



BCSC British Columbia Securities Commission

# QUARTERLY AND YEAR END REPORT

BC FORM 51-901  
(previously Form 61)

**Freedom of Information and Protection of Privacy Act:** The personal information requested on this form is collected under the authority of and used for the purpose of administering the Securities Act. Questions about the collection or use of this information can be directed to the Supervisor, Financial Reporting (604-899-6729), PO Box 10142, Pacific Centre, 701 West Georgia Street, Vancouver BC V7Y 1L2. Toll Free in British Columbia 1-800-373-6393

## INSTRUCTIONS

This report must be filed by Exchange Issuers within 60 days of the end of their first, second and third fiscal quarters and within 140 days of their year end. "Exchange issuer" means an issuer whose securities are listed and posted for trading on the Canadian Venture Exchange and are not listed and posted on any other exchange or quoted on a trading or quotation system in Canada. Three schedules must be attached to this report as follows:

### SCHEDULE A: FINANCIAL STATEMENTS

Financial statements prepared in accordance with generally accepted accounting principles are required as follows:

*For the first, second and third financial quarters:*

Interim financial statements prepared in accordance with section 1751 of the CICA Handbook, including the following: balance sheet, income statement, statement of retained earnings, cash flow statement, and notes to the financial statements.

The periods required to be presented, consistent with CICA Handbook section 1751, are as follows:

- a balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding fiscal year;
- a statement of retained earnings cumulatively for the current fiscal year-to-date, with a comparative statement for the comparable year-to-date period of the immediately preceding fiscal year; and
- income statements and cash flow statements for the current interim period and cumulatively for the current fiscal year-to-date, with comparative statements for the comparable interim periods (current and year-to-date) of the immediately preceding fiscal year.

*For the financial year end:*

Annual audited financial statements prepared on a comparative basis.

Exchange Issuers with a fiscal year of less than or greater than 12 months should refer to National Policy No. 51 *Changes in the Ending Date of a Financial Year and in Reporting Status* for guidance.

Issuers in the development stage are directed to the guidance provided in CICA Accounting Guideline AcG-11 *Enterprises in the Development Stage* that states "enterprises in the development stage are encouraged to disclose in the income statement and in the cash flow statement cumulative balances from the inception of the development stage."

Issuers that have been involved in a reverse take-over should refer to the guidance found in BCIN #52-701 (previously NIN #91/21) with respect to such transactions including the requirement for disclosure of supplementary information regarding the legal parent's prior financial operations.

### SCHEDULE B: SUPPLEMENTARY INFORMATION

The supplementary information set out below must be provided when not included in Schedule A.

#### 1. *Analysis of expenses and deferred costs*

Provide a breakdown of amounts presented in the financial statements for the following: deferred or expensed exploration, expensed research, deferred or expensed development, cost of sales, marketing expenses, general and administrative expenses, and any other material expenses reported in the income statement and any other material deferred costs presented in the balance sheet.

The breakdown should separately present, at a minimum, each component that comprises 20% or more of the total amount for a material classification presented on the face of the financial statements. All other components of a material classification may be grouped together under the heading "miscellaneous" or "other" in the cost breakdown; the total for "miscellaneous" should not exceed 30% of the total for a material classification.

Breakdowns are required for the year-to-date period only.  
Breakdowns are not required for comparative periods.

Issuers in the development stage are reminded that Section 3(9)(b) of the BC Securities Commission's Rules requires a schedule or note to the financial statements containing an analysis of each of exploration, research, development and administration costs, whether expensed or deferred and if the issuer is a natural resource issuer, that analysis for each material property. Because the analysis required by Rule 3(9)(b) must be included in the financial statements, the information does not have to be repeated in Schedule B. Consistent with CICA Accounting Guidelines AcG-11, staff considers an issuer to be in the development stage when it is devoting substantially all of its efforts to establishing a new business and planned principal operations have not commenced. Further, in staff's view, the lack of significant revenues for the past two years normally indicates that an issuer is in the development stage.

#### 2. *Related party transactions*

Provide disclosure of all related party transactions as specified in Section 3840 of the CICA Handbook.

