

THE MEDIPATTERN CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION.

October 9, 2007

INFORMATION CONCERNING THE MEDIPATTERN CORPORATION FOR THE YEARS ENDING JUNE 30, 2007 AND 2006

Overview

The Medipattern Corporation (TSX-V: MKI) (Medipattern or the Company) is the result of the April 22, 2005 amalgamation of a Capital Pool Company (CPC), Skoobins Resources Inc., and Medipattern, which was a Canadian Controlled Private Corporation prior to this amalgamation. The Company was originally founded in 1999 under the Business Corporations Act (Ontario).

Medipattern's goal is to deliver medical imaging software that enhances practitioner workflow while improving interpretive and diagnostic confidence. Medipattern's software looks for patterns in images to help radiologists assess the need to biopsy a selected area of interest, and then immediately and automatically generates a report that is available in various standard medical imaging formats, thereby improving workflow. This type of technology is referred to as computer-aided diagnosis or CAD. Medipattern based its software on its proprietary platform technology, CADENZA™, built to support a wide range of medical imaging applications. Medipattern built its platform to take advantage of the many other applications it will develop for automatic detection and diagnosis of medical images. The Company's initial product offering is a CAD application designed to analyze ultrasound images. This first clinical indication is for breast ultrasound and is being marketed as B-CAD™. B-CAD uses pattern recognition methods to help radiologists analyze images to assist them in assessing the need to biopsy a selected nodule. B-CAD then standardizes and automates the reporting process in conformity with the Breast Imaging Reporting And Data System (BI-RADS®) Ultrasound Lexicon, as recommended by the American College of Radiology (ACR).

The Company's software is designed to be installed directly in ultrasound machines, Picture Archiving and Communication Systems (PACS), and Reporting Systems (RS), integrated into Workstations, or used as a standalone application running on a PC. These are the most common ways in which a radiologist accesses medical images in clinics, hospitals, and imaging centers.

In June 2007, Medipattern announced the signing of a five-year development, licensing, and distribution agreement for ultrasound-based CAD with GE Healthcare LLC of England. The agreement enables GE Healthcare to resell the current B-CAD product line, while collaboratively developing and customizing CAD for GE's future solutions. The Company also has a marketing agreement with Cedara Software Corp., a division of Merge Healthcare (NASDAQ: MRGE; TSX: MRG) to distribute B-CAD through Merge's worldwide sales channels. Merge develops medical imaging software distributed through direct sales, major medical original equipment manufacturers (OEMs), and value-added resellers (VARs) throughout the world. In November 2006, this agreement was amended and Medipattern is now responsible for end-user sales and selected OEMs, except in Japan where Cedara retains exclusivity for both OEMs and end-users. Cedara retains a non-exclusive arrangement for end-user sales and an exclusive arrangement for selected OEMs. As a result, Medipattern has built its own sales, marketing, and product support teams, as evidenced by recent events listed below.



There is a clinical need to improve breast cancer diagnosis that has created significant demand for CAD products. Mammography's false negatives (approximately 15%) allow cancer to progress to more advanced stages that are increasingly difficult and costly to treat. Mammography's false positives lead to unnecessary biopsies. More than 8 million breast ultrasound exams are performed annually in the United States, leading to more than 1,300,000 breast biopsies. Only approximately 220,000 of these biopsies are proven to be positive (i.e., malignant). Negative biopsies not only cause emotional distress, but can result in internal scarring that can complicate interpretation of subsequent mammograms.

Ultrasound is the accepted standard for further evaluation of breast lesions in patients who have suspicious mammogram results. The results of an ultrasound test are used to aid in the decision to biopsy.

How B-CAD Works

The Company's marketing claim is that B-CAD is designed to help radiologists identify sonographic characteristics associated with breast lesions and assist them in assessing the need to biopsy a selected nodule. Based on pattern recognition technology, B-CAD provides an automated feature extraction tool that highlights user-selected regions of interest in a breast ultrasound image. The software tool analyzes, segments, and classifies those selected areas, and then automatically pre-populates a report, based on user input and annotations entered during the analysis process. This report is formatted in accordance with the ACR BI-RADS® Ultrasound Lexicon and may be archived or sent directly to a referring physician. This basic principle is applied for 2D and 3D images as well as in other modalities, such as our B-CADMRI™.

General

The Company develops CAD software applications for medical imaging. Medipattern is marketing its B-CAD application in the United States (US) under a 510(k) clearance from the US Food and Drug Administration (FDA); in Canada under the Canadian Medical Devices Conformity Assessment System (CMDCAS); and in Europe under the Full Quality Assurance System Approval Certificate allowing for CE-MDD Marking. Medipattern maintains Quality Systems Regulation (QSR) in compliance with the USA FDA and the ISO 13485:2003 standard, which is the medical-device-specific standard based on ISO 9001. Registration to this standard indicates that a company has Quality Management System processes in place that have been assessed for their ability to meet customer and regulatory requirements. Health Canada requires the appropriate regulatory and quality system requirements. Health Canada will only accept quality system certificates that have been issued by special third-party auditing organizations under CMDCAS.

