PIMCO NEW YORK MUNICIPAL INCOME FUND
Form 3
January 23, 2017

FORM 3

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

OMB APPROVAL

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INITIAL STATEMENT OF BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person *
Â WANG QI

(Last) (First) (Middle)

C/O PIMCO,Â 650 NEWPORT CENTER DRIVE

(Street)

NEWPORT BEACH,Â CAÂ 92660

(City) (State) (Zip)

2. Date of Event Requiring Statement (Month/Day/Year)
01/12/2017

3. Issuer Name **and** Ticker or Trading Symbol
PIMCO NEW YORK MUNICIPAL INCOME FUND [PNF]

4. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

_____ Director _____ 10% Owner
_____ Officer __X__ Other
(give title below) (specify below)
SEE REMARKS

5. If Amendment, Date Original Filed(Month/Day/Year)

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Beneficially Owned

1.Title of Security (Instr. 4)	2. Amount of Securities Beneficially Owned (Instr. 4)	3. Ownership Form: Direct (D) or Indirect (I) (Instr. 5)	4. Nature of Indirect Beneficial Ownership (Instr. 5)

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

SEC 1473 (7-02)

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Table II - Derivative Securities Beneficially Owned (*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 4)	2. Date Exercisable and Expiration Date (Month/Day/Year)		3. Title and Amount of Securities Underlying Derivative Security (Instr. 4)		4. Conversion or Exercise Price of Derivative Security	5. Ownership Form of Derivative Security: Direct (D) or Indirect	6. Nature of Indirect Beneficial Ownership (Instr. 5)
	Date Exercisable	Expiration Date	Title	Amount or Number of Shares			

(I)
(Instr. 5)

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
WANG QI C/O PIMCO 650 NEWPORT CENTER DRIVE NEWPORT BEACH,Â CAÂ 92660	Â	Â	Â	SEE REMARKS

Signatures

/s/ Joel Reynolds, Attorney-in-Fact for Qi Wang	01/23/2017
**Signature of Reporting Person	Date

Explanation of Responses:

No securities are beneficially owned

* If the form is filed by more than one reporting person, *see* Instruction 5(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

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Remarks:

PacificÂ InvestmentÂ ManagementÂ CompanyÂ LLCÂ ("PIMCO")Â isÂ theÂ investmentÂ adviserÂ ofÂ theÂ Issuer.Â The

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *See* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. 0in .0001pt;text-align:left;">

2.44

10.00

3.52

2004

8.42

3.17

11.5

4.12

2005

6.47

4.00

7.89

4.85

2006

7.55

3.93

8.79

4.51

2007

4.40

1.33

5.21

1.37

NASDAQ (US$)

TSX (C$)

High

Low

High

Low

2006

First quarter

6.69

5.05

7.80

5.85

Second quarter

7.55

5.40

8.79

6.01

Third quarter

6.09

4.90

6.67

5.52

Fourth quarter

6.18

3.93

7.11

4.51

2007

First quarter	
	4.40
	2.90
	5.21
	3.41
Second quarter	
	4.18
	3.25
	4.75
	3.45
Third quarter	
	3.65
	2.27
	3.90

2.40

Fourth quarter

2.73

1.33

2.74

1.37

Last six months

Explanation of Responses:

Sept-07	
	2.96
	2.36
	3.10
	2.41
Oct-07	
	2.73
	1.84
	2.74
	1.75
Nov-07	
	2.05

1.50

1.91

1.42

Dec-07

1.93

1.33

1.93

1.37

Jan-08

1.80

1.44

1.80

1.47

Feb-08

1.68

1.32

1.69

1.28

76

Explanation of Responses:

B. Plan of distribution.

Not applicable.

C. Markets.

Our common shares are listed and posted for trading on the TSX and are quoted on the NASDAQ.

D. Selling shareholders.

Not applicable.

E. Dilution.

Not applicable.

F. Expenses of the issuer.

Not applicable.

Item 10. Additional Information

A. Share capital.

Not applicable.

B. Memorandum and articles of association.

The Company is governed by its restated articles of incorporation (the Restated Articles of Incorporation) under the *Canada Business Corporations Act* (the CBCA) and by its bylaws (the bylaws). The Company s Restated Articles of Incorporation are on file with the Corporations Directorate of Industry Canada under Corporation Number 264271-9. The Restated Articles of Incorporation do not include a stated purpose and do not place any restrictions on the business that the Company may carry on.

Inspection Rights of Shareholders

Under the CBCA, shareholders are entitled to be provided with a copy of the list of registered shareholders of the Company. In order to obtain the shareholder list, the Company must be provided with an affidavit including, among other things, a statement that the list will only be used for the purposes permitted by the CBCA. These permitted purposes include an effort to influence the voting of shareholders of the Company, an offer to acquire securities of the Company and any other matter relating to the affairs of the Company. The Company is entitled to charge a reasonable fee for the provision of the shareholder list and must deliver that list no more than ten days after receipt of the affidavit described above.

Under the CBCA, shareholders of the Company have the right to inspect certain corporate records, including its Restated Articles of Incorporation and bylaws and minutes of meetings and resolutions of the shareholders. Shareholders have no statutory right to inspect minutes of meetings and resolutions of directors of the Company. Shareholders of the Company have the right to certain financial information respecting the Company. In addition to the annual and quarterly financial statements required to be filed under applicable securities laws, under the CBCA the Company is required to place before every annual meeting of shareholders its audited comparative annual financial statements. In addition, shareholders have the right to examine the financial statements of each of its subsidiaries and any other corporate entity whose accounts are consolidated in the financial statements of the Company.

Directors

The minimum number of directors of the Company is five and the maximum number is fifteen. In accordance with the Company s bylaws and the CBCA, a majority of its directors must be residents of Canada. In order to serve as a director, a person must be a natural person at least 18 years of age, of sound mind, not bankrupt, and must not be prohibited by any court from holding the office of director. For as long as the Company is a company that publicly distributes its securities, at least two-thirds of its directors must not be officers or employees of the Company or its subsidiaries. Neither the Restated Articles of Incorporation, bylaws, nor the Act, impose any mandatory retirement requirements for directors.

The directors are elected by a majority of the votes cast at the annual meeting at which an election of directors is required, to hold office until the election of their successors except in the case of resignations or if their offices become vacant by death or otherwise. Subject to the provisions of the Company s bylaws, all directors may, if still qualified to serve as directors, stand for re-election. The Board of Directors is not replaced at staggered intervals but is elected annually.

Under the Company s bylaws and the Restated Articles of Incorporation, a director of the Company need not be a shareholder.

The directors are entitled to remuneration as shall from time to time be determined by the Board of Directors or by a committee to which the Board of Directors may delegate the power to do so. Under the mandate of the Company s Corporate Governance, Nominating and Human Resources Committee, such committee, comprised of a majority of independent directors, is tasked with making recommendations to the Board of Directors concerning director remuneration.

The Company s bylaws provide that a director shall promptly disclose to the Company any interest he or she has in any undertaking or association that is likely to place him or her in a situation of conflict of interest, as well as the rights he or she may assert thereagainst, indicating, should such be the case, the nature and value thereof. Likewise, the CBCA and the Company s bylaws provide that a director who is a party to, or who is a director or officer of, or has a material interest in, any person who is a party to a material contract or transaction or proposed material contract or transaction with the Company must disclose to the Company the nature and extent of his or her interest at the time and in the manner provided by the CBCA, or request that same be entered in the minutes of the meetings of the Board of Directors, even if such contract, in connection with the normal business activity of the Company, does not require the approval of either the directors or the shareholders. At the request of the president or any director, the director placed in a situation of conflict of interest must leave the meeting while the Board of

Directors discusses the matter. The CBCA and the Company s bylaws prohibit such a director from voting on any resolution to approve the contract or transaction unless the contract or transaction:

- relates primarily to his or her remuneration as a director, officer, employee or agent of the Company or an affiliate;

- is for indemnity or insurance for director s liability as permitted by the CBCA; or
- is with an affiliate of the Company.

The CBCA provides that the Board of Directors may, on behalf of the Company and without authorization of its shareholders:

- borrow money upon the credit of the Company;
- issue, reissue, sell or pledge debt obligations of the Company;
- give a guarantee on behalf of the Company to secure performance of an obligation of any person; and
- mortgage, hypothecate, pledge or otherwise create a security interest in all or any property of the Company, owned or subsequently acquired, to secure any obligation of the Company.

The shareholders have the ability to restrict such powers through the Company s Restated Articles of Incorporation or bylaws (or through a unanimous shareholder agreement), but no such restrictions are in place.

In addition, the Company s bylaws provide that the Board of Directors may:

- subject to the provisions of the Company s Restated Articles of Incorporation, accept subscriptions, allot, issue all or part of the unissued shares of the Company, grant options in respect of such shares or otherwise dispose thereof to such persons, on such terms and conditions and for such consideration and in such manner not contrary to the CBCA or the Restated Articles of Incorporation of the Company as the directors think fit; and
- from time to time as it may deem advisable and to the extent permitted by the CBCA, declare and pay to the shareholders, according to their rights, dividends in money or property or in the form of shares of the Company.

The CBCA prohibits the giving of a guarantee to any shareholder, director, officer or employee of the Company or of an affiliated corporation or to an associate of any such person for any purpose or to any person for the purpose of or in connection with a purchase of a share issued or to be issued by the Company or its affiliates, where there are reasonable grounds for believing that the Company is or, after giving the guarantee, would be unable to pay its liabilities as they become due, or the realizable value of the Company s assets in the form of assets pledged or encumbered to secure a guarantee, after giving the guarantee, would be less than the aggregate of the Company s liabilities and stated capital of all classes. These borrowing powers may be varied by the Company s bylaws or its Restated Articles of Incorporation. However, the Company s bylaws and Restated Articles of Incorporation do not contain any restrictions on or variations of these borrowing powers.

Pursuant to the Company s bylaws, the directors of the Company manage and administer the business and affairs of the Company and exercise all such powers and authority as the Company is authorized to exercise pursuant to the Act, the Restated Articles of Incorporation and the bylaws. The general duties of a director or officer of the Company under the CBCA are to act honestly and in good faith with a view to the best interests of the Company and to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. Any breach of these duties may lead to liability to the Company and its shareholders for breach of fiduciary duty. In addition, a breach of certain provisions of the CBCA, including the improper payment of dividends or the improper purchase or redemption of shares, will render the directors who authorized such action liable to account to the Company for any amounts improperly paid or distributed.

The Company s bylaws provide that the Board of Directors may, from time to time, appoint from amongst their number committees of the Board of Directors, and delegate to any such committee any of the powers of the Board of Directors except those which pursuant to the CBCA a committee of the Board of Directors has no authority to exercise. As such, the Board of Directors has two standing committees: the Audit Committee and the Corporate Governance, Nominating and Human Resources Committee.

Subject to the limitations provided by the CBCA, the Company must indemnify a director or an officer of the Company, a former director or officer of the Company or a person who acts or acted at the Company s request as a director or officer of a body corporate of which the Company is or was a shareholder or creditor, and his or her heirs and legal representatives, against all costs, losses, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by him or her in respect of any civil, criminal or administrative action or proceeding to which he or she is made a party by reason of having been a director or officer of the Company or such body corporate, provided:

(a) he or she acted in good faith in the best interests of the Company; and

(b) in the case of a criminal or an administrative action or proceeding that is enforced by a monetary penalty, he or she had reasonable grounds to believe that his or her conduct was lawful.

The directors of the Company are authorized to indemnify from time to time any director or other person who has assumed or is about to assume in the normal course of business any liability for the Company or for any corporation controlled by the Company, and to secure such director or other person against any loss by the pledge of all or part of the movable or immovable property of the Company through the creation of a hypothec or any other real right in all or part of such property or in any other manner.

Share Capitalization

The Company s Restated Articles of Incorporation authorize the issuance of an unlimited number of Common Shares and an unlimited number of Preferred Shares. All classes are without nominal or par value. The Restated Articles of Incorporation do not authorize the issuance of any other class of shares. On March 14, 2008, there were 53,187,470 Common Shares and no Preferred Shares issued and outstanding.

Common Shares: The holders of the Common Shares are entitled to one vote for each Common Share held by them at all meetings of shareholders, except meetings at which only shareholders of a specified class of shares are entitled to vote. In addition, the holders are entitled to receive dividends if, as and when declared by the Board of Directors on the Common Shares. Finally, the holders of the Common Shares are entitled to receive the remaining property of the Company upon any liquidation, dissolution or winding-up of the affairs of the Company, whether voluntary or involuntary. Shareholders have no liability to further capital calls as all shares issued and outstanding are fully paid and non-assessable.

Preferred Shares: The First and Second Preferred Shares are issuable in series with rights and privileges specific to each class. The holders of Preferred Shares are not entitled to receive notice of or to attend or vote at meetings of shareholders. No Preferred Shares of the Company have been issued to date.

The holders of First Preferred Shares are entitled to preference and priority to any participation of holders of Second Preferred Shares, Common Shares or shares of any other class of shares of the share capital of the Company ranking junior to the First Preferred Shares in regards to dividends and, in the event of the liquidation of the Company, the distribution of its property upon its dissolution or winding-up, or the distribution of all or part of its assets among the shareholders, to an amount equal to the value of the consideration paid in respect of such shares outstanding, as credited to the issued and paid-up share capital of the Company, on an equal basis, in proportion to the amount of their respective claims in regard to such shares held by them. The holders of Second Preferred Shares are entitled to preference and priority to any participation of holders of Common Shares or shares of any other class of shares of the share capital of the Company ranking junior to the Second Preferred Shares in regards to dividends and, in the event of the liquidation of the Company, the distribution of its property upon its dissolution or winding-up, or the distribution of all or part of its assets among the shareholders, to an amount equal to the value of the consideration paid in respect of such shares outstanding, as credited to the issued and paid-up share capital of the Company, on an equal basis, in proportion to the amount of their respective claims in regard to such shares held by them.

The Board of Directors may, from time to time, provide for series of Preferred Shares to be created and issued, but the issuance of any Preferred Share is subject to the general duties of the directors under the CBCA to act honestly and in good faith with a view to the best interests of the Company and to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The issuance of any Preferred Shares in the face of a take-over bid for the Company would be examined in light of these duties of the directors and other applicable case law.

Shareholder Actions

The CBCA provides that shareholders of the Company may, with leave of a court, bring an action in the name of and on behalf of the Company for the purpose of prosecuting, defending or discontinuing an action on behalf of the Company. In order to grant leave to permit such an action, the CBCA provides that the court must be satisfied that the directors of the Company were given adequate notice of the application, the shareholder is acting in good faith and that it appears to be in the Company s best interests that the action be brought.

Shareholder Rights Plan

Objectives and Background of the Shareholder Rights Plan

The fundamental objectives of the Company s Shareholder Rights Plan (the Rights Plan) are to provide adequate time for the Company s Board of Directors and shareholders to assess an unsolicited take-over bid for the Company, to provide the Board of Directors with sufficient time to explore and develop alternatives for maximizing shareholder value if a take-over bid is made, and to provide shareholders with an equal opportunity to participate in a take-over bid.

The Rights Plan encourages a potential acquiror who makes a take-over bid to proceed either by way of a Permitted Bid , which requires a take-over bid to satisfy certain minimum standards designed to promote fairness, or with the concurrence of the Company s Board of Directors. If a take-over bid fails to meet these minimum standards and the Rights Plan is not waived by the Board of Directors, the Rights Plan provides that holders of Common Shares, other than the potential acquiror, will be able to purchase additional Common Shares at a significant discount to market, thus exposing the potential acquiror of Common Shares to substantial dilution of its holdings.

Summary of the Rights Plan

The following is a summary of the principal terms of the Rights Plan, which summary is qualified in its entirety by reference to the terms thereof. The Rights Plan is filed as an exhibit to this annual report on Form 20-F.

Operation of the Rights Plan

Pursuant to the terms of the Rights Plan, one right was issued in respect of each Common Share outstanding as at the close of business on March 29, 2004 (the Record Time). In addition, one right will be issued for each additional Common Share issued after the Record Time and prior to the earlier of the Expiration Time and the Separation Time (as defined below). The rights have an initial exercise price equal to the Market Price (as defined below) of the Common Shares as determined at the Separation Time, multiplied by five, subject to certain adjustments, and they are not exercisable until the Separation Time. Upon the occurrence of a Flip-in Event (as defined below), each right will entitle the holder thereof, other than an Acquiring Person (as defined below), to purchase from the Company one Common Share upon payment to the Company of 50% of the Market Price of the Common Shares on the Toronto Stock Exchange on the date of consummation or occurrence of such Flip-in Event, subject to certain anti-dilution adjustments.

Trading of Rights

Until the Separation Time, the rights trade with the Common Shares and are represented by the same share certificates as the Common Shares or an entry in the Company s securities register in respect of any outstanding Common Shares. From and after the Separation Time and prior to the Expiration Time, the rights are evidenced by rights certificates and trade separately from the Common Shares. The rights do not carry any of the rights attaching to the Common Shares such as voting or dividend rights.

Separation Time

The rights will separate from the Common Shares to which they are attached and become exercisable at the time (the Separation Time) of the close of business on the eighth business day after the earliest to occur of:

- the first date (the Stock Acquisition Date) of a public announcement of facts indicating that a person has become an Acquiring Person (as defined below);
- the date of the commencement of, or first public announcement of the intention of any person (other than the Company or any of its subsidiaries) to commence a take-over bid or a share exchange bid for more than 20% of the outstanding Common Shares of the Company other than a Permitted Bid or a Competing Permitted Bid (as defined below); and
- the date upon which a Permitted Bid or a Competing Permitted Bid ceases to be a Permitted Bid or a Competing Permitted Bid, as the case may be.

The Separation Time can also be such later time as may from time to time be determined by the Board of Directors.

Flip-in Event

The acquisition by a person (an Acquiring Person), including others acting jointly or in concert with such person, of more than 20% of the outstanding Common Shares, other than by way of a Permitted Bid, a Competing Permitted Bid or in certain other limited circumstances described in the Rights Plan, is referred to as a Flip-in Event .

Definition of Market Price

Market Price is generally defined in the Rights Plan, on any given day on which a determination must be made, as the average of the daily closing prices per Common Share on each of the 20 consecutive Trading Days (as defined below) through and including the Trading Day immediately preceding such date of determination; subject to certain exceptions. Trading Day is generally defined as the day on which the principal Canadian or United States stock exchange (as determined by the Board of Directors acting in good faith) on which the Common Shares are listed or admitted to trading is open for the transaction of business.

Exercise of Rights

Upon the Separation Time or the effective date of the Flip-in Event, whichever occurs first, each right (other than those held by the Acquiring Person) will entitle the holder thereof to purchase from the Company one Common Share upon payment to the Company of 50% of the Market Price of the Common Shares of the Company on the Stock Acquisition Date subject to certain anti-dilution adjustments.

