# CANNASAT THERAPEUTICS INC.
# SECOND QUARTER REPORT
# June 30, 2008

**Unaudited**

# CANNASAT THERAPEUTICS INC.
# June 30, 2008

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# CANNASAT THERAPEUTICS INC.

## Interim Balance Sheets

| | | June 30, 2008 (unaudited) | | December 31, 2007 (audited) |
|---|---|---|---|---|
| **ASSETS** | | | | |
| CURRENT | | | | |
| Cash and cash equivalents | $ | 1,454,819 | $ | 787,469 |
| Sundry receivables | | 34,080 | | 70,893 |
| | | 1,488,899 | | 858,362 |
| EQUIPMENT (Note 4) | | 6,729 | | 7,593 |
| LONG-TERM INVESTMENT (Note 5) | | - | | 887,690 |
| DEFERRED COMPENSATION EXPENSE (Note 6(c)) | | 64,000 | | 112,000 |
| OTHER INTANGIBLE ASSETS (Note 7) | | 200,000 | | 200,000 |
| | $ | 1,759,628 | $ | 2,065,645 |
| **LIABILITIES** | | | | |
| CURRENT | | | | |
| Accounts payable and accrued liabilities (Note 9) | $ | 323,406 | $ | 370,446 |
| Current portion of notes payable (Note 8) | | 100,000 | | 100,000 |
| | | 423,406 | | 470,446 |
| COMMITMENTS (Notes 6 and 10) | | | | |
| GOING CONCERN (Note 2) | | | | |
| **SHAREHOLDERS' EQUITY** | | | | |
| SHARE CAPITAL (Note 6(b)) | | 8,281,538 | | 7,805,573 |
| CONTRIBUTED SURPLUS (Note 6(e)) | | 1,080,520 | | 1,000,372 |
| DEFICIT | | (8,025,836) | | (7,210,746) |
| | | 1,336,222 | | 1,595,199 |
| | $ | 1,759,628 | $ | 2,065,645 |

APPROVED BY THE BOARD:

“Peter Palframan”, Director          “David Hill”, Director

# CANNASAT THERAPEUTICS INC.
## Interim Statements of Operations and Deficit

| | Three Months Ending June 30, | | Six Months Ending June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| | (unaudited) | (unaudited) | (unaudited) | (unaudited) |
| REVENUE | | | | |
| Interest income | $ 3,215 | $ 10,402 | $ 8,310 | $ 28,389 |
| EXPENSES | | | | |
| General and administrative | 336,120 | 266,337 | 562,484 | 506,486 |
| Research and development | 224,347 | 248,266 | 390,669 | 385,449 |
| Amortization of equipment | 432 | 566 | 863 | 1,132 |
| Stock option compensation expense | 70,208 | 61,820 | 128,148 | 119,123 |
| Recovery on scientific research | - | - | (26,454) | - |
| | 631,107 | 576,989 | 1,055,710 | 1,012,190 |
| LOSS BEFORE EQUITY GAIN (LOSS) | (627,892) | (566,587) | (1,047,400) | (983,801) |
| GAIN (LOSS) FROM EQUITY ACCOUNTED INVESTMENT (Note 5) | - | (38,291) | (22,626) | (64,918) |
| GAIN ON SALE OF EQUITY ACCOUNTED INVESTMENT (Note 5) | 254,936 | - | 254,936 | - |
| NET LOSS FOR THE PERIOD | (372,956) | (604,878) | (815,090) | (1,048,719) |
| DEFICIT, BEGINNING OF PERIOD | (7,652,880) | (5,421,811) | (7,210,746) | (4,977,970) |
| DEFICIT, END OF PERIOD | $ (8,025,836) | $ (6,026,689) | $ (8,025,836) | $ (6,026,689) |
| LOSS PER SHARE - basic and diluted | $ (0.01) | $ (0.01) | $ (0.01) | $ (0.02) |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | 73,349,344 | 69,010,896 | 71,991,285 | 67,538,245 |

