

**CANNASAT THERAPEUTICS INC.**  
**(Formerly Cannasat Pharmaceuticals Inc.)**  
**SECOND QUARTER REPORT**  
**JUNE 30, 2006**

**Unaudited**

**CANNASAT THERAPEUTICS INC.**  
**(Formerly Cannasat Pharmaceuticals Inc.)**  
**June 30, 2006**

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**CANNASAT THERAPEUTICS INC.**  
**(Formerly Cannasat Pharmaceuticals Inc.)**  
**Balance Sheets**

	June 30, 2006 (unaudited)	December 31, 2005 (audited)
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash and cash equivalents	\$ 1,359,242	\$ 632,219
Sundry receivables	218,274	178,631
	<u>1,577,516</u>	<u>810,850</u>
CAPITAL ASSETS (Note 3)	10,901	2,615
LONG-TERM INVESTMENT (Note 4)	1,480,733	1,539,689
DEFERRED COSTS (Note 5)	-	207,308
DEFERRED COMPENSATION EXPENSE	256,000	304,000
OTHER INTANGIBLE ASSETS (Note 7)	200,000	200,000
	<u>\$ 3,525,150</u>	<u>\$ 3,064,462</u>
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	\$ 292,437	\$ 399,838
Current portion of notes payable (Note 8)	100,000	100,000
	<u>392,437</u>	<u>499,838</u>
NOTES PAYABLE (Note 8)	-	20,900
	<u>392,437</u>	<u>520,738</u>
COMMITMENTS (Notes 4, 6 and 11)		
<b>SHAREHOLDERS' EQUITY</b>		
SHARE CAPITAL (Note 6(b))	6,584,448	4,954,753
CONTRIBUTED SURPLUS (Note 6(e))	386,150	248,206
DEFICIT	(3,837,885)	(2,659,235)
	<u>3,132,713</u>	<u>2,543,724</u>
	<u>\$ 3,525,150</u>	<u>\$ 3,064,462</u>

The accompanying notes are an integral part of these Financial Statements

APPROVED BY THE BOARD

..... Director

..... Director

**CANNASAT THERAPEUTICS INC.**  
**(Formerly Cannasat Pharmaceuticals Inc.)**  
**Statements of Operations and Deficit**

	Three Months Ending		Six Months Ending	
	June 30,		June 30,	
	2006	2005	2006	2005
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
<b>REVENUE</b>				
Interest income	\$ 22,003	\$ 12,822	\$ 33,580	\$ 24,549
<b>EXPENSES</b>				
General and administrative	353,227	283,246	564,204	513,843
Research and development	262,326	77,215	430,779	145,413
Amortization of capital assets	438	560	715	560
Stock option compensation expense (Note 6)	78,789	26,680	157,578	111,911
	694,780	387,701	1,153,276	771,727
<b>LOSS BEFORE EQUITY LOSS</b>	(672,777)	(374,879)	(1,119,696)	(747,178)
<b>LOSS FROM EQUITY ACCOUNTED INVESTMENT</b>	(37,583)	(15,078)	(58,956)	(30,156)
<b>NET LOSS FOR THE PERIOD</b>	(710,360)	(389,957)	(1,178,652)	(777,334)
<b>DEFICIT, BEGINNING OF PERIOD</b>	(3,127,525)	(1,142,860)	(2,659,235)	(755,483)
<b>DEFICIT, END OF PERIOD</b>	\$ (3,837,885)	\$ (1,532,817)	\$ (3,837,887)	\$ (1,532,817)
<b>LOSS PER SHARE - basic and diluted</b>	\$ (0.01)	\$ (0.01)	\$ (0.02)	\$ (0.02)
<b>WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING</b>	62,064,513	42,657,852	58,416,643	41,936,628

The accompanying notes are an integral part of these Financial Statements

(Formerly Cannasat Pharmaceuticals Inc.)