#### 3. *Summary of securities issued and options granted during the period*

Provide the following information for the year-to-date period:

- (a) summary of securities issued during the period, including date of issue, type of security (common shares, convertible debentures, etc.), type of issue (private placement, public offering, exercise of warrants, etc.) number, price, total proceeds, type of consideration (cash, property, etc.) and commission paid, and
  - (b) summary of options granted during the period, including date, number, name of optionee for those options granted to insiders, generic description of other optionees (e.g. "employees"), exercise price and expiry date.
- #### 4. Summary of securities as at the end of the reporting period
- Provide the following information as at the end of the reporting period:
- (a) description of authorized share capital including number of shares for each class, dividend rates on preferred shares and whether or not cumulative, redemption and conversion provisions
  - (b) number and recorded value for shares issued and outstanding,
  - (c) description of options, warrants and convertible securities outstanding, including number or amount, exercise or conversion price and expiry date, and any recorded value, and
  - (d) number of shares in each class of shares subject to escrow or pooling agreements.

#### 5. *List the names of the directors and officers as at the date this report is signed and filed.*

**SCHEDULE C: MANAGEMENT DISCUSSION AND ANALYSIS**



1. **General Instructions**
  - (a) Management discussion and analysis provided management with the opportunity to discuss an issuer's business, current financial results, position and future prospects.
  - (b) Focus the discussion on material information, including liquidity, capital resources, known trends, commitments, events, risks or uncertainties, that is reasonably expected to have a material effect on the issuer.
  - (c) For an issuer with active ongoing operations the discussion should be substantive (e.g. generally two to four pages in length); for an issuer with limited operations the discussion may not be as extensive (e.g. generally two to four pages in length); for an issuer with limited operations the discussion may not be as extensive (e.g. one page).
  - (d) The discussion must be factual, balanced and non-promotional.
  - (e) Where the discussion relates to a mineral project, as defined in National Instrument 43-101 "Standards of Disclosure for Mineral Projects," the disclosure must comply with NI 43-101.
2. **Description of Business**  
Provide a brief description of the issuer's business. Where an issuer is inactive and has no business, disclose these facts together with a description of any plans to reactivate and the business the issuer intends to pursue.
3. **Discussion of Operations and Financial Condition**  
Provide a meaningful discussion and analysis of the issuer's operations for the current year-to-date period presented in the financial statements. Discuss the issuer's financial condition as at the date of the most recent balance sheet presented in the financial statements.  
  
The following is a list of items that should be addressed in management's discussion and analysis of the issuer's operations and financial condition. This is not intended to be an exhaustive list of the relevant items.
  - (a) expenditures included in the analysis of expenses and deferred costs required under Securities Rule 3(9)(b) and Schedule B;
  - (b) acquisition or abandonment of resource properties material to the issuer including material terms of any acquisition or disposition;
  - (c) acquisition or disposition of other material capital assets including material terms of the acquisition, or disposition;
  - (d) material write-off or write-down of assets;
  - (e) transactions with related parties, disclosed in Schedule B or the notes to the financial statements;
  - (f) material contracts or commitments;
  - (g) material variances between the issuer's financial results and information previously disclosed by the issuer, (for example if the issuer does not achieve revenue and profit estimates previously released, discuss this fact and the reasons for the variance);
  - (h) material terms of any existing third party investor relations arrangements or contracts including:
    - i. the name of the person;
    - ii. the amount paid during the reporting period; and
    - iii. the services provided during the reporting period;
4. **Subsequent Events**  
Discuss any significant events and transactions that occurred during the time from the date of the financial statements up to the date that this report is certified by the issuer.
5. **Financings, Principal Purposes and Milestones**
  - (a) in a tabular format, compare any previously disclosed principal purposes from a financing to actual expenditures made during the reporting period.
  - (b) Explain any material variances and the impact, if any, on the issuer's ability to achieve previously disclosed objectives and milestones.
6. **Liquidity and Solvency**  
Discuss the issuer's working capital position and its ability to meet its ongoing obligations as they become due.