# CANNASAT THERAPEUTICS INC.
## Interim Statements of Cash Flows

| | Three Months Ending June 30, 2008 (unaudited) | Three Months Ending June 30, 2007 (unaudited) | Six Months Ending June 30, 2008 (unaudited) | Six Months Ending June 30, 2007 (unaudited) |
|---|---|---|---|---|
| OPERATING | | | | |
| Net loss for the period | $ (372,956) | $ (604,878) | $ (815,090) | $(1,048,719) |
| Items not affecting cash | | | | |
| (Gain) Loss from equity accounted investment | (254,936) | 38,291 | (232,310) | 64,918 |
| Amortization of equipment | 431 | 566 | 863 | 1,132 |
| Shares issued for services | 25,000 | - | 25,000 | - |
| Stock option compensation expense | 70,208 | 61,820 | 128,148 | 119,123 |
| | (532,253) | (504,201) | (893,389) | (863,546) |
| Changes in non-cash operating working capital items | | | | |
| Sundry receivables | 25,823 | 13,547 | 36,813 | (10,509) |
| Accounts payable and accrued liabilities | (2,198) | (87,382) | (47,039) | (146,592) |
| | (508,628) | (578,036) | (903,615) | (1,020,647) |
| INVESTING | | | | |
| Proceeds from sale of long term investment (Note 5) | 1,120,000 | - | 1,120,000 | - |
| FINANCING | | | | |
| Exercise of stock options | - | - | - | 19,500 |
| Private placements, net of issue costs | - | 774,789 | 450,965 | 774,789 |
| | - | 774,789 | 450,965 | 794,289 |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS DURING THE PERIOD | 611,372 | 196,753 | 667,350 | (226,358) |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 843,447 | 787,252 | 787,469 | 1,210,363 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | 1,454,819 | 984,005 | 1,454,819 | $ 984,005 |
| CASH AND CASH EQUIVALENTS CONSIST OF: | | | | |
| Cash | $ 90,645 | $ 110,209 | $ 90,645 | $ 110,209 |
| Cash equivalents | 1,364,174 | 873,796 | 1,364,174 | 873,796 |
| | $ 1,454,819 | $ 984,005 | $ 1,454,819 | $ 984,005 |

SUPPLEMENTARY CASH FLOW INFORMATION (Note 11)

## 1. DESCRIPTION OF BUSINESS

Cannasat Therapeutics Inc. (the "Company") is a specialty pharmaceutical company with a focus on developing a portfolio of cannabinoid-based pharmaceutical products. 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"), a capital pool company, were amalgamated on March 15, 2006 under the Business Corporations Act (Canada) and continued as one company with the name "Cannasat Therapeutics Inc.".

## 2. ACCOUNTING POLICIES AND GOING CONCERN

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 for the preparation of interim financial information and follow the same accounting policies and methods of application as the audited financial statements of the Company for the year ended December 31, 2007. These statements should be read in conjunction with the audited financial statements of the Company for the year ended December 31, 2007. 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 interim financial statements. Operating results for the six months ended June 30, 2008 may not be indicative of the results that may be expected for the full year ending December 31, 2008.

While these interim financial statements have been prepared on the basis of accounting principles applicable to a going concern, several adverse conditions and events cast substantial doubt upon the validity of this assumption. The Company has used cash of $6,284,404 in operating activities from inception to June 30, 2008 and has an accumulated deficit of $8,025,836 as at June 30, 2008. The Company will be pursuing further financings. The Company's continued existence is dependent upon its ability to obtain additional financing as needed and to attain profitable operations.

If the going concern assumption were not appropriate for these financial statements, adjustments would be necessary to the carrying values of assets and liabilities, the reported net loss and the balance sheet classifications used.

## 3. CHANGES IN ACCOUNTING POLICIES

*(a) Accounting Changes*

Effective January 1, 2008, the Company adopted the following accounting standards recently issued by the CICA:

*(i) Capital Disclosures*

In December 2006, the CICA issued Section 1535, "Capital Disclosures", which establishes guidelines for the disclosure of information on an entity's capital and how it is managed. This enhanced disclosure enables users to evaluate the entity's objectives, policies and processes for managing capital. The Company has included disclosures recommended by this new section in Note 3(c) to these interim financial statements.

*(ii) Financial Instruments – Disclosure and Presentation*

In December 2006, the CICA issued Section 3862, "Financial Instruments – Disclosure", and Section 3863, "Financial Instruments – Presentation" to replace the existing Section 3861 "Financial Instruments – Disclosure and Presentation". Section 3862 requires enhanced disclosure on the nature and extent of financial instrument risks and how an entity manages those risks. Section 3863 carries forward the existing presentation requirements and provides additional guidance for the classification of financial instruments. The Company has included disclosures recommended by this new section in Notes 3(c) and 3(d) to these interim financial statements.