**Statements of Cash Flows**

	Three Months Ending June 30,		Six Months Ending June 30,	
	2006 (unaudited)	2005 (unaudited)	2006 (unaudited)	2005 (unaudited)
<b>NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING ACTIVITIES</b>				
<b>OPERATING</b>				
Net loss for the period	\$ (710,360)	\$ (389,957)	\$ (1,178,652)	\$ (777,334)
Items not affecting cash				
Loss from equity accounted investment	37,583	15,078	58,956	30,156
Amortization of capital assets	438	560	715	560
Stock option compensation expense	78,789	26,680	157,578	111,911
	(593,550)	(347,639)	(961,403)	(634,707)
Changes in non-cash operating working capital items				
Sundry receivable	(8,229)	(40,265)	(39,644)	(57,298)
Accounts payable and accrued liabilities	(103,438)	218,891	(107,399)	332,518
	(705,217)	(169,013)	(1,108,446)	(359,487)
<b>INVESTING</b>				
Acquisition of capital assets	-	-	(9,000)	-
	-	-	(9,000)	-
<b>FINANCING</b>				
Deferred costs	-	-	207,308	-
Notes payable	(20,900)	-	(20,900)	-
Common shares issued	113,624	-	1,658,061	-
Class A common shares issued	-	380,000	-	568,850
	92,724	380,000	1,844,469	568,850
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS DURING THE PERIOD</b>	(612,493)	210,987	727,023	209,363
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	1,971,735	989,659	632,219	991,283
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	\$ 1,359,242	\$ 1,200,646	\$ 1,359,242	\$ 1,200,646
<b>SUPPLEMENTARY CASH FLOW INFORMATION</b>				
Cash and cash equivalents comprise the following:				
Cash	\$ 72,387	\$ 128,820	\$ 72,387	\$ 128,820
Cash equivalents	1,286,855	1,071,826	1,286,855	1,071,826
	\$ 1,359,242	\$ 1,200,646	\$ 1,359,242	\$ 1,200,646

**SUPPLEMENTARY CASH FLOW INFORMATION (Note 12)**

The accompanying notes are an integral part of these Financial Statements

(Formerly Cannasat Pharmaceuticals Inc.)

**Notes to the Unaudited Interim Financial Statements**

**June 30, 2006**

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**1. DESCRIPTION OF BUSINESS**

Cannasat Therapeutics Inc. (the “Company”) is a research and development company committed to the development of novel cannabinoid-based prescription medicines for patients with unmet medical needs. Cannasat Pharmaceuticals Inc. was incorporated under the Canada Business Corporations Act on January 16, 2004 and changed its name from Cannasat Pharmaceuticals Inc. to Cannasat Therapeutics Inc. on January 25, 2005. Cannasat Therapeutics Inc. (“Cannasat”) and Lonsdale Public Ventures Inc. (“Lonsdale”) were amalgamated on March 15, 2006 under the Business Corporations Act (Canada) and continued as one company with the name “Cannasat Therapeutics Inc.”.

**2. BASIS OF ACCOUNTING**

These interim financial statements are unaudited and have not been reviewed by the Company’s auditors. The management of the Company has prepared these interim financial statements in accordance with Canadian Generally Accepted Accounting Principles and follow the same accounting policies and methods of application as the audited financial statements of the company for the year ended December 31, 2005. These statements should be read in conjunction with the audited financial statements of Cannasat for the year ended December 31, 2005. The disclosure in these interim financial statements does not conform in all respects to Generally Accepted Accounting Principles in Canada for annual financial reporting.

In the opinion of management, all adjustments considered necessary for fair presentation have been included in these financial statements. Operating results for the six months ended June 30, 2006 may not be indicative of the results that may be expected for the full year ending December 31, 2006.

**3. CAPITAL ASSETS**

	June 30, 2006		
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
	\$	\$	\$
Computer equipment	5,746	2,240	3,506
Furniture and Fixtures	7,650	255	7,395
<b>Total</b>	<b>13,396</b>	<b>2,495</b>	<b>10,901</b>

	December 31, 2005		
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
	\$	\$	\$
Computer equipment	4,396	1,781	2,615

Capital assets are recorded at cost and are amortized on the diminishing balance method based on their estimated useful life as follows:

- Computer equipment - 30% per annum
- Furniture and Fixtures - 20% per annum

(Formerly Cannasat Pharmaceuticals Inc.)