**How to File Under National Instrument 13-101 – System for Electronic Document Analysis and Retrieval (SEDAR)**

BC Form 51-901 Quarterly and Yearly end Reports are filed under Category of Filing: Continuous Disclosure and Filing Type: Interim Financial Statements or Annual Financial Statements. Schedule A (Financial Statements) is filed under Document Type: Interim Financial Statements or Annual Financial Statements. Schedule B (Supplementary Information) and Schedule C (Management Discussion) are filed under Document Type: BC Form 51-901 (Previously Document type Form 61 (BC)).

**Meeting the Form Requirements**

BC Form 51-901 consists of three parts: Instructions to schedules a, B and C, issuer details and a certificate. To comply with National Instrument 13-101 it is not necessary to reproduce the instructions that are set out in BC Form 51-901. A cover page to the schedules titled BC Form 51-901 that includes the issuer details and certificate is all that is required to meet the BC Form 51-901 requirements. The form of certificate should be amended so as to refer to one or two of the three schedules required to complete the report.

<b>ISSUER DETAILS</b>			FOR QUARTER ENDED		DATE OF REPORT		
NAME OF ISSUER <b>HEDLEY TECHNOLOGIES INC.</b>			September 30, 2004		YY	MM	DD
ISSUER ADDRESS <b>2601 MATHESON BLVD. E., SUITE 5</b>					04	11	18
CITY <b>MISSISSAUGA</b>	PROVINCE <b>ONTARIO</b>	POSTAL CODE <b>L4W 5A8</b>	ISSUER FAX NO. ( 905) 206-1413	ISSUER TELEPHONE NO. ( 905) 206-0013			
CONTACT NAME <b>JOSEPH ARCURI</b>			CONTACT POSITION <b>CFO</b>		CONTACT TELEPHONE NO. ( 905) 206-0013 X-301		
CONTACT EMAIL ADDRESS: jarcuri@hedleytech.com		WEB SITE ADDRESS <b>www.hedleytech.com</b>					
<b>Certificate</b> <i>The three schedules required to complete this Report are attached and the disclosure contained therein has been approved by the Board of Directors. A copy of this Report will be provided to any shareholder who requests it.</i>							
DIRECTOR'S SIGNATURE 		PRINT FULL NAME <b>PETER D. LOCKHARD</b>		DATE SIGNED 2004/11/18			
DIRECTOR'S SIGNATURE 		PRINT FULL NAME <b>RENE C. GOEHRUM</b>		DATE SIGNED 2004/11/18			

**HEDLEY TECHNOLOGIES INC.  
CONSOLIDATED BALANCE SHEET  
AS AT SEPTEMBER 30, 2004 AND DECEMBER 31, 2003**

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	<b>September 30</b>	<b>December 31</b>
	<b>2004</b>	<b>2003</b>
<b>ASSETS</b>		
<b>Current</b>		
Cash	\$ 101,926	\$ 183,416
Accounts receivable	146,545	77,972
Other receivable	400,000	-
Inventories	59,388	70,157
Prepaid expenses and deposits	10,094	410,045
	<u>717,953</u>	<u>741,590</u>
Equipment (at net book value)	26,351	31,796
	<u><b>\$ 744,304</b></u>	<u><b>\$ 773,386</b></u>
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	\$ 221,429	\$ 166,529
Deposits payable	70,656	-
	<u>292,085</u>	<u>166,529</u>
<b>SHAREHOLDERS' EQUITY</b>		
Share capital	6,854,828	6,842,828
Contributed surplus	23,755	23,755
Deficit	(6,426,364)	(6,259,726)
	<u>452,219</u>	<u>606,857</u>
	<u><b>\$ 744,304</b></u>	<u><b>\$ 773,386</b></u>

Approved by the Directors



**DIRECTOR**



**DIRECTOR**

**HEDLEY TECHNOLOGIES INC.  
CONSOLIDATED STATEMENT OF OPERATIONS AND DEFICIT  
FOR THE NINE AND THREE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003**