*(b) Recent Accounting Pronouncements*

*(i) International Financial Reporting Standards ("IFRS")*

In January 2006, the CICA Accounting Standards Board ("ACSB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with IFRS by the end of 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS.

*(c) Capital Management*

The company manages its capital structure and makes adjustments to it, based on the funds available to the company, in order to support its research and development activities. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The products which the Company currently has in its pipeline are in the research and development stage; as such the company is dependent on external financing to fund its activities. In order to carry out the planned research and development and pay for administration costs, the Company will spend its existing working capital and raise additional amounts as needed.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable.

There were no changes in the Company's approach to capital management during the six months ended June 30, 2008.

continued…

## 3. CHANGES IN ACCOUNTING POLICIES

*(d) Financial Risk Factors*

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

*(i) Credit Risk*

The Company has no significant concentration of credit risk arising from operations. Financial instruments included in other assets consist of goods and services tax due from the Federal Government of Canada. Management believes that the credit risk concentration with respect to these financial instruments is remote.

*(ii) Liquidity Risk*

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at June 30, 2008, the Company had a cash balance of $1,454,819 and sundry receivables of $34,080 (December 31, 2007 - $787,469 and $70,893) to settle current liabilities of $323,406 (December 31, 2007 - $370,446). All of the Company's financial liabilities have contractual maturities of less than 30 days and are subject to normal trade terms.

*(iii) Market Risk*

*(a) Interest rate risk*

The Company has cash balances and $100,000 in interest-bearing debt at a rate of 8% per annum (see Note 8) as at June 30, 2008. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. The Company considers interest rate risk to be minimal as investments are short term, the Company has a relatively small amount of interest-bearing debt, and future financing will be primarily secured from private placements.

*(b) Foreign currency risk*

The Company's functional currency is the Canadian dollar and most purchases are transacted in Canadian dollars. The Company funds certain research and development expenses in the United States and Europe on a cash call basis using the US Dollar and the EURO currency converted from its Canadian dollar bank accounts held in Canada. Management believes the foreign exchange risk derived from currency conversions is negligible and therefore does not hedge its foreign exchange risk.

*(c) Price risk*

The Company is exposed to price risk with respect to Active Pharmaceutical Ingredient (API) prices used in research and development activities. The Company closely monitors API prices in the United States and Europe to determine the appropriate course of action to be taken by the company.

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## 3. CHANGES IN ACCOUNTING POLICIES

*(e) Sensitivity Analysis*

The Company has designated its cash as held-for-trading, measured at fair value. Amounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities, which are measured at amortized cost.

As at June 30, 2008, the carrying and fair value amounts of the Company's financial instruments are the same, and there were no changes that occurred that attributed to credit risk.

The company does not hold significant balances in foreign currencies to give rise to exposure to foreign exchange risk.

Price risk is remote since the Company is still not a producing entity.

## 4. EQUIPMENT

| | June 30, 2008 | | |
|---|---|---|---|
| | Cost<br>$ | Accumulated Amortization<br>$ | Net Book Value<br>$ |
| Computer equipment | 5,746 | 3,974 | 1,772 |
| Furniture and fixtures | 7,650 | 2,693 | 4,957 |
| Total | 13,396 | 6,667 | 6,729 |

**5. LONG-TERM INVESTMENT**

| | June 30, 2008 | December 31, 2007 |
|---|---|---|
| 268,585 Class A common shares representing 0% (December 31, 2007 – 12.06%) of the voting shares of Prairie Plant Systems Inc., recorded on an equity basis | $ - | $ 887,690 |

During the three months ended June 30, 2008, the Company sold its investment in Prairie Plant Systems Inc. for $1,120,000. In addition, the strategic alliance agreement between the Company and PPS was terminated. The historical perspective of the PPS investment is included below.

In August 2004, the Company 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.

On August 17, 2004, the Company entered into a strategic alliance agreement with Prairie Plant Systems Inc. In order to maintain this strategic alliance agreement, commencing in the fiscal year of Prairie Plant Systems Inc. ending October 31, 2005, the Company has made an on-going commitment to 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. The Company has expended the required $250,000 commitment for the fiscal years of Prairie Plant Systems Inc. ended October 31, 2007, 2006 and 2005. The strategic alliance in the original agreement was to expire on October 31, 2016.