Highlights for Fiscal 2007

- July 2006 – Medipattern's B-CAD named Product Innovation of the Year by Frost & Sullivan. The Medipattern Corporation was recognized by the analyst team at Frost & Sullivan with their second award as a result of a comprehensive review of the US CAD market, a study that analyzed the existing participants in the market and anticipated market acceptance of innovative technologies.
- September 2006 – Conducted sales training on B-CAD with Kodak CARESTREAM™ sales team.
- Fall 2006 – Expanded marketing program to build awareness of B-CAD and B-CADMRI focusing on the Canadian, European, and US markets. Key elements include exposure at upcoming tradeshows, increasing advertising campaign, and co-marketing arrangements with new and existing partners.
- November 2006 – Amended Cedara Agreement. Under this amended agreement, Medipattern is primarily responsible for global end-user sales with the exception of Japan. Cedara and Medipattern divide up responsibility for selected OEMs.

- November 2006 – Participated in Radiological Society of North America (RSNA) conference in various booths;
- November 2006 – Agreed to build a customized version of B-CAD for SonoCiné.
- November 2006 – Finalized software collaboration, development, and license agreement for B-CADMRI with Confirma, Inc. of Kirkland WA, USA.
- November 2006 – Hired Janet Sterritt as Vice-President of Sales and Marketing, and Drew Sala as Director of International Sales.
- December 2006 – Began to build a reseller network, announcing the signing of the first reseller agreement with MammoSolutions of Houston, Texas.
- January – March 2007 – Continued to build reseller network throughout the USA, Puerto Rico, Europe, China, and the Far East.
- March 2007 – Launched B-CAD 1.2 at Northwestern in Chicago. B-CAD 1.2 associates multiple views of the same breast lesion and can track multiple lesions for the same patient in one record and automatically documents the results.
- March 2007 – Integrated B-CAD with Sectra’s breast imaging workstation. Sectra is a Swedish IT and medical technology company and a major supplier of diagnostic imaging systems in a PACS (Picture Archiving and Communication System) environment.
- March 2007 – Participated in the European Congress of Radiology (ECR) conference with the Company’s own booth as well as other booths including Kodak, Confirma, Sectra, and Cedara.
- June 2007 – Announced a five-year collaborative sales and development agreement for ultrasound-based CAD with GE Medical Systems Ultrasound and Primary Care Diagnostics, LLC.

Business Strategy of Medipattern

B-CAD

The Company signed an agreement with Cedara, a division of Merge Healthcare, on September 4, 2004 to market, sell, and provide aftermarket support for the B-CAD technology. Cedara and Merge compete in the global healthcare software and service business, focused on distributing products to OEMs and VARs and through direct sales to imaging centers, hospitals, and clinics.

Medipattern and Cedara made amendments to the existing agreement in November 2006 as described earlier, where for the most part, Medipattern is now responsible for end-user sales and selected OEMs while Cedara retains exclusivity with selected OEMs.

Subsequent to the amendments, Medipattern entered into a Global Sales, License, and Development agreement directly with GE Healthcare, where GE will distribute B-CAD through its worldwide network. Also, Medipattern will develop customized B-CAD applications using proprietary GE file formats in both 2D and 3D.



To advance the Company's profile and reputation, Medipattern has formed strategic relationships with luminaries – industry experts – to support the development of its products. To that, Medipattern adds seasoned industry sales and marketing expertise. This forms the core of the Company's business model for both B-CAD and future indications and modalities. Using this approach of validation and direct selling through resellers, Medipattern will seed the market with direct sales to end users and leverage developing relationships with large international companies to sell and distribute its products and services to OEMs, end users, and resellers. In addition, Medipattern has been contracted to integrate its software into other technology. At this point, such agreements include the integration or development of B-CAD for Sectra's PACS offering and Orison Corporation and SonoCiné Inc., both of which utilize B-CAD as a standard component for their automated whole-breast ultrasound system.

B-CADMRI

Medipattern's demonstration of its B-CADMRI at the Radiology Society of North America (RSNA) conference in Chicago, early in December 2005, led to the receipt of the Frost & Sullivan 2006 Medical Imaging Innovation of the Year Award. This new application in CAD for MRI added a second modality to the Company's CADENZA product family. Both management and Frost & Sullivan believe that not only Medipattern's ability to cross the modality barrier from ultrasound to MRI, but the focus of B-CADMRI on identification and analysis of morphological features of lesions in breast images, are firsts among CAD companies.

The Company has established a non-exclusive relationship with Confirma, Inc. of Bellevue, WA, the leader in MRI CAD workstations, to include B-CADMRI in its product offering. A prototype version of an integrated product was demonstrated at RSNA 2006 in late November in Chicago, Ill. This work with Confirma led to the signing of a Definitive Software Collaboration, Development, and License Agreement with Confirma. Confirma plans to release the morphology software library developed by Medipattern as an integral part of its upcoming release of CADstream™ 5.0 at RSNA 2007. Confirma currently has over 750 installations worldwide with more than 2,500 users of their software. Confirma sells directly to end users, and through OEMs such as GE, Philips Medical Systems, Bayer Healthcare, and CARESTREAM (formerly Kodak Healthcare).

Future Developments

While the primary focus of the Company's CAD software is improving the use of ultrasound and MRI to interpret breast images, there are numerous other potential applications of its expertise. Medipattern will continue to examine such other applications concurrent with the further development of B-CAD to determine their medical and commercial attractiveness. Management believes that its CAD expertise can be applied to other imaging modalities in addition to ultrasound and MRI, such as CT, PET, or X-ray.