	Nine Months Ended		Three Month Period	
	September 30		July – September	
	2004	2003	2004	2003
<b>Revenue</b>				
Sales	\$ 645,425	\$ 746,451	\$ 242,253	\$315,257
Cost of goods sold	250,636	344,820	81,799	92,167
Gross profit	394,789	401,631	160,454	223,090
Royalties and other income	-	720	-	720
	394,789	402,351	160,454	223,810
<b>Expenses</b>				
Amortization and depreciation	5,373	122,911	1,802	28,286
Consultants	87,130	113,738	24,204	39,815
Management salaries	171,389	92,667	57,502	33,500
Equipment rental	479	471	-	159
Interest and bank charges	6,885	4,438	2,372	1,510
Foreign exchange	2,726	23,594	6,619	255
Legal and accounting	20,314	21,755	8,398	6,906
Office and miscellaneous	32,825	39,418	10,652	12,652
Printing and shareholder relations	7,595	7,517	1,347	1,905
Rent	12,163	11,469	4,076	3,878
Salary and benefits	111,955	126,557	33,979	44,228
Selling and marketing	39,350	25,929	23,868	9,370
Transfer agent and filing fees	9,119	10,216	2,260	1,374
Travel and accommodations	49,304	25,797	12,782	6,053
Warehousing	4,820	2,051	1,733	1,856
	561,427	628,528	191,594	191,747
<b>(Loss) Gain from operations</b>	(166,638)	(226,177)	(31,140)	32,063
<b>Gain on settlements</b>	-	11,063	-	11,063
<b>(Loss) Gain for the period</b>	(166,638)	(215,114)	(31,140)	43,126
<b>Deficit, beginning of period</b>	( 6,259,726)	(5,844,851)	(6,395,224)	(6,103,091)
<b>Deficit, end of period</b>	(\$ 6,426,364)	( \$ 6,059,965)	(\$ 6,426,364)	(\$ 6,059,965)
<b>(Loss) Gain per share</b>	(\$ 0.014)	(\$ 0.018)	(\$ 0.003)	\$ 0.003

**HEDLEY TECHNOLOGIES INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS  
FOR THE NINE AND THREE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003**

	Nine Months Ended		Three Month Period	
	September 30		July - September	
	2004	2003	2004	2003
<b>Operating activities</b>				
Net (loss) gain for the period	(\$ 166,638)	(\$ 215,114)	(\$ 31,140)	\$ 43,126
Items not requiring cash				
Amortization and depreciation	5,373	122,911	1,802	28,286
Other	72	-	-	-
	(161,193)	(92,203)	(29,338)	71,412
Change in non-cash working capital items:				
Accounts and other receivable	(468,573)	(104,397)	(70,678)	87,605
Inventories	10,769	(474,296)	11,011	(20,195)
Prepaid expenses and deposits	399,951	29,830	(82,851)	-
Accounts payable and accrued liabilities	54,900	124,830	98,069	(59,389)
<b>Cash (applied to) received from operating activities</b>	(164,146)	(516,236)	(73,787)	79,433
<b>Investing activities</b>				
Purchase of capital assets	-	(1,067)	-	-
Patents and deferred costs	-	(11,819)	-	(13)
<b>Cash used in investing activities</b>	-	(12,886)	-	(13)
<b>Financing activities</b>				
Proceeds from customer deposits	70,656	-	-	-
Proceeds from shares issued	-	400,000	-	-
Proceeds from exercised warrants	12,000	-	-	-
<b>Cash from financing activities</b>	82,656	400,000	-	-
<b>Increase (decrease) in cash</b>	(81,490)	(129,122)	(73,787)	79,420
<b>Cash, beginning of period</b>	183,416	418,295	175,713	209,753
<b>Cash, end of period</b>	\$ 101,926	\$ 289,173	\$ 101,926	\$ 289,173

**Schedule A**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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**1. Basis of presentation**

These consolidated financial statements present the accounts of Hedley Technologies Inc. (the "Company") and its two wholly owned subsidiaries, Hedley Technologies (USA) Inc. and HTI Agritech Inc. Hedley Technologies (USA) Inc. (formerly HTI Agritech (USA) Inc.) was incorporated on May 13, 1994 in the state of Washington, USA. HTI Agritech was incorporated on January 30, 1996 in the Province of British Columbia, Canada. Both subsidiaries commenced operations during 1996.