On August 17, 2004, the difference between the cost of the long-term investment in PPS and the underlying net book value of the assets acquired in PPS was calculated to be approximately $952,000. Of this difference $36,000 was related to PPS property, $566,000 was related to current and expected contracts in favour of PPS, and $350,000 was related to goodwill. The underlying depreciable contracts valued at $566,000 are amortized at an annual rate of approximately $81,000 and is included in the calculation of the loss from equity accounted investment.

**6. SHARE CAPITAL**

*a) Authorized*

Unlimited number of common shares with no par value

*b) Issued*

A summary of common shares, stock options and common share purchase warrants issued is as follows:

| | as at December 31, 2007 | | | |
|---|---|---|---|---|
| | Number of shares # | Number of options # | Number of warrants # | Net Proceeds $ |
| Common | 70,010,516 | - | - | 7,541,430 |
| Stock options | - | 3,243,740 | - | - |
| Common share purchase warrants | - | - | 4,939,402 | 264,143 |
| Total | 70,010,516 | 3,243,740 | 4,939,402 | 7,805,573 |

| | as at June 30, 2008 | | | |
|---|---|---|---|---|
| | Number of shares # | Number of options # | Number of warrants # | Net proceeds $ |
| Common | 73,468,849 | - | - | 7,949,750 |
| Stock options | - | 4,693,740 | - | - |
| Common share purchase warrants | - | - | 7,911,649 | 331,788 |
| Total | 73,468,849 | 4,693,740 | 7,911,649 | 8,281,538 |

A summary of common shares and number of shares issuable on exercise of stock options and warrants is as follows:

| | as at June 30, 2008 | | | |
|---|---|---|---|---|
| | Number of shares # | Number of shares issuable on exercise of options # | Number of shares issuable on exercise of warrants # | Total # |
| Common | 73,468,849 | - | - | 73,468,849 |
| Stock options | - | 7,046,214 | - | 7,046,214 |
| Common share purchase warrants | - | - | 9,661,649 | 9,661,649 |
| Total | 73,468,849 | 7,046,214 | 9,661,649 | 90,176,712 |

continued…

**6. SHARE CAPITAL**

*b) Issued (continued)*

At June 30, 2008, the following common shares, and common share purchase warrants were issued for the proceeds noted.

| | Number of Shares # | Proceeds $ | Share Issuance Costs $ | Net Proceeds $ |
|---|---|---|---|---|
| **Total Shares and Proceeds, December 31, 2007** | 70,010,516 | 8,409,582 | 868,152 | 7,541,430 |
| March 14, 2008 (i) | 3,333,333 | 423,725 | 40,405 | 383,320 |
| June 27, 2008 (iii) | 125,000 | 25,000 | - | 25,000 |
| **Total Shares and Proceeds, June 30, 2008** | 73,468,849 | 8,858,307 | 908,557 | 7,949,750 |

| | Number of Warrants # | Proceeds $ | Share Issuance Costs $ | Net Proceeds $ |
|---|---|---|---|---|
| **Total Share Purchase Warrants and Proceeds, December 31, 2007** | 4,939,402 | 293,985 | 29,842 | 264,143 |
| March 14, 2008 (i) | 3,333,333 | 76,298 | 8,653 | 67,645 |
| Expired Warrants (ii) | (361,086) | - | - | - |
| **Total Share Purchase Warrants and Proceeds, June 30, 2008** | 7,911,649 | 370,283 | 38,495 | 331,788 |
| **TOTAL PROCEEDS FROM SHARES AND WARRANTS, JUNE 30, 2008** | | 9,228,590 | 947,052 | 8,281,538 |

i) On March 14, 2008, Cannasat issued 3,333,333 units at $0.15 per unit for gross proceeds of $500,000. Each unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to acquire one common share of Cannasat for $0.20 per share until the earlier of March 14, 2009 and the period ending 20 days after prior written notice from Cannasat that the closing price of its shares on the Toronto stock Exchange has been at least $0.30 per share for 20 consecutive trading days. The fair value of the warrants was estimated at $67,645.

ii) On March 15, 2008, 361,086 warrants expired. These warrants had been issued on March 22, 2006 in lieu of compensation and their fair value of $46,365 was recorded directly to Contributed Surplus.