**Notes to the Unaudited Interim Financial Statements****June 30, 2006**

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**4. LONG-TERM INVESTMENT**

	June 30, <u>2006</u>	December 31, <u>2005</u>
268,585 Class A common shares representing 14.94% (December 31, 2005 – 16.06%) of voting shares, and 140,000 Class A common share purchase warrants exercisable at \$2.00 per share of Prairie Plant Systems Inc., recorded on an equity basis	\$ 1,000,733	\$ 1,059,689
Loan receivable, 7%, convertible to Class A common shares of Prairie Plant Systems Inc.	<u>480,000</u>	<u>480,000</u>
	<u>\$ 1,480,733</u>	<u>\$ 1,539,689</u>

In August 2004, Cannasat acquired 268,585 Class A common shares and 140,000 Class A common share purchase warrants of Prairie Plant Systems Inc. at a purchase price of \$1,120,001. The warrants were for additional Class A common shares and were exercisable at \$2.00 per share expiring May 14, 2006. The Company did not exercise these warrants.

The loan receivable due from Prairie Plant Systems Inc. is secured by a general security agreement. The loan has no fixed principal repayment terms and may be converted into Class A common shares at \$4.17 per share up to July 31, 2007. Interest is payable monthly on the principal balance at an annual rate of 7%. As at August 24, 2006 interest is paid in full to February 2006 with an agreement to settle the outstanding balance by the end of September 2006.

On August 17, 2004, Cannasat entered into a strategic alliance agreement with Prairie Plant Systems Inc. In order to maintain this strategic alliance agreement, Cannasat has made an on-going commitment to, commencing in the fiscal year of Prairie Plant Systems Inc. ending October 31, 2005, spend or contribute at least \$250,000 per fiscal year on one or more of the following cannabis or cannabinoid related activities: product development, clinical trials, pursuit of other strategic relationships, public relations, regulatory affairs, communications, marketing, and/or other such activities as the parties may reasonably agree upon. Cannasat has already exceeded the \$250,000 commitment in the first six months of Cannasat's current fiscal year, thereby ensuring that the strategic alliance agreement will be in effect for the year ended December 31, 2006. The initial term of the strategic alliance expires on October 31, 2016.

The difference between the cost of the investment and the underlying net book value of the assets acquired was approximately \$952,000 and has been allocated to property in the amount of \$36,000, contracts in the amount of \$566,000 and goodwill of \$350,000. The underlying depreciable contracts will be amortized at an annual rate of approximately \$81,000.

**5. DEFERRED COSTS**

At December 31, 2005, Cannasat had deferred costs totaling \$207,308 which consisted primarily of professional fees related to the amalgamation and private placement disclosed in Note 6(b). These deferred charges were allocated to share capital upon completion of the amalgamation and financing transaction on March 15, 2006.

(Formerly Cannasat Pharmaceuticals Inc.)

**Notes to the Unaudited Interim Financial Statements**

**June 30, 2006**

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**6. SHARE CAPITAL**

a) *Authorized*  
 Unlimited numbers of  
 Common shares with no par value

b) *Issued*  
 A summary of the foregoing common shares, Class A common shares and Class A common share purchase warrants issued is as follows:

	Number of Shares #	Number of Warrants #	Net Proceeds \$
June 30, 2006			
Common	62,199,957	-	6,359,187
Common share purchase warrants *	-	1,500,000	225,261
			<u>6,584,448</u>
December 31, 2005			
Common	12,000,000	-	60,000
Class A common	9,449,238	-	4,669,492
Class A common share purchase warrants *	-	1,500,000	225,261
			<u>4,954,753</u>

\* Note: For each warrant issued, the holder is entitled to 4.5 Common shares. This arises due to anti-dilution provisions attached to the warrants which were triggered in the August 2005 restructuring (1.5x) and the March 2006 going public transaction (3x).