Note on Forward-Looking Commentary

Forward-looking comments may be included in the material in this document. Any forward-looking statements are subject to risk and uncertainty. Actual results and the timing of certain events may differ materially from those projected in the forward-looking statements. Many factors can cause results to differ materially from those expressed or implied in the forward-looking statements, such as changes in management, competition in the market, technological change, product liability, requirements for additional capital, and regulatory oversight. Medipattern has no obligation to publicly release revisions to any of these forward-looking statements.

The following discussion should be read in conjunction with the financial statements and the notes thereto.

Critical Accounting Policies

Deferred Technology Charges: Costs incurred with respect to the development of patent applications are capitalized as deferred technology charges. Once the patents are approved they will be classified as intangible

assets and will then be amortized over the estimated useful life of the patent. These deferred charges are tested for impairment by comparing their carrying value with the corresponding fair market value. As at June 30, 2007, no patent had been approved. However, should management determine that certain deferred technology charges are impaired or should certain development work be abandoned or sold, the capitalized cost relating to this work will be written down to fair market value.

Research and Development: Research costs are expensed as incurred. Development costs are also expensed as incurred until such time as these costs meet the criteria for capitalization and amortization under Canadian Generally Accepted Accounting Principles (GAAP).

Revenue Recognition: The Company sells its products and services based on the terms and conditions of customer contracts, which may encompass multiple elements, including software sales, technology access fees, royalties, professional services, and maintenance fees. The Company recognizes revenue in accordance with the criteria applicable in the CICA Handbook section 3400, guidance by Emerging Issues Committee (EIC) as discussed in EIC 141 and EIC 142. The total fee for a multiple element arrangement is allocated to each element based upon objective evidence of the fair value of each element. Fair value is established through the Company's policy to charge customers the same price as when the element is sold separately. When fair value cannot be determined, revenue is recognized only as the final elements are delivered or over the term of the agreement for the entire agreement fee.

Royalty or licensing revenue from the sale of units made under the agreement with Cedara is tied to end-user sales. Therefore, the revenue is recognized after the third-party sale occurs when the extent of such a sale is determinable; otherwise, it is deferred and recognized over the anticipated exclusivity period (if applicable) of the agreement since there is no recourse to repay any of the proceeds from the sale of licenses to Cedara under the agreement.

Royalty or licensing revenue from sales made under standard reseller agreements is recognized in accordance with the terms and conditions of these agreements. Revenue is recognized when the product has been delivered, when there are no significant obligations remaining, when fees are fixed and determinable, when there is no recourse to any of the licenses purchased by the reseller, and when collection is reasonable assured. If the sale is contingent upon additional terms and conditions outside the standard reseller agreement, the revenue is deferred until all the terms and conditions of the sale have been met.

Professional services revenues are recognized as the work is performed.

Direct software sales and technology access fees are recognized when the product has been delivered, when no significant obligations remain, when fees are fixed and determinable, when collection is reasonably assured, and persuasive evidence of an arrangement exists. If the sale is contingent upon successful installation and subsequent customer acceptance, the revenue is deferred until customer acceptance is achieved.

Maintenance fees are recognized over the respective contract periods.

Funds received in advance of being earned are deferred until the above-noted criteria are met.



RESULTS OF OPERATIONS

The following table sets forth selected financial information for the period indicated.

	2007	2006
REVENUE:		
Technology access fees	\$ -	\$ 289,350
Royalty income	210,196	109,396
Professional fees	197,025	76,627
Interest	109,272	96,201
	<u>516,493</u>	<u>571,574</u>
OPERATING EXPENSES		
Research and development	1,162,565	1,231,357
Administration and product support	1,038,376	1,024,119
Sales and marketing	797,440	299,841
Amortization of property and equipment	44,905	36,350
	<u>3,043,286</u>	<u>2,591,667</u>
LOSS BEFORE UNDERNOTED	(2,526,793)	(2,020,093)
Writedown of deferred technology charges	(58,701)	(8,235)
Writedown of loans payable to shareholders	-	5,134
Gain on conversion of debt	-	24,276
	<u>(2,585,494)</u>	<u>(1,998,918)</u>
NET LOSS	<u>\$ (2,585,494)</u>	<u>\$ (1,998,918)</u>

ANNUAL FINANCIAL INFORMATION – ANNUAL FINANCIAL INFORMATION FOR THE FISCAL YEAR ENDED JUNE 30, 2007 AND COMPARED TO JUNE 30, 2006.

1. Net Sales or Total Revenues.

Medipattern pre-sold B-CAD licenses in January 2005, in the amount of \$492,280 to Cedara and recorded this pre-sale as deferred revenue. In November 2005, Cedara issued their GMA approval making B-CAD commercially available for sale. As a result of this approval, Medipattern initiated the recognition of this deferred revenue as income in November 2005. The recognition of the deferred revenue as income is on a straight-line basis over an expected period of exclusivity under the agreement with Cedara. As a result, Medipattern recognized \$164,093 as royalty income (2006 - \$109,396). In the event that sales exceed the minimum levels contemplated, revenue recognition will be accelerated. Additional royalty revenue of \$46,103 resulted from the licensing of B-CAD through Medipattern's newly assembled reseller network. Therefore, total royalty income in 2007 is \$210,196 (2006 - \$109,396).

Professional service fees in the amount of \$197,025 were earned in 2007 (2006 - \$76,627) under contracts for software development work performed. Professional service fees are generally earned for development work done to customize B-CAD for a specific customer.