iii) On June 27, 2008, 125,000 common shares, valued at $25,000, were issued for consulting services provided during the second quarter of 2008. The Board of Directors of the Company approved this share issuance on June 25, 2008.

continued…

**6. SHARE CAPITAL (continued)**

*c) Stock options and warrants*

A summary of the status of options as of June 30, 2008:

| | Number of Options | Number of shares issuable on exercise of options | Weighted Exercise Price (/share) |
|---|---|---|---|
| | # | # | $ |
| Options outstanding at December 31, 2007 | 3,243,740 | 5,896,214 | 0.280 |
| Exercised | - | - | - |
| Granted | 1,600,000 | 1,600,000 | 0.200 |
| Cancelled or expired | (150,000) | (450,000) | 0.317 |
| Outstanding as at June 30, 2008 | 4,693,740 | 7,046,214 | 0.260 |

The weighted average grant date fair value of the stock options issued during the period ended June 30, 2008 is $0.15.

Fair value of the options granted during the period ended June 30, 2008, has been estimated on the date of issue using the Black-Scholes pricing model with the following assumptions: expected dividend yield of 0%, expected volatility of 94% and 98%, risk free return interest rate of 3.27% and expected life of 5 years.

In February 2004, 2,610,000 options granted were determined to have a value of $513,485. Of this amount, $109,485 was expensed in 2004, $100,000 was expensed during the year ended December 31, 2005, $96,000 was expensed during the year ended December 31, 2006, and $96,000 was expensed during the year ended December 31, 2007 and $48,000 was expensed in the period ended June 30, 2008. The remaining $64,000 was deferred to future periods.

continued…

**6. SHARE CAPITAL (continued)**

*c) Stock options and warrants (continued)*

Stock options issued and outstanding as at June 30, 2008 are as follows:

| Number of Options | Number of Shares issuable on exercise of options | Effective Strike Price ($/share) | Vesting Date | Expiry Date |
|---|---|---|---|---|
| # | # | $ | | |
| 50,000 | 150,000 | 0.283 | August 18, 2004 | August 18, 2009 |
| 150,000 | 450,000 | 0.283 | December 31, 2004 | December 31, 2009 |
| 66,666 | 66,666 | 0.200 | December 25, 2008 | June 25, 2010 |
| 66,667 | 66,667 | 0.200 | June 25, 2009 | June 25, 2010 |
| 66,667 | 66,667 | 0.200 | December 25, 2009 | June 25, 2010 |
| 8,333 | 25,000 | 0.317 | December 31, 2005 | June 30, 2010 |
| 41,667 | 125,000 | 0.283 | June 30, 2006 | June 30, 2010 |
| 292,500 | 244,974 | 0.239 | July 28, 2005 | July 28, 2010 |
| 66,667 | 200,000 | 0.317 | August 31, 2006 | August 31, 2010 |
| 220,620 | 220,620 | 0.300 | December 4, 2006 | December 3, 2010 |
| 8,333 | 25,000 | 0.317 | December 31, 2005 | December 31, 2010 |
| 41,666 | 125,000 | 0.283 | December 31, 2006 | December 31, 2010 |
| 11,770 | 11,770 | 0.300 | January 4, 2007 | January 3, 2011 |
| 11,770 | 11,770 | 0.300 | February 4, 2007 | February 3, 2011 |
| 11,770 | 11,770 | 0.300 | March 4, 2007 | March 3, 2011 |
| 50,000 | 150,000 | 0.283 | March 23, 2007 | March 23, 2011 |
| 11,770 | 11,770 | 0.300 | April 4, 2007 | April 3, 2011 |
| 11,770 | 11,770 | 0.300 | May 4, 2007 | May 3, 2011 |
| 11,770 | 11,770 | 0.300 | June 4, 2007 | June 3, 2011 |
| 8,333 | 25,000 | 0.317 | December 31, 2005 | June 30, 2011 |
| 58,333 | 175,000 | 0.283 | June 30, 2007 | June 30, 2011 |
| 150,000 | 450,000 | 0.283 | June 30, 2007 | June 30, 2011 |
| 66,667 | 200,000 | 0.317 | August 31, 2007 | August 31, 2011 |
| 50,000 | 150,000 | 0.283 | August 31, 2007 | August 31, 2011 |
| 250,000 | 750,000 | 0.283 | November 1, 2007 | November 1, 2011 |
| 50,000 | 50,000 | 0.300 | December 4, 2007 | December 3, 2011 |
| 16,667 | 50,000 | 0.283 | December 31, 2007 | December 31, 2011 |
| 100,000 | 300,000 | 0.283 | December 31, 2007 | December 31, 2011 |
| 86,667 | 86,667 | 0.250 | November 24, 2007 | May 24, 2012 |
| 86,667 | 86,667 | 0.250 | May 24, 2008 | May 24, 2012 |
| 86,667 | 86,667 | 0.250 | November 24, 2008 | May 24, 2012 |
| 316,671 | 316,671 | 0.250 | June 25, 2008 | June 25, 2012 |
| 316,664 | 316,664 | 0.250 | June 25, 2009 | June 25, 2012 |
| 316,664 | 316,664 | 0.250 | June 25, 2010 | June 25, 2012 |
| 16,667 | 50,000 | 0.283 | June 30, 2008 | June 30, 2012 |
| 66,667 | 200,000 | 0.317 | August 31, 2008 | August 31, 2012 |