*Amalgamation*

On March 15, 2006, Cannasat amalgamated with Lonsdale pursuant to an Amalgamation Agreement under the Canada Business Corporations Act and continued as one corporation with the name "Cannasat Therapeutics Inc."

Lonsdale was a capital pool company that traded on the TSX Venture Exchange (the "Exchange") whose principal business was to identify and evaluate assets or businesses with a view to completing a Qualifying Transaction. The amalgamation between Cannasat and Lonsdale constituted the Qualifying Transaction for Lonsdale pursuant to the policies of the Exchange.

In accordance with the Amalgamation Agreement, holders of Lonsdale Common Shares were issued 6,532,662 Common Shares of the Company. In addition, the holders of Lonsdale's options (1,155,000) are entitled to acquire 967,336 Common Shares of the Company. At June 30, 2006, 135,500 options were exercised to acquire 113,485 common shares. Proceeds of these transactions totaled \$27,100.

In accordance with the Amalgamation Agreement, the security holders of Cannasat received an aggregate of 55,226,115 Common Shares of the Company, and replacement warrants (2,090,000) to acquire 9,405,000 Common Shares of the Company and replacement options (1,525,000) to acquire 4,575,000 Common Shares of the Company. At June 30, 2006, 62,500 replacement warrants were exercised to acquire 281,250 common shares. Proceeds of these transactions totaled \$65,625.



(Formerly Cannasat Pharmaceuticals Inc.)

## Notes to the Unaudited Interim Financial Statements

June 30, 2006

## 6. SHARE CAPITAL (continued)

## b) Issued (continued)

Immediately following the amalgamation, 35,058,879 Common Shares of the Company were subject to escrow and are to be released over a period of 72 months on the basis of 5% six months after the final Exchange bulletin (March 23, 2006), 5% every six months thereafter for the next 18 months and 10% every six months thereafter for the next 48 months. A further 705,000 Common Shares of the Company were subject to escrow and are to be released over a period of 36 months on the basis of 10% on the date of the final Exchange bulletin and 15% every six months thereafter.

Share issuance costs related to the Common Shares and share purchase warrants have been charged to equity on a pro-rata basis. There have been no dividends paid or declared to date.

The following common shares, Class A common shares and Class A common share purchase warrants were issued for the proceeds noted.

Date	Number of shares #	Amalgamation - replacement common shares #	Proceeds \$	Share Issuance Costs \$	Net Proceeds \$
<u>Common shares</u>					
Balance, December 31, 2005	12,000,000	23,049,390	60,000	-	60,000
<u>Class A common shares</u>					
Balance, December 31, 2005	9,449,238	28,347,717	4,932,738	263,246	4,669,492
February 8, 2006	1,276,336	3,829,008	1,148,703	56,000	1,092,703
	10,725,574	32,176,725	6,081,441	319,246	5,762,195
Total Shares (Cannasat)	22,725,574	55,226,115	6,141,441	319,246	5,822,195
March 15, 2006 (Lonsdale)	7,800,000	6,532,662	779,151	-	779,151
Amalgamation costs				373,784	(373,784)
Total Shares (Cannasat and Lonsdale), March 31, 2006	30,525,574	61,758,777	6,920,592	693,030	6,227,562
April 14, 2006		281,250	65,625		65,625
May 3, 2006		46,445	20,900		20,900
May 24, 2006		77,438	18,492		18,492
June 2, 2006		36,047	8,608		8,608
Exercise of stock options - reallocation of valuation		-	18,000		18,000
Total, June 30, 2006		62,199,957	7,052,217	693,030	6,359,187
<u>Class A common share purchase warrants</u>					
August 18, 2004	1,500,000	1,500,000	240,000	14,739	225,261
			7,292,217	707,769	6,584,448

**Notes to the Unaudited Interim Financial Statements**

**June 30, 2006**

**6. SHARE CAPITAL (continued)**

*c) Class A common shares and share purchase warrants*

The fair value of the Cannasat warrants has been estimated to be \$240,000, which value has been segregated from the proceeds of the initial issuance of the Class A common shares.