In 2006, Medipattern received a payment in the amount of \$289,350 for access to certain technology relating to research and development work on the design of a 3D, whole-breast scanner. This was a one-time payment.

2. Interest Income.

The policy of the Company limits the type of investments to only the most creditworthy instruments for terms

not to exceed one year. The Company has invested the proceeds of its financings in Canadian T-bill accounts, US\$ Money Market accounts, and guaranteed investment certificates to derive interest income for 2007 of \$109,272 (2006 - \$96,201). The interest rates have ranged from 3.25% to 4.30% for these financial instruments since July 1, 2005.

3. Research and Development.

The following table illustrates the comparative expense category information for significant components of R&D costs:

	2007	2006
Salaries and benefits	\$ 942,794	\$ 733,840
Contract fees	271,196	214,215
Consulting fees	200,932	257,179
Licensing fees	17,983	11,174
Other	14,716	14,949
Tax credits applied	(285,056)	-
	<u>\$ 1,162,565</u>	<u>\$ 1,231,357</u>

R&D expenditures continue to be dedicated to the development and enhancement of the Company's software application B-CAD. R&D costs are currently directed toward enhancements to the ultrasound software, B-CAD, for upcoming new releases and the further development of B-CADMRI. Research costs are expensed as incurred. Development costs are also expensed as incurred unless such costs meet the criteria for capitalization and amortization under Canadian GAAP.

Medipattern is eligible for Ontario Innovation Tax Credits under the Ministry of Finance of Ontario's OITC program. In 2007, the Company received a tax credit under this program in the amount of \$19,833 that related to the tax period ending June 30, 2005 and a tax credit relating to the tax period ending June 30, 2006 in the amount of \$125,053. In addition, the Company estimates that for the period ending June 30, 2007, it will be eligible for additional OITC recoverable in the amount of \$149,495. Management has now determined that there is reasonable assurance that these income tax credits will be recoverable and according to the accounting policy, these amounts are now recorded in the period as a reduction to the related expenses or capital costs.

In aggregate, \$285,056 has been applied to the related research and development expense categories in the 2007 (June 30, 2006 - \$0). This is the main reason R&D expenses decreased by \$68,792 to \$1,162,565 in 2007 from \$1,231,357 in 2006.

Actual R&D expenses increased steadily throughout 2007 to meet the demand of our OEM contracts for customized development work on B-CAD and to bring new releases of B-CAD to the market. Additional development staff were hired to meet this demand, resulting in an increase of salary and related expenses to \$942,794 in 2007 (2006 - \$733,840). Contract fees are paid to systems designers and architects to assist the Company in its software development activities. Additional software development costs were contracted to a third party in order to accelerate the addition of specific workflow functionality resulting in an increase to software development contract fees to \$271,196 in 2007 (2006 - \$214,215). Consulting fees continued to be directed toward development of the Company's FDA, clinical, and luminary strategy. However, the Company is using its own staff to take on more of those activities. For this reason, consulting fees decreased to \$200,932 in 2007 (2006 - \$257,179).



4. Finance and Administration.

The following table sets forth comparative expense category information illustrating the nature and changes in costs incurred in 2007 and 2006.

	2007	2006
Salaries and benefits	\$ 317,982	\$ 341,588
Professional fees	246,150	203,864
Stock compensation expense	119,769	165,913
Investor relations	98,000	102,621
Insurance	60,665	70,856
Rent	53,678	48,496
Business communications	52,729	23,556
Other	89,823	67,225
	<u>\$ 1,038,796</u>	<u>\$ 1,024,119</u>

Finance and administrative costs have remained relatively stable during the past year. Total costs in 2007 increased by \$14,677 to \$1,038,796 (2006 - \$1,024,119). Salaries and benefits decreased slightly. The major factor contributing to this decrease results from reassigning the duties of certain staff from finance and administration to sales and marketing. For this reason, salaries and benefits decreased \$23,606 when compared to last year. Stock options issued to employees and directors in fiscal years ending 2007 and 2006 continue to be amortized over the vesting period of the options, resulting in an administrative operating expense of \$119,769 for 2007 (2006 - \$165,913). The reduction in this expense category is mainly due to the forfeiture of stock options during Q2 2007. Professional fees in the amount of \$246,150 (2006 - \$203,864) include legal, accounting, and recruiting fees. The major reason for the increase is the significant rise in the recruiting fees incurred to bring in senior software design and development staff. Insurance expense attributable to insurance premiums to cover product liability, errors and omissions, directors' and officers' coverage, and key-man insurance totaled \$60,665 for 2007 (2006 - \$70,856). These costs have decreased slightly due to negotiation of better rates on insurance in fiscal 2007. Investor relations costs totaled \$98,000 for the 2007 (2006 - \$102,621). This expense is directly attributable to work performed by the Company's investor relations firm, IRonside Investor Relations Inc. (formerly CIRIS) who assists the Company with investor and public relations-related tasks and issues, including the website and the annual report. Rental costs have increased slightly due to the rental of an apartment for a few months to save money on hotel accommodations for consultants and contractors who were in Toronto on a continuing basis during Q3 2007. Business communications costs include courier, postage, and telecommunication expenses. These costs increased significantly to \$52,729 in 2007 (2006 - \$23,556) due to the hiring of additional employees, a number of whom are located in the US. Other expenses consist of office expenses and shareholder services, among other costs, in the amounts of \$17,227 and \$16,940 in 2007 (2006 - \$11,375 and \$18,940 respectively). Other costs, which include recruiting fees, banking fees, website maintenance, customs and brokerage fees, etc., have remained manageable.