Permitted Bid Requirements

The requirements of a Permitted Bid include the following:

(1) the take-over bid must be made by means of a take-over bid circular;

(2) the take-over bid must be made to all holders of Common Shares wherever resident, on identical terms and conditions, other than the bidder;

(3) the take-over bid must not permit Common Shares tendered pursuant to the bid to be taken up or paid for:

a) prior to the close of business on a date which is not less than 60 days following the date of the bid, and

b) then only if at such date more than 50% of the then outstanding Common Shares held by shareholders other than any other Acquiring Person, the bidder, the bidder s affiliates or associates, persons acting jointly or in concert with the bidder and any employee benefit plan, deferred profit-sharing plan, stock participation plan or trust for the benefit of employees of the Company or any of its subsidiaries, unless the beneficiaries of such plan or trust direct the manner in which the Common Shares are to be voted or direct whether the Common Shares are to be tendered to a take-over bid (the Independent Shareholders), have been deposited or tendered to the take-over bid and not withdrawn;

(4) the take-over bid must allow Common Shares to be deposited, unless the take-over bid is withdrawn, at any time up to the close of business on the date that the Common Shares are to be first taken up and paid for;

(5) the take-over bid must allow Common Shares to be withdrawn until taken up and paid for; and

(6) if more than 50% of the then outstanding Common Shares held by Independent Shareholders are deposited or tendered to the take-over bid and not withdrawn, the bidder must make a public announcement of that fact and the take-over bid must remain open for deposits and tenders of Common Shares for not less than 10 days from the date of such public announcement.

The Rights Plan allows a competing Permitted Bid (a Competing Permitted Bid) to be made while a Permitted Bid is in existence. A Competing Permitted Bid must satisfy all the requirements of a Permitted Bid other than the requirements set out in clauses (3) and (6) above and must not permit Common Shares tendered or deposited pursuant to the bid to be taken up or paid for (a) prior to the close of business on a date which is not earlier than the latter of the last day on which the bid must be open for acceptance after the date of the bid under applicable Canadian provincial securities legislation and the earliest date on which Common Shares of the Company may be taken up and paid for under any earlier Permitted Bid or Competing Permitted Bid that is then in existence, and (b) then only if at such date more than 50% of the then outstanding Common Shares held by the Independent Shareholders have been deposited or tendered to the take-over bid and not withdrawn. In the event that the requirement set forth in (b) of this paragraph is satisfied, the competing bidder must make a public announcement of the fact and the take-over bid must remain open for deposits and tenders of Common Shares for not less than 10 days from the date of such public announcement.

Waiver and Redemption

The Board of Directors may, prior to the occurrence of a Flip-in Event, waive the dilutive effects of the Rights Plan in respect of, among other things, a particular Flip-in Event resulting from a take-over bid made by way of a take-over bid circular to all holders of Common Shares of the Company. In such an event, such waiver shall also be deemed to be a waiver in respect of any other Flip-in Event occurring under a take-over bid made by way of a take-over bid circular to all holders of Common Shares prior to the expiry of the first mentioned take-over bid. The Board of Directors may, at any time prior to the Separation Time, elect to redeem all but not less than all of the outstanding rights at a price of C$0.00001 each.

Amendment to the Rights Plan

The Rights Plan may be amended to correct any clerical or typographical error or to make such changes as are required to maintain the validity of the Rights Plan as a result of any change in any applicable legislation, regulations or rules thereunder, without the approval of the holders of the Common Shares or rights. Prior to the Separation Time, the Company may, with the prior consent of the holders of Common Shares, amend, vary or delete any of the provisions of the Rights Plan in order to effect any changes which the Board of Directors, acting in good faith, considers necessary or desirable. The Company may, with the prior consent of the holders of rights, at any time after the Separation Time and before the Expiration Time, amend, vary or delete any of the provisions of the Rights Plan. The Rights Plan, including the amendments thereto and the restatement thereof, was approved by the Board of Directors on March 2, 2007, was signed on March 5, 2007 and was ratified and confirmed by the Company s shareholders on May 2, 2007.

Fiduciary Duty of Board

The Rights Plan will not detract from or lessen the duty of the Board of Directors to act honestly and in good faith with a view to the best interests of the Company and its shareholders. The Board of Directors will continue to have the duty and power to take such actions and make such recommendations to the Company s shareholders as are considered appropriate.

Exemptions for Investment Advisors

Fund managers, investment advisors (for fully-managed accounts), trust companies (acting in their capacities as trustees and administrators), statutory bodies whose business includes the management of funds, and administrators of registered pension plans are exempt under the Rights Plan from triggering a Flip-in Event, provided that they are not making, or are not part of a group making, a take-over bid.

Action Necessary to Change Rights of Shareholders

In order to change the rights of its shareholders, the Company would need to amend its Restated Articles of Incorporation to effect the change. Such an amendment would require the approval of holders of two-thirds of the issued and outstanding shares cast at a duly called special meeting. For certain amendments such as those creating a class of Preferred Shares, a shareholder is entitled under the CBCA to dissent in respect of such a resolution amending the Restated Articles of Incorporation and, if the resolution is adopted and the Company implements such changes, demand payment of the fair value of its shares.

Disclosure of Share Ownership

In general, under applicable securities regulation in Canada, a person or company who beneficially owns, directly or indirectly, voting securities of an issuer or who exercises control or direction over voting securities of an issuer or a combination of both, carrying more than ten percent of the voting rights attached to all the issuer s outstanding voting securities is an insider and must, within ten days of becoming an insider, file a report in the required form effective the date on which the person became an insider, disclosing any direct or indirect beneficial ownership of, or control or direction over, securities of the reporting issuer.

Additionally, securities regulation in Canada provides for the filing of a report by an insider of a reporting issuer whose holdings change, which report must be filed within ten days from the day on which the change takes place.

Section 13 of the *United States Securities Exchange Act of 1934* (the Exchange Act) imposes reporting requirements on persons who acquire beneficial ownership (as such term is defined in the Rule 13d-3 under the Exchange Act) of more than five percent of a class of an equity security registered under Section 12 of the Exchange Act. The Company s Common Shares are so registered. In general, such persons must file, within ten days after such acquisition, a report of beneficial ownership with the SEC containing the information prescribed by the regulations under Section 13 of the Exchange Act. This information is also required to be sent to the issuer of the securities and to each exchange where the securities are traded.

Meeting of Shareholders

An annual meeting of shareholders is held each year for the purpose of considering the financial statements and reports, electing directors, appointing auditors and fixing or authorizing the Board of Directors to fix their remuneration and for the transaction of other business as may properly come before a meeting of shareholders. Any annual meeting may also constitute a special meeting to take cognizance and dispose of any matter of which a special meeting may take cognizance and dispose. Under the bylaws, the president of the Company has the power to call a meeting of shareholders.

While the bylaws provide that one or more shareholders who hold at least 20% of the outstanding voting shares of the Company may requisition the directors of the Company to call a meeting of shareholders for the purpose stated in the requisition, the CBCA provides that the holders of not less than 5% of the outstanding voting shares of the Company may so requisition the directors of the Company. Except in limited circumstances, including where a meeting of shareholders has already been called and a notice of meeting already given or where it is clear that the primary purpose of the requisition is to redress a personal grievance against the Company or its directors, officers or shareholders, the directors of the Company, on receipt of such requisition, must call a meeting of shareholders. If the directors fail to call a meeting of shareholders within twenty-one days after receiving the requisition, any shareholder who signed the requisition may call the meeting of shareholders and, unless the shareholders resolve otherwise at the meeting, the Company shall reimburse the shareholders for the expenses reasonably incurred by them in requisitioning, calling and holding the meeting of shareholders.

The CBCA also provides that, except in limited circumstances, a resolution in writing signed by all of the shareholders entitled to vote on that resolution at a meeting of shareholders is as valid as if it had been passed at a meeting of shareholders.

A quorum of shareholders is present at an annual or special meeting of shareholders, regardless of the number of persons present in person at the meeting, if the holder or holders of shares representing at least twenty percent of the outstanding voting shares at such meeting are present in person or represented in accordance with the Company s bylaws. In the case where the CBCA, the Restated Articles of Incorporation or the bylaws of the Company require or permit the vote by class of holders of a given class of shares of the share capital of the Company, the quorum at any meeting will be one or more persons representing twenty percent of the outstanding shares of such class.

Notice of the time and place of each annual or special meeting of shareholders must be given not less than twenty-one days, nor more than fifty days, before the date of each meeting to each director, to the auditor and to each shareholder entitled to vote thereat. If the address of any shareholder, director or auditor does not appear in the books of the Company, the notice may be sent to such address as the person sending the notice may consider to be most likely to reach such shareholder, director or auditor promptly. Every person who, by operation of the CBCA, transfers or by any other means whatsoever, becomes entitled to any share, shall be bound by every notice given in respect of such share which, prior to the entry of his or her name and address on the register of the Company, is given to the person whose name appears on the register at the time such notice is sent. Notice of meeting of shareholders called for any other purpose other than consideration of the financial statements and auditor s report, election of directors and reappointment of the incumbent auditor, must state the nature of the business in sufficient detail to permit the shareholder to form a reasoned judgment on and must state the text of any special resolution or bylaw to be submitted to the meeting.

Limitations on Right to Own Securities

Neither Canadian law nor the Company s Restated Articles of Incorporation or bylaws limit the right of a non-resident to hold or vote Common Shares of the Company, other than as provided in the Investment Canada Act (the Investment Act). The Investment Act prohibits implementation of certain direct reviewable investments by an individual, government or agency thereof, corporation, partnership, trust or joint venture that is not a Canadian, as defined in the Investment Act (a non-Canadian), unless, after review, the minister responsible for the Investment Act is satisfied or is deemed to be satisfied that the investment is likely to be of net benefit to Canada. An investment in the Common Shares of the Company by a non-Canadian (other than a WTO Investor, as defined below) would be reviewable under the Investment Act if it were an investment to acquire direct control of the Company, and the book value of the assets of the Company were C$5.0 million or more (provided that immediately prior to the implementation of the investment the Company was not controlled by WTO Investors). An investment in Common Shares of the Company by a WTO Investor (or by a non-Canadian other than a WTO Investor if, immediately prior to the implementation of the investment, the Company was controlled by WTO Investors) would be reviewable under the Investment Act if it were an investment to acquire direct control of the Company and the value of the assets of the Company equaled or exceeded C$295 million (for 2008). A non-Canadian, whether a WTO Investor or otherwise, would be deemed to acquire control of the Company for purposes of the Investment Act if he or she acquired a majority of the Common Shares of the Company. The acquisition of less than a majority, but at least one-third of the shares, would be presumed to be an acquisition of control of the Company, unless it could be established that the Company was not controlled in fact by the acquirer through the ownership of the shares. In general, an individual is a WTO Investor if he or she is a national of a country (other than Canada) that is a

member of the World Trade Organization (WTO Member) or has a right of permanent residence in a WTO Member. A corporation or other entity will be a WTO Investor if it is a WTO Investor-controlled entity, pursuant to detailed rules set out in the Investment Act. The United States is a WTO Member. Certain transactions involving the Company s Common Shares would be exempt from the Investment Act, including: (a) an acquisition of the shares if the acquisition were made in the ordinary course of that person s business as a trader or dealer in securities; (b) an acquisition of control of the Company in connection with the realization of a security interest granted for a loan or other financial assistance and not for any purpose related to the provisions of the Investment Act; and (c) an acquisition of control of the Company by reason of an amalgamation, merger, consolidation or corporate reorganization, following which the ultimate direct or indirect control in fact of the Company, through the ownership of voting interests, remains unchanged.

C. Material contracts.

Other than as disclosed herein under Shareholder Rights Plan , and except for contracts entered into in the ordinary course of business, there are no material contracts to which the Company or any of its subsidiaries is a party other than the employment agreements and change of control agreements with our executive officers as described below.

The Company and/or its subsidiaries have entered into employment agreements (the Employment Agreements) with each of the named Executive Officers. The Employment Agreements provide that the Company will pay the executives a base salary, an annual bonus and stock options which will be reviewed annually in accordance with the Company s policies. The Employment Agreements have an indefinite term, except for Dr. Engel, whose employment agreement is for a term of 32 months expiring in August 2010. In addition, each of the Employment Agreements, except for Dr. Engel s, provides that, if the Company terminates the employment of a Named Executive Officer without cause, then the executive will be entitled to receive a lump-sum payment, less statutory deductions, of the equivalent of 24 months in the case of Dr. Mazzo, 18 months in the case of Messrs. Turpin and Paradis and 12 months in the case of Dr. Blake and Ms. McDonald.

The Company has also entered into change of control agreements (the Change of Control Agreements) with each of the Named Executive Officers, except for Dr. Engel. Under such agreements, if a change of control (as defined in the Change of Control Agreements) occurs and the Company terminates the employment of the executive without cause, or if the executive terminates his employment for good reason, then the executive will be entitled to receive a lump-sum payment, less statutory deductions, of the equivalent of twenty-four (24) months in the case of Dr. Mazzo and eighteen (18) months in the case of Mr. Turpin, Dr. Blake, Ms. McDonald and Mr. Paradis of (i) their annual base salary, (ii) the maximum amount of their bonus, and (iii) the benefits, calculated on a yearly basis, including car allowances, but excluding operating costs and excluding any stock options which were held by such executive at the time of termination of employment.

D. Exchange controls.

Canada has no system of exchange controls. There are no exchange restrictions on borrowing from foreign countries or on the remittance of dividends, interest, royalties and similar payments, management fees, loan repayments, settlement of trade debts or the repatriation of capital. There are no limits on the rights of non-Canadians to exercise voting rights on their Common Shares of the Company.

E. Taxation.

THE FOLLOWING SUMMARY IS OF A GENERAL NATURE ONLY AND IS NOT INTENDED TO BE, NOR SHOULD IT BE CONSTRUED TO BE, LEGAL OR TAX ADVICE TO ANY PARTICULAR HOLDER. CONSEQUENTLY, HOLDERS ARE URGED TO CONSULT THEIR OWN TAX ADVISORS FOR ADVICE AS TO THE TAX CONSEQUENCES OF AN INVESTMENT IN THE COMMON SHARES HAVING REGARD TO THEIR PARTICULAR CIRCUMSTANCES.

The following summary describes the principal Canadian federal income tax consequences to a purchaser who acquires Common Shares (a holder) who, for the purposes of the Canadian federal Income Tax Act, R.S.C. 1985, as amended (The Tax Act), deals at arm s length with, and is not affiliated with, the Corporation and holds Common Shares as capital property. The Common Shares will generally be considered to be capital property for this purpose unless either the holder holds such Common Shares in the course of carrying on a business, or the holder has held or acquired such Common Shares in a transaction or transactions considered to be an adventure in the nature of trade.

This summary is not applicable to a holder an interest in which is a tax shelter investment as defined in the Tax Act, or to a holder which is a financial institution as defined in the Tax Act subject to the mark-to-market rules set out therein. Such holders should consult their own tax advisors.

This summary is based upon the current provisions of the Tax Act and the regulations thereunder and the Company s understanding of the current published administrative practices and policies of the Canada Revenue Agency (CRA). It also takes into account all proposed amendments to the Tax Act and the regulations publicly released by the Minister of Finance (Canada) (Tax Proposals), and assumes that all such Tax Proposals will be enacted as currently proposed. No assurance can be given that the Tax Proposals will be enacted in the form proposed or at all. This summary does not otherwise take into account or anticipate any changes in law, whether by way of legislative, judicial or administrative action or interpretation, nor does it address any provincial, territorial or foreign tax considerations.

The current published policy of the CRA is that certain entities (including most limited liability companies (LLC s)) that are treated as being fiscally transparent for United States federal income tax purposes do not qualify as residents of the United States and therefore are not entitled to relief from Canadian tax under the provisions of the Canada-United States Income Tax Convention (the Convention). However, on September 21, 2007, Canada and the United States jointly released the fifth protocol revising the Convention (the Protocol). Although not yet in force, the Protocol provides, *inter alia*, for the extension of treaty benefits to LLC s in certain circumstances. **Prospective investors should consult their own tax advisors to determine their entitlement to relief under the Convention based on their particular circumstances.**

Holders Not Resident in Canada

The following discussion applies to a holder of Common Shares who, at all relevant times, for purposes of the Tax Act and any applicable income tax treaty or convention, is neither resident nor deemed to be resident in Canada and does not, and is not deemed to, use or hold Common Shares, in carrying on a business or part of a business in Canada (a Non-Resident holder). In addition, this discussion does not apply to an insurer who carries on an insurance business in Canada and elsewhere or to an authorized foreign bank (as defined in the Tax Act).

Disposition of Common Shares

A Non-Resident holder will not be subject to tax under the Tax Act in respect of any capital gain realized by such Non-Resident holder on a disposition of Common Shares unless the Common Shares constitute taxable Canadian property (as defined in the Tax Act) of the Non-Resident holder at the time of disposition and the holder is not entitled to relief under the applicable income tax treaty or convention. As long as the Common Shares are then listed on a designated stock exchange (which currently includes the NASDAQ and the TSX), the Common Shares generally will not constitute taxable Canadian property of a Non-Resident holder, unless at any time during the 60-month period immediately preceding the disposition, the Non-Resident holder, persons with whom the Non-Resident holder did not deal at arm s length, or the Non-Resident holder together with all such persons, owned 25% or more of the issued shares of any class or series of shares of the capital stock of the Corporation. As long as the Common Shares are listed on the NASDAQ, the TSX or another recognized stock exchange , a Non-Resident

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holder who disposes of Common Shares that are taxable Canadian property will not be required to fulfill the requirements of section 116 of the Tax Act.

Taxation of Dividends on Common Shares

Dividends paid or credited or deemed to be paid or credited on the Common Shares to a Non-Resident holder will be subject to a Canadian withholding tax in the amount of 25%. Such withholding tax may be reduced by virtue of the provisions of an income tax treaty or convention between Canada and the country of which the Non-Resident holder is a resident. Under the Convention, the rate of withholding tax in respect of dividends or deemed dividends beneficially owned by a resident of the United States is generally reduced to 15%.

Holders Resident in Canada

The following discussion applies to a holder of Common Shares who, at all relevant times, for purposes of the Tax Act and any applicable income tax treaty or convention, is resident in Canada (a Canadian holder). Certain Canadian holders whose Common Shares might not otherwise qualify as capital property may, in certain circumstances, treat the Common Shares and other Canadian securities as defined in the Tax Act, as capital property by making an irrevocable election provided by subsection 39(4) of the Tax Act.