These financial statements have been prepared on the basis that the company will be able to realize its assets and satisfy its liabilities in the normal course of business. The Company has incurred substantial losses in its operating history resulting in a deficit of \$ 6,426,364 as at September 30, 2004. Continued operation of the Company as a going concern is dependent upon it obtaining adequate additional financing and/or generating sufficient revenues from its products.

All intercompany transactions have been eliminated in the consolidated financial statements. The accounts of Hedley Technologies (USA) Inc. have been consolidated using the temporal method of foreign currency translation.

**The financial statements contained herein have neither been reviewed nor audited by the Company's auditors.**

**2. Significant accounting policies**

The accounting policies of the Company are in accordance with Canadian Generally Accepted Accounting principles and their basis of application is consistent with that of the previous year. Outlined below are the policies considered to be particularly significant.

**(a) Equipment**

Equipment is stated at cost. The Company records amortization of equipment at the following rates and methods:

Furniture	20% declining balance
Equipment	20% declining balance
Mould and design drawings	20% declining balance
Computer equipment	30% declining balance

**(b) Inventories**

Finished goods and raw materials are stated at the lower of cost and net realizable value.

**(c) Foreign currency translation**

Amounts denominated in foreign currencies have been translated into Canadian dollars as follows:

- i. Monetary assets and liabilities at the rate of exchange prevailing at the balance sheet date;
- ii. Non-monetary assets and liabilities at the rate of exchange prevailing at the time of acquisition of the assets or assumption of the liabilities; and

**Schedule A**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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- iii. Revenue and expenses at rates approximating the rates of exchange prevailing on the transaction date except for amortization, which is translated at the same rate as the assets to which it relates.

Gains or losses on translation are included in current period's operations.

**(d) Future income taxes**

Income taxes are accounted for under the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that substantive enactment or enactment occurs.

**(e) Use of estimates by management**

The preparation of financial statements in conformity with Canadian Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

**(f) Revenue recognition**

Revenue resulting from the sale of goods is recognized when goods are shipped to and accepted by distributors, resellers or final customers.

**(g) Equipment**

Equipment consists of the following:

<b>September 30, 2004</b>	<b>Cost</b>	<b>Accumulated Amortization</b>	<b>Net Book Value</b>
Furniture	\$ 33,022	\$ 28,486	\$ 4,536
Equipment	26,266	21,750	4,516
Mould and design drawings	24,552	13,868	10,684
Computer Equipment	68,936	62,321	6,615
	<b>\$ 152,776</b>	<b>\$ 126,425</b>	<b>\$ 26,351</b>

**3. Income taxes**

As at December 31, 2003, the Company has accumulated operating losses for Canadian tax purposes of approximately \$ 2,202,000 and for American tax purposes of approximately US \$ 451,000, which may be carried forward to reduce taxable income in future years. The Canadian losses expire between the years 2004 and 2010, and the American losses expire between the years 2017 and 2022. The potential income tax benefits arising from these losses

**Schedule A**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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and carryforward amounts are not recorded as a future income tax asset due to the uncertainty of their utilization.

The Company also has excess of unamortized capital cost over net book value of equipment of approximately \$ 409,000, which can be used to reduce taxable income in future years. The company also has a carryforward of Investment Tax Credits of \$ 101,800 and a balance of Scientific Research and Experimental Development expenditures of approximately \$ 427,500 which can be carried forward and used to reduce taxable income in future years.

**4. Insurance Coverage**

The Company's insurance coverage expired on January 1, 2003 the Company continues to operate without insurance coverage.

**5. Financial instruments and concentration of risk**

The carrying values of cash, accounts receivable, long-term investment, accounts payable and accrued liabilities approximate their respective fair values.

It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial statements.