5. Sales and Marketing.

The following table sets forth comparative expense category information illustrating the nature and changes in costs incurred in 2007 and 2006.

	2007	2006
Salary and benefits	\$ 392,865	\$ 116,935
Advertising and promotion	116,753	44,704
Business development	172,300	81,828
Marketing - research and materials	40,544	38,948
Conferences and trade shows	48,694	8,236
Other	26,284	9,190
	<u>\$ 797,440</u>	<u>\$ 299,841</u>

Sales and marketing expenses increased substantially to \$797,440 for 2007 (2006 - \$299,841). As mentioned above, certain existing resources were reallocated to the sales and marketing efforts of the Company and a new position of Vice President of Sales and Marketing was established. The Vice President will be working directly with our resellers and with Cedara to assist in creating greater awareness of Medipattern with certain OEMs and end users. As well, she is responsible for overseeing product placement to end users such as radiologists and ultrasound technicians through our reseller network. In addition, a customer service representative was hired in February to support the sales effort by providing installation, training, and support services. As a result of this, salary and benefits increased substantially to \$392,865 (2006 – \$116,935). Prior to renegotiating the agreement with Cedara, which was completed November 26, 2006, Medipattern had relied exclusively on Cedara to provide all sales and marketing support and none of Medipattern's internal resources were allocated to this activity. Medipattern is now taking the responsibility to build up its own sales and marketing force and is ramping up its profile at conferences and trade shows to create much greater awareness among end users and OEMs. The Company is now investing in additional advertising and promotional activities, which amounted to \$116,753 for 2007 (2006 – \$44,704). This included sales materials and journal advertising as the Company assumed a more active role in all aspects of marketing and sales, especially as related to end-user sales. This is a result of the comprehensive review that management has undertaken to advance the sales and marketing of B-CAD. The Company also increased its spending on market research and business development activities as it takes a more active role in the actual cycle of selling B-CAD. Business development activity increased to \$172,300 in 2007 (2006 - \$81,828). This increase is directly attributable to the increase in travel and travel related costs in order to properly assemble the reseller network and work with them and their customers to meet their requirements. Marketing cost increased slightly to \$40,544 in 2007 (2006 – \$38,948). These costs relate to subscriptions to marketing research providers and designing and preparing appropriate sales and marketing collateral.

Medipattern also stepped up its attendance and profile at a number of important trade shows and conferences, resulting in a significant increase in those costs in 2007. This increase is directly attributable to attendance at numerous conferences and trade shows and supporting the Company's own booth at these shows. In the past, Medipattern relied either on Cedara or other OEMs to display B-CAD. However, Medipattern management has decided to accelerate its brand recognition through its own efforts. As a result, costs will continue to increase in a measured way to support sales and marketing efforts for the foreseeable future.



6. Liquidity and Capital Resources.

Working Capital: Critical to the ongoing viability of Medipattern is its ability to fund its operations until sufficient revenue can be derived from professional service fees or software licensing. The demand on working capital is growing as the Company is taking over the role of sales and marketing from Cedara and contracts are being negotiated and signed with OEMs. Wherever possible, management is attempting to obtain professional service fees for any customization work being done for specific deployment of B-CAD to help offset the drain on working capital. Working capital has decreased to \$1,579,389 as at June 30, 2007 (2006 - \$4,076,254). This decrease results from the ongoing net cost of funding the operating activities of the Company for the fiscal year ended June 30, 2007. As at June 30, 2007, current assets are \$2,056,278 (2006 - \$4,533,771) and current liabilities are \$476,889 (2006 - \$457,517). Included in current liabilities is the current portion of deferred revenue in the amount of \$164,093 (2006 - \$164,093).

Cash and Debt Reduction Realized by Financing Activities: Small financing activities took place during 2007. These related to the exercise of 12,000 stock options at \$0.25 per common share in April 2007 and the exercise of 234,986 common share purchase warrants at a price of \$0.47 per common share in May 2007. Proceeds from these two transactions were \$3,000 and \$110,443 respectively. A number of financing activities took place during the year ending June 30, 2006. During fiscal 2006, 72,000 stock options were exercised. 10,000 stock options were exercised at a price of \$0.55 per share, 56,500 stock options were exercised at \$0.50 per share and 5,500 stock options were exercised at \$0.435 per share for total proceeds of \$30,643. In April 2006, Medipattern closed a private placement in the amount of \$2,500,000 and in June 2006 certain Agent options were exercised in the amount of \$98,864. In addition, in January 2006, debt in the amount of \$80,903 was exchanged for 80,895 common shares of the Company in settlement of a consulting fee for services provided in the fiscal year ending in 2002. The debt was exchanged at a price of \$1.00 per common share. At the time of the exchange of debt for shares, the common shares were trading at \$0.70 per common share, resulting in forgiveness of debt in the amount of \$24,276, which is reported as other income. A second exchange of debt took place in June 2006, when loans payable to shareholders in the amount of \$114,119 were exchanged for 188,603 common shares. This debt was exchanged at a price of approximately \$0.60 per common share.