Taxation of Dividends on Common Shares

Dividends received or deemed to be received on the Common Shares will be included in a Canadian holder s income for purposes of the Tax Act. Such dividends received or deemed to be received by a Canadian holder that is an individual (other than certain trusts) will be subject to the gross-up and dividend tax credit rules generally applicable under the Tax Act in respect of dividends received on shares of taxable Canadian corporations. Generally, a dividend will be eligible to the enhanced gross-up and dividend tax credit if the recipient receives written notice from the corporation designating the dividend as an eligible dividend (within the meaning of the Tax Act). There may be limitations on the ability of the Corporation to designate dividends as eligible dividends. A Canadian holder that is a corporation will include such dividends in computing its income and will generally be entitled to deduct the amount of such dividends in computing its taxable income. A Canadian holder that is a private corporation or a subject corporation (as such terms are defined in the Tax Act), may be liable under Part IV of the Tax Act to pay a refundable tax of 331/3% on dividends received or deemed to be received on the Common Shares to the extent such dividends are deductible in computing the holder s taxable income.

Disposition of Common Shares

A disposition, or a deemed disposition, of a Common Share by a Canadian holder will generally give rise to a capital gain (or a capital loss) equal to the amount by which the proceeds of disposition of the share, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base of the share to the holder. Such capital gain (or capital loss) will be subject to the treatment described below under Taxation of Capital Gains and Capital Losses .

Additional Refundable Tax

A Canadian holder that is a Canadian-controlled private corporation (as such term is defined in the Tax Act) may be liable to pay an additional refundable tax of 62/3% on certain investment income including amounts in respect of Taxable Capital Gains , as defined below.

Taxation of Capital Gains and Capital Losses

In general, one half of any capital gain (a Taxable Capital Gain) realized by a Canadian holder in a taxation year will be included in the holder s income in the year. Subject to and in accordance with the provisions of the Tax Act, one half of any capital loss (an Allowable Capital Loss) realized by a Canadian holder in a taxation year must be deducted from Taxable Capital Gains realized by the holder in the year and Allowable Capital Losses in excess of Taxable Capital Gains may be carried back and deducted in any of the three preceding taxation years or carried forward and deducted in any subsequent taxation year against net taxable capital gains realized in such years. The amount of any capital loss realized by a Canadian holder that is a corporation on the disposition of a Common Share may be reduced by the amount of dividends received or deemed to be received by it on such Common Share (or on a share for which the Common Share has been substituted) to the extent and under the circumstances prescribed by the Tax Act. Similar rules may apply where a corporation is a member of a partnership or a beneficiary of a trust that owns Common Shares, directly or indirectly, through a partnership or a trust. A Taxable Capital Gain realized by a Canadian holder who is an individual may give rise to liability for alternative minimum tax.

Certain U.S. Federal Income Tax Considerations

The following discussion is a summary of certain U.S. federal income tax consequences applicable to the ownership and disposition of Common Shares (Shares) by a U.S. Holder (as defined below), but does not purport to be a complete analysis of all potential U.S. federal income tax effects. This summary is based on the Internal Revenue Code of 1986, as amended (the Code), U.S. Treasury regulations promulgated thereunder, Internal Revenue Service (IRS) rulings and judicial decisions in effect on the date hereof. All of these are subject to change, possibly with retroactive effect, or different interpretations.

This summary does not address all aspects of U.S. federal income taxation that may be relevant to particular U.S. Holders in light of their specific circumstances (for example, U.S. Holders subject to the alternative minimum tax provisions of the Code) or to holders that may be subject to special rules under U.S. federal income tax law.

This summary also does not discuss any aspect of state, local or foreign law, or U.S. federal estate or gift tax law as applicable to U.S. Holders. In addition, this discussion is limited to U.S. Holders holding Shares as capital assets. For purposes of this summary, U.S. Holder means a beneficial holder of Shares who or that for U.S. federal income tax purposes is:

- an individual citizen or resident of the United States;
- a corporation or other entity classified as a corporation for U.S. federal income tax purposes created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate, the income of which is subject to U.S. federal income taxation regardless of its source; or
- a trust, if a court within the United States is able to exercise primary supervision over the administration of such trust and one or more U.S. persons (within the meaning of the Code) have the authority to control all substantial decisions of the trust, or if a valid election is in effect to be treated as a U.S. person.

If a partnership or other entity or arrangement classified as a partnership for U.S. federal income tax purposes holds Shares, the U.S. federal income tax treatment of a partner generally will depend on the status of the partner and the activities of the partnership. Such a partner should consult its own tax advisor as to the tax consequences of the partnership owning and disposing of Shares.

Dividends

Subject to the passive foreign investment company (PFIC) rules discussed below, distributions paid by the Company out of current or accumulated earnings and profits (as determined for U.S. federal income tax purposes), before reduction for any Canadian withholding tax paid with respect thereto, will generally be taxable to a U.S. Holder as foreign source dividend income, and will not be eligible for the dividends received deduction

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generally allowed to corporations. Distributions in excess of current and accumulated earnings and profits will be treated as a non-taxable return of capital to the extent of the U.S. Holder s adjusted tax basis in the Shares and thereafter as capital gain. However, the Company does not maintain calculations of its earnings and profits in accordance with U.S. federal income tax accounting principles. U.S. Holders should therefore assume that any distribution by the Company with respect to Shares will constitute ordinary dividend income. U.S. Holders should consult their own tax advisors with respect to the appropriate U.S. federal income tax treatment of any distribution received from the Company.

For taxable years beginning before January 1, 2011, dividends paid by the Company should be taxable to a non-corporate U.S. Holder at the special reduced rate normally applicable to long term capital gains, provided that certain conditions are satisfied. A U.S. Holder will not be able to claim the reduced rate for any year in which the Company is treated as a PFIC. See Passive Foreign Investment Company Considerations below.

Under current law payments of dividends by the Company to non-Canadian investors are generally subject to a 25 percent Canadian withholding tax. The rate of withholding tax applicable to U.S. Holders that are eligible for benefits under the Canada-United States Tax Convention (1980) (the Treaty) is reduced to a maximum of 15 percent.

Dividends paid in Canadian dollars will be included in income in a U.S. dollar amount calculated by reference to the exchange rate in effect on the day the dividends are received by the U.S. Holder, regardless of whether the Canadian dollars are converted into U.S. dollars at that time. If dividends received in Canadian dollars are converted into U.S. dollars on the day they are received, the U.S. Holder generally will not be required to recognise foreign currency gain or loss in respect of the dividend income.

A U.S. Holder will generally be entitled, subject to certain limitations, to a credit against its U.S. federal income tax liability, or a deduction in computing its U.S. federal taxable income, for Canadian income taxes withheld by the Company. U.S. Holders should consult their tax advisors concerning the foreign tax credit implications of the payment of Canadian taxes.

Sale or Other Taxable Disposition

Subject to the PFIC rules discussed below, upon a sale or other taxable disposition of Shares, a U.S. Holder generally will recognize capital gain or loss for U.S. federal income tax purposes equal to the difference, if any, between the amount realized on the sale or other taxable disposition and the U.S. Holder s adjusted tax basis in the Shares.

This capital gain or loss will be long-term capital gain or loss if the U.S. Holder s holding period in the Shares exceeds one year. Long-term capital gains of non-corporate U.S. Holders are currently eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations. Any gain or loss will generally be U.S. source for U.S. foreign tax credit purposes.

Passive Foreign Investment Company Considerations

A foreign corporation will be classified as a PFIC for any taxable year in which, after taking into account the income and assets of the corporation and certain subsidiaries pursuant to applicable look-through rules, either (i) at least 75 percent of its gross income is passive income or (ii) at least 50 percent of the average value of its assets is attributable to assets which produce passive income or are held for the production of passive income.

If the Company is classified as a PFIC for any taxable year during which a U.S. Holder owns Shares, the U.S. Holder, absent certain elections (including a mark-to-market election), will generally be subject to adverse rules (regardless of whether the Company continues to be classified as a PFIC) with respect to (i) any excess distributions (generally, any distributions received by the U.S. Holder on the Shares in a taxable year that are greater than 125 percent of the average annual distributions received by the U.S. Holder in the three preceding taxable years or, if shorter, the U.S. Holder s holding period for the Shares) and (ii) any gain realized on the sale or other disposition of Shares.

Under these adverse rules (a) the excess distribution or gain will be allocated rateably over the U.S. Holder s holding period, (b) the amount allocated to the current taxable year and any taxable year prior to the first taxable year in which the Company is classified as a PFIC will be taxed as ordinary income, and (c) the amount allocated to each of the other taxable years during which the Company was classified as a PFIC will be subject to tax at the highest rate of tax in effect for the applicable class of taxpayer for that year and an interest charge will be imposed with respect to the resulting tax attributable to each such other taxable year.

The Company believes it was not a PFIC for the 2007 taxable year. However, since the fair market value of the Company s assets may be determined in large part by the market price of the Shares, which is likely to fluctuate, and the composition of the Company s income and assets will be affected by how, and how quickly, the Company spends any cash that is raised in any financing transaction, no assurance can be provided that the Company would not be classified as a PFIC for the 2008 taxable year and for any future taxable year.

U.S. Holders should consult their tax advisors regarding the potential application of the PFIC regime.

Information Reporting and Backup Withholding

The proceeds of a sale or other disposition, as well as dividends paid with respect to Shares by a U.S. payor, generally will be reported to the IRS and to the U.S. Holder as required under applicable regulations. Backup withholding tax may apply to these payments if the U.S. Holder fails to timely provide an accurate taxpayer identification number or otherwise fails to comply with, or establish an exemption from, such backup withholding tax requirements. Certain U.S. Holders (including, among others, corporations) are not subject to the information reporting or backup withholding tax requirements described herein. U.S. Holders should consult their tax advisors as to their qualification for exemption from backup withholding tax and the procedure for obtaining an exemption.

F. Dividends and paying agents.

Not applicable.

G. Statement by experts.

Not applicable.

H. Documents on display.

We are subject to the information requirements of the Securities Exchange Act of 1934, as amended. In accordance with these requirements, we file reports and other information with the United States Securities and Exchange Commission. These materials, including this annual report on Form 20-F and the exhibits thereto, may be inspected and copied at the Commission s Public Reference Room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. The public may obtain information on the operation of the Commission s Public Reference Room by calling the

Commission in the United States at 1-800-SEC-0330. The Commission also maintains a website at www.sec.gov that contains reports, proxy statements and other information regarding registrants that file electronically with the Commission. The Company s annual reports and some of the other information submitted by the Company to the Commission may be accessed through this website. In addition, material filed by the Company can be inspected on the Canadian Securities Administrators electronic filing system, SEDAR, accessible at the website www.sedar.com. This material includes the Company s Management Information Circular for its annual meeting to be held on May 7, 2008 to be furnished to the SEC on Form 6-K, which provides information including directors and officers , remuneration and indebtedness, principal holders of securities and securities authorized for issuance under equity compensation plans. Additional financial information is provided in our annual financial statements for the year ended December 31, 2007 and our Management s Discussion and Analysis relating to these statements. These documents are also accessible on SEDAR (www.sedar.com).

I. Subsidiary information.

The subsidiaries of the Company are set forth under Item 4C Organizational Structure.

Item 11. Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency Risk

Since the Company operates on an international scale, it is exposed to currency risks as a result of potential exchange rate fluctuations. For the year ended December 31, 2007, there were no significant operations using forward-exchange contracts and no significant forward-exchange contract is outstanding as of today.

Credit Risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist primarily of cash and cash equivalents, short-term investments and accounts receivable. Cash and cash equivalents are maintained with high-credit quality financial institutions. Short-term investments consist primarily of bonds issued by high-credit quality corporations and institutions. Consequently, management considers the risk of non-performance related to cash and cash equivalents and investments to be minimal.

Generally, we do not require collateral or other security from customers for trade accounts receivable; however, credit is extended following an evaluation of creditworthiness. In addition, we perform ongoing credit reviews of all our customers and establish an allowance for doubtful accounts when accounts are determined to be uncollectible.

Interest Rate Risk

We are exposed to market risk relating to changes in interest rates with regard to our short-term investments.

Item 12. Description of Securities Other than Equity Securities

A. Debt securities.

Not applicable.

B. Warrants and rights.

Not applicable.

C. Other securities.

Not applicable.

D. American depositary shares.

Not applicable.

PART II

Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

Item 14. Material Modification to the Rights of Security Holders and Use of Proceeds

None.

Item 15. Controls and Procedures

The Registrant s management, including the Registrant s Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company s disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended), as of December 31, 2007. Based on that evaluation, as of December 31, 2007, the Registrant s Chief Executive Officer and Chief Financial Officer concluded that the Registrant s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Registrant in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to management, including the Registrant s Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Management s Report on Internal Control over Financial Reporting

The Registrant s management is responsible for establishing and maintaining adequate internal control over financial reporting. The Registrant s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in Canada.(1)

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(1) Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP) and significant differences in measurement and disclosure from generally accepted accounting principles in United States (U.S. GAAP) are set out in Note 24 to our consolidated financial statements included in Item 18 to this report.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Registrant s management, with the participation of the Registrant s Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Registrant s internal control over financial reporting based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, the Registrant s management has concluded that, as of December 31, 2007, the Registrant s internal control over financial reporting was effective.

The effectiveness of the Registrant s internal control over financial reporting as of December 31, 2007 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included in Item 18 of this Annual Report on Form 20-F.

Changes in Internal Control over Financial Reporting

There has been no change in the Registrant s internal control over financial reporting that occurred during the year ended December 31, 2007 that have materially affected, or are reasonably likely to materially affect, the Registrant s internal control over financial reporting.

Item 16. [Reserved]

Item 16A. Audit Committee Financial Expert

The Board of Directors of the Registrant has determined that the Registrant has at least one audit committee financial expert (as defined in paragraph 16(b) of General Instruction B to Form 20-F). The name of the audit committee financial expert of the Registrant is Mr. Gérard Limoges, FCA, the Audit Committee s Chairman. The Commission has indicated that the designation of Mr. Limoges as the audit committee financial expert of the Registrant does not: (i) make Mr. Limoges an expert for any purpose, including without limitation for purposes of Section 11 of the Securities Act of 1933, as amended, as a result of this designation; (ii) impose any duties, obligations or liability on Mr. Limoges that are greater than those imposed on him as a member of the Audit

Committee and the Board of Directors in the absence of such designation; or (iii) affect the duties, obligations or liability of any other member of the Audit Committee or the Board of Directors. The other members of the Audit committee are Ms. Martha Byorum and Mr. Pierre MacDonald who are all independent. For a description of their respective education and experience, please refer to Item 6A.

Item 16B. Code of Ethics

On March 29, 2004, the Board of Directors adopted a Code of Ethical Conduct , which was amended by the Board of Directors on November 3, 2004, December 13, 2005 and March 2, 2007. The December 13, 2005 amendment incorporates changes to the duty to report violations consistent with applicable laws. The Registrant has selected an independent third party supplier to provide a confidential and anonymous communication channel for reporting concerns about possible violations to the Registrant s Code of Ethical Conduct as well as financial and/or accounting irregularities or fraud. A copy of the Code of Ethical Conduct, as amended, is attached as Exhibit 11.1 to this annual report on Form 20-F and is also available on the Registrant s Web site at www.aeternazentaris.com in Investors/Governance. The Code of Ethical Conduct is a code of ethics as defined in paragraph (16)(b) of General Instruction B to Form 20-F. The Code of Ethical Conduct applies to all of the Registrant s employees, directors and officers, including the Registrant s principal executive officer, principal financial officer, and principal accounting officer or controller, or persons performing similar functions, and includes specific provisions dealing with integrity in accounting matters, conflicts of interest and compliance with applicable laws and regulations. The Registrant will provide this document without charge to any person or company upon request to the Corporate Secretary of the Registrant, at its head office at 1405 du Parc-Technologique Boulevard, Quebec City, Quebec, G1P 4P5, Canada.

Item 16C. Principal Accountant Fees and Services

(All amounts are in US dollars)

A Audit Fees

During the financial years ended December 31, 2007 and 2006, our principal accountant, PricewaterhouseCoopers LLP, billed us aggregate amounts of $284,973 and $253,587 respectively for the audit of our annual consolidated financial statements and services in connection with statutory and regulatory filings.

B Audit-related Fees

During the financial years ended December 31, 2007 and 2006, our principal accountant, PricewaterhouseCoopers LLP, billed us aggregate amounts of $306,804 and $204,555 respectively for audit or attest services not required by statute or regulation, employee benefit plan audits, due diligence services, and accounting consultations on proposed transactions, including the review of prospectuses and the delivery of customary consent and comfort letters in connection therewith.

C Tax Fees

During the financial years ended December 31, 2007 and 2006, our principal accountant, PricewaterhouseCoopers LLP, billed us aggregate amounts of $43,182 and $29,084 respectively for services related to tax compliance, tax planning and tax advice.

D All Other Fees

During the financial years ended December 31, 2007 and 2006, our principal accountant, Pricewatherhouse Coopers LLP, billed us aggregate amounts of $4,508 and $568 respectively for services not included in audit fees, audit-related fees and tax fees.

E Audit Committee Pre-Approval Policies and Procedures

Under applicable Canadian securities regulations, we are required to disclose whether our Audit Committee has adopted specific policies and procedures for the engagement of non-audit services and to prepare a summary of these policies and procedures. The Audit Committee Charter (attached as Exhibit 11.6 to this annual report) provides that it is such committee s responsibility to approve all audit engagement fees and terms as well as reviewing policies for the provision of non-audit services by the external auditors and, when required, the framework for pre-approval of such services. The Audit Committee delegates to its Chairman the pre-approval of such non-audit fees. The pre-approval by the Chairman is then presented to the Audit Committee at its first scheduled meeting following such pre-approval.

For each of the years ended December 31, 2006 and 2007, none of the non-audit services provided by our external auditor were approved by the Audit Committee pursuant to the de minimis exception to the pre-approval requirement for non-audit services.

During the financial year ended on December 31, 2007, only full-time permanent employees of our principal accountant, PricewaterhouseCoopers LLP, performed work to audit our financial statements.

Item 16D. Exemptions from the Listing Standards for Audit Committees

None.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

None.

PART III

Item 17. Financial Statements

We have elected to provide financial statements pursuant to Item 18.

Item 18. Financial Statements

The financial statements appear on pages 96 through 155.

Æterna Zentaris Inc.

Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(expressed in thousands of US dollars)

Report of Independent Registered Public Accounting Firm

To the Shareholders of Æterna Zentaris Inc.

We have completed an integrated audit of the consolidated financial statements and internal control over financial reporting of Æterna Zentaris Inc. as at December 31, 2007 and audits of its 2006 and 2005 consolidated financial statements. Our opinions, based on our audits, are presented below.