**Schedule B**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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**1. For the Nine Months Ended September 30, 2004**

**a) Selling and marketing**

	<b>2004</b>
Product trademark, registrations and permits	\$ 19,462
Freight-out and brokerage	683
Advertising materials	1,500
Conferences and exhibitions	8,200
Product advertising and promotions	9,505
	<b>\$ 39,350</b>

**b) Office and miscellaneous**

	<b>2004</b>
Utilities and maintenance	\$ 2,012
Office supplies	7,473
Postage and courier	7,666
Insurance	-
Telephone	13,927
Other	1,747
	<b>\$ 32,825</b>

**2. Related Party Transactions**

None

**3. For the Nine Months Ended September 30, 2004:**

**a) Securities Issued**

The following securities were issued during the period:

Date of Issue	Type of Security	Type of Issue	Number of Shares	Price per Share	Total Proceeds	Consideration
March 17, 2004	Common	Exercise of Warrants	70,000	\$ 0.10	\$ 7,000	Cash
May 3, 2004	Common	Exercise of Warrants	50,000	\$ 0.10	\$ 5,000	Cash

**Schedule B**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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**b) Options Granted**

On July 12, 2004, 30,000 options were issued at an exercise price of \$0.17 per share expiring on July 12, 2009 of which 25,000 were issued to certain Company directors and the remaining 5,000 to an employee.

**4. As at September 30, 2004:**

**a) Share Capital**

Authorized 100,000,000 common shares without par value; and  
25,000,000 preferred shares without par value

**b) Shares issued and outstanding**

	<u>Number of Shares</u>	<u>Amount</u>
Balance at beginning of year	12,195,195	\$ 6,854,828
Exercise of warrants	<u>120,000</u>	<u>12,000</u>
Balance at the end of the period	<u>12,315,195</u>	<u>\$ 6,854,828</u>

There are no preferred shares issued and outstanding.

**c) i) Stock Options**

The Company has granted stock options to directors and employees entitling them to acquire common shares of the Company as follows:

<b>Number of Shares</b>	<b>Exercise Price</b>	<b>Expiry Date</b>
740,000	\$0.10	January 17, 2006
150,000	\$0.10	December 19, 2007
20,000	\$0.10	October 31, 2007
105,000	\$0.25	October 30, 2008
30,000	\$0.17	July 12, 2009
<b>1,045,000</b>		

**ii) Warrants**

During 2003, the Company closed a private placement which included the sale of 2,000,000 units at a price of \$0.10 per unit. Each unit consisted of one common share and one warrant to purchase one common share at \$0.10 until March 4, 2005. As at September 30, 2004 there remain 1,880,000 warrants outstanding.

**d) Escrow Shares**

None

**Schedule B**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2004**

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**5. a) List of Directors**

René C. Goehrum	Milton Wakefield
Douglas Larson	Peter Lockhard

**b) List of Officers**

René C. Goehrum – Chairman and Chief Executive Officer  
Douglas Larson – President and Chief Operating Officer  
Joseph Arcuri – Chief Financial Officer

**Schedule C**  
**To Quarterly Report of Hedley Technologies Inc.**  
**For the Nine Months Ended September 30, 2003**

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The following discussion is based on Hedley Technologies Inc.'s ("Hedley" or the "Company") interim consolidated financial statements for the nine months ended September 30, 2004, which were prepared in accordance with Canadian generally accepted accounting principles. The discussion of financial conditions and results of operations should be read in conjunction with the consolidated financial statements and notes. These consolidated financial statements were prepared by the Company's management and were neither reviewed nor audited by the Company's auditors.

## **Description of Business**

Hedley Technologies Inc. is a publicly traded life science company that acquires or licenses, products and commercializes proprietary science-based technologies that advance human health and public safety.

In late 2002 the Company made the strategic decision to focus on human health related technologies, initially in the medical diagnostic field and most recently in the specialty pharmaceutical industry. Under this direction, Hedley will be concentrating primarily on the sales and marketing of products which do not require further research or development and are poised for commercialization. Further, an integral part of Hedley's strategy will be to form alliances through licensing or partnership agreements with manufacturers of branded or generic products.

Hedley's first investment in this direction occurred in early 2003 when it acquired the INSTI<sup>®</sup> HIV-1/HIV-2 Rapid Antibody Test ("INSTI<sup>®</sup>") Global Master Distributorship rights under a long-term licensing and distribution agreement. This strategy was further augmented by announcements made late in the third quarter of 2004 and shortly thereafter, that Hedley would be acquiring two speciality pharmaceutical companies: Axxess Pharma Inc. and Medicor Pharmaceuticals Inc. (see Material Contracts below).