continued…

**6. SHARE CAPITAL (continued)**

*c) Stock options and warrants (continued)*

| Number of Options | Number of Shares issuable on exercise of options | Effective Strike Price ($/share) | Vesting Date | Expiry Date |
|---|---|---|---|---|
| # | # | $ | | |
| 50,000 | 50,000 | 0.300 | December 4, 2008 | December 3, 2012 |
| 200,000 | 200,000 | 0.200 | April 4, 2009 | April 4, 2013 |
| 200,000 | 200,000 | 0.200 | April 4, 2010 | April 4, 2013 |
| 200,000 | 200,000 | 0.200 | April 4, 2011 | April 4, 2013 |
| 266,666 | 266,666 | 0.200 | June 25, 2009 | June 25, 2013 |
| 266,667 | 266,667 | 0.200 | June 25, 2010 | June 25, 2013 |
| 266,667 | 266,667 | 0.200 | June 25, 2011 | June 25, 2013 |
| 4,693,740 | 7,046,214 | | | |

The total number of common shares that are issuable pursuant to stock options that are exercisable as at June 30, 2008 is 4,476,219.

Details of the warrants outstanding as at June 30, 2008 are as follows:

| | Number of warrants # | Number of shares issuable on exercise of warrants # | Weighted Exercise Price (/share) $ |
|---|---|---|---|
| Outstanding and exercisable as at December 31, 2007 | 4,939,402 | 6,689,402 | 0.259 |
| Granted | 3,333,333 | 3,333,333 | 0.200 |
| Exercised | | - | - |
| Cancelled or expired | (361,086) | (361,086) | 0.300 |
| Outstanding and exercisable as at June 30, 2008 | 7,911,649 | 9,661,649 | 0.237 |

The weighted average grant date fair value of the warrants issued during the period ended June 30, 2008 is $0.02. Fair value of the warrants granted during the period ended June 30, 2008 has been estimated on the date of issue using the Black-Scholes pricing model with the following assumptions: expected dividend yield 0%, expected volatility 108%, risk-free interest rate 2.63%, and expected life of one year.

continued…

**6. SHARE CAPITAL (continued)**

Warrants outstanding and exercisable as at June 30, 2008 are as follows:

| Number of Warrants # | Number of shares issuable on exercise of warrants # | Effective Strike Price (/share) $ | Fair value $ | Expiry Date |
|---|---|---|---|---|
| 1,907,500 | 1,907,500 | 0.300 | 103,950 | August 3, 2008 |
| 1,895,112 | 1,895,112 | 0.300 | 160,193 | October 24, 2008 |
| 275,704 | 275,704 | 0.220 | 30,904 | October 24, 2008* |
| 3,333,333 | 3,333,333 | 0.200 | 67,645 | March 14, 2009 |
| 500,000 | 2,250,000 | 0.222 | 120,000 | March 16, 2009* |
| 7,911,649 | 9,661,649 | | 482,692 | |

* These warrants were issued as compensation for services performed and their fair value is recorded in contributed surplus. The remaining warrants were issued pursuant to private placements and their fair value is recorded as part of share capital.

*d) Escrowed shares*

On March 15, 2006, Cannasat amalgamated with Lonsdale Public Ventures ("Lonsdale"), a capital pool company. For details of the amalgamation see Note 6(d) in the audited financial statements of the Company for the year ended December 31, 2007.

