees based in France. The related restructuring costs pertaining to legal and contractual obligations of \$1,251,923 were expensed in the fourth quarter of 2008. The remaining restructuring costs incurred to complete the process amounted to \$378,406 and were expensed in the first quarter of 2009. Management does not anticipate further costs and deems that this restructuring process is complete. The provision for restructuring charges included in accounts payable and accrued liabilities as at March 31, 2009 amounted to \$207,000.

## Ambrilia Biopharma Inc.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2009

(unaudited)

#### 7. Restructuring charges [cont'd]

During the first quarter of 2008, the Company decided to streamline its activities and a restructuring plan was implemented which resulted in the departure of the Executive Vice-President, Business Development, Licensing and IP. Under the terms of an agreement dated February 29, 2008 between the Company and its former Executive Vice-President, Business Development, Licensing and IP, the former employee received severance of \$510,601 in cash, benefits and immediate vesting of outstanding options. In addition, the Company has a pre-existing obligation upon settlement of the \$100,000 loan under the Company's Employee Share Purchase Loan Program and a related amount of \$98,300 was expensed in the quarter for a total of \$608,901.

#### 8. Segmented information

	2009		2008	
	Three months ended March 31,	As at March 31,	Three months ended March 31,	As at December 31,
	Revenues \$	Property, plant and equipment and intellectual property \$	Revenues \$	Property, plant and equipment and intellectual property \$
Canada	16,536	15,579,113	248,850	16,544,161
France	2,203	7,004,268	11,640	7,461,846
<b>Total</b>	<b>18,739</b>	<b>22,583,381</b>	<b>260,490</b>	<b>24,006,007</b>

#### 9. Comparative figures

Certain comparative figures have been reclassified in order to conform to the presentation adopted in the current period.