As part of its business, Hedley also manufactures and markets two products, namely Protect-It<sup>®</sup> and Insecolo<sup>™</sup>.

**Protect-It<sup>®</sup>** is a non-chemical, food-safe grain insecticide. The patented formula contains a natural mineral called diatomaceous earth ("DE"). Protect-It<sup>®</sup> was developed through collaborative research with the Winnipeg based Cereal Research Centre of Agriculture and Agri-Food Canada. Protect-It<sup>®</sup> is used as a preventative treatment against insect infestations in stored grains. It is registered for use in Canada, the United States, China, Croatia and Syria.

**Insecolo<sup>™</sup>** is a natural insecticide for home and garden use made from a patented formula of DE and food grade additives. It is registered for use in Canada, the United States and Japan.

**INSTI<sup>®</sup> HIV-1/HIV-2 Rapid Antibody Test** is a rapid in vitro qualitative test for the detection of antibodies to Human Immunodeficiency Viruses Types 1 and 2 (collectively referred to as HIV-1/2) in human whole blood, serum or plasma. The test is intended for use by trained personnel in medical facilities, clinical laboratories, and emergency care situations as a point-of-care test capable of providing results in less than sixty seconds. INSTI<sup>®</sup> clinical trials were completed in the second quarter of 2004 by the manufacturer and a dossier has been prepared and submitted to Health Canada for product approval. During this quarter, INSTI<sup>®</sup> received approval and registration from the Department of Health, Bureau of Food & Drugs for the Republic of the Philippines.

## **Results from Operations**

Sales for the nine months ended September 30<sup>th</sup>, 2004 were \$ 645,425 down \$101,026 (13.5%) from the same period in 2003 (\$ 746,451) and resulted entirely from lower Insecolo<sup>™</sup> sales. Year-to-date Insecolo<sup>™</sup> sales decreased 47% when compared to the prior year due to benefits derived in the previous year from initial investments made in inventory by our customer. Despite the overall decrease in dollar sales volume, gross margin declined 2% or \$7,562 when compared to the prior year.

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The net loss for the period ended September 30, 2004 was \$ 166,638 (2003 - \$ 215,114) down \$ 48,476 from the equivalent prior period. The net loss per share for the nine month period was \$0.014 down from \$ 0.018 per share for the period ending September 30, 2003. The decrease in year-to-date operating losses resulted from a decrease in depreciation charges of \$ 117,538, a \$ 20,868 decrease in foreign currency losses. These reductions in expenses were offset by increased human resources expenses of \$37,512, selling and marketing costs \$ 13,421 and travel and accommodation costs of \$ 23,507.

Total operating expenses for the quarter amounted to \$ 191,594, compared to \$ 191,747 for the equivalent prior year period. This decrease relates to decreased depreciation charges for the quarter offset by increased travel expenses and market development both of which were focused on INSTI<sup>®</sup>. Depreciation and amortization for the quarter decreased \$ 26,484 and is a reflection of the Company's reduced research and development initiatives and its migration to sales network and channel development. Net loss from operations for the current quarter increased by \$ 63,203 due to the numerous inventory deliveries fulfilled in the first and second quarters of the year which reduced third quarter deliveries.

As at September 30, 2004 current assets were \$ 717,953, down \$ 22,637 from December 31, 2003. Cash on hand at quarter end was down \$ 81,490 from December 31, 2003. Accounts receivable balances have increased when compared to prior fiscal year end due to the seasonality of the business. Accounts payable and accrued liabilities have increased by \$ 54,900 from fiscal 2003 year end, a significant portion of which relates to unpaid salaries to senior officers of the Company who have agreed to defer a portion of their base compensation.

During this fiscal year-to-date, 120,000 warrants have been exercised, at an exercise price of \$ 0.10, thus netting the Company a total of \$ 12,000. Of the 2,000,000 warrants issued as part of a 2003 private placement, 1,880,000 warrants remain outstanding and expire on March 4, 2005. As at September 30, 2004, 12,315,195 common shares were issued and outstanding.