*d) Employee and non-employee stock options and warrants*

During the six months ended June 30, 2006, 361,086 compensation options were issued to the Agents that were engaged in the private placement forming a part of the Qualifying Transaction. Each option entitles the holder to purchase one common share of the Company at a price of \$0.30 per common share. These options expire on March 15, 2007.

A summary of the status of the options and warrants as of June 30, 2006 and changes during the period is as follows:

	Weighted Exercise Price	# Shares issuable on exercise of options
Options outstanding at December 31, 2005	0.290	4,575,000
Lonsdale Options	0.239	967,336
Granted during the period	0.300	361,086
Exercised	0.239	(113,485)
Cancelled or expired	-	-
<b>Outstanding and exercisable as at June 30, 2006</b>	<b>0.283</b>	<b>5,789,937</b>

Fair value of the options granted during the period has been estimated on the date of issue using the Black-Scholes pricing model with the following assumptions: dividend yield 0%, expected volatility 75%, risk-free interest rate 4% and expected life of 2 years.

In consideration of the provision of the services of certain consultants, Cannasat granted the consultants warrants entitling the consultants to acquire up to an aggregate of 577,500 Class A common shares at \$1.00 per share ("Cannasat B warrants") and 12,500 Class A common shares at \$1.25 per share ("Cannasat C warrants").

Fair value of the options and warrants granted to non-employees has been estimated on the date of issue using management's estimate of the value of the consulting services provided. Compensation related to consulting services in the amount of \$111,375 was expensed during the year ended December 31, 2005 (2004 - \$41,625).

Details of the Cannasat B and Cannasat C warrants outstanding as at June 30, 2006 are as follows:

Number of Warrants Issued *	Exercised	Outstanding at June 30, 2006 *	Expiry Date	Exercise Price
12,500	12,500	-		\$1.25
55,000	50,000	5,000	August 18, 2009	\$1.00
22,500		22,500	September 1, 2009	\$1.00
500,000		500,000	September 27, 2007	\$1.00
<b>590,000</b>	<b>62,500</b>	<b>527,500</b>		

\* Note: For each warrant issued, the holder is entitled to 4.5 Common shares. This arises due to anti-dilution provisions attached to the warrants which were triggered in the August 2005 restructuring (1.5x) and the March 2006 going public transaction (3x).

**(Formerly Cannasat Pharmaceuticals Inc.)****Notes to the Unaudited Interim Financial Statements****June 30, 2006**

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**6. SHARE CAPITAL (continued)***e) Contributed surplus*

Contributed surplus represents the fair value of stock option compensation earned by directors, officers, employees and certain consultants of the Company as follows:

Closing Balance, December 31, 2005	\$	248,206
Options exercised during the period		(18,000)
Compensation earned during the period		155,944
<hr/>		
Balance, June 30, 2006	\$	386,150

**7. OTHER INTANGIBLE ASSETS**

On June 10, 2005, Cannasat entered into a licence agreement with a research and development company. In order to acquire the licence Cannasat executed and delivered two promissory notes on June 30, 2005 (see Note 8) in the aggregate principal amount of \$100,000 and agreed to issue 117,648 Class A common shares at an aggregate subscription price of \$100,000 at a deemed value of \$0.85 per share (pre-amalgamation price). In addition to the acquisition costs, Cannasat has agreed to pay a combination of milestone-based payments and royalties.

**8. NOTES PAYABLE**

Agreements were made by Cannasat to settle accounts with two suppliers one of which is also a warrant holder. Two non-interest bearing promissory notes were issued in the aggregate amount of \$20,900, payable within 30 days following the going public date if this date occurs prior to September 1, 2009. Otherwise, the notes expire and no amount is due and payable. The notes may be paid in cash or the issuance of common shares equal in number to the value of the notes, each at the option of the issuer. On May 3, 2006 46,445 common shares were issued to retire these notes.