Subsequent to the year-end, the Company completed a financing in the amount of \$5,203,000 on August 2, 2007. As a result of this financing an additional 4,730,000 common shares were issued. Shortly thereafter, on August 17, 2007 the Underwriters exercised their over-allotment option and issued an additional 473,900 common shares for gross proceeds of \$521,290.

Operating Cash Flows: Cash used in operations for the year ending June 30, 2007 was \$2,648,241 (2006 - \$1,805,682). On a monthly average basis, the Company anticipates that it will require \$325,000 to \$375,000 to fund current levels of operating activity as compared to last year where operating cash requirements ranged from \$200,000 to \$250,000, until such time as it begins generating sufficient revenues to fund its ongoing operations or goes back to market to raise additional capital. As described in the previous section, in order to execute the Company's business plan, a financing was completed in August 2007, subsequent to the year end, in the amounts of \$5,203,000 and \$521,290, which significantly increases the available working capital of the Company. In the previous fiscal period ending June 30, 2006 a private placement in the amount of \$2,500,000 was priced at \$0.50 per common share. This financing transaction was completed in April 2006. Any forecast of future cash inflows or outflows is subject to a certain amount of uncertainty; therefore, it may be necessary to raise additional capital to meet business objectives and longer-term liquidity demands. If the additional capital is raised through the sale of equity or convertible debt securities, this would result in dilution to the existing shareholders. There can be no assurances that any of these financing alternatives will be available in the amounts and under terms that would be acceptable to management.

7. Other Assets.

Deferred Technology Charges: Medipattern has four patent applications pending, which comprise two patent application families, each family including a US application and an application under the Patent Cooperation Treaty (PCT application) which is an international patent law treaty. The subject matter of one patent application family is intended to cover technology relating to computer-aided analysis of image data obtained from multiple modalities, including (2D, 3D, and temporal) ultrasound, MRI, and MRS data, and application of artificial intelligence to automated generation of diagnostic assessment of detected lesions based on results of pattern recognition in and feature extraction from medical imaging data, among others. The subject matter covered by the second patent application family relates to the same general type of technology but is more focused on B-CAD applications. During the year, management determined that it would no longer pursue the patent on the design of the whole-breast ultrasound scanner. All the research and development costs relating to the development of the prototype ultrasound scanner had previously been expensed as incurred. However, certain legal costs and application fees relating to the filing of the patent applications had been deferred. The total amount deferred relating to the ultrasound scanner technology was \$58,701. As a result of management's decision not to continue to pursue the patent application, this amount has been written off. The deferred technology balance is \$135,496 as at June 30, 2007 (June 30, 2006 - \$161,677). The remaining capitalized costs relate directly to the Company's core technologies.

Management determined that it would use the technology that it developed for the ultrasound whole-breast scanner to assist other companies to bring their products to market so that Medipattern could license its B-CAD technology as the integrated, diagnostic software application. This strategy would ensure that Medipattern would not directly compete with those companies to whom Medipattern is attempting to sell its B-CAD solution. The remaining deferred technology charges were incurred to develop patent applications relating to the ultrasound technology B-CAD and B-CADMRI. Therefore, these capitalized costs relate directly to the Company's continuing core CAD technologies. At such time that the patents are approved, management will review the expected life of the technology and the expected revenue that may be generated from the technology in order to determine the estimated useful life at that time and begin to amortize the cost of the intangible item over the estimated useful life.

Property and Equipment: The net book value of property and equipment is \$77,780 (2006 - \$71,108). The increase in capital cost before depreciation is mainly attributable to the purchase of laptop computers for new staff and marketing demonstrations. No other significant purchase was necessary.

8. Other Liabilities.

Deferred Revenue: Deferred revenue decreased to \$218,791 as at June 30, 2007 (2006 - \$382,884). This balance includes the current and long-term portions of \$164,093 and \$54,698 respectively (2006 - \$164,093 and \$218,791 respectively). The deferred revenue arose when Medipattern pre-sold B-CAD licenses in January 2005 in the amount of \$492,280 to Cedara. Through the end of October 2005, the entire amount received was reported as deferred revenue. In November 2005, circumstances changed that allowed the Company to begin to recognize the deferred revenue as income. First, Medipattern completed the integration of B-CAD into Cedara's platform technology, and there are no further costs that Medipattern has to incur on their 1.0 software release. Second, Cedara issued their General Market Availability (GMA) approval in November 2005, which means that the product is available for commercial sale. The deferred revenue will now be recognized over the anticipated exclusivity period of the contract, which is expected to extend for 36 months from the time Cedara released their GMA approval (i.e. November 2008). Recognition could be accelerated in the event that sales of B-CAD exceed the minimum levels contemplated by this accounting methodology.



9. Description of Securities.

The Company has authorized an unlimited number of common shares. As at June 30, 2007, there were 37,768,846 common shares issued and outstanding (2006 – 37,521,860). There are no other classes of shares authorized. In 2007, the number of common shares increased by 246,986 which resulted from the exercising of 12,000 stock options and the exercising of 234,986 common share purchase warrants. In fiscal 2006, the number of common shares increased by 5,568,771 as a result of a number of different financing transactions as follows: (i) the exercise of 299,273 stock options with an average exercise price of \$0.44; (ii) the conversion of \$80,903 of debt to 80,895 common shares; (iii) the conversion of loans payable to shareholders of \$114,419 into 188,604 common shares; and (iv) a private placement of \$2,500,000 at a price of \$0.50 per common share for a total of 5,000,000 common shares.