The Company continues to operate without property and liability insurance and continues to seek appropriate coverage.

**Material Contracts**

To strengthen its business, diversify its operations and accelerate growth, Hedley is now executing on a strategy to compete in the speciality pharmaceutical market. The Company has announced two acquisitions that will form both a platform for growth as a specialty pharmaceutical company and provide a pipeline of products to be commercialized over the next four years.

The first of these acquisitions was announced on September 29 of this quarter and involved the signing of a Letter of Intent with Axxess Pharma Inc. ("Axxess"). Axxess is a privately owned pharmaceutical and diagnostic company located in Markham, Ontario. Axxess is focused primarily in the areas of dermatology, therapeutic nutrition and pain management both in prescription and over-the-counter ("OTC") medicines. It has distribution networks within Canada and internationally, principally selling to hospitals, wholesale distributors and pharmacies. Hedley has negotiated a share for share transaction to acquire Axxess and intends to invest in operations and working capital to grow the business to its full potential. Axxess has nine products that are currently sold in Canada and an additional ten products that are approved for sale, or have been sold in Canada in the past.

The parties have agreed in principle and have executed a Letter of Intent under which Hedley will issue 2.2 million shares in return for 100% of the shares of Axxess Pharma Inc. with a further 1.2 million shares available should certain performance criteria be met over a twenty-four month period following the close of the transaction. The transaction is expected to close by January 31, 2005 and is subject to normal due diligence and other conditions. It is Hedley's intention to continue to market the Axxess product line under the Axxess Pharma brand.

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Axxess' leading product is Triferexx<sup>®</sup>, a polysaccharide-iron complex used in the prevention and treatment of iron deficiency anemia, and nutritional megaloblastic anemia. During the nine month period ended September 30, 2004, Triferexx<sup>®</sup> sales increased 67% over the same period in 2003. Triferexx<sup>®</sup> is proving to be widely accepted amongst Nephrologists, Oncologists and Gynaecologists due to its unique capabilities. Triferexx<sup>®</sup> delivers a high level of elemental iron (150mg) while minimizing any gastrointestinal and other side effects commonly experienced with other iron preparations. This allows for high compliance rates amongst patients. Triferexx<sup>®</sup> competes in a market that totals over 1 million prescriptions per year.

Shortly after the end of the third quarter, Hedley announced that it had signed a Letter of Intent with Medicor Pharmaceuticals Inc. ("Medicor"). Medicor owns licensing arrangements with manufacturers of a portfolio of over 100 internationally proven pharmaceutical products which include both over-the-counter and prescription medicines. The therapeutic areas covered by this portfolio include anti-infectives, gastro-intestinals and others that complement those products owned and distributed by Axxess. Hedley will focus on ensuring that certain of these licensed products obtain Canadian regulatory approval and are marketed and distributed nationwide.

Under the Letter of Intent, Hedley may issue up to 1.4 million shares should performance criteria be met over the life of the acquired licensing agreements. The acquisition is expected to close by January 15, 2005 and is subject to normal due diligence and other conditions.

**Material Differences in Actual Use of Proceeds**

There has been no material difference in the actual use of proceeds from any previous disclosure by the issuer regarding the intended use of the proceeds.

**Investor Relations Activities**

Investor relations functions were accomplished through personnel whose duties include dissemination of news releases, investor communications and general day-to-day operations of the company. Mr. René Goehrum, Chairman and Chief Executive Officer, Mr. Douglas Larson, President and Chief Operating Officer and Mr. Joseph Arcuri, Chief Financial Officer, assist in the implementation of our investor relations program.

**Legal Proceedings, Liquidity and Solvency**

At this time, the Company is not aware of any legal or other contingent obligations. Working capital at September 30, 2004 was \$425,868 versus \$575,061 on December 31, 2003. Other than normal trade payables the Company is debt-free. Based on management's estimates and projections the Company will require further working capital, in the first quarter of 2005, to execute its business plan. In the event that material sales do not occur, management will seek additional capital through a public or private equity placement or other form of financing.