Immediately following the amalgamation, 38,705,837 common shares of the Company were subject to escrow. 34,608,879 of these escrowed shares are to be released over a period of 72 months on the basis of 5% to be released six months after the final Exchange bulletin (March 23, 2006), 5% to be released every six months thereafter for the next 18 months and 10% to be released every six months thereafter for the next 48 months. The remaining 4,096,958 escrowed shares are to be released over a period of 36 months on the basis of 10% to be released on the date of the final Exchange bulletin and 15% to be released every six months thereafter.

At June 30, 2008, 27,687,104 of the 72-month release shares and 1,229,090 of the 36-month release shares are still subject to escrow.

*e) Contributed Surplus*

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

| | |
|---|---|
| Balance, December 31, 2007 | $ 1,000,372 |
| Compensation – stock option expense during the period – employee | 78,360 |
| Compensation – stock option expense during the period – non-employee | 1,788 |
| Balance, June 30, 2008 | $ 1,080,520 |

## 7. OTHER INTANGIBLE ASSETS

On June 10, 2005, the Company entered into a licence agreement with a research and development company. The License fee of $200,000 was satisfied by the execution and delivery of two promissory notes on June 30, 2005 (see Note 8) in the aggregate principal amount of $100,000 and the issuance of 117,648 Class A common shares at an aggregate subscription price of $100,000. In addition to the acquisition costs, the Company has agreed to pay a combination of milestone-based payments and royalties. The licence is for patents that have been issued in certain jurisdictions and are currently pending in others.

## 8. NOTES PAYABLE

Promissory notes in the aggregate principal amount of $100,000 were issued by the Company on June 30, 2005 in connection with the acquisition of the agreement for the worldwide 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 was due on demand no earlier than December 30, 2005, following which it may be converted in whole or in part into common shares no later than June 30, 2009 at $0.2833 per share 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, 88,236 Class A common shares at $0.2833 per share may be issued at the option of the issuer as full and final settlement of the note. The second promissory note may also be converted in whole or in part into common shares no later than June 30, 2009 at $0.2833 per share at the option of the holder.

## 9. RELATED PARTY TRANSACTIONS

Related party transactions have been recorded at the exchange amount that is management's estimate of the fair value of such transactions as follows:

| | Six Months Ending, June 30 | |
|---|---|---|
| | 2008 | 2007 |
| Management fees | $ 80,000 | $ 75,000 |
| Director fees | 14,800 | - |
| | $ 94,800 | $ 75,000 |

At June 30, 2008, included in accounts payable and accrued liabilities is $11,204 (December 31, 2007 - $21,797) due to officers and directors of the Company. At June 30, 2008, included in sundry receivables is $8,364 (December 31, 2007 - 9,393) due from officers of the Company. These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

## 10. COMMITMENTS

The Company is party to certain management contracts for its executive officers. Minimum management contract termination commitments remaining under the agreements are approximately $206,000 and are all payable within one year.

The Company has entered into a research and development contract requiring total payments of approximately $26,131 which are due upon the completion of certain performance criteria.

## 11. SUPPLEMENTARY CASH FLOW INFORMATION

| | Three Months Ending June 30, | | Six Months Ending June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| Income taxes paid | $ - | $ - | $ - | $ - |
| Interest paid | 659 | 2,004 | 659 | 5,258 |
| The following significant transactions did not generate or use cash: | | | | |
| Common shares issued for services | (25,000) | - | (25,000) | - |
| Contributed surplus | 46,208 | 68,724 | 80,148 | 676,249 |
| Compensation expense | (70,208) | (61,820) | (128,148) | (119,123) |

## 12. SUBSEQUENT EVENTS

On August 12, 2008 the Company announced that it closed a non-brokered private placement of units effective August 8, 2008. The Company issued an aggregate of 1,175,000 Units at a price of $0.20 per Unit raising gross proceeds of $235,000. Each Unit consists of one common share and one common share purchase warrant. Each common share purchase warrant entitles the holder to acquire one common share at a price of $0.22 for a period ending on the earlier of 18 months from the closing date, and a period ending 20 days after prior written notice from the Company that the closing price of its shares on the principal stock exchange of the Company has been at least $0.30 per share for 20 consecutive trading days.