The number of stock options decreased in 2007 to 2,901,500 (June 30, 2006 – 3,464,000). The number of warrants outstanding also decreased. As at June 30, 2007 warrants outstanding totaled 1,205,270 (2006 – 6,420,765). The number of stock options and warrants decreased significantly during 2007. Warrants outstanding decreased by 5,215,495 to 1,205,270. A total of 4,980,509 warrants expired on October 22, 2006 and 234,986 common share purchase warrants were exercised in May 2007. Stock options decreased by 562,500. Agent options in the amount of 503,500 expired without exercise, 307,000 stock options were forfeited as a result of a resignation and 12,000 stock options were exercised. This was partially offset by the issuance of 260,000 stock options to new employees.

	2007	Weighted Avg Exercise Price	2006	Weighted Avg Exercise Price
Common Shares	37,768,846	N/A	37,521,860	N/A
Warrants	1,205,270	\$ 1.25	6,420,765	\$ 0.76
Options	2,901,500	\$ 0.59	3,464,000	\$ 0.58
Fully diluted	<u>41,875,616</u>		<u>47,406,625</u>	

The weighted average life of the options outstanding is 2.59 years (2006 - 3.10 years) and the exercise prices range from \$0.25 to \$2.50 per share. The weighted average life of the warrants is 0.77 years (2006 – 0.59 years) and the exercise price of all remaining warrants is \$1.25 per common share.

10. Other Information.

Contractual Obligations: The Company has no long-term contractual obligations to any supplier or service provider. The lease of the Company's premises expired in January 2006. There is no remaining obligation under this lease. Management is currently undergoing a review of the Company's real estate requirements before signing a new lease and will continue in the existing premises on a month-to-month basis until a determination is made.

Material Off-Balance Sheet Arrangements: There are no material off-balance sheet arrangements.

Related-Party Transactions: As at June 30, 2007, the Company has no related-party transactions. In fiscal 2006, loans from founding shareholders in the amount of \$114,419 were exchanged for common shares of Medipattern as described in Section 9 above.

Subsequent Event: On August 2, 2007, the Company completed a financing in the amount of \$5,203,000 at a price of \$1.10 per common share. This resulted in the issuance of an additional 4,730,000 common shares.

Shortly thereafter, on August 17, 2007, the Underwriters exercised their over-allotment option and issued an additional 473,900 common shares for gross proceeds of \$521,290. As a result of these transactions, the number of common shares outstanding increased from 37,768,846 to 42,972,746.

11. Controls and Procedures.

Disclosure controls and procedures are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the Chief Executive Officer and the Chief Financial Officer, on a timely basis so that the appropriate decisions can be made regarding public disclosure.

The Chief Executive Officer and the Chief Financial Officer of the Company conducted an evaluation of the disclosure controls and concluded that they were effective to provide reasonable assurance that material information regarding the disclosures was made known to them on a timely basis.

12. Business and Financial Risk Factors.

Limited Operating History: Medipattern has a limited operating history upon which its business can be evaluated. Its business and prospects must be considered in light of the risk, expenses, and difficulties frequently encountered by companies in the early stage of development. Such risks include the unpredictable nature of Medipattern's business, Medipattern's ability to anticipate and adapt to a dynamic market, and the ability to identify, attract, and retain qualified personnel. There can be no assurance that Medipattern will be successful in addressing these risks.

Operating Results: There is no assurance that Medipattern will earn profits in the future, or that profitability will be sustained. Medical diagnostic businesses typically require significant financial resources, and there is no assurance that future revenues will be sufficient to generate the funds required to continue Medipattern's business development and marketing activities. If Medipattern does not have sufficient capital to fund its operations, it may be required to reduce its sales and marketing efforts or forego certain business opportunities.

Management: The medical diagnostics field involves a substantial degree of risk, which a combination of experience, knowledge, and careful evaluation may not be able to overcome. Shareholders must rely on the ability, expertise, judgment, direction, and integrity of the management of Medipattern. The Company's success will be dependent on the services of a number of key personnel, including its executive officers and other key employees, the loss of any one of whom could have an adverse effect on its operations and business prospects. The future performance of the Company is dependent on the services of a number of personnel, including the President and Chief Executive Officer, the Chief Technology Officer, and the Chief Financial Officer. To partially offset this risk, the Company has employment agreements with these three executive officers and carries \$2 million of key-man life insurance on the President and CEO. The ongoing success of the Company will also depend on its ability to attract and retain highly qualified engineering, management, manufacturing, marketing, and sales personnel. Failure to hire and retain such personnel could have a material adverse effect.

Competitive Market: Medipattern encounters and expects to continue to encounter intense competition in the breast imaging market. Competitors include large multinational corporations, including GE Medical Systems, Siemens, Philips, Toshiba, and Hitachi, as well as a number of other companies such as Hologic Corporation, iCAD, and U-Systems. These companies typically have a large installed base and greater financial, management, manufacturing, sales and marketing, and other resources. As a result, they may be able to more quickly adapt to new or emerging technologies and changes in customer requirements, or to devote greater resources to the development, manufacture, promotion, and sale of their products. Medipattern also faces competition from sellers of used imaging equipment, particularly general radiology systems, at prices substantially below the prices of new products.