Consolidated financial statements

We have audited the accompanying consolidated balance sheets of Æterna Zentaris Inc. as at December 31, 2007 and December 31, 2006, and the related consolidated statements of earnings, comprehensive income, changes in shareholders equity and cash flows for each of the years in the three-year period ended December 31, 2007. We have also audited the financial statement schedule on the change in the valuation allowance on future income tax assets included in Form 20-F. 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 and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. A financial statement audit also includes assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and December 31, 2006 and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2007 in accordance with Canadian generally accepted accounting principles. Furthermore, in our opinion, the financial statement schedule on the change in the valuation allowance on future income tax assets included in Form 20-F presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

Internal control over financial reporting

We have also audited Æterna Zentaris Inc. s internal control over financial reporting as at December 31, 2007, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the annual report under the title Management s Report on Internal Control over Financial Reporting . Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as at December 31, 2007 based on criteria established in *Internal Control Integrated Framework* issued by the COSO.

Chartered Accountants

Quebec, Quebec, Canada

March 4, 2008

Comments by Auditors for U.S. Readers on Canada-U.S. Reporting Differences

In the United States of America, reporting standards for auditors require the addition of an explanatory paragraph (following the opinion paragraph) when there are changes in accounting principles that have a material effect on the comparability of the Company s financial statements, such as the changes described in note 3 to the consolidated financial statements. Our report to the Shareholders dated March 4, 2008 is expressed in accordance with Canadian reporting standards which do not require a reference to such changes in accounting principles in the auditor s report when the changes are properly accounted for and adequately disclosed in the financial statements.

Chartered Accountants

Quebec, Quebec, Canada

March 4, 2008

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Æterna Zentaris Inc.

Consolidated Balance Sheets

(expressed in thousands of US dollars)

	As at December 31, 2007 $	2006 $
Assets		
Current assets		
Cash and cash equivalents	10,272	8,939
Short-term investments (note 22)	31,115	51,550
Accounts receivable		
Trade	6,170	6,795
Other (note 7)	3,044	2,733
Income taxes		931
Inventory (note 8)	5,406	5,044
Prepaid expenses	3,573	2,631
Future income tax assets (note 18)		21,953
Current assets of discontinued operations (note 5)		1,147
	59,580	101,723
Investment in an affiliated company (note 4)		57,128
Property, plant and equipment (note 10)	7,460	13,001
Long-lived assets held for sale (note 6)	13,999	
Deferred charges and other long-term assets (note 9)	1,441	1,354
Intangible assets (note 11)	30,391	37,351
Goodwill (note 12)	10,492	9,509
Non-current assets of discontinued operations (note 5)		3,425
	123,363	223,491
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 13)	16,084	9,735
Income taxes	23	
Deferred revenues	5,373	5,570
Current portion of long-term debt	775	686
Current liabilities of discontinued operations (note 5)		319
	22,255	16,310
Deferred revenues	3,333	8,468
Long-term debt (note 14)		687
Employee future benefits (note 15)	9,184	8,167
Future income tax liabilities (note 18)		10,365

Non-current liabilities of discontinued operations (note 5)		615
	34,772	44,612
Commitments and contingencies (note 23)		
Shareholders Equity		
Share capital (note 16)	30,566	168,466
Other capital	79,306	6,226
Deficit	(42,997)	(10,114)
Accumulated other comprehensive income	21,716	14,301
	88,591	178,879
	123,363	223,491
Basis of presentation (note 2)		

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

Approved by the Board of Directors

Jürgen Ernst, MBA	Director	Gérard Limoges, FCA	Director

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Æterna Zentaris Inc.

Consolidated Statements of Changes in Shareholders Equity

For the years ended December 31,

(tabular amounts in thousands of US dollars, except common shares data)

	Common shares (number of)	Share capital $	Other capital $	Deficit $	Accumulated other comprehensive income $	Total $
Balance December 31, 2004	**45,670,909**	**127,585**	**6,059**	**(53,795)**	**20,227**	**100,076**
Net earnings for the year				10,571		10,571
Foreign currency translation adjustment					(8,290)	(8,290)
Issued pursuant to the stock option plan						
For cash	25,000	130				130
Conversion option related to convertible term loans			2,129			2,129
Issued shares pursuant to acquisition of Echelon	443,905	2,737				2,737
Share issue expenses		(108)				(108)
Stock based compensation costs			2,286			2,286
Balance December 31, 2005	**46,139,814**	**130,344**	**10,474**	**(43,224)**	**11,937**	**109,531**
Net earnings for the year				33,390		33,390
Conversion of convertible term loans	6,955,088	37,786	(6,339)	(280)		31,167
Foreign currency translation adjustment					4,007	4,007
Foreign currency translation adjustment related to disposal of Atrium					(1,643)	(1,643)
Issued pursuant to the stock option plan						
For cash	22,000	81				81
Ascribed value from Other capital		29	(29)			
Issued pursuant to acquisition of Echelon	23,789	163				163
Issued pursuant to acquisition of a patent from a senior officer (note 21)	28,779	175				175
Share issue expenses		(112)				(112)
Stock based compensation costs			2,120			2,120
Balance December 31, 2006	**53,169,470**	**168,466**	**6,226**	**(10,114)**	**14,301**	**178,879**

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

	Common shares (number of)	Share capital $	Other capital $	Deficit $	Accumulated other comprehensive income	Total
Balance December 31, 2006	**53,169,470**	**168,466**	**6,226**	**(10,114)**	**14,301**	**178,879**
Effect of the application of new accounting standards (note 3)				(587)	(41)	(628)
Distribution of Atrium (note 4)		(137,959)	71,122		(5,624)	(72,461)
Net (loss) for the period				(32,296)		(32,296)
Foreign currency translation adjustment					13,783	13,783
Variation in the fair value of short-term investments, net of income taxes					51	51
Issued pursuant to the stock option plan						
For cash	18,000	33				33
Ascribed value from Other capital		26	(26)			
Disposal of Shares of Echelon (note 5)					(754)	(754)
Stock based compensation costs			1,984			1,984
Balance December 31, 2007	**53,187,470**	**30,566**	**79,306**	**(42,997)**	**21,716**	**88,591**

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

	2007 $	2006 $	2005 $
Accumulated Other Comprehensive Income,			
Consisting of the following:			
Foreign currency translation adjustments	21,706	14,301	11,937
Variation in fair market value of short-term investments, net of income taxes	10		
Accumulated Other Comprehensive income	21,716	14,301	11,937
Deficit	(42,997)	(10,114)	(43,224)
Total Accumulated Other Comprehensive Income and Deficit	(21,281)	4,187	(31,287)

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

Æterna Zentaris Inc.

Consolidated Statements of Earnings

For the years ended December 31,
(expressed in thousands of US dollars, except shares and per share data)

	Years ended December 31, 2007 $	2006 $	2005 $
Revenues	42,068	38,799	44,813
Operating expenses			
Cost of sales, excluding depreciation and amortization	12,930	11,270	8,250
Selling, general and administrative	20,403	16,478	14,403
Research and development costs	39,248	27,422	25,544
Research and development tax credits and grants	(2,060)	(1,564)	(317)
Depreciation and amortization			
Property, plant and equipment	1,562	2,816	1,665
Intangible assets	4,004	6,148	4,279
Impairment of long-lived asset held for sale (note 6)	735		
	76,822	62,570	53,824
Loss from operations	(34,754)	(23,771)	(9,011)
Other revenues (expenses)			
Interest income	1,904	1,441	1,235
Interest expense			
Long-term debt and convertible term loans	(85)	(1,270)	(6,979)
Other		(163)	(31)
Foreign exchange (loss) gain	(1,035)	319	(87)
Loss on disposal of equipment	(28)		
Gain on disposal of a long-term investment		409	
	756	736	(5,862)
Share in the results of an affiliated company		1,575	
Loss before income taxes	(33,998)	(21,460)	(14,873)
Income tax recovery (expense) (note 18)	1,961	29,037	(609)
Net (loss) earnings from continuing operations	(32,037)	7,577	(15,482)
Net (loss) earnings from discontinued operations (notes 4 &5)	(259)	25,813	26,053
Net (loss) earnings	(32,296)	33,390	10,571
Net (loss) earnings per share from continuing operations			
Basic	(0.61)	0.14	(0.34)
Diluted	(0.61)	0.14	(0.34)
Net (loss) earnings per share from discontinued operations			
Basic	(0.00)	0.50	0.57
Diluted	(0.00)	0.48	0.57

Net (loss) earnings per share			
Basic	(0.61)	0.64	0.23
Diluted	(0.61)	0.62	0.23
Weighted average number of shares (note 20)			
Basic	53,182,803	52,099,290	46,139,814
Diluted	53,182,803	52,549,260	46,139,814

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

Æterna Zentaris Inc.

Consolidated Statements of Comprehensive Income

For the years ended December 31,

(expressed in thousands of US dollars, except shares and per share data)

	Years ended December 31,		
	2007	**2006**	**2005**
	$	**$**	**$**
Net earnings (loss) for the period	(32,296)	33,390	10,571
Other comprehensive income:			
Foreign currency translation adjustments	13,783	4,007	(8,290)
Reclassification adjustment related to disposal of Atrium		(1,643)	
Reclassification adjustment related to disposal of Echelon	(754)		
Variation in fair market value of short-term investments, net of income taxes	51		
Comprehensive income (loss)	(19,216)	35,754	2,281

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

Æterna Zentaris Inc.

Consolidated Statements of Cash Flows

(expressed in thousands of US dollars, except shares and per share data)

	Years ended December 31, 2007 $	2006 $	2005 $
Cash flows from operating activities			
Net earnings (loss) for the year	(32,296)	33,390	10,571
Net (earnings) loss from discontinued operations	259	(25,813)	(26,053)
Net earnings (loss) from continuing operations	(32,037)	7,577	(15,482)
Items not affecting cash and cash equivalents			
Depreciation and amortization	5,566	8,964	5,944
Stock-based compensation costs	1,984	2,120	2,286
Future income taxes	(1,868)	(29,160)	520
Gain on disposal of a long-term investment		(409)	
Share in the results of an affiliated company		(1,575)	
Employee future benefits	164	(115)	2,338
Deferred charges and other long term assets	510	(841)	2,707
Deferred revenues	(6,368)	(3,258)	(10,291)
Accretion on long term borrowings	82	1,227	4,479
Loss on disposal of property, plant and equipment	28		
Impairment of long-lived asset held for sale	735		
Foreign exchange loss (gain) on long-term items denominated in foreign currency	641	(587)	381
Change in non-cash operating working capital items (note 17)	4,901	187	4,488
Net cash used in continuing operating activities	(25,662)	(15,870)	(2,630)
Net cash provided by discontinued operating activities	132	23,827	15,564
Net cash provided by (used in) operating activities	(25,530)	7,957	12,934
Cash flows from financing activities			
Repayment of long-term debt	(751)	(718)	(655)
Issuance of shares pursuant to the exercise of stock options	33	81	130
Share issue expenses	(366)	(112)	(108)
Net cash used in continuing financing activities	(1,084)	(749)	(633)
Net cash provided by (used in) discontinued financing activities	(230)	(7,825)	89,558
Net cash provided by (used in) financing activities	(1,314)	(8,574)	88,925
Cash flows from investing activities			
Purchase of short-term investments	(6,180)	(79,300)	(25,945)
Proceeds from sale of short-term investments	33,405	49,267	26,771
Proceeds from sale of a long-term investment		1,387	
Business acquisitions, net of cash and cash equivalents acquired		(32)	(37)
Purchase of property, plant and equipment	(3,702)	(1,845)	(1,114)
Proceeds from sale of property, plant and equipment	729		
Acquisition of amortizable intangible assets	(67)	(5)	(558)
Net cash provided by (used in) continuing investing activities	24,185	(30,528)	(883)
Net cash provided by (used in) discontinued investing activities	2,238	11,878	(94,699)
Net cash provided by (used in) in investing activities	26,423	(18,650)	(95,582)
Effect of exchange rate changes on cash and cash equivalents	1,337	1,356	(2,748)
Net change in cash and cash equivalents	916	(17,911)	3,529

Cash and cash equivalents Beginning of year	9,356	27,267	23,738
Cash and cash equivalents End of year	10,272	9,356	27,267
Cash and cash equivalents related to:			
Continuing operations	10,272	8,939	12,234
Discontinued operations		417	15,033
	10,272	9,356	27,267
Cash and cash equivalents components:	10,195	9,174	27,093
Cash	77	182	174
Cash equivalents	10,272	9,356	27,267

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

Æterna Zentaris Inc.

Notes to Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(tabular amounts in thousands of US dollars,

except share/option and per share/option data and as otherwise noted)

1 Incorporation and nature of activities

Æterna Zentaris Inc. (Æterna Zentaris or the Company), incorporated under the Canada Business Corporations Act, is a global biopharmaceutical company focused on endocrine therapy and oncology with expertise in drug discovery, development and commercialization.

Our pipeline encompasses compounds at all stages of development, from drug discovery through marketed products. The two highest priority clinical programs are our lead value driver, cetrorelix for benign prostatic hyperplasia (BPH) and our lead oncology program, AEZS-108 for endometrial and ovarian cancers.

2 Summary of significant accounting policies

Basis of presentation

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles. These financial statements differ in certain respects from those prepared in accordance with United States generally accepted principles (US GAAP) and do not provide certain disclosures which would be found in US GAAP financial statements, as permitted by the regulations of the Securities and Exchange Commission of the United States. These recognition, measurement differences and disclosure differences as it relates to the Company are described in note 24 Summary of differences between generally accepted accounting principles in Canada and in the United States .

Evaluation of Going Concern, Results of Operations, and Management s Plans:

After reviewing its strategic plan and the corresponding budget and forecasts, management believes that the Company currently has sufficient cash and cash equivalents to fund planned expenditures and execute its focused strategy for at least the next 12 months. Management expects to derive additional cash from potential sale of non-core assets and financing.

Basis of consolidation

These consolidated financial statements include all companies in which the Company, directly or indirectly has more than 50% of the voting rights or over which it exercises control. Companies are included in the consolidation from the date that control is transferred to the Company while companies sold are excluded from the consolidation from the date that control ceases. The purchase method of accounting is used to account for acquisitions. Intercompany transactions, balances and unrealized gains and losses on transactions between the companies included in the basis of consolidation are eliminated.

Investments in affiliated companies

Investments in companies over which the Company is to exercise significant influence, generally participation of between 20% and 50% of the voting rights, but over which it does not exercise control, are accounted for by using the equity method. The Company s share of its affiliated results of operations is recognized in the statement of earnings.

Æterna Zentaris Inc.

Notes to Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(tabular amounts in thousands of US dollars,

except share/option and per share/option data and as otherwise noted)

Accounting estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts of assets and liabilities reported in the financial statements. Those estimates and assumptions also affect the disclosure of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the years. Significant estimates include the allowance for doubtful accounts, provisions for obsolete inventory, future income tax assets and liabilities, the useful lives of property, plant and equipment and intangible assets, the valuation of intangible assets and goodwill, the fair value of options granted and employee future benefits and certain accrued liabilities. Actual results could differ from those estimates.

Foreign currency translation

Reporting currency and self-sustaining subsidiaries

The Company uses the US dollar as its reporting currency. Assets and liabilities of the Company and its self-sustaining subsidiaries whose functional currency is other than the US dollar are translated using the exchange rate in effect at the balance sheet date. Revenues and expenses are translated at the average rate in effect during the year. Translation gains and losses are included in the statement of comprehensive income.

Foreign currency transactions and integrated foreign subsidiaries

The financial statements of integrated foreign operations and transactions denominated in currencies other than the functional currency are re-measured into the functional currency using the temporal method. Under this method, monetary assets and liabilities are re-measured, in the functional currency, at the exchange rate in effect on the date of the balance sheet. Non-monetary assets and liabilities are re-measured at historical rates, unless such assets and liabilities are carried at market, in which case, they are translated at the exchange rate in effect on the date of the balance sheet. Revenues and expenses are re-measured at the monthly average exchange rate. Transaction gains and losses resulting from such re-measurement are reflected in the statements of earnings.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with banks, exclusive of bank advances, as well as all highly liquid short-term investments. The Company considers all highly liquid short-term investments having a term of less than three months at the acquisition date to be cash equivalents.

Æterna Zentaris Inc.

Notes to Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(tabular amounts in thousands of US dollars,

except share/option and per share/option data and as otherwise noted)

Short-term investments

Short-term investments consist mainly of bonds which do not meet the Company s definition of cash and cash equivalents.

In accordance with the new requirements of Canadian Institute Chartered Accountants (CICA) 3855 Financial Instruments , adopted by the Company on January 1, 2007, short-term investments are classified as available-for-sale investments. The Company recognizes transactions on the settlement date. These investments are recognized at fair value. Unrealized gains and losses are recognized, net of income taxes, if any, in Comprehensive income . Upon the disposal or impairment of these investments, these gains or losses are reclassified in the consolidated statement of earnings. See note 3.

Prior to 2007, short-term investments were valued at the lower of amortized cost and market value.

Inventory

Inventory is valued at the lower of cost and market value. Cost is determined using the first in, first out basis. Cost of finished goods and work in progress includes raw materials, labour and manufacturing overhead under the absorption costing method. Market value is defined as replacement cost for raw materials and as net realizable value for finished goods and work in progress.

Property, plant and equipment and depreciation

Property, plant and equipment are recorded at cost, net of related government grants and accumulated depreciation. Depreciation is calculated using the following methods and annual rates:

	Methods	**Annual rates %**

Building	Straight-line	5
Equipment	Declining balance and straight-line	20
Office furniture	Declining balance and straight-line	10 and 20
Computer equipment	Straight-line	25 and 33 1/3
Automotive equipment	Straight-line	20
Leasehold improvements	Straight-line	Remaining lease term

Deferred charges

Deferred charges relate to deferred upfront payments made by a subsidiary in connection with research and development collaborations, and to financing charges with regard to the filing of a shelf-prospectus during 2007. These deferred charges are included in the statement of earnings over the progress of the research and development work related to the contracts and over the term of the convertible term loans, respectively. Financing charges are included in the Share Capital as soon as the financing is completed, at the latest in 2009.

Æterna Zentaris Inc.

Notes to Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(tabular amounts in thousands of US dollars,

except share/option and per share/option data and as otherwise noted)

Intangible assets

Intangible assets with finite useful lives consist of in-process research and development, acquired in business combinations, patents and trademarks, as well as technology and other. Patents and trademarks represent costs, including professional fees, incurred for the filing of patents and the registration of trademarks for product marketing and manufacturing purposes, net of related government grants and accumulated amortization. Intangible assets with finite useful lives are amortized on a straight-line basis over their estimated useful lives of eight to fifteen years for in-process research and development and patents, ten years for trademarks and from three to ten years for technology and other.