In an unrelated transaction, promissory notes in the aggregate principal amount of \$100,000 were issued by Cannasat on June 30, 2005 in connection with the acquisition of the agreement for the world-wide licence to make, use or sell certain licensed products (see Note 7). The notes bear interest at 8% per annum, calculated monthly and payable in quarterly installments effective January 1, 2006. The first note in the principal amount of \$50,000 is due on demand no earlier than December 30, 2005 and may be converted in whole or in part into common shares no later than June 30, 2009 at \$0.85 per share (pre-amalgamation price) at the option of the holder. The second promissory note also with a principal amount of \$50,000 is due on demand no earlier than the date of issuance of filed patents in specific jurisdictions. In the event that the filed patents are not issued, 29,412 Class A common shares at \$0.85 per share (pre-amalgamation price) may be issued at the option of the issuer as full and final settlement of the note. The second promissory note may be converted in whole or in part into common shares no later than June 30, 2009 at \$0.85 (pre-amalgamation price) per share at the option of the holder.

(Formerly Cannasat Pharmaceuticals Inc.)

**Notes to the Unaudited Interim Financial Statements**

**June 30, 2006**

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**9. RELATED PARTY TRANSACTIONS**

During the periods presented, the Company made payments to Hill & Gertner Capital Corporation, which is a corporation in which the Company's chief executive officer and another director control. Related party transactions have been recorded at the exchange amount which is management's estimate of the fair value of such transactions as follows:

	June 30, <u>2006</u>	June 30, <u>2005</u>
Rent and office expenses and services	\$ -	\$ 79,700
Management fees	\$ 72,000	\$ 72,000
Commissions for shares issued	\$ -	\$ 16,650

Commencing September 1, 2005 Cannasat contracted directly with third parties for premises and office services.

**10. INCOME TAXES**

At December 31, 2005, the Company has approximately \$2,355,000 of non-capital losses, which, under certain circumstances can be used to reduce the taxable income of future years. The tax effect is not recorded in these financial statements. The non-capital losses expire as follows:

<u>Available To</u>	<u>Amount (\$)</u>
2014	595,000
2015	<u>1,760,000</u>
	<u>2,355,000</u>

Income tax recoveries for the current period are not included in the above schedule.

**11. COMMITMENTS**

The Company has entered into research and development obligations requiring total payments in the amount of \$70,000. The Company expects to retire these obligations by September 30, 2006.

**12. SUPPLEMENTARY INFORMATION**

The following significant transactions did not generate or use cash:

	Three Months Ending		Six Months Ending	
	June 30,		June 30,	
	2006	2005	2006	2005
Class A common shares	\$ 38,900	\$ -	\$ (67,266)	\$ -
Contributed surplus	\$ 36,789	\$ 59,911	\$ 386,150	\$ 117,286
Compensation expense	\$ (78,789)	\$ (26,680)	\$ (157,578)	\$ (111,911)
Deferred expense	\$ -	\$ -	\$ (207,308)	\$ -
Income taxes paid	\$ -	\$ -	\$ -	\$ -
Interest paid	\$ -	\$ -	\$ -	\$ -

**Notes to the Unaudited Interim Financial Statements**

**June 30, 2006**

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**13. SUBSEQUENT EVENTS**

On August 3, 2006 the company completed a non-brokered private placement of 3,815,000 units at a price of \$0.20 per unit raising gross proceeds of \$763,000. Each unit consists of one common share and one-half of one share purchase warrant. Each whole share purchase warrant entitled its holder to acquire one common share at a price of \$0.30 until August 3, 2008. The common shares issued under the private placement are subject to a hold period of four months expiring on December 4, 2006. A commission of 8% was paid in connection with subscribers for units introduced through brokers.

On August 21, 2006, the Company received \$34,206 from Canada Revenue Agency pertaining to a Scientific Research and Experimental Development claim for the period ended December 31, 2004, submitted on June 30, 2006.