Technological Change: Current medical diagnostic technology is susceptible to technological advances and the introduction of new software applications. It is also subject to changing technical standards, market trends, and customer preferences, and to competitive pressures which can, among other things, necessitate revisions in pricing strategies, price reductions, and reduced profit margins. The success of Medipattern will depend on its ability to secure technological superiority in its services and operations, and maintain such superiority in the face of new technologies. No assurance can be given that further modification of the B-CAD technology will not be required in order to meet demands or to make changes necessitated by developments made by competitors which might render such technology less competitive. The future success of Medipattern will be, in part, influenced by its ability to continue to adapt to change.

Product Liability: The current medical device industry is susceptible to personal injury claims resulting from design defects that may result in misdiagnosis of a disease or condition. Medipattern has sought to mitigate the risk of liability by designing the initial product as an interactive tool, directed by a learned intermediary, which includes adequate instructions for use, user interface dialog prompts, and error messages designed to alert the user to potential misuse or error. Further mitigation has been included in the product labeling, which indicates that patient management decisions should not be made based solely on the results of B-CAD analysis. The success of Medipattern will depend on its ability to train and support the clinical personnel who use this device as part of their diagnostic process, and to monitor use and performance of this device in the clinical environment.

Additional Capital Requirements/Ability to Continue as a Going Concern: Medipattern may require additional financing in order to make further development investments or take advantage of unanticipated opportunities. The ability of Medipattern to arrange such financing in the future will depend in part upon prevailing capital market conditions, as well as upon the business success of Medipattern. There can be no assurance that Medipattern will be successful in its efforts to arrange additional financing on terms satisfactory to Medipattern. If additional financing is raised by the issuance of shares or other forms of convertible securities from treasury, control of Medipattern may change and shareholders may suffer additional dilution. If adequate funds are not available, or are not available on acceptable terms, Medipattern may not be able to take advantage of opportunities, or otherwise respond to competitive pressures and remain in business.

Regulatory Environment: The Medipattern medical software applications are subject to review and approval by the US Food and Drug Administration prior to commercial distribution in the US. The FDA will determine the classification of the Medipattern product(s) under the Medical Devices Act of 1976. Generally, this regulatory scheme requires the FDA to assign each new device into one of three classifications: Class I (requires general controls and no submission); Class II (requires general controls and a 510(k) Premarket Notification); and Class III (requires Premarket Approval (PMA) and prior approval of the manufacturing process). These assignments are based upon the intended use of the device and any new issues of safety and/or effectiveness raised by the use, design, or manufacturability of the product. To date, Medipattern has successfully designed and labeled its initial product offering to obtain a 510(k) approval from the FDA. However, there can be no assurance that the FDA will classify future iterations of the product as Class II or that the FDA will not require a PMA for future product enhancements. For a 510(k) filing, the FDA is required to review the submission within 90 days and notify the manufacturer of the clearance of the product, or specify the additional information required to allow clearance of the device, or notify the manufacturer that the FDA has determined that the product is not substantially equivalent to products legally marketed in the US. There can be no assurances that the FDA will accept future generations of our product under a 510(k) submission or that the FDA will clear future submissions of the B-CAD product enhancements within 90 days or at all. Medipattern's success in its regulatory strategy will depend on its ability to seek and retain expert regulatory advice from individuals known to have a strong working relationship with FDA and experience in this specific

field of medicine. The Company also is required to maintain a quality system in compliance with the US Quality System Regulation (21 CFR 820) and maintain compliance with the design control regulations. The Company is subject to audit at any time by the FDA, to ensure compliance with these regulatory requirements. Failure to maintain these requirements may result in a notice of violation, a warning, or further action by the FDA, including remedies involving seizure and injunction. Medipattern's success in maintaining compliance with the applicable quality system regulations will depend on its ability to retain individuals known to have quality assurance and design control expertise and experience in this specific field.

Protection of the Company's Intellectual Property: The Company's success will depend in significant part, on its ability to obtain, maintain, and enforce patent and trade-mark protection. No assurance can be given that actions or claims alleging trademark, patent, or copyright infringement will not be brought against the Company with respect to current or future use of the Company's intellectual property, or that, if such actions are brought, the Company will ultimately prevail. Any such claiming parties may have significantly greater resources than the Company to pursue litigation of such claims. Any such claims, whether with or without merit, could be time consuming, result in costly litigation, cause delays in introducing new or improved services, require the Company to enter into additional royalty or licensing agreements, or cause the Company to discontinue use of the challenged intellectual property at potential significant expense to the Company associated with the marketing of a new name or the development or purchase of replacement technology, all of which could have a material adverse effect on the Company.

The Company expects to rely on patents to protect a significant part of its intellectual property and competitive position. The Company's patent applications pending, and patents that may be issued in the future, may not afford meaningful protection for its technologies and products. In addition, the Company's current and future patent applications may not result in the issuance of patents in Canada, the US, or other countries. Legal standards relating to the validity of patents and the proper scope of their claims are still evolving. If the Company is not able to obtain and enforce adequate patent protection, the Company's ability to prevent competitors from making, using, and selling competing products will be limited, which could have a material adverse effect on the Company's business, financial condition, or results of operations.

ADDITIONAL INFORMATION RELATING TO MEDIPATTERN MAY BE ACCESSED BY VISITING THE SEDAR WEBSITE AT www.sedar.com.