Goodwill

Goodwill represents the excess of the purchase price over the fair values of the net assets of entities acquired at the respective dates of acquisition. Goodwill is not amortized and is subject to an annual impairment test, or more frequently if events or changes in circumstances indicate that it might be impaired. Testing for impairment is accomplished mainly by determining whether the fair value of a reporting unit, based upon discounted cash flows, exceeds the net carrying amount of that reporting unit as of the assessment date. If the fair value is greater than the carrying amount, no impairment is necessary. In the event that the carrying amount exceeds the sum of the discounted cash flows, a second test must be performed whereby the fair value of the segment s goodwill must be estimated to determine if it is less than its carrying amount. Fair value of goodwill is estimated in the same way as goodwill is determined at the date of the acquisition in a business combination, that is, the excess of the fair value of the reporting unit over the fair value of the identifiable net assets of the reporting unit.

Impairment of long-lived assets

Property, plant and equipment and intangible assets with finite lives are reviewed for impairment when events or circumstances indicate that costs may not be recoverable. Impairment exists when the carrying value of the asset is greater than the undiscounted future cash flows expected to be provided by the asset. The amount of impairment loss, if any, is the excess of its carrying value over its fair value, which fair value is determined based upon discounted cash flows or appraised values, depending on the nature of assets.

Employee future benefits

The Company s subsidiary in Germany maintains defined contribution and unfunded defined benefit plans as well as other benefit plans for its employees. Its obligations are accrued under employee benefit plans and the related costs. In this regard, the following policies have been adopted:

The cost of pension and other benefits earned by employees is actuarially determined using the projected unit credit method and benefit method prorated on length of service and management s best estimate of salary escalation, retirement ages of employees and employee turnover.

The net actuarial gain (loss) of the benefit obligation is recorded in the statement of earnings as it arises.

For defined contribution plans, the pension expenses recorded in the statement of earnings is the amount of contribution the Company is required to pay for services rendered by employees.

Æterna Zentaris Inc.

Notes to Consolidated Financial Statements

December 31, 2007, 2006 and 2005

(tabular amounts in thousands of US dollars,

except share/option and per share/option data and as otherwise noted)

Deferred revenues

Deferred revenues relate to upfront payments received by a subsidiary in connection with research cooperation agreements. These revenues are included in the statement of earnings based on the progress of the research and development work related to the contracts.

Revenue recognition

The Company is currently in a phase in which potential products are being further developed or marketed jointly with strategic partners. The existing licensing agreements usually foresee one-time payments (upfront payments), payments for research and development services in the form of cost reimbursements, milestone payments and royalty receipts for licensing and marketing product candidates. Revenues associated with those multiple-element arrangements are allocated to the various elements based on their relative fair value. Agreements containing multiple elements are divided into separate units of accounting if certain criteria are met, including whether the delivered element has stand-alone value to the customer and whether there is objective and reliable evidence of the fair value of the undelivered obligation(s). The consideration received is allocated among the separate units based on each unit s fair value or using the residual method, and the applicable revenue recognition criteria are applied to each of the separate units.

License fees representing non-refundable payments received upon the execution of license agreements are recognized as revenue upon execution of the license agreements when the Company has no significant future performance obligations and collectability of the fees is assured. Upfront payments received at the beginning of licensing agreements are not recorded as revenue when received but are amortized based on the progress to the related research and development work. This progress is based on estimates of total expected time or duration to complete the work which is compared to the period of time incurred to date in order to arrive at an estimate of the percentage of revenue earned to date.

Milestone payments, which are generally based on developmental or regulatory events, are recognized as revenue when the milestones are achieved, collectability is assured, and when there are no significant future performance obligations in connection with the milestones.

In those instances where the Company has collected upfront or milestone payments but has ongoing future obligations related to the development of the drug product, management considers the milestone payments and the remaining obligations under the contract as a single unit of accounting. In those circumstances where the collaboration does not require specific deliverables at specific times or at the end of the contract term, but rather the Company s obligations are satisfied over a period of time, revenue recognition is deferred and amortized over the period of its future obligations.

Royalty revenue, based on a percentage of sales of certain declared products sold by third parties, is recorded when the Company has fulfilled the terms in accordance with the contractual agreement, has no future obligations, the amount of the royalty fee is determinable and collection is reasonably assured.

Revenues from sales of products are recognized, net of estimated sales allowances and rebates, when title passes to customers, which is at the time goods are shipped, when there are no future performance obligations, when the purchase price is fixed and determinable, and collection is reasonably assured.

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Stock-based compensation costs

Since January 1, 2003, the Company accounts for all forms of employee stock-based compensation using the fair value-based method.

The fair value of stock options is determined using the Black-Scholes option pricing model and stock-based compensation expense is recognized over the vesting period of the options and credited to Other Capital, and any consideration received by the Company on the exercise of stock options is credited to Share Capital. Other capital component of the stock-based compensation is transferred to Share Capital upon the issuance of shares.

Prior to this date, no stock-based compensation costs were recognized for grants of stock-based awards to employees. However, the Company is required to disclose pro forma information with respect to net earnings and net earnings per share as if stock-based compensation costs were recognized in the financial statements for all reporting years using the fair value-based method for outstanding stock options granted during 2002 (note 16).

Income taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined according to differences between the carrying amounts and tax bases of the assets and liabilities. Future income tax assets and liabilities are measured using substantively enacted and enacted tax rates expected to apply in the years in which the differences are expected to reverse.

The Company establishes a valuation allowance against future income tax assets if, based on available information, it is not more likely than not that some or all of the future income tax assets will be realized.

Research and development costs

Research costs are expensed as incurred. Development costs are expensed as incurred except for those which meet generally accepted criteria for deferral, which are capitalized and amortized against operations over the estimated period of benefit. No costs have been deferred during any periods.

Research and development tax credits and grants

The Company is entitled to scientific research and experimental development (SR&ED) tax credits granted by the Canadian federal government (Federal) and the government of the Province of Québec (Provincial). Federal SR&ED tax credits are earned on qualified Canadian SR&ED expenditures at a rate of 20% and can only be used to offset Federal income taxes otherwise payable. Refundable Provincial SR&ED tax credits are generally earned on qualified SR&ED salaries, subcontracting and university contract expenses incurred in the Province of Québec, at a rate of 17.5%.

SR&ED tax credits and grants are accounted for using the cost reduction method. Accordingly, tax credits and grants are recorded as a reduction of the related expenses or capital expenditures in the period the expenses are incurred. The refundable portion of SR&ED tax credits is recorded in the year in which the related expenses or capital expenditures are incurred and the non-refundable portion of SR&ED tax credits and grants is recorded at such time, provided the Company has reasonable assurance the credits or grants will be realized.

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Earnings (loss) per share

Basic net earnings (loss) per share is calculated using the weighted average number of common shares outstanding during the year.

Diluted net earnings (loss) per share is calculated based on the weighted average number of common shares outstanding during the year, plus the effects of dilutive common share equivalents such as options and convertible term loans. This method requires that diluted net earnings (loss) per share be calculated using the treasury stock method, as if all common share equivalents had been exercised at the beginning of the reporting period, or period of issuance, as the case may be, and that the funds obtained thereby were used to purchase common shares of the Company at the average trading price of the common shares during the period.

3 New accounting standards

Accounting changes

Effective January 1, 2007, the Company adopted CICA Handbook Section 1506 Accounting Changes . This Section establishes criteria for changes in accounting policies, accounting treatment and disclosures regarding changes in accounting policies, estimates and corrections of errors. In particular, this Section allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information. Furthermore, this section requires disclosure of when an entity has not applied a new source of GAAP that has been issued but is not yet effective. Such disclosures are provided below.

Financial instruments

In January 2005, the CICA issued four new accounting standards in relation with financial instruments: section 3855 Financial Instruments Recognition and measurement , section 3865 Hedges , section 1530 Comprehensive Income and section 3251 Equity .

Section 3855 expands on section 3860 Financial Instrument - Disclosure and Presentation , by prescribing when a financial instrument is to be recognized on the balance sheet and at what amount. It also specifies how financial instrument gains and losses are to be presented.

Section 3865 provides alternative treatments to section 3855 for entities which choose to designate qualifying transactions as hedges for accounting purposes. It replaces and expands on Accounting Guideline AcG-13 Hedging Relationships , and the hedging guidance in Section 1650 Foreign Currency Translation by specifying how hedge accounting is applied and what disclosure is necessary when it is applied.

Section 1530 Comprehensive Income introduces a new requirement to temporarily present certain gains and losses outside net income.

Consequently, Section 3250 Surplus has been revised as Section 3251 Equity . Sections 1530, 3251, 3855 and 3865 were adopted by the Company on January 1, 2007.

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Recognition of financial assets and liabilities

Following the adoption of Section 3855, the Company classified its financial instruments as follows:

Cash	Held for trading
Short-term investments	Available-for-sale securities
Accounts receivable	Loans and receivable
Accounts payable and accrued liabilities	Other financial liabilities
Long-term debt	Other financial liabilities

Short-term investments

The short-term investments are classified as available-for-sale investments. The Company recognizes transactions on the settlement date.

These investments are recognized at fair value. Unrealized gains and losses are recognized, net of income taxes, if any, in Comprehensive income . Upon the disposal or impairment of these investments, these gains or losses are reclassified in the consolidated statement of earnings.

As a result of the application of CICA 3855, a difference of $41,000 between the carrying amount and the fair value of investments classified as available-for-sale is recognized as an adjustment to the opening balance of Accumulated other comprehensive income , net of income taxes.

Effective interest rate method

Premiums and discounts on short-term investments and long-term debt are accounted for using the effective interest rate method.

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The impact of the use of the effective interest rate method amounted to $587,000 and was recognized as an adjustment to the opening balance of deficit, net of income taxes.

Transition

The Company has elected to use January 1 2003, as the transition date for embedded derivatives

The recognition, derecognition and measurement methods used other than the adjustment described above for the short-term investments and the long-term debt, have not changed from the methods of periods prior to the effective date of the new standards. Consequently, there were no further adjustments to record on transition.

General standards of financial statement presentation

In May of 2007, the CICA amended Section 1400, General Standards of Financial Statement Presentation to change the guidance related to management s responsibility to assess the ability of the entity to continue as a going concern. Management is required to make an assessment of an entity s ability to continue as a going concern and should take into account all available information about the future, which is at least, but not limited to, 12 months from the balance sheet date. Disclosure is required of material uncertainties related to events or conditions that may cast significant doubt upon the entity s ability to continue as a going concern.

The amendments to Section 1400 apply to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. The Company s management has elected to early adopt this requirement; adoption was effective on January 1, 2007 and the related disclosure is provided in Note 2.

Impact of accounting pronouncements not yet adopted

Capital Disclosure

The CICA issued Section 1535, Capital Disclosures . This standard establishes guidelines for disclosure of information regarding an entity s capital which will enable users of its financial statements to evaluate an entity s objectives, policies and processes for managing capital, including disclosures of any externally imposed capital requirements and the consequences of non-compliance. The new requirements will be effective starting January 1, 2008. Although the new standard provides for additional disclosure only, with no measurement impact, the Company is currently in the process of evaluating the impact that these additional disclosure standards will have on the Company s financial statements.

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Financial Instruments Disclosures and Financial Instruments - Presentation

The CICA issued Section 3862, Financial Instruments Disclosures and Section 3863, Financial Instruments Presentation which replace Section 3861, Financial Instruments Disclosure and Presentation . The new disclosure standard requires the disclosure of additional detail of financial asset and liability categories as well as a detailed discussion on the risks associated with the company s financial instruments. The presentation requirements are carried forward unchanged. These new standards will be effective starting January 1, 2008. Although the new standard provides for additional disclosure only, with no measurement impact, the Company is currently in the process of evaluating the impact that these additional disclosure standards will have on the Company s financial statements.

Inventories

The CICA issued Section 3031, Inventories which will replace existing Section 3030 with the same title. This standard requires that inventories should be measured at the lower of cost and net realizable value, and includes guidance on the determination of cost, including allocation of overheads and other costs. The standard also requires that similar inventories within a consolidated group be measured using the same method. It also requires the reversal of previous write-downs to net realizable value when there is a subsequent increase in the value of inventories. The new Section is effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008. The Company is currently evaluating the impact of this new standard.

Goodwill and intangible assets

In February 2008, the CICA issued Section 3064, Goodwill and intangible assets, replacing Section 3062, Goodwill and other intangible assets and Section 3450, Research and development costs. Various changes have been made to other sections of the CICA Handbook for consistency purposes. The new Sections will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for its fiscal year beginning January 1, 2009. 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. The Company is currently evaluating the impact of the adoption of this new Section on its consolidated financial statements.

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4 Distribution of the remaining interest in Atrium Biotechnologies Inc.

During 2006, the Company completed a lengthy and detailed review process whereby it examined a number of strategic alternatives for how best to pursue and implement its business plan of becoming a pure play biopharmaceutical company with a focus on endocrine therapy and oncology. Among the alternatives considered was the divestiture of Æterna Zentaris interest in Atrium Biotechnologies Inc., now Atrium Innovation Inc. (Atrium) and the resulting focus on advancing its development pipeline.

On September 19, 2006, the Company initiated a Secondary Offering to sell 3,485,000 Atrium Subordinate Voting Shares at a price of CAN$15.80 per share.

On October 18, 2006, the Company closed this Secondary Offering for net proceeds of $45 million. The gain on the disposal of this investment amounted to $29,248,000 including $1,643,000 related to cumulative translation adjustments.

Concurrently with the closing of the Secondary Offering and in accordance with the articles of Atrium, the Company s remaining Atrium Multiple Voting Shares were automatically converted into Atrium Subordinate Voting Shares on a one-for-one basis such that the Company subsequently owned 11,052,996 Atrium Subordinate Voting Shares representing approximately 36.1% of the issued and outstanding shares of Atrium.

As of October 18, 2006, Atrium was excluded from the consolidation since the Company s control ceased. Furthermore, given the distribution of the remaining Atrium shares discussed below, all historical operations and cash flows recorded through the consolidation of Atrium until that date have been reported as discontinued operations and therefore, these operations and cash flows are presented as such in the statement of earnings and in the statement of cash flows.

On December 15, 2006, the Company s shareholders approved a reduction in the stated capital of the Company in an amount equal to the fair market value of its remaining interest in Atrium for the purpose of effecting a special distribution in kind of all 11,052,996 subordinate voting shares of Atrium held by the Company. On January 2, 2007, Æterna Zentaris shareholders received approximately 0.2079 of an Atrium subordinate voting share for each one of their common shares.

This special distribution has been accounted for as a nonreciprocal transfer to shareholders measured at the carrying value of the investment in Atrium on January 2, 2007. As the special distribution is considered as a taxable transaction for the Company and treated as a reduction of the stated capital for tax purposes, the share capital of the Company has been reduced by the fair value of the Atrium shares distributed of $137,959,000, the long-term investment in Atrium $57,128,000 has been removed from the balance sheet and the difference, taking into account the related income taxes of $15,333,000 and cumulative translation adjustment of $5,624,000, has been recorded as Other Capital for an amount of $71,122,000.

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For the years ended December 31, 2007, 2006 and 2005, previously consolidated revenues and expenses of Atrium, representing the former Active Ingredients & Specialty Chemicals Segment as well as the Health & Nutrition Segment, have been reclassified from continuing operations to discontinued operations, as follows:

	Years ended December 31,		
	2007	**2006**	**2005**
	$	**$**	**$**
Revenues		239,535	200,863
Earnings before the following items		28,360	21,414
Gain on disposal of Atrium shares		29,248	
Income tax expense (a)		(19,923)	(6,838)
Gain (loss) on dilution of investments (b)		(628)	19,002
Earnings before non-controlling interest		37,057	33,578
Non-controlling interest		(10,967)	(7,064)
Net earnings from discontinued operations		26,090	26,514

(a) In 2006, an amount of $7,006,000 is related to the gain on disposal of Atrium shares and an amount of $5,692,000 is related to future income tax liabilities on unremitted earnings of Atrium.

(b) Gain (loss) on dilution of investments

Following the exercise of Atrium s stock options, Atrium issued 627,500 subordinate voting shares between January 1 and October 18, 2006. As a consequence, a loss on dilution amounting to $628,000 was recognized.

On April 6, 2005, Atrium completed its Initial Public Offering through the issuance of 4,166,667 subordinate voting shares at a price of CAN$12.00 per share for total gross proceeds of $40,957,000 (CAN$50,000,000). Immediately prior to the closing of the aforementioned offering, Atrium completed the acquisition of the non-controlling interest in Unipex Finance S.A.S. for an amount of $7,289,000. This amount was settled through the issuance of 741,584 subordinate voting shares of Atrium at the offering price of CAN$12.00 per share. Moreover, pursuant to the acquisition of Douglas Laboratories by Atrium in December 2005, Atrium issued 917,532 subordinate voting shares at a price of CAN$10.95 per share. Following the exercise of Atrium s stock options during 2005, Atrium also issued 387,000 subordinate voting shares at an average price of CAN$2.28 for total proceeds of $884,000. As a consequence of these transactions, the Company s economic interest in Atrium decreased from 61.1% to 48.46%, generating a gain on dilution of investments amounting to $19,002,000.

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5 Acquisition and disposal of Echelon Biosciences Inc.

On January 1, 2005, the Company completed the acquisition of 100% of the issued and outstanding common shares of Echelon Biosciences Inc. (Echelon) for a total consideration of $2,935,522, of which an amount of $36,718 including all acquisition-related costs, was paid cash, net of cash and cash equivalents acquired of $161,734, and the balance was paid through the issuance of 443,905 common shares of the Company, the price per share corresponded to the weighted moving average trading prices of the Company for the last fifteen consecutive trading days ending on December 31, 2004. The acquisition was subject to contingent payments specified in the agreement for an approximate amount of $3,500,000 of which an amount of $2,900,000 was payable in shares and the balance of $600,000 payable in cash at the latest in January 2008, based on contractual conditions being met. During 2005, an amount of $196,000 had been recorded as contingent consideration payable, thus having the effect of increasing goodwill. This amount has been settled through a cash payment of $32,000 and the issuance of 23,789 common shares of the Company. As of January 1, 2008 the remaining conditions were not met, and as such, no additional consideration will be paid.

During 2007, the Company continued its review process whereby it examined a number of strategic alternatives for how best continue the pursuit and implementation of its business plan of becoming a pure play biopharmaceutical company with a focus on endocrine therapy and oncology. Among the alternatives considered was the divestiture of Æterna Zentaris investment in Echelon and the resulting focus on advancing its development pipeline.

At September 30, 2007, the Company performed a preliminary impairment test on the goodwill related to Echelon. According to the preliminary test results, an estimated impairment loss of $500,000 was recorded.

On November 30, 2007, Æterna Zentaris sold all issued and outstanding shares of Echelon to Frontier Scientific, Inc. for an upfront payment of $2,600,000 and a $600,000 contingent consideration. From that date, Echelon was excluded from the consolidation, and all historical operations and cash flows recorded through the consolidation of Echelon until that date have been reported as discontinued operations. The contingency consideration is based on the Echelon reaching specific sales levels in 2008 and 2009.

For the years ended December 31, 2007, 2006 and 2005, consolidated revenues and expenses of Echelon have been reclassified from continuing operations to discontinued operations, as follows:

	Years ended December 31,		
	2007	**2006**	**2005**
	$	**$**	**$**
Revenues	2,358	2,593	2,391
Loss before the following items	(206)	(369)	(577)
Goodwill impairment	(500)		
Loss on disposal of Echelon shares, net of cumulative translation adjustment	(44)		
Income tax recovery	491	92	116
Net loss from discontinued operations	(259)	(277)	(461)

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Major classes of assets and liabilities as of December 31, 2006 have been reclassified and are presented as discontinued operations as follows:

	$
Assets	
Current assets	
Cash	417
Other current assets	730
Current assets of discontinued operations	1,147
Intangible assets	1,755
Goodwill	1,239
Property, Plant & Equipment	431
Non-current assets of discontinued operations	3,425
	4,572
Liabilities	
Current liabilities of discontinued operations	319
Long-term debt	17
Future Income Tax Liabilities	598
Non-current liabilities of discontinued operations	615
	934

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6 Long-lived assets held for sale

During 2007, the Company continued its review process whereby it examined a number of strategic alternatives for how best continue the pursuit and implementation of its business plan of becoming a pure play biopharmaceutical company with a focus on endocrine therapy and oncology. As part of its strategy to finance with non-dilutive vehicles, using non-core assets, the Company decided to dispose of its building and land located in Quebec City, as well as its rights to intangible property, Impavido (Miltefosine) and certain equipment. As at December 31, 2007, the assets reclassified as long-lived assets held for sale , are as follows:

Asset	Cost	Accumulated depreciation and amortization	Net Book Value
	$	$	$
Building and Land	11,181	3,919	7,262
Equipment	1,347	1,164	183
Intangible property	11,851	5,297	6,554
Total assets held for sale	24,379	10,380	13,999

The Company estimates that the net realizable value of all the assets exceeds their carrying value. Furthermore, at the time when the assets were considered held for sale, all amortization or depreciation ceased.

Following an estimation of the fair value by Management after having received certain preliminary offers by third parties, the Company recorded an impairment charge of $735,000 (CAN$729,000) against the asset related to the building and land held for sale. The Company expects to complete a sale transaction in the first six months of 2008.

In 2006, following the decision to terminate the pharmaceutical development of one of its products, the Company recorded an impairment on related manufacturing equipment in order to bring it down to its fair value, which was based on the Company s best estimate of the realisable value. Accordingly, during 2006, an amount of $1,060,856 has been recorded as an impairment loss included in depreciation of property, plant and equipment. The Company sold some of these assets in 2007 and is now actively in the process of selling the remainder of this equipment and estimates that the assets will be sold within the next year, at a net selling price which exceeds their carrying value.

On March 1, 2008, the Company entered into a definite purchase and sale agreement with respect to all rights related to the manufacture, production, distribution, marketing, sale and/or use of Impavido® (miltefosine) with Paladin Labs Inc., for an aggregate purchase price of approximately $9,200,000 (CAN$9,125,000) payable in cash, subject to certain post-closing purchase price adjustments.

Completion of the transactions contemplated by the purchase agreement is subject to customary closing conditions, including the parties having received certain third-party consents and approvals. The sale is anticipated to be finalized early in the first six months of 2008.

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7 Other receivables

	As at December 31, 2007 $	2006 $
Interest	272	592
Grants *	1,060	857
Research and development tax credits recoverable	252	103
Commodity taxes	453	880
Other	1,007	301
	3,044	2,733

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* These grants represent a holdback of a contribution from a federal program called Technology Partnerships Canada (TPC). The Company received a contribution equivalent to 30% of the eligible expenses incurred by the Company in the development of an angiogenesis inhibitor in oncology, dermatology and ophthalmology. Since the pharmaceutical development has been terminated, the Company does not expect to make any reimbursements in connection with this program.

8 Inventory

	As at December 31, 2007 $	2006 $
Raw materials	3,399	3,233
Work in progress	1,602	1,070
Finished goods	405	741
	5,406	5,044

9 Deferred charges and other long-term assets

	As at December 31,	
	2007	**2006**
	$	**$**
Deferred charges	1,051	1,151
Other	390	203
	1,441	1,354

Included in the above deferred charges is $392,000 of cost related to the filing of a shelf prospectus on September 19, 2007.

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10 Property, plant and equipment

	As at December 31, 2007		2006	
	Cost $	Accumulated depreciation $	Cost $	Accumulated depreciation $
Land			52	
Building (note 6)			11,031	3,280
Equipment	9,379	3,923	10,997	6,867
Office furniture	1,261	648	641	492
Computer equipment	1,174	805	1,047	840
Automotive equipment	38	36	32	30
Leasehold improvements	1,170	150	719	9
	13,022	5,562	24,519	11,518
Less:				
Accumulated depreciation	5,562		11,518	
Net amount	7,460		13,001	

11 Intangible assets

	As at December 31,			
	2007		2006	
	Cost $	Accumulated amortization $	Cost $	Accumulated Amortization $
In-process research and development, patents and trademarks (note 6)	47,758	17,514	55,388	18,187
Technology and other	740	593	619	469
	48,498	18,107	56,007	18,656
Less: Accumulated amortization	18,107		18,656	
Net amount	30,391		37,351	

In 2006, following the decision to terminate the pharmaceutical development of certain products, the Company recorded an impairment on certain patents and trademarks. Accordingly, an amount of $1,815,172 has been recorded as an impairment loss included in amortization of intangible assets.

The amortization expense for intangible assets in each of the next five fiscal years will amount to $3,191,000 in 2008, $3,181,000 in 2009, $3,153,000 in 2010, 2011 and 2012.

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12 Goodwill

The change in the carrying value is as follows:

	Continuing operations $	Discontinued operations $
Balance as at December 31, 2005	8,559	110,610
Acquisitions		6,623
Adjustments		(2,109)
Impact of foreign exchange rate	950	2,520
Reduction of goodwill related to the sale of shares of Atrium (note 4)		(116,405)
Balance as at December 31, 2006	9,509	1,239
Impact of foreign exchange rate	983	212
Reduction and impairment of goodwill related to disposal of Echelon (note 5)		(1,451)
Balance as at December 31, 2007	10,492	

13 Accounts payable and accrued liabilities

	As at December 31, 2007 $	2006 $
Trade payable	11,404	6,962
Salaries and employee benefits	1,628	1,095
Other accrued liabilities	3,052	1,678
	16,084	9,735

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14 Long-term debt

	As at December 31,	
	2007	**2006**
	$	**$**
Loan from the federal and provincial governments, nominal value of CAN$800 discounted at an effective rate of 8.43% (CAN $769 in 2007, and CAN$1,600 in 2006) non-interest bearing, payable in five annual equal and consecutive instalments since July 2004.	775	1,373
Less: Current portion	775	686
		687

The principal instalment due on long-term debt for the next year amounts to $775,000 in 2008.

15 Employee future benefits

The Company s subsidiary in Germany provides unfunded defined benefit pension plans and unfunded postemployment benefit plans for some groups of employees. Provisions for pension obligations are established for benefits payable in the form of retirement, disability and surviving dependant pensions.

The following table provides a reconciliation of the changes in the plans accrued benefits obligations:

	Pension benefit plans			Other benefit plans		
	2007	2006	2005	2007	2006	2005
	$	$	$	$	$	$
Obligation Beginning of year	7,547	6,932	5,634	620	523	398
Current service cost	352	293	200	29	39	23
Interest cost	269	293	269	52	22	19
Actuarial loss (gain)	(490)	(674)	1,748	104	53	182
Benefits paid	(70)	(64)	(65)	(81)	(70)	(43)
Effect of foreign currency exchange rate changes	782	767	(854)	70	53	(56)
Obligation End of year	8,390	7,547	6,932	794	620	523
Expenses (recovery) recognized	131	(88)	2,217	185	114	224

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The significant actuarial assumptions adopted to determine the Company s accrued benefits obligations are as follows:

	Pension benefit plans			Other benefit plans		
Actuarial assumptions	**2007**	**2006**	**2005**	**2007**	**2006**	**2005**
	%	%	%	%	%	%
Discount rate for expenses	4.50	4.00	5.25	4.50	4.00	5.25
Discount rate for liabilities	5.70	4.50	4.00	5.70	4.50	4.00
Pension benefits increase	2.00	1.25	1.25	2.00	1.25	1.25
Rate of compensation increase	2.75 to 3.75	2.75 to 3.75	2.75 to 3.75	2.75	2.75	2.75

The last actuarial reports give effect to the pension and postemployment benefit obligations as at December 31, 2007. The next actuarial reports are planned for December 2008.

In accordance with the assumptions used as at December 31, 2007, the benefits expected to be paid in each of the next five fiscal years will amount to $135,114 in 2008, $303,725 in 2009, $307,736 in 2010, $349,426 in 2011 and $474,368 in 2012. Furthermore, total benefits amounting to $2,707,485 are expected to be paid from 2013 to 2017.

Cash required in the next year to fund the plans will approximate the amount of expected benefits.

Defined contribution plans

Total expenses amount to $285,824 in 2007 ($263,810 in 2006 and $215,788 in 2005) for defined contribution pension plans.

The Company also sponsors a 401K plan in its U.S. subsidiary. Under this plan, the Company may contribute a discretionary amount equal to a percentage of employee contributions to the plan and may also make discretionary profit sharing contribution. During the year ended December 31, 2007, the Company did not record any contribution.

Total cash payments for employee future benefits in 2007, consisting of cash contributed by the Company to its defined contribution plans as well as direct payments to retired employees, amount to $436,696 ($398,340 in 2006 and $323,382 in 2005).

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16 Share capital

(a) Authorized

Unlimited number of shares of the following classes:

Common, voting and participating, one vote per share

Preferred, first and second ranking, issuable in series, with rights and privileges specific to each class.

As at December 31, 2007, there are no preferred shares issued and outstanding.

(b) Issued

	As at December 31, 2007		2006		2005	
	Number	**Amount $**	**Number**	**Amount $**	**Number**	**Amount $**
Common shares						
Balance Beginning of year	53,169,470	168,466	46,139,814	130,344	45,670,909	127,585
Conversion of convertible term loans			6,955,088	37,786		
Issued pursuant to the stock option plan	18,000	33	22,000	81	25,000	130
Ascribed value from Other Capital		26		29		
Issued pursuant to the acquisition of a patent from a senior officer (note 21)			28,779	175		
Issuance pursuant to acquisition of Echelon			23,789	163	443,905	2,737
Reduction of the stated capital (note 4)		(137,959)				
Share issue expenses				(112)		(108)
Balance End of year	53,187,470	30,566	53,169,470	168,466	46,139,814	130,344

(c) Common share issues

Pursuant to the exercise of stock options, the Company issued, during fiscal 2007, 18,000 common shares for total proceeds of $33,200. In the prior fiscal year 2006, 22,000 common shares were issued for total proceeds of $81,000. Consequently, stock-based compensation costs of $26,000 ($29,000 in 2006) relating to those exercised options have been reclassified from other capital to share capital.

On February 14 and 17, 2006, the Solidarity Fund QFL (the Fund) and SGF Santé inc. (SGF) have respectively exercised their right to early convert the entirety of their convertible term loans in the principal amount of CAN$12.5 million each that they had extended to the Company in April 2003 and that were to mature on March 31, 2006. In accordance with the terms of the convertible term loans, and additional arrangements between the Company, the Fund and SGF, Æterna Zentaris has issued to each of the loan holders 3,477,544 of its common shares upon conversion of their loans, representing the principal and interest due to the stated maturity date under the loans, based on the conversion price that had been agreed upon in the loan agreements.

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For accounting purposes, the convertible term loans are separated between debt and equity, the equity portion representing the value of the holders conversion options. As a consequence of this transaction, the Company recorded a loss on settlement of long-term debt amounting to $599,190, representing an inducement to the original terms of the loan agreements. An amount of $280,000 was recorded in the statement of deficit, and the remainder was charged to expense in the statement of earnings and was included in the accretion on convertible term loans in the statement of cash flows.

(d) Shareholder right plan

On March 29, 2004, the Company adopted a shareholder right plan (the Rights Plan). The continuation of the Rights Plan and its amendments and restatement has been approved by the Board of Directors on March 5, 2007. The rights issued to the shareholders under the Rights Plan will be exercisable, under certain conditions, only when a person or entity, including any related party(ies), acquires or announces his (its) intention to acquire more than twenty (20) percent of the outstanding common shares of the Company (as such, shares may be redesignated or reclassified) without complying with the permitted bid provisions of the Rights Plan or without approval of the Company s Board of Directors. Should such an acquisition occur, each right would, upon exercise, entitle a holder, other than the person pursuing the acquisition together with its related party(ies), to purchase common shares of the Company at a fifty (50) percent discount to the market price of the Company s shares at that time.

(e) Company s stock option plan

In December 1995, the Company s Board of Directors adopted a stock option plan (the Stock Option Plan) for its directors, senior executives, employees and other collaborators providing services to the Company. The number of shares that are issuable under the Stock Option Plan was amended by a resolution adopted by the shareholders on May 2, 2007. This resolution increased the Plan s limit specifying the limit of options from 4,543,744 to ten percent (10%) of the outstanding shares.

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On May 23, 2007, the Toronto Stock Exchange accepted a stock option pool totalling $5,317,947. In 2007, 870,000 options were granted in U.S. dollars and 815,000 options were granted in Canadian dollars. Options granted under the Stock Option Plan expire after a maximum period of ten years following the date of grant. Options granted under the Stock Option Plan generally vest over a three-year period. The following table summarizes the stock option activity under the Stock Option Plan:

	2007		2006		2005	
Canadian dollar denominated awards	**Number**	**Weighted average exercise price (CAN$)**	**Number**	**Weighted average exercise price (CAN$)**	**Number**	**Weighted average exercise price (CAN$)**
Balance Beginning of year (*)	3,490,092	4.00	3,843,592	6.16	3,480,592	6.58
Granted	815,000	3.24	45,000	6.41	686,500	5.63
Exercised	(18,000)	1.96	(22,000)	3.98	(25,000)	6.31
Expired			(346,000)	7.68	(65,000)	8.34
Forfeited	(151,000)	4.93	(30,500)	6.21	(233,500)	10.31
Balance End of year	4,136,092	3.83	3,490,092	6.02	3,843,592	6.16
Options exercisable End of year	3,300,593	4.02	2,736,099	5.88	2,260,930	6.17

(*) Following the one-time distribution of the Company s remaining interest in Atrium on January 2, 2007 and as contemplated under the Stock Option Plan (see note 4), the Board of Directors of the Company approved an equitable adjustment to all unexercised options outstanding pursuant to the Stock Option Plan. The adjustment was a reduction in the exercise price of all outstanding stock options of CAN$2.02 per common share. Furthermore, in 2007 the Board of Directors approved the extension of the option period from 1 month to 3 years on 875,000 options in connection with the departure of executive members.

The total intrinsic value for stock options exercised amounted to CAN$24,040 in 2007 (CAN$68,959 in 2006 and CAN$28,750 in 2005) There is no tax benefit realized by the Company as the compensation cost related to stock options is not deductible for income tax purposes.

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The following table summarizes the stock options outstanding as at December 31, 2007:

	Options outstanding			
Exercise price (CAN$)	**Number**	**Weighted average remaining contractual life (years)**	**Weighted average exercise price (CAN$)**	**Global intrinsic value**
1.68 to 2.50	1,311,593	6.74	1.88	Nil
2.51 to 3.75	1,062,500	6.13	3.56	Nil
3.76 to 5.50	669,666	7.12	4.47	Nil
5.51 to 6.00	798,000	6.27	5.83	Nil
6.01 to 8.88	294,333	4.41	6.59	Nil
	4,136,092	6.39	3.83	Nil

	Options currently exercisable		
Exercise price (CAN$)	**Number**	**Weighted average exercise price (CAN$)**	**Global intrinsic value**
1.68 to 2.50	939,924	1.91	Nil
2.51 to 3.75	862,498	3.56	Nil
3.76 to 5.50	405,838	4.44	Nil
5.51 to 6.00	798,000	5.83	Nil
6.01 to 8.88	294,333	6.59	Nil
	3,300,593	4.02	Nil

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	2007		2006		2005	
US dollar denominated awards	**Number**	**Weighted average exercise price (US$)**	**Number**	**Weighted average exercise price (US$)**	**Number**	**Weighted average exercise price (US$)**
Balance Beginning of year						
Granted	870,000	2.79				
Balance End of year	870,000	2.79				
Options exercisable End of year						

	Options outstanding			
Exercise price (US$)	**Number**	**Weighted average remaining contractual life (years)**	**Weighted average exercise price (US$)**	**Global intrinsic value**
1.68 to 2.50	375,000	9.95	1.82	Nil
2.51 to 3.75	470,000	9.27	3.50	Nil
3.76 to 5.50	25,000	9.35	3.96	Nil
	870,000	9.56	2.79	Nil

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As at December 31, 2007, the total compensation cost related to nonvested stock options not yet recognized amounted to $1,366,409 ($1,071,651 in 2006). This amount is expected to be recognized over a weighted average period of 1.88 years (1.34 years in 2006).

The Company settles stock options exercised through the issuance of common shares from treasury.

The factors considered in developing the assumptions used in the Black-Scholes option pricing model are the following:

(a) The risk-free interest rate is based on Canadian Government Bond constant maturity interest rate whose term is consistent with the expected life of the stock options.

(b) The historical volatility of the Company s stock price as well as future expectations are used to establish the expected stock price volatility.

(c) The Company estimates the expected life of stock options based upon employee s historical data related to the exercise of stock options and post-vesting employment terminations.

Assumptions used in determining stock-based compensation costs

The table below shows the assumptions used in determining stock-based compensation costs under the Black-Scholes option pricing model:

	Years ended December 31, 2007	2006	2005
Dividend yield	Nil	Nil	Nil
Expected volatility	57.2%	58.1%	62.1%
Risk-free interest rate	3.88%	4.06%	3.92%
Expected life (years)	4.62	5.77	5.80
Weighted average grant date fair value	US$1.93 and CAN$2.25	CAN$3.67	CAN$3.33

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Had compensation costs been determined using the fair value method at the date of grant for awards granted in 2002 under this stock option plan, the Company s pro forma net earnings, basic and diluted net earnings per share after giving effect to the grant of these options in 2002 are:

	Year ended December 31, 2005 $
Pro forma net earnings	10,429
Pro forma net earnings per share	
Basic	0.23
Diluted	0.23

17 Statements of cash flows

	Years ended December 31, 2007 $	2006 $	2005 $
Change in non-cash operating working capital items			
Accounts receivable	1,371	2,686	1,474
Inventory	148	650	(534)
Prepaid expenses	(708)	263	(802)
Accounts payable and accrued liabilities	5,340	1,848	4,977
Income taxes	(1,250)	(5,260)	(627)
	4,901	187	4,488

See note 4 for details related to non-cash transactions of the distribution of the remaining interest in Atrium.

	Years ended December 31, 2007 $	2006 $	2005 $
Additional information			
Interest paid			
From continuing operations		4	34
From discontinued operations	9	7,784	1,908
Income taxes paid (recovered)			
From continuing operations	(937)	5,756	709
From discontinued operations	7	8,698	6,084

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18 Income taxes

The reconciliation of the combined Canadian federal and Québec provincial income tax rate to the income tax (expense) recovery from continuing operations is as follows:

	Years ended December 31, 2007	2006	2005
Combined federal and provincial statutory income tax rate	32.02%	32.02%	31.02%
Income tax recovery based on statutory income tax rate	$ 10,886	$ 6,872	$ 4,613
Change in valuation allowance	(6,963)	22,644	(5,403)
Accretion on convertible term loans		(258)	(1,448)
Stock-based compensation costs	(635)	(679)	(739)
Difference in statutory income tax rate of foreign subsidiaries	(16)	994	(133)
Change in enacted rate used	(1,345)	2,428	2,780
Tax loss consolidation strategy (note 21)		(2,376)	(827)
Other	34	(588)	548
	$ 1,961	$ 29,037	$ (609)

Loss before income taxes

The loss before income taxes from continuing operations is allocated as follows:

	2007 $	2006 $	2005 $
Canada	(10,556)	(10,436)	(15,983)
Germany	(23,276)	(11,024)	1,110
United States	(166)		
	(33,998)	(21,460)	(14,873)

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	Years ended December 31,		
	2007	**2006**	**2005**
	$	**$**	**$**
Income tax recovery (expense) is represented by:			
Current	93	(123)	(89)
Future	1,868	29,160	(520)
	1,961	29,037	(609)
Current			
Foreign	93	(123)	(89)
Future			
Domestic	(284)	25,036	
Foreign	2,152	4,124	(520)
	1,868	29,160	(520)
	1,961	29,037	(609)

Foreign operations are predominantly in Germany.

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Significant components of future income tax assets and liabilities are as follows:

	As at December 31, 2007 $	2006 $
Future income tax assets		
Current		
Deferred revenues	1,738	2,303
Inventory	658	157
Operating losses carried forward		17,996
Research and development costs		1,497
	2,396	21,953
Long-term		
Research and development costs	12,119	11,425
Share issue expenses	91	229
Operating losses carried forward	17,145	7,101
Property, plant and equipment	1,973	1,455
Intangible assets and goodwill	206	206
Employee future benefits	648	966
Deferred revenues	1,211	3,658
Other	144	
	33,537	25,040
Valuation allowance	(23,289)	(13,337)
	10,248	11,703
	12,644	33,656
Future income tax liabilities		
Long-term		
Accounts receivable	48	11
Investment in an affiliated company		5,829
Property, plant and equipment	190	121
Deferred charges and other long-term assets	2,434	604
Intangible assets	9,376	14,798
Investment tax credits	573	629
Other	23	76

	12,644	22,068
Future income tax assets (liabilities), net		11,588
Classified as follows:		
Future income tax assets		21,953
Future income tax liabilities		(10,365)
		11,588

As at December 31, 2007, the Company has estimated non-refundable research and development tax credits of $7,004,150 which can be carried forward to reduce Canadian federal income taxes payable and expire from 2011 to 2027. No tax benefit has been accounted for in connection with those credits.

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As at December 31, 2007, the Company had available operating losses in Canada. The following table summarizes the year of expiry of these operating losses by tax jurisdiction:

	Canada	
Year of expiry	**Federal** **$**	**Provincial** **$**
2010	3,275	Nil
2014	9,801	Nil
2015	6,936	Nil
	20,012	Nil

Furthermore, the Company had available operating losses in Germany amounting to $45M for which there is no expiry date.

The carryforwards and the tax credits claimed could be subjected to a review and a possible adjustment by tax authorities.

19 Segment information for continuing operations

Subsequent to the divestiture in Atrium in 2006, the Company operates in one single operating segment, being the biopharmaceutical segment.

Information by geographic region

Revenues by geographic region are detailed as follows:

	Years ended December 31,		
	2007	**2006**	**2005**
	$	**$**	**$**
Canada	400	25	103
United States	5,911	4,094	4,553
Europe			
Switzerland	23,316	20,681	19,567
United Kingdom	5,343	5,257	6,707
Netherlands	2,031	1,748	11,720
Other	70	809	108
Japan	1,862	6,114	
Other	3,135	71	2,055
	42,068	38,799	44,813

Revenues have been allocated to geographic regions based on the country of residence of the related customers.

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Customers who represent more than 10% of revenues are as follows:

	2007	**2006**	**2005**
	%	**%**	**%**
Customer 1	59	52	44
Customer 2	13	13	26
Customer 3	5	9	15

The following table presents revenues by source:

	2007	**2006**	**2005**
	$	**$**	**$**
Revenues			
Sales and royalties	28,825	25,123	21,252
License fees	12,843	13,652	23,530
Other	400	24	31
	42,068	38,799	44,813

Long-lived assets by geographic region are detailed as follows:

	Years ended December 31,	
	2007	**2006**
	$	**$**
Canada	7,643	8,821
United States	841	11
Germany	53,858	51,029
	62,342	59,861

Long-lived assets consist of property, plant and equipment, long-lived assets held for sale, intangible assets and goodwill.

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20 Earnings (loss) per share

The following table sets forth the computation of basic and diluted net earnings (loss) per share:

	2007 $	2006 $	2005 $
Net earnings (loss) from continuing operations	(32,037)	7,577	(15,482)
Net earnings (loss) from discontinued operations	(259)	25,813	26,053
Impact of assumed conversion of dilutive stock options of Atrium		(754)	(552)
Net earnings (loss) from discontinued operations, adjusted for dilution effects	(259)	25,059	25,501
Net earnings (loss) adjusted for dilution effects	(32,296)	32,636	10,019
Basic weighted average number of shares outstanding	53,182,803	52,099,290	46,139,814
Dilutive effect of stock options	500,171	449,970	286,868
Diluted weighted average number of shares outstanding	53,682,974	52,549,260	46,426,682
Items excluded from the calculation of diluted net earnings (loss) per share because the exercise price was greater than the average market price of the common shares or due to their anti-dilutive effect			
Stock options	3,164,499	1,893,539	2,169,697
Common shares which would have been issued following the conversion of the convertible term loans		776,237	6,043,564

For the years ended December 31, 2007 and 2005, the diluted amounts per share were the same amounts as the basic amounts per share since the dilutive effect of stock options and convertible term loans was not included in the calculation; otherwise, the effect would have been anti-dilutive. Accordingly, the diluted amounts per share for those years were calculated using the basic weighted average number of shares outstanding.

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21 Related party transactions

	2007 $	2006 $	2005 $
Administrative revenues	Nil	35	33
Lease revenues	Nil	304	248
Subcontracting revenues and sales of raw materials	Nil	66	92
Subcontracting expenses	Nil	44	337
Patent acquired from a senior officer	Nil	175	

On December 15, 2006, the Company s shareholders approved a reduction in the stated capital of the Company in an amount equal to the fair market value of its remaining interest in Atrium for the purpose of effecting a special distribution in kind of all 11,052,996 Subordinate Voting Shares of Atrium held by the Company. This transaction was completed on January 2, 2007, thus eliminating the related party relationship.

These above transactions in 2006 and 2005 with our former subsidiary Atrium and a senior officer were in the normal course of operations. They were measured at the exchange amount, which is the amount of consideration established and agreed upon by the related parties. The price of the shares issued for the acquisition of the patent was based on the closing trading price of the Company s shares on February 28, 2006, being the day before the signing of the agreement.

The transactions with Atrium include amounts that occurred before October 18, 2006 and that were previously eliminated from the consolidated financial statements but which will continue to occur after the disposal.

At the end of the year 2006, amounts due to and (from) the former subsidiary were payable (redeemable) on demand and resulted from the transactions mentioned above.

Tax loss consolidation strategy

On September 15, 2005, the Company obtained a one-day loan of $129 million from a financial institution to advance $129 million to its former subsidiary Atrium by way of a subordinate 7% interest-bearing promissory note. This note was unsecured and payable on demand.

On the same day, Atrium acquired $129 million in preferred shares from 4296672 Canada Inc., a wholly-owned subsidiary of the Company. The dividend rate on the preferred shares was 7.05%. 4296672 Canada Inc. used the proceeds to advance $129 million to the Company through an interest-free loan, payable on demand. Then, the funds were used by the Company to repay the one-day loan to the financial institution.

With respect to that arrangement that terminated in October 2006, when the Company ceased to be the controlling shareholder of Atrium, we had received a tax ruling delivered by Canada Revenue Agency. All transactions have been eliminated during the consolidation process and income tax savings resulting from the interest expense deduction have been presented as discontinued operations.

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22 Financial instruments

Short-term investments

	2007 $	2006 $
Discount notes bearing interest at effective annual rates ranging from 3.94% to 4.23% in 2007 and at an annual rate of 4.29% to 4.31% in 2006, maturing on different dates from May to December 2008, in 2006 investments matured from March to June 2007.	5,178	8,649
Bonds, bearing interest at effective annual rates ranging from 2.81% to 4.43% in 2007 and from 2.81% to 4.43% in 2006, maturing on different dates from January to November 2008; and in 2006 from March 2007 to November 2008	25,937	42,901
	31,115	51,550

Short-term investments totalled CAN$30,844,000 in 2007 and CAN$60,076,000 in 2006.

Fair value

Cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities are financial instruments whose fair value approximates their carrying value due to their short-term maturity. The fair value of short-term investments is $31,115,066 ($51,589,289 in 2006). The fair value of long-term debt has been established by discounting the future cash flows at an interest rate corresponding to that which the Company would currently be able to obtain for loans with similar maturity dates and terms. The approximate fair value of long-term debt is $775,000 ($1,342,000 in 2006).

Foreign currency risk

Since the Company operates on an international scale, it is exposed to currency risks as a result of potential exchange rate fluctuations. As at December 31, 2007 and 2006, there are no significant forward exchange contracts outstanding.

Credit risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, short-term investments and accounts receivable. Cash and cash equivalents are maintained with high-credit quality financial institutions. Short-term investments consist primarily of bonds issued by high-credit quality institutions and corporations. Consequently, management considers the risk of non-performance related to cash and cash equivalents and short-term investments to be minimal.

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Generally, the Company does not require collateral or other security from customers for trade accounts receivable; however, credit is extended following an evaluation of creditworthiness. In addition, the Company performs on-going credit reviews of all its customers and establishes an allowance for doubtful accounts when accounts are determined to be uncollectible. Allowance for doubtful accounts amounted to $nil and $7,000 as at December 31, 2007 and 2006, respectively.

Interest rate risk

The Company s exposure to interest rate risk is as follows:

Cash and cash equivalents	Variable interest rate
Short-term investments	Fixed interest rate
Accounts receivable	Non-interest bearing
Accounts payable and accrued liabilities	Non-interest bearing
Long-term debt	Non-interest bearing

23 Commitments, contingencies and guarantee

The Company is committed to various operating leases for its premises plus service and manufacturing contract as follows:

Year	**Minimum Lease Commitments $**	**Service & Manufacturing Commitments $**	**Total Commitments $**
2008	2,092	13,295	15,387
2009	2,172	6,652	8,824
2010	2,092	300	2,392
2011	2,098		2,098
2012 and beyond	2,072		2,072
Total	10,526	20,247	30,773

Rent expenses for operating leases, which may have escalating rentals over the term of the lease, are recorded on a straight-line basis over the term of the lease. The rent expense under the operating leases for the periods ending December 31, 2007, 2006 and 2005 was respectively $1,937,000, $1,878,000 and $1,545,000.

In October 2004, the Company entered into a $2.5 M (1.75 M) bank guarantee in favour of one of its landlords in Germany with respect to the Company s lease obligation. This guarantee will mature in 2009.

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Contingencies

In the normal course of operations, the Company may become involved in various claims and legal proceedings mainly related to contract terminations, employee lay-offs and other employee-related matters. As at December 31, 2007 there are no known or anticipated contingencies or disputes pending against the company.

24 Summary of differences between generally accepted accounting principles in Canada and in the United States

As a company listed on the NASDAQ Global Market, the Company is required to reconcile its financial statements for significant measurement differences between generally accepted accounting principles as applied in Canada (Canadian GAAP) and those applied in the United States (U.S. GAAP). Furthermore, additional significant disclosures required under U.S. GAAP and Regulation S-X of the Securities and Exchange Commission in the United States (SEC) are also provided in the accompanying financial statements and notes. The following summarizes the significant quantitative differences between Canadian and U.S. GAAP, as well as other significant disclosures required under U.S. GAAP and Regulation S-X of the SEC not already provided in the accompanying financial statements.

The following summary sets out the material adjustments to the Company s reported net earnings (loss), net earnings (loss) per share and shareholders equity which would be made to conform with U.S. GAAP:

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Statements of Earnings

		Years ended December 31, 2007 $	2006 $	2005 $
Net earnings (loss) for the year under Canadian GAAP		(32,296)	33,390	10,571
Accretion on convertible term loans	(c)		502	4,479
Loss on conversion of convertible term loans	(c)		(280)	
Amortization of in-process R&D	(a)	1,546	2,348	1,610
Other	(b)		(10)	(32)
Reclassification adjustment related to the sale of Echelon	(e)	(754)		
Deferred taxes	(d)	(5,430)	(959)	
Income tax effects of the above adjustments		(494)	(729)	(658)
Net earnings (loss) for the year under U.S. GAAP		(37,428)	34,262	15,970
Out of which:				
Net earnings (loss) from continuing operations		(36,415)	8,449	(10,083)
Net earnings (loss) from discontinued operations		(1,013)	25,813	26,053
Basic net earnings (loss) per share		(0.70)	0.66	0.34
From continuing operations		(0.68)	0.16	(0.22)
From discontinued operations		(0.02)	0.50	0.56
Diluted net earnings (loss) per share		(0.70)	0.65	0.34
From continuing operations		(0.68)	0.16	(0.22)
From discontinued operations		(0.02)	0.49	0.56
Weighted average number of shares (note 20) under U.S. GAAP				
Basic		53,182,803	52,099,290	46,139,814
Diluted		53,182,803	52,549,260	46,139,814

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Reconciliation of shareholders equity to conform to U.S. GAAP

The following summary sets out the significant differences between the Company s reported shareholders equity under Canadian GAAP as compared to U.S. GAAP. Please see corresponding explanatory notes for additional information.

		Years ended December 31, 2007 $	2006 $
Shareholders equity in accordance with Canadian GAAP		88,591	178,879
In-process R&D	(a)	(14,181)	(14,348)
Other	(b)		39
Deferred tax effect	(d)		5,134
		74,410	169,704

Statement of comprehensive income

		Years ended December 31, 2007 $	2006 $	2005 $
Net earnings (loss) for the year under U.S. GAAP		(37,428)	34,262	15,970
Other comprehensive income (loss)				
Foreign currency translation adjustments		12,607	4,654	(7,660)
Reclassification adjustment related to the sale of shares of Atrium			(1,643)	
Change in fair value of investments	(f)	(29)	(274)	(139)
Change in fair value of interest rate swap, net of income taxes	(g)		78	(78)
Comprehensive income		(24,850)	37,077	8,093

Accumulated other comprehensive income, net of related income taxes, consists of the following:

	As at December 31, 2007	2006
	$	$
Foreign currency translation adjustments	19,809	12,826
Unrealized gains on investments	10	39
Accumulated other comprehensive income	19,819	12,865

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The following table summarizes the shareholders equity activity under U.S. GAAP since December 31, 2004:

	Share Capital $	Deficit $	Other Capital $	Accumulated Other Comprehensive Income $	Shareholders Equity $
Balance as at December 31, 2004	126,991	(64,084)	5,825	17,927	86,659
Net earnings as per U.S. GAAP		15,970			15,970
Stock-based compensation costs			2,286		2,286
Variation in fair value of investments				(139)	(139)
Variation in fair value of interest rate swap				(78)	(78)
Exercise of stock options	130				130
Issuance of shares pursuant to a business acquisition	2,737				2,737
Share issue expenses	(108)				(108)
Foreign currency translation adjustments				(7,660)	(7,660)
Balance as at December 31, 2005	129,750	(48,114)	8,111	10,050	99,797
Net earnings as per U.S. GAAP		34,262			34,262
Stock-based compensation costs			2,120		2,120
Variation in fair value of investments				(274)	(274)
Variation in fair value of interest rate swap				78	78
Exercise of stock options	110		(29)		81
Conversion of convertible term loans	30,403				30,403
Issuance of shares pursuant to:					
a contingent consideration paid upon business acquisition	163				163
acquisition of a patent from a senior officer	175				175
Share issue expenses	(112)				(112)
Foreign currency translation adjustments				3,011	3,011
Balance as at December 31, 2006	160,489	(13,852)	10,202	12,865	169,704
Net loss as per U.S. GAAP		(37,428)			(37,428)
Stock-based compensation costs			1,984		1,984
Variation in fair value of investments				(29)	(29)
Distribution of Atrium (note 4)	(137,959)		71,122	(5,624)	(72,461)
Issuance of shares pursuant to stock option plan	33				33

Exercise of Stock Options	26		(26)		
Foreign currency translation adjustments				12,607	12,607
Balance as at December 31, 2007	22,589	(51,280)	83,282	19,819	74,410

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Balance Sheets

The following table summarizes the significant differences between the balance sheet items under Canadian GAAP as compared to U.S. GAAP as at December 31, 2007 and 2006:

		As at December 31, 2007		As at December 31, 2006	
		As reported $	U.S. GAAP $	As reported $	U.S. GAAP $
Intangible assets	(a)	36,945	22,764	39,106	24,758
Future income tax liabilities	(a)			10,963	5,829

Statements of cash flows

For the years ended December 31, 2007, 2006 and 2005, there are no significant differences between the statements of cash flows under Canadian GAAP as compared to U.S. GAAP.

(a) Research and development costs

Under U.S. GAAP, in-process research and development acquired in a business combination is written off at the time of acquisition. Under Canadian GAAP, in-process research and development acquired in a business combination is capitalized and amortized over its estimated useful life. Balance includes intangible assets held for sale, and assets and liabilities from discontinued operations.

(b) Other

Other adjustments required when considering the significant differences between Canadian and U.S. GAAP include individually minor amounts related to the following items:

financing costs arising from the convertible notes (see (c) below) allocated to other capital under Canadian GAAP that are amortized in earnings under U.S. GAAP;

organization costs deferred and amortized under Canadian GAAP that are expensed as incurred under U.S. GAAP.

(c) Convertible term loans

Under Canadian GAAP, proceeds from the issuance of convertible term loans are allocated among long-term convertible term loans and shareholders equity, resulting in a debt discount that is amortized to expense over the term of the loans. The financing costs related to those loans have been allocated on a pro-rata basis between deferred charges and other capital. Under U.S. GAAP, those costs are all included in deferred charges and amortized over the term of the loans, and convertible term loans are totally considered as long-term debt. Furthermore, under U.S. GAAP, the entire incremental consideration to induce conversion is recorded in earnings.

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(d) Deferred taxes

This adjustment reflects differences related to the accounting for valuation allowance for U.S. GAAP purposes that arise from timing differences.

(e) Cumulative translation adjustment related to the sale of Echelon

Under Canadian GAAP, a gain or loss equivalent to a proportionate amount of the exchange gain or loss accumulated in the translation adjustment has to be recognized in income when there has been a reduction of a net investment in a foreign operation. Under U.S. GAAP, a gain or loss should only be recognized in income in the case of a substantial or complete liquidation of a net investment in a foreign operation being the substantial or complete liquidation of the Company.

(f) Investments

Investments, which are classified as available-for-sale securities, include the Company s investment in discount notes, commercial paper and bonds for which the Company does not have the positive intent or ability to hold to maturity and an investment in shares of a publicly traded company. Under U.S. GAAP, available-for-sale securities are carried at fair value with unrealized gains and losses net of the related tax effects as part of other comprehensive income.

Under Canadian GAAP, these investments were valued at the lower of amortized cost and market value before January 1, 2007. Since this date, there is no difference in accounting under Canadian and U.S. GAAP.

(g) Interest rate swap

Under Canadian GAAP, prior to 2007, the Company accounted for Atrium s interest rate swap using the accrual method. U.S. GAAP requires all derivative instruments to be recognized at fair value on the consolidated balance sheet. Under U.S. GAAP, this swap has been designated as a cash flow hedge. Accordingly, the changes in fair value are recorded in other comprehensive income until the related interest expense is recorded in income.

(h) Recently adopted and pending accounting pronouncements

FASB Statement No. 123R Share-Based Payment (SFAS 123R)

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued SFAS 123R which replaces FASB Statement No. 123 (SFAS 123), Accounting for Stock-Based Compensation , and eliminates the ability to account for share-based payment transactions using APB Opinion No. 25, Accounting for Stock Issued to Employees . SFAS 123R covers the accounting requirements for a wide range of share-based compensation arrangements. SFAS 123R requires that compensation cost for employee stock-based compensation be measured based on the grant-date fair value and recognized in the financial statements over the vesting period (fair value method).

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The Company adopted SFAS 123R on January 1, 2006 using the modified prospective application method of transition and its adoption had no significant impact on its consolidated financial statements. On January 1, 2003, the Company had already adopted the prospective application method of transition of SFAS 123, which required that all new awards granted to employees on or after January 1, 2003 be accounted for at fair value. The fair value of awards granted was estimated using the Black-Scholes option pricing model.

FASB Statement No. 158 Employer s Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS 158)

In September 2006, the FASB issued SFAS 158. This statement amends SFAS 87, Employers Accounting for Pensions , and SFAS 106, Employers Accounting for Post-Retirement Benefits Other than Pensions , to require recognition of the over funded or under funded status of pension and other postretirement benefit plans on the balance sheet. Under SFAS 158, gains and losses, prior service costs and credits, and any remaining transition amounts under SFAS 87 and SFAS 106 that have not yet been recognized through net periodic benefit cost will be recognized in OCI, net of tax effects, until they are amortized as a component of net periodic cost.

SFAS 158 is effective for the fiscal year ending after December 15, 2006, except for the measurement date provisions, which are effective for fiscal years ending after December 15, 2008. The Company adopted this standard on December 31, 2006 and its adoption had no impact on its consolidated financial statements.

FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48)

In June 2006, the FASB issued FASB interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), an interpretation of FASB Statement No. 109, Accounting for Income Taxes . FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires that the Company recognize the impact of a tax position in the financial statements if that position is more likely than not of being sustained on audit, based on the technical merits of the position. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure. The provisions of FIN 48 are effective beginning January 1, 2007 with the cumulative effect of the change in accounting principle recorded as an adjustment to the opening balance of deficit. The Company adopted this interpretation on January 1, 2007 and this adoption had no impact on the Company s consolidated financial statements. Upon the adoption of FIN 48, the Company elected to classify interest and penalties in interest expense.

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FASB Statement No. 157 Fair Value Measurements (SFAS 157)

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company will adopt this statement on January 1, 2008, and has not yet assessed the impact its adoption will have on its consolidated financial statements.

FASB Statement No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (SFAS 159)

On February 15, 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 , which permits entities to choose to measure many financial instruments and certain other items at fair value. Most of the provisions of this statement apply only to entities that elect the fair value option. However, the amendment to SFAS 115, Accounting for Certain Investments in Debt and Equity Securities , applies to all entities with available-for-sale and trading securities. This statement is effective for fiscal years beginning after November 15, 2007. The Company will adopt this statement on January 1, 2008 and has not yet determined if it will elect to use the fair value option.

EITF Issue No. 07-3 Accounting for Advance Payments for Goods or Services to be Received for Use in Future Research and Development Activities (EITF 07-3)

In June 2007, EITF 07-3 provides clarification surrounding the accounting for nonrefundable research and development advance payments, whereby such payments should be recorded as an asset when the advance payment is made and recognized as an expense when the research and development activities are performed. EITF 07-3 is effective for interim and annual reporting periods beginning after December 15, 2007. The Company will adopt the provisions of EITF 07-3 on January 1, 2008. The Company is currently assessing the impact of EITF 07-3 on its results of operations and financial condition.

EITF Issue No. 07-1 - Accounting for Collaborative Agreements Related to the Development and Commercialization of Intellectual Property (EITF)

The Emerging Issues Task Force has adopted the accounting for arrangements under which companies participate in the development and commercialization of intellectual property into commercially viable products. The ETIF defines a collaborative arrangement is a contractual arrangement that involves a joint operating activity. These arrangements involve two (or more) parties who are both (a) active participants in the activity and (b) exposed to significant risks and rewards dependent on the commercial success of the activity. A company may receive revenues and incur costs under such arrangements as well as make or received payments from the other participant in the arrangement. The EITF concluded revenues earned and costs incurred by a company should be presented gross or net depending on whether the company is the principal in the arrangement. The EITF has approved this pronouncement in December 2007 and it will

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become effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. The Company is currently assessing the impact on the presentation of revenues and costs within the Company s financial statements.

(i) Other disclosures

Research and development tax credits

Under Canadian GAAP, all research and development tax credits are recorded as a reduction of costs in the statements of operations. Under U.S. GAAP, tax credits that are refundable against taxable income are recorded in the income taxes. These tax credits amounted to $1,862,000 in 2007, $1,684,000 in 2006 and $nil in 2005. This difference has no impact on the net earnings (loss) and the net earnings (loss) per share figures for the reporting years.

Furthermore, under U.S. GAAP, the future income tax assets related to the unrecognized tax credits totalled $7,004,000 in 2007 and $5,683,000 in 2006. However, a valuation allowance corresponding to the same amounts has been accounted for in 2007 and 2006.

Long-lived assets

Under U.S. GAAP, long-lived assets by geographic region only consist of property, plant and equipment which are detailed as follows:

	2007 **$**	**2006** **$**
Canada	7,631	8,798
Germany	6,436	4,203
United States	838	
	14,905	13,001

Available-for-sale securities

The Company uses the specific identification method in order to reclassify the gains or losses realized out of accumulated other comprehensive income into the statement of earnings.

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The gross realized gains and gross realized losses included in the statement of earnings, the unrealized holding gain or loss on available-for-sale securities as well as the amount of gains and losses reclassified out of accumulated other comprehensive income into the statement of earnings are as follows:

	2007 **$**	**2006** **$**	**2005** **$**
Gross realized gains		410	17
Gross realized losses	67	21	
Unrealized gains		126	197
Unrealized losses	42	67	67
Gains reclassified	53	390	269
Losses reclassified	30	78	

Available-for-sale securities maturity dates:

	$
Within one year	31,115
One to five years	
	31,115

As at December 31, 2007, available-for-sale securities are composed of:

	$
Government debt securities	5,778
Municipal debt securities	5,130
Corporate debt securities	20,207
	31,115

Research and collaboration agreements

As part of our strategy to enhance our development capabilities and to fund, in part, our capital requirements, we have entered into collaboration agreements with several pharmaceutical companies, which we refer to as our partners . Pursuant to our collaboration, the Company received upfront payments, license fees, milestone payments and has the potential to receive royalty payments in the future. Upfront payments are typically non-refundable payments received upon the signature of an agreement and are amortized over the estimated research and development (R&D) period. License fees are typically contractually obligated payments to fund R&D over the term of collaboration and include milestone payments, as well as R&D contract services. Milestone payments are contingent payments made only upon achievement of specified milestones, such as selection of candidates for drug development, the commencement or termination of clinical trials or receipt of regulatory approvals and achievement of a certain level of sales. If drugs are successfully developed and commercialized as a result of our collaboration agreements, we will receive royalty payments based upon net sales of those drugs developed under the collaboration. Finally, R&D contract services fees are research and development activities performed by the Company on behalf of our partners and for which the Company has the right to receive compensation.

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Ardana Bioscience

In 2002, the Company entered into a license and collaboration agreement with Ardana Bioscience Ltd., a subsidiary of Ardana plc (Ardana). Ardana was granted an exclusive worldwide license to develop and commercialize the growth hormone secretagogue (EP-1572). Ardana undertakes, at its own cost, all activities necessary to obtain regulatory and marketing approvals for the substance. In return, the Company received 1.75 million (approximately $1.7 million) as upfront payment upon signing of the agreement. The Company is also eligible to receive payments of up to an aggregate of 7 million (approximately $9.2 million) upon Ardana s successful achievement of clinical development and regulatory milestones, in addition to low double-digit royalties on future net worldwide net sales of EP-1572.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $3.0 million, $1.5 million and $1.8 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $nil, $nil and $nil, respectively.

In 2002, the Company granted an exclusive license to Ardana to develop and commercialize teverelix, a luteinizing hormone-releasing hormone (LHRH) antagonist, for all therapeutic uses worldwide with the exception of Japan, Korea and Taiwan. On April 2, 2004, Ardana acquired full worldwide rights and was assigned the intellectual property rights relating to teverelix and the underlying microcrystalline suspension technology for the use of teverelix and any other potential LHRH antagonists. The Company received 3.25 million (approximately $3.2 million) in 2002 and 5 million (approximately $6.1 million) in 2004 as upfront payments upon signature of the agreement in 2002 and upon the assignment of the substance in 2004 respectively. The agreement also provides, among other things, 7 million (approximately $9.2 million) of guaranteed payments until December 2006, 15 million (approximately $19.8 million) upon successful achievement of a certain level of sales and low single-digit royalties on future worldwide net sales.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $3.5 million, $3.6 million and $5.1 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were less than $0.1 million, $0.3 million and $0.6 million, respectively.

Keryx Biopharmaceuticals

Following the acquisition of AOI Pharma, Inc. in January 2004 by Keryx Biopharmaceuticals, Inc. (Keryx), Keryx has taken over the license and collaboration agreement signed with AOI Pharma, Inc. in September 2002. Upon signature of this agreement in 2002, the Company received $0.5 million as upfront payment. Keryx undertakes, at its own cost, all clinical activities necessary to obtain regulatory and marketing approvals of perifosine, a signal transduction inhibitor, for all uses in the United States, Canada and Mexico. The agreement provides, among other things, availability of data generated by both parties free of charge. The Company is also eligible to receive payments of up to an aggregate of $18.3 million upon Keryx s successful achievement of clinical development and regulatory milestones, in addition to

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scale-up royalties (from high single to low double-digit) on future net sales in the United States, Canada and Mexico.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $1.7 million, $0.7 million and $0.9 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $0.9 million, $0.9 million and $0.9 million, respectively.

Nippon Kayaku

In 2006, we entered into a licensing and collaboration agreement with Nippon Kayaku Co. Ltd. (Nippon Kayaku). Under the terms of the agreement, we granted Nippon Kayaku an exclusive license to develop and market ozarelix, a LHRH antagonist, for all potential oncological indications in Japan. In return, the Company received 1.5 million (approximately $1.9 million) as upfront payment upon signature. The agreement provides, among other things, availability of data generated by both parties free of charge. The Company is eligible to receive payments of up to an aggregate of 18 million (approximately $23.8 million) upon Nippon Kayaku s successful achievement of clinical development, regulatory milestones and a certain level of sales, in addition to low double-digit royalties on potential net sales. Furthermore, as indicated below regarding the Spectrum Pharmaceuticals, Inc. (Spectrum) R&D agreement, Spectrum is entitled to receive fifty percent of any upfront, milestone payments and royalties received from any research and collaboration agreement signed by the Company for the development and commercialization of ozarelix in Japan.

Revenues recognized under the agreement for the years ended December 31, 2007 and 2006 were $0.5 million and $0.2 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007and 2006 were $0.1 million and $0.1 million, respectively.

Shionogi

In 1995, the Company entered into a research and collaboration agreement with Shionogi and Co. (Shionogi). The Company granted Shionogi a license to develop, use, commercialize and manufacture cetrorelix, our LHRH antagonist, in Japan and for all human indications. Under the agreement, Shionogi is responsible, at its own cost, for all activities necessary to obtain regulatory and marketing approvals for cetrorelix. The agreement provides, among other things, availability of data generated by both parties free of charge. Upon signature of this agreement, the Company received 1.3 million (approximately $1.4 million) as upfront payment and was eligible to receive milestone payments of up to an aggregate of 5.4 million (approximately $7.1 million) upon Shionogi s successful achievement of clinical development and regulatory milestones. To date, the Company received 4.4 million (approximately $5.8 million) of these milestone payments. Since the development of cetrorelix is completed in the *in vitro* fertilization (IVF), Control Ovarian Stimulation (COS) and Assisted Reproductive Technology (ART) in Japan, the Company does not expect to receive further development milestone payments.

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In addition, upon commercialization of cetrorelix in benign prostatic hyperplasia (BPH), the Company will be entitled to a manufacturing margin.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $nil, $3.8 million and $nil, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $nil, $1 million and $0.3 million, respectively.

Solvay Pharmaceuticals

In 2002, the Company entered into a research and collaboration agreement with Solvay Pharmaceuticals Bv, a subsidiary of Solvay SA (Solvay). The Company granted Solvay an exclusive license to develop, use, commercialize and manufacture cetrorelix worldwide (ex-Japan) and for all indications excluding IVF/COS/ART. Under the agreement, Solvay was responsible, at its own cost, for all activities necessary to obtain regulatory and marketing approvals for cetrorelix in different indications including, uterine myoma, endometriosis and BPH. The agreement provides, among other things, availability of data generated by both parties free of charge. Upon signature of this agreement, the Company received 6 million (approximately $6.2 million) as upfront payment and was eligible to receive milestone payments of up to an aggregate of 18 million (approximately $23.8 million) upon Solvay s successful achievement of clinical development and regulatory milestones, in addition to low double-digit royalties on future worldwide (ex-Japan) net sales of cetrorelix.

In December, 2005, Æterna Zentaris and Solvay amended the agreement whereas the Company regained exclusive worldwide (ex-Japan) rights for cetrorelix for the BPH indication solely, without any financial compensation payable to Solvay. In May 2007, the parties entered into a termination agreement whereby the Company regained exclusive worldwide (ex-Japan) rights for cetrorelix in all indications, including endometriosis and uterine myoma, without any financial compensation payable to Solvay.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $2.0 million, $1.2 million and $4.5 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $1.9 million, $0.6 million and $0.6 million, respectively.

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Spectrum Pharmaceuticals

In 2004, the Company entered into a licensing and collaboration agreement with Spectrum Pharmaceuticals, Inc. (Spectrum) for ozarelix, a LHRH antagonist. Under the terms of the agreement, the Company granted Spectrum an exclusive license to develop and commercialize ozarelix for all potential indications in North America (including Canada and Mexico) as well as India. The agreement provides, among other things, availability of data generated by both parties free of charge. Upon signature of this agreement, the Company received 2 million as upfront payment (approximately $2.4 million) of which an amount of 1 million was paid cash and the balance paid through the issuance of shares of the capital of Spectrum. The Company is eligible to receive payments of up to an aggregate of 18.5 million (approximately $24.4 million) upon Spectrum s successful achievement of clinical development and regulatory milestones, in addition to royalties (scale-up royalties from high single to low double-digit) on potential net sales. In consideration of the amounts paid by Spectrum under this agreement, Spectrum is entitled to receive fifty percent of any upfront, milestone payments and royalties received from any research and collaboration agreement signed by the Company for the development and commercialization of ozarelix in Japan.

Revenues recognized under the agreement for the years ended December 31, 2007, 2006 and 2005 were $1.9 million, $2.9 million and $2.6 million, respectively.

Corresponding R&D costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $0.6 million, $1.7 million and $2.6 million, respectively.

Tulane University

In 2002, the Company signed license agreements with the Tulane Educational Fund (Tulane) with regard to various substances, including cetrorelix. Under the agreements, we obtained exclusive worldwide licenses to use Tulane s patents to develop, manufacture, market and distribute these substances.

The agreement provides the payment by the Company of single-digit royalties on future worldwide net sales for all indications, except BPH, where it provides the payment of low single-digit royalties. Tulane is entitled to receive a low double-digit royalty on any lump sum, periodic or other cash payments received by the Company from sub-licensees.

Costs incurred under the agreement for the years ended December 31, 2007, 2006 and 2005 were $0.1million, $0.3 million and $0.4 million, respectively.

25 Comparative figures

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

Item 19. Exhibits

Exhibit Index

1.1	Articles
1.2	By-Laws
2	Shareholder Rights Plan
4.1	Stock Option Plan
4.2	Employment Agreement for Dr. Paul Blake
4.3	Employment Agreement for Dr. Jürgen Engel
4.4	Employment Agreement for Dr. David J. Mazzo
4.5	Employment Agreement for Ms. Ellen McDonald
4.6	Employment Agreement for Mr. Mario Paradis
4.7	Employment Agreement for Dr. Nicholas J. Pelliccione
4.8	Employment Agreement for Mr. Dennis Turpin
8.1	Subsidiaries of Æterna Zentaris Inc. (see Item 10.I of this annual report)
11.1	Code of Ethical Conduct
11.6	Audit Committee Charter
12.1	Certification of the Principal Executive Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002
12.2	Certification of the Principal Financial Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002
13.1	Certificate of the Principal Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
13.2	Certificate of the Principal Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

ÆTERNA ZENTARIS INC.

Dennis Turpin
Senior Vice President and Chief Financial Officer

Date: March 28